"It is governance, stupid"

■ *T. K. Jayaraman*

The Monetary Policy Committee (MPC) of the Reserve Bank of India (RBI) at the end of its first bi-monthly meeting of the new fiscal year on April 5, 2018, took the decision to maintain its benchmark repo interest rate at 6%. This decision has been taken for the next two months. Consequently, the reverse repo rate was left unchanged at 5.75% and the bank rate at 6.25%. The decision was expected.

Two reasons

The signs were clear that the Indian economy did not show signs of either heating up or show any worrying decline in growth since the last bi-monthly meeting of February 2018 of the last fiscal year.

Lower inflation at 4.8% during January–February 2018 than the projected 5.1% for the first quarter of 2018-19 was the chief reason that prompted the MPC decision. As vegetable prices had also declined in March, RBI reduced the projected inflation rate to 4.5% for the last quarter of 2017-18 from 5.1% to 4.5%. Assuming the continuation of favourable conditions, including normal monsoon, the projected inflation now for the first half of 2018-19 has also been stepped down from the range of 5.1-5.6% to the range of 4.7-5.1%; and for the second half, from the range of 4.5- 4.6% to just 4.4%.

Second reason was that concerns about decrease in growth were not seen to be alarming. RBI noted that the economy was being driven by consumption and there were also some indications of improvements in investment activities and credit flows. Further, although the growth in the just ended fiscal year was 6.6%, being one of the lowest in last four years, the RBI was confident that the economy would grow at 7.4% in 2018-19. It was also expected that India's projected growth rate would beat China's projected growth rate of 6.5%. Above all, the RBI felt that trade war with the announced imposition of tariffs on steel and aluminum and subsequent assertions of retaliatory action by China would not have an immediate impact on India and hence the growth projections of 7.4% do not have to be revised. So, according to the RBI, the Indian economy is not growing at any break-neck speed nor are there any indications of inflationary pressures for the present.

"A Goldilocks Economy"

The popular description of such an economy is "Goldilocks economy". The term was widely used when any reference was made to the US economy in the 1990s, when growth was not causing any inflation (that is not too hot) or when growth was low but not leading to recession (that it is not too cold). Such an economy is given the name after the little girl in the popular children's fairy tale, *Goldilocks and the Three Bears*. Goldilocks liked the *Baby Bear's* soup, as it was just the right temperature, neither too hot nor too cold.

The RBI knows it has to be ready for any eventualities. The RBI is following a monetary policy framework of "inflation targeting" and the mandate is on "price stability with growth". The medium-term target is to maintain the consumer price index (CPI) inflation of 4% within a band of +/- 2%, while supporting growth.

Upside risks

The MPC highlighted the upside risks. They include warnings on adverse effects emanating from any bloated government budgets as the country is already in an election mode. Of course the other unfavourable effects would be arising out of revised minimum support prices on food items, besides the continuing effects of HRA, effects of any monsoon failures, either total or partial and effects of the volatile crude oil prices. The RBI did not ignore the likely trade war. The impact of trade war would start to be felt once the tariffs are imposed by the US on imports from China and the retaliatory actions by China would materialise.

So for the time being, things on the monetary side of economy look quiet: low inflation with growth; and rise trade protectionism sentiments have yet to assert its influence on the external sector of the Indian economy.

Can the government remain content?

Results of the latest bi-monthly Consumer Confidence Survey (CCS) are not good.

The RBI conducts a bi-monthly survey of about 5,400 respondents (adults above age 21+) in the six cities of Bangalore, Chennai, Delhi, Hyderabad, Kolkata, and Mumbai in regard to their prevailing views on current situation in comparison to a year ago; and their expectations for next one year on household income, spending, and general economic conditions affecting their lives. From the information collected, the RBI survey calculates two index numbers: Current Situation Index (CSI) and the other, the Future Expectation Index (FEI).

The CSI has been falling for the last one year. It was 96.9 in December 2017, which was the last round. It fell further to 95.1 in the latest round which is March 2018. Index below 100

indicates pessimism. Clearly the urban consumer's pessimism is rising. The FEI does not inspire any confidence either: It fell to 117.4 in March 2018 round from 122.6 in the previous December 2017 round.

Fear of losing hard earned money

Among the easily identifiable reasons, two stand out. One is the fear of the banking regime as a whole. Public sector banks (dominating the banking sector with 70% share of business) are known to have around 80% of the total bad loans of the banking system. They were ₹8,40,058 crores, amounting to 10.2% of total advances.

The public sector banks were also known for scams. The "mother of scams of all times" of ₹12,700 crore were detected in the first half of March last month with the third largest public sector bank: the Punjab National Bank (PNB). The PNB has the largest number of bank scams in the history of banking in India and the exact number is 389. The second half of March news was about a three-bank fraud by the Chennai based Nathella Sampathu Chetty jewelers. The amount was around ₹ 350 crore. The defrauded banks are State Bank of India, Union Bank of India and HDFC.

Every urban-based consumer has a bank account. He knows, as long as public sector banks exist, bad loans and scams will be continuing as an "old normal". He cannot do anything of his own except shifting his funds to private banks. He had every reason to believe that private sector banks would be more efficient and "business-like" and can say" no" to politicians.

The "new normal"

With what happened in ICICI which is India's largest private bank has shaken the confidence of the consumers. Its CEO has betrayed the confidence of its customers. Added to that instance, we have the latest news that private sector banks would also be saddled with bad loans. The rattling news is the third largest private sector bank which is the Axis Bank's bad loans have doubled up in the latest September quarter to reach at ₹8,772 crore from the June quarter figure of ₹3,638 crore. With this, Axis Bank's gross non-performing assets are 4.2% of its loans, rising from 2.5% of last quarter.

To cap it all, the chief executives of three private sector banks were to receive bonuses: The ICICI CEO was to get ₹2.2 crore, Axis Bank CEO: ₹1.35 crore, and HDFC CEO: ₹2.9 crore. It is only postponed as the RBI has kept them on-hold. By postponing the bonuses, the government seems to be anxious to do something for salvaging its credibility before elections in 2019. Rephrasing the famous slogan, "It is the economy, stupid" used by the Democrats in the 1992 US presidential campaign, one could say, "It is governance, stupid!"

— Dr T .K. Jayaraman is an Adjunct Professor, Amrita School of Business, Bengaluru Campus.

[The views expressed by the author in this article is his own.]