

**Institute of South Asian Studies (ISAS)**

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***India and the Economic crisis –  
Impact, policy responses and future prospects***



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# *Structure of Talk*

- **Impact of global crisis on real economy, demand external sector credit , financial markets, fiscal and banking**
- **Responses – monetary (including external account), regulatory and fiscal measures**
- **Impact of response on financial markets and real sector**
- **Policy challenges and future prospects**

# *Global Crisis*

- **Impact on Emerging Markets**
  - **Trade route**
  - **Credit route**
  - **Banking route**
  - **Capital flows**

# **Indian Economy - Highlights**

Item		*1990-91 to 1999-00 (10 years)	*2003-04 to 2007-08 (5 years)	2008-09
<b>1</b>	<b>Real GDP ( % change )</b>	<b>5.7</b>	<b>8.8</b>	<b>6.7</b>
	<b>a) Agriculture ( % change )</b>	<b>3.2</b>	<b>5.1</b>	<b>1.6</b>
	<b>b) Industry ( % change )</b>	<b>5.7</b>	<b>8.1</b>	<b>2.6</b>
	<b>c) Services ( % change )</b>	<b>7.1</b>	<b>10.4</b>	<b>9.4</b>
<b>2</b>	<b>Per Capita Income ( % change )</b>	<b>3.6</b>	<b>7.3</b>	<b>4.9</b>
<b>3</b>	<b>Fiscal Deficit ( % of GDP )</b>	<b>5.9</b>	<b>3.7</b>	<b>6.1 RE</b>
<b>4</b>	<b>Broad Money ( M<sub>3</sub> ) Growth ( % change )</b>	<b>17.2</b>	<b>19.9</b>	<b>18.6</b>
<b>5</b>	<b>Bank Credit to Commercial Sector ( % of GDP )</b>	<b>28.8</b>	<b>47.5</b>	<b>55.5</b>
<b>6</b>	<b>Scheduled Commercial Banks ( % change )</b>			
	<b>a) Aggregate Deposits</b>	<b>17.2</b>	<b>21.2</b>	<b>19.9</b>
	<b>c) Non-Food Credit</b>	<b>15.4</b>	<b>23.3</b>	<b>17.8</b>
	<b>d) Investments in Government Securities</b>	<b>20.9</b>	<b>19.8</b>	<b>20.6</b>
<b>7</b>	<b>Average Wholesale Price Index ( % change )</b>	<b>8.1</b>	<b>4.9</b>	<b>8.3</b>
<b>8</b>	<b>Current Account ( % of GDP )</b>	<b>-1.3</b>	<b>-0.4</b>	<b>-2.6</b>
<b>9</b>	<b>Foreign Exchange Reserves ( US \$ Billion )</b>	<b>21.7</b>	<b>183.0</b>	<b>252</b>

\* Average; RE – Revised Estimates

## ***... After the Crisis – Impact on Real Economy***

### **Growth Rates of Real GDP (Quarterly) (per cent)**

<b>Sector</b>	<b>2008 – 2009</b>				<b>2009 - 2010</b>
	<b>Q1</b>	<b>Q2</b>	<b>Q3</b>	<b>Q4</b>	<b>Q1</b>
<b>Agriculture and Allied Activities</b>	<b>3.0</b>	<b>2.7</b>	<b>-0.8</b>	<b>2.7</b>	<b>2.4</b>
<b>Industry</b>	<b>5.1</b>	<b>4.8</b>	<b>1.6</b>	<b>-0.5</b>	<b>4.2</b>
<b>Services</b>	<b>10.0</b>	<b>9.8</b>	<b>9.5</b>	<b>8.4</b>	<b>7.7</b>
<b>Real GDP at Factor Cost</b>	<b>7.8</b>	<b>7.7</b>	<b>5.8</b>	<b>5.8</b>	<b>6.1</b>

## ***Impact on Demand Condition***

**Demand side of GDP (1999-2000 Prices) (per cent)**

Item	2007-08*	2008-09#	2008-09				2009-2010
			Q1	Q2	Q3	Q4	
1	2	3	4	5	6	7	8
<b>Growth Rates</b>							
(i) Private Final Consumption Expenditure	8.5	2.9	4.5	2.1	2.3	2.7	1.6
(ii) Government Expenditure	7.4	20.2	-0.2	2.2	56.6	21.5	10.2
(iii) Gross Fixed Capital Formation	12.9	8.2	9.2	12.5	5.1	6.4	4.2
(iv) Exports	2.1	12.8	25.6	24.3	7.1	-0.8	-10.9
Less Imports	6.9	17.9	27.4	35.3	21.7	-5.7	-21.1

\*: Quick Estimates      #: Revised Estimates.

