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TENURE AS RBI GOVERNOR - Under Rajan, A GLASS HALF FULL

Rajan has ushered in many changes in an eventful 33 months as RBI chief, but it has not been easy going. While inflation is down, his handling of liquidity could have been better. That said, there is no denying he has laid the groundwork for a financial market that can match those in the developed world, says Gayatri Nayak

When Raghuram Rajan became the governor of the Reserve Bank of India nearly three years ago, the expectation was that he would unleash the capitalist thoughts of Chicago tradition on Indian central banking.

But 33 months later, the industry is disappointed because it didn't have its way on lower interest rates, and bankers are grumbling that they are being targeted for the faults of the polity and corrupt bureaucracy.

While his term comes to an end in early September, the past three years have seen many changes at the regulator, and the many promised still remain on the drawing board, raising questions as to whether the groundwork laid out would be used to build a superstructure -an industry that would be advanced and efficient matching the financial markets of the developed world.

The agenda set by Rajan himself was long, though he called it a short-term one from inflation targeting to trading of receivables to help small companies ease their cash crunch. Nearly half of them have been executed, and many are still in the works.

“His policy focus has been on two key pressure points, ie, containing inflation and currency volatility ,“ says Radhika Rao, economist at DBS in Singapore. “Notable progress has been made on both these fronts, also helped by a conducive external environment of low commodity prices and accommodative global policies.“

While economists and politicians like Subramanian Swamy are divided over inflation targeting and its impact on the economy , at least the government seems to have bought it as a policy goal. Consumer inflation, which used to run at double digits three years ago, has more than halved, though many would attribute the decline to the global slump in commodity prices and the collapse in crude oil price. But, in the process, Rajan upset many a constituency , especially the industry used to easy money .

One of the missteps of his tenure has been the way RBI has handled liquidity , which, the markets say , is because of the ineffectiveness of the interest rate cuts. After months of holding back rigidly to its policy of keeping the money market in deficit, he promised to correct the stance and move to a neutral stance.

The difference he brought to regulation was the way banks are treated by the central bank -historically , banks have been treated with kid gloves. The RBI has often ceded to the requests of banks on provisioning and has come up with ways to roll over bad loans. But, under Rajan, these practices ended.

Corporate Debt Restructuring, an euphemism for sweeping the recognition of stress in loans under the carpet, was buried. To move ahead, banks were forced to monitor the payments. Those accounts that missed the payments on the 60th day were classified as Special Mention Accounts (SMA) I and those that did not pay for 90 days were termed as SMA II. Banks had to get into action to prevent SMA II accounts from becoming a bad loan.

Some of these ideas were not new, but they suffered in the past due to non-cooperation from banks. Rajan created a repository of large accounts where banks were mandated to share details of defaulters with peers. While investors in general cheered the `clean-up' by

Rajan, those invested in banking stocks would never have imagined the damage to their portfolio. Many bankers still believe it is unfair on them, though they admit it would be good in the long term for the industry as well as the economy .

“AQR (asset quality review) is known to all,“ said Bank of Baroda executive director BB Joshi. “It's always good to keep the legacy

behind... It helps to concentrate on the right kind of business.“

(with inputs from Atmadip Ray)

**RADHIKA RAO,**
ECONOMIST, DBS, SINGAPORE

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