**Source:** Central Statistical Organisation.

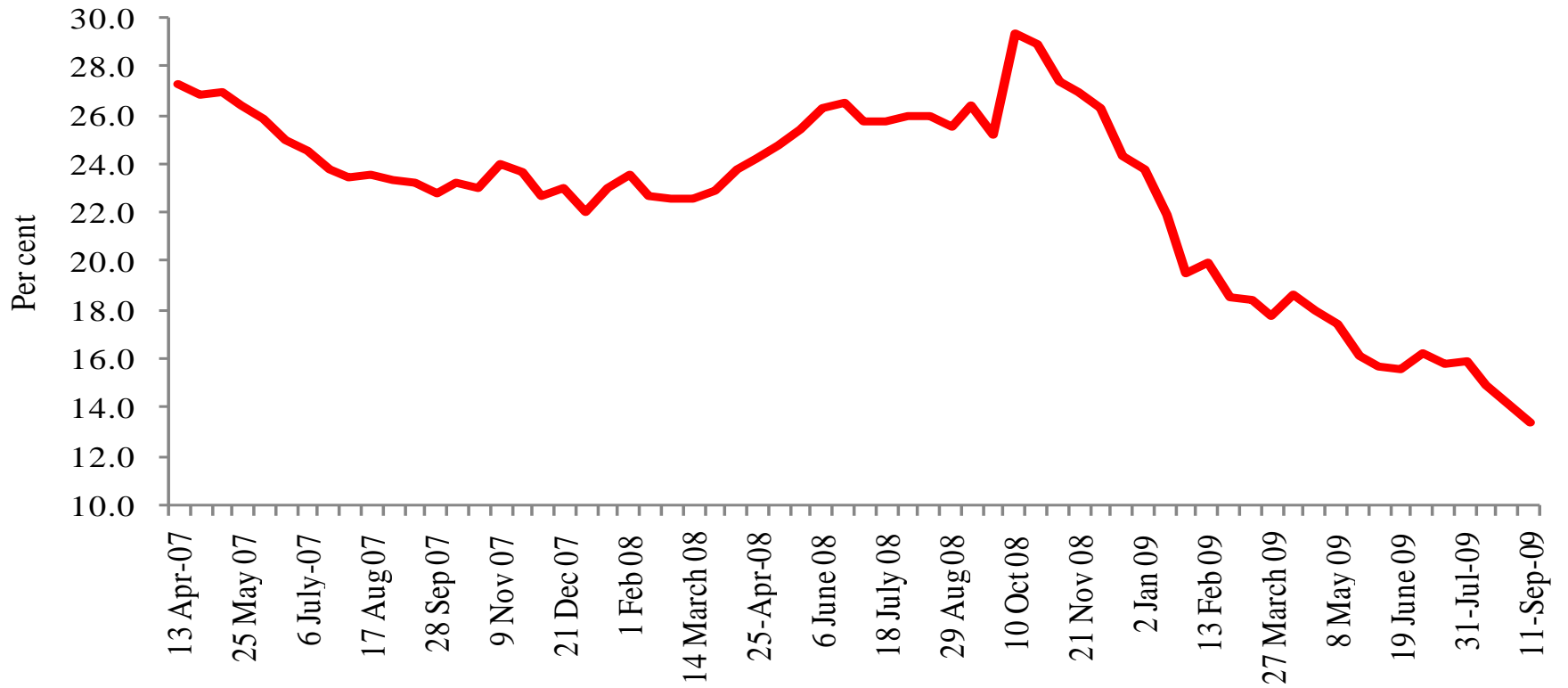
# *Impact on Capital Flows*

## Net Capital Flows (US\$ billion)

Item	2008-09	2008-09				2009-10
	April-March	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar	Apr-Jun
1	2	3	4	5	6	7
<b>1. Inward FDI</b>	<b>35.0</b>	<b>11.9</b>	<b>8.8</b>	<b>6.3</b>	<b>8.0</b>	<b>9.5</b>
<b>2. FII's</b>	<b>-15.0</b>	<b>-5.2</b>	<b>-1.4</b>	<b>-5.8</b>	<b>-2.6</b>	<b>8.2</b>
<b>3. External Commercial Borrowings</b>	<b>8.2</b>	<b>1.5</b>	<b>1.7</b>	<b>3.9</b>	<b>1.1</b>	<b>-0.4</b>
<b>4. NRI Deposits</b>	<b>4.3</b>	<b>0.8</b>	<b>0.3</b>	<b>1.0</b>	<b>2.2</b>	<b>1.8</b>
<b>5. Other Banking Capital</b>	<b>-7.7</b>	<b>1.9</b>	<b>1.9</b>	<b>-6.0</b>	<b>-5.4</b>	<b>-5.2</b>
<b>6. Short-term Trade Credits</b>	<b>-5.8</b>	<b>2.4</b>	<b>1.3</b>	<b>-4.0</b>	<b>-5.5</b>	<b>-3.1</b>

# *Non-Food Bank Credit*

## **Non-Food Bank Credit Growth (Year-on-Year)**



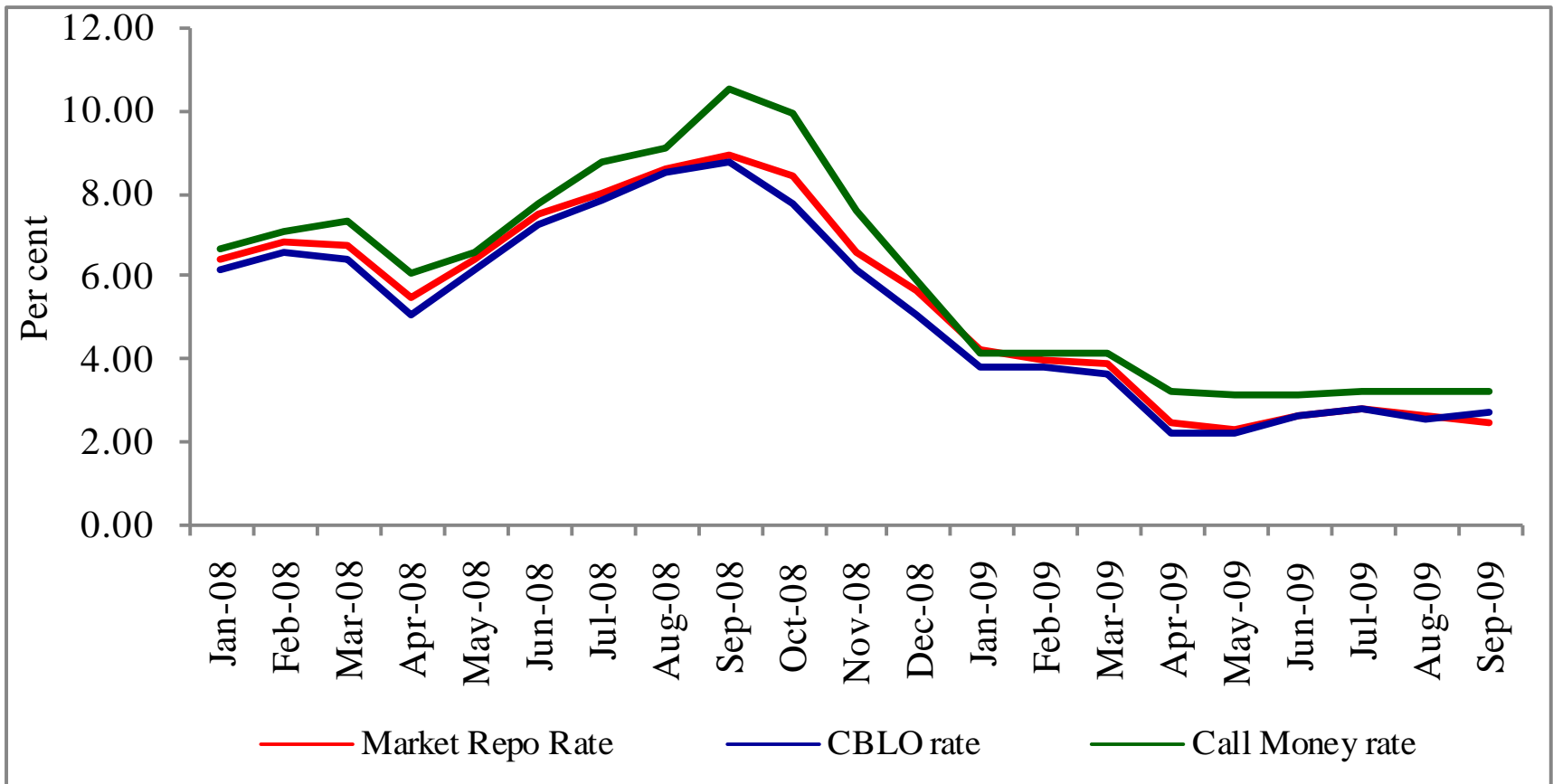
# ***Mobilisation of Bank Deposits – Rates rise and drop as credit demand rises and falls***

**Deposit Rates of Public Sector banks (range) ( per cent)**

	<b>March 2007</b>	<b>March 2008</b>	<b>Sept. 2008</b>	<b>Dec. 2009</b>	<b>March 2009</b>	<b>June 2009</b>
<b>Up to 1 year</b>	<b>2.75 - 8.75</b>	<b>2.75 - 8.50</b>	<b>2.75 - 10.25</b>	<b>2.75 - 10.25</b>	<b>2.75 - 8.25</b>	<b>1.00 - 7.00</b>
<b>&gt; 1year-3 years</b>	<b>7.25 - 9.50</b>	<b>8.25 - 9.25</b>	<b>8.75 - 10.25</b>	<b>8.50 - 10.75</b>	<b>8.00 - 9.25</b>	<b>6.50 - 8.00</b>
<b>&gt; 3 years</b>	<b>7.50 - 9.50</b>	<b>8.00 - 9.00</b>	<b>8.50 - 9.75</b>	<b>8.50 - 9.75</b>	<b>7.50 - 9.00</b>	<b>7.00 - 8.50</b>

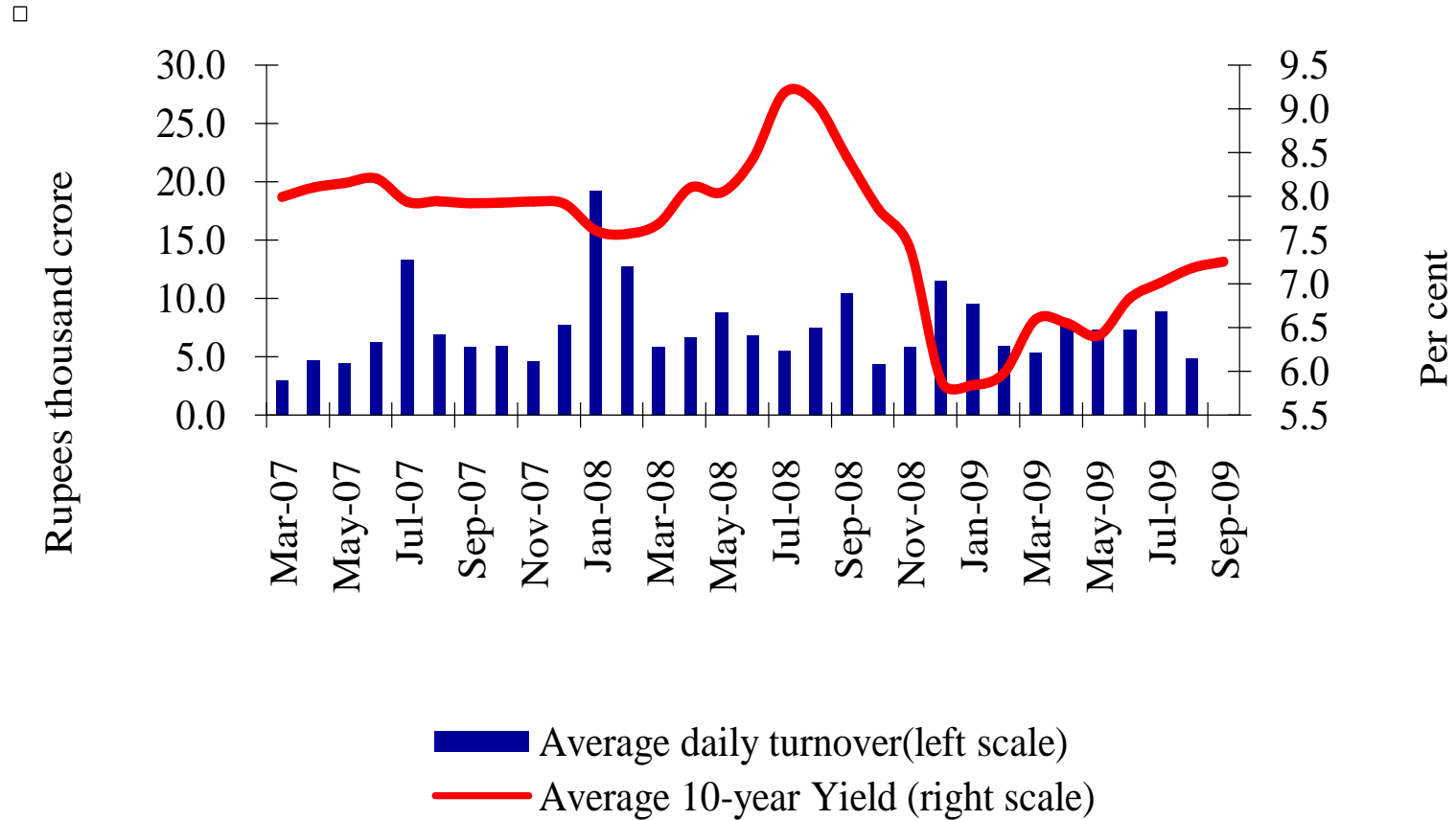
# Trends in Money Market

## Money Market Interest Rates

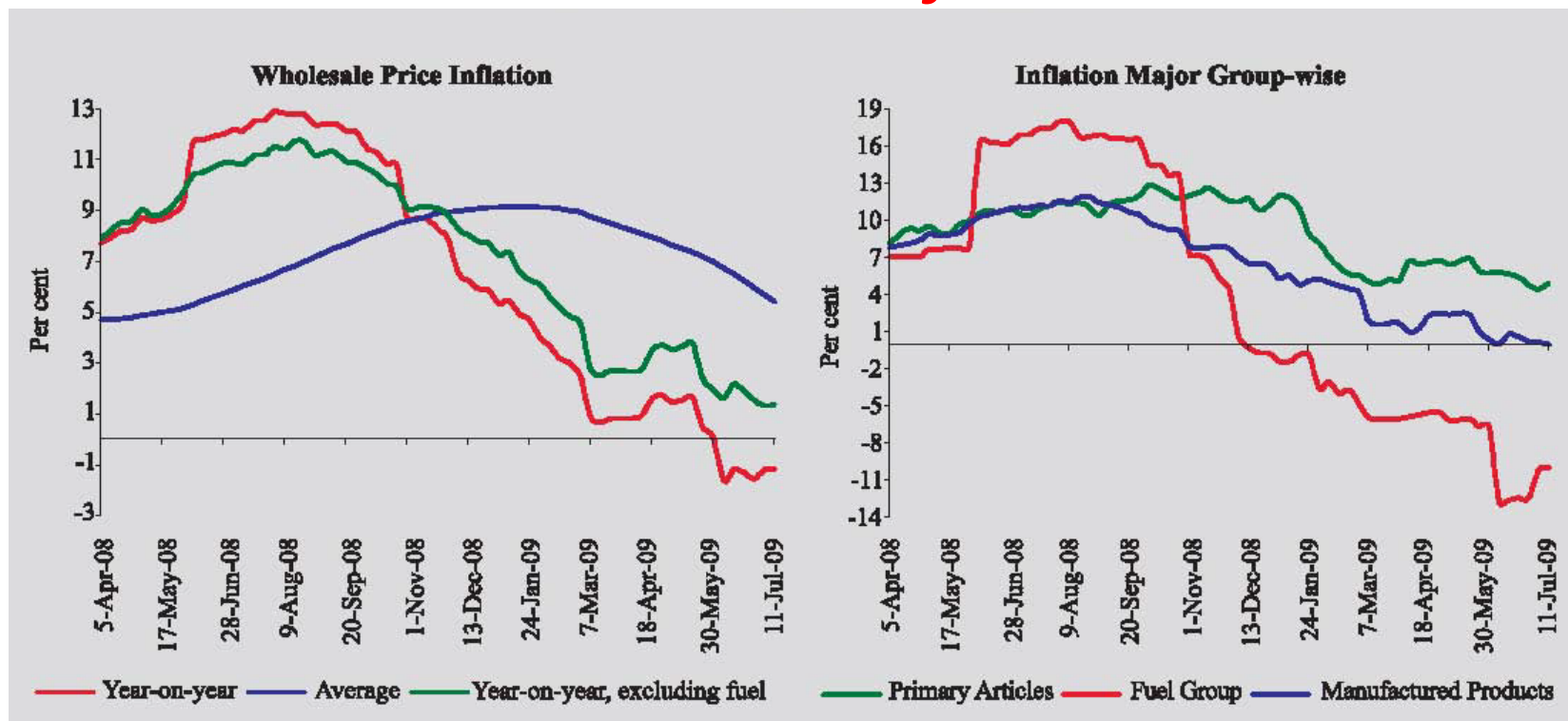


# G Secs – Firming up of Yields

## Average Daily Turnover and Yields in Government Securities Market



# Annual WPI Inflation



## WPI Inflation – declined sharply and turned negative

- Significant correction in international oil and other commodities prices
- High base effect – due to sharp increases in commodities prices in first half 2008-09.

## Consumer Price Indices (CPIs) – remain at elevated levels

- Mainly due to increase in the prices of food and primary articles

## ***Impact on Indian Banking Sector***

- **Banking system largely remained insulated - a few banks suffered some MTM losses – no systemic concern**
- **Indian banks position 2008-09 - reflected strength and resilience:**
  - **CRAR increased from 13.01% to 13.15% .**
  - **Gross and net NPA ratios stood at 2.42% and 1.12 % respectively**
  - **ROA increased from 0.99% to 1.02%; ROE from 12.52% to 13.25%**
  - **NIM increased from 2.37%. to 2.44%**
  - **Non-interest income registered a growth of 24.8%**

## ***Policy Response – Monetary Measures***

- **CRR reduced from 9 % to 5%; SLR reduced from 25% to 24%**
- **Repo rate reduced: 9 % to 4.75 %; Reverse repo: 6% to 3.25%**
- **Fresh issuances under MSS stopped**
  - **buyback of existing MSS securities resorted**
- **Term repo introduced through banks for MFs, NBFCs**
- **Special refinance facilities for specialized FIs**
  - **SIDBI, NHB and EXIM Bank**
- **Measures for forex liquidity**
  - **Sale of forex and swap facility (for overseas branches)**
  - **increase in interest rate ceilings on non-resident deposits (by 175 bps)**
  - **Easing of restrictions on ECB and on short-term trade credits**

# ***Regulatory Response***

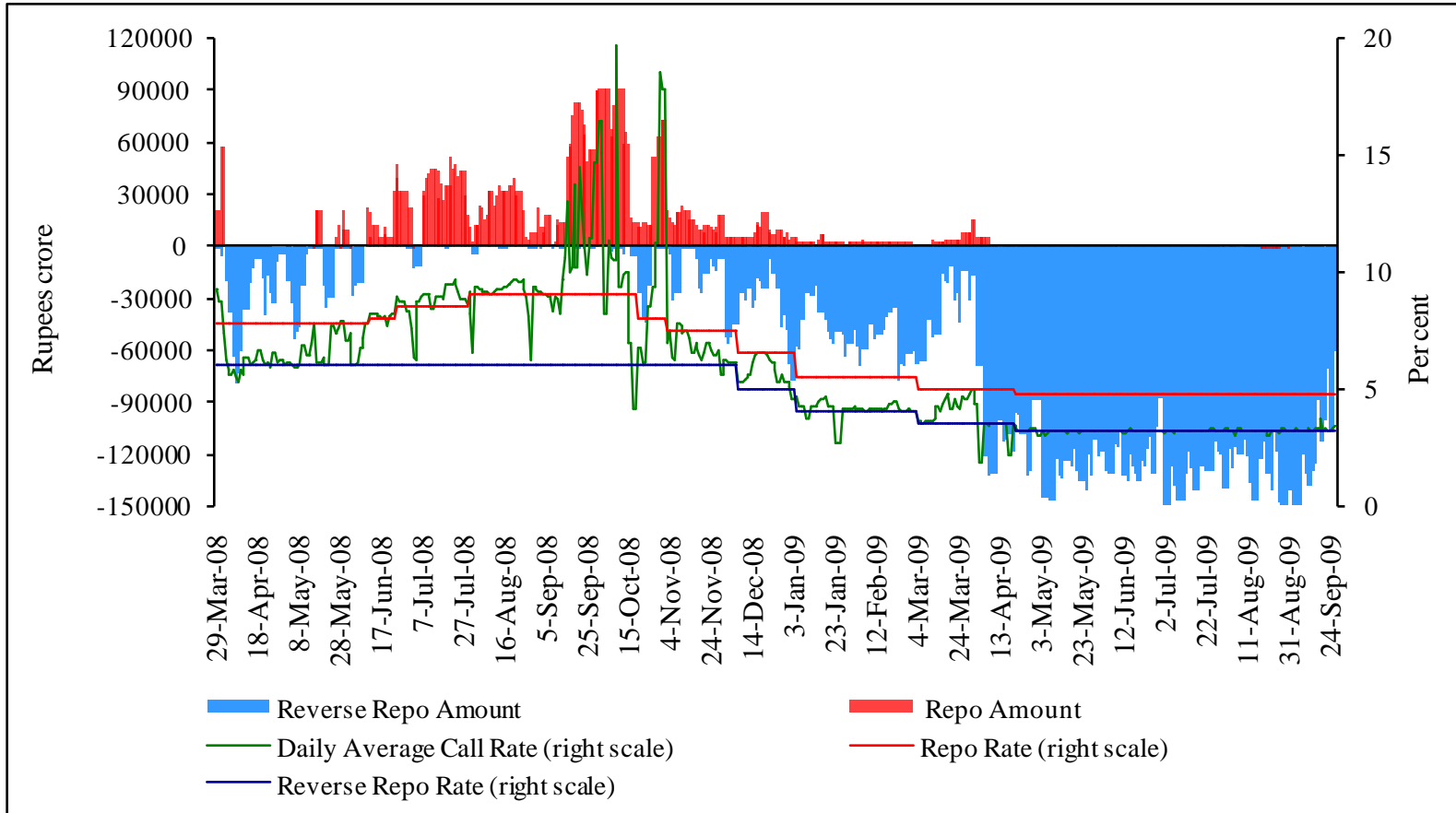
- **For mitigating pro-cyclicality**
  - **Provisioning for standard assets reduced to uniform level of 0.40% (except direct agricultural and SME advances at 0.25% as hitherto); earlier it had been raised to 1 % for specific sectors**
  - **Risk weights on unrated claims on corporates, claims secured by CRE and claims on NBFC-ND-SI reduced from 150 % to 100%**
- **For preserving the economic/productive value of assets**
  - **restructured accounts permitted to be treated as standard assets provided standard in Sep 2008**
- **NBFCs, in view of their need for raising capital, have been:**
  - **allowed to issue perpetual debt instruments**
  - **allowed time of one more year to comply with 15% CRAR**

# ***Fiscal Response***

- **Central Government invoked emergency provisions of FRBM Act from the fiscal targets and launched two stimulus packages in Dec'08 and Jan '09 amounting to 3% of GDP**
- **The stimulus packages included additional public spending, particularly:**
  - **Capital expenditure, Government guaranteed funds for infrastructure spending**
  - **Cuts in indirect taxes**
  - **Expanded guarantee cover for credit to MSEs**
  - **Additional support to exporters**
- **The stimulus packages came on top of already announced measures:**
  - **Expanded safety-net for rural poor**
  - **Farm loan waiver package and**
  - **Salary increases for government staff**

# Impact of Policy Actions

## Movement of the LAF and Call Money Rates

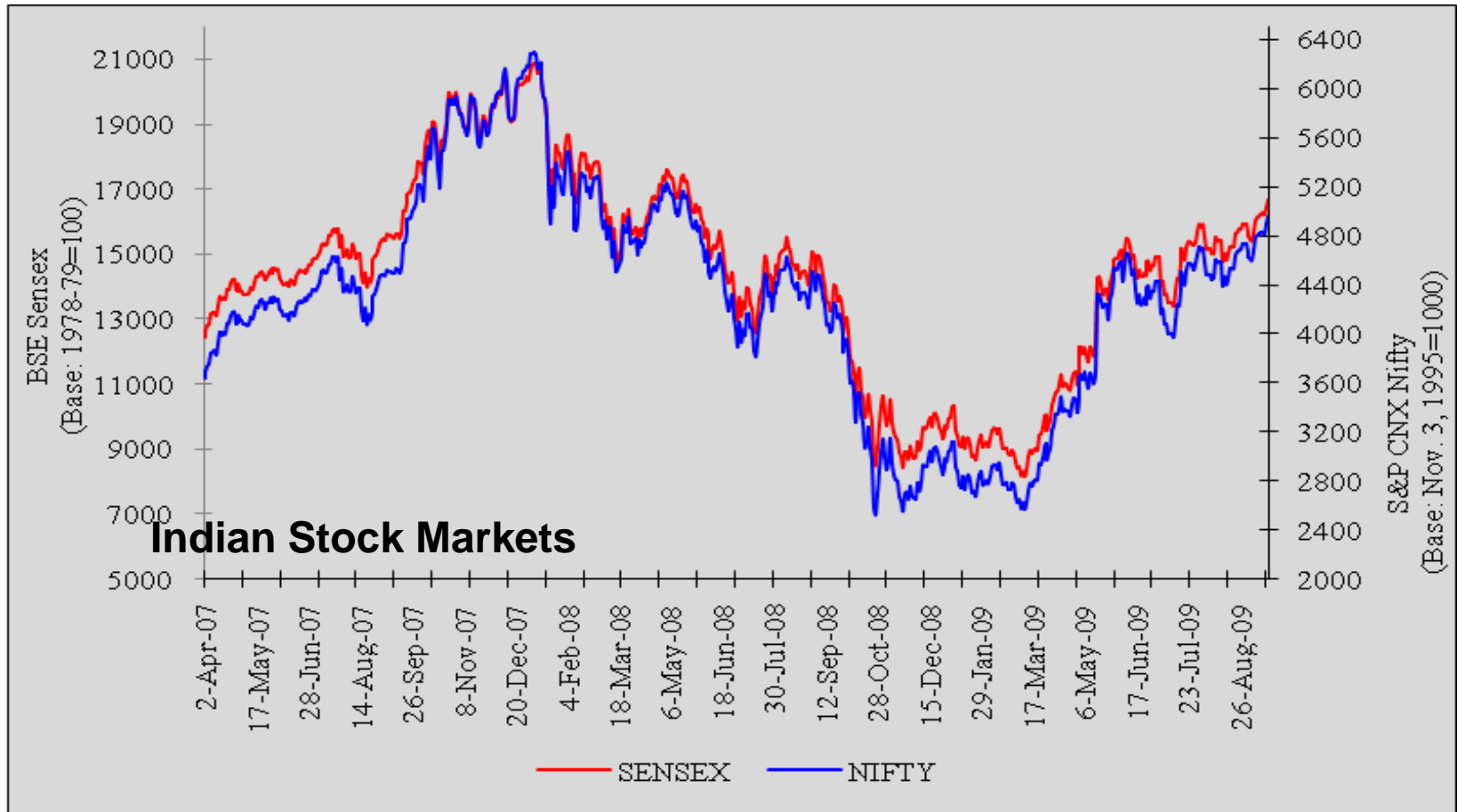


- **Inter-bank call rate reverts to (within) LAF corridor - LAF window in net absorption mode**

## ***Impact on Exchange Rate, Capital Flows, G Secs***

- **Appreciation in exchange rate of rupee to Rs.46.40 per dollar (Oct 09) vis-à-vis sharp depreciation from Rs.40.02 per US dollar (April 08) to Rs.51.23 per US dollar (March 09)**
- **Revival in capital inflows, particularly foreign investments – Capital account turnaround to a positive balance of US\$6.7 billion during the first quarter of 2009-10**
- **Overall, marginal increase in reserves on BoP basis (i.e. excluding valuation) during the first quarter of 2009-10**
- **10-year benchmark g secs yield softened relatively**

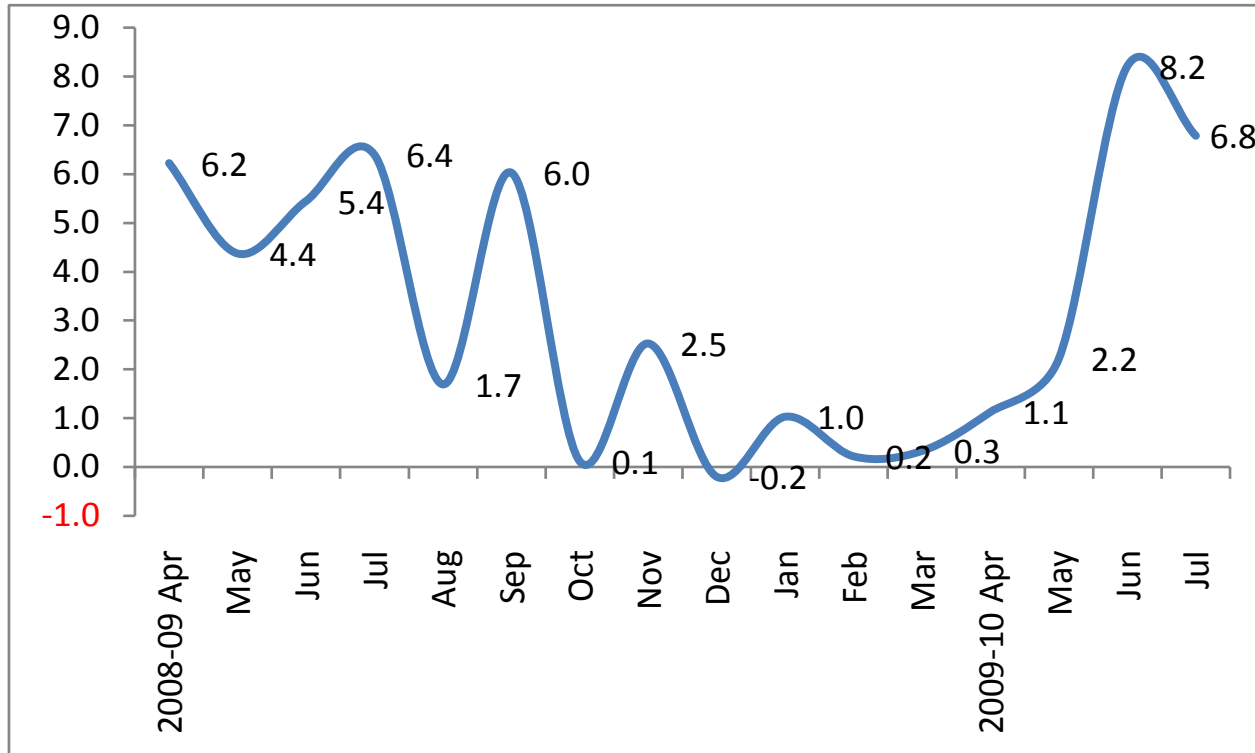
# Indian Stock Markets



- **Equity market revived indicating restoration of investor's confidence**

# Industrial Sector

Growth in Index of Industrial Production (Y-o-Y)



- Latest data on GDP indicates revival of growth mainly led by industrial sector
- On the demand side, growth led by higher Government consumption

## ***Fiscal Impact***

- **Deviation from fiscal consolidation path**
  - **Centre's fiscal deficit target (2008-09) - revised from 2.5 per cent to 6.2 per cent of GDP**
  - **Combined fiscal deficit (Centre and States) reached 10.7 per cent of GDP**
  - **Net market borrowings (Centre and States) jumped from 3.5 % of GDP in 2007- 08 to 7.5 % of GDP) in 2008-09**

## *Challenges faced by RBI*

- **Exiting accommodative monetary stance - Growth vs inflation**
- **Management of large capital flows**
- **Strengthening monetary transmission**
- **Managing government borrowing**
- **Financial development for inclusive growth – agriculture, SME and infrastructure**

## ***Future Prospects***

- **Infrastructure sector key to growth - implementation, funding and pricing**
- **Access to affordable credit, especially SME**
- **Capital formation in agriculture to increase productivity**
- **Skills – education and training**
- **Fiscal consolidation and quality of adjustment**

***Thank You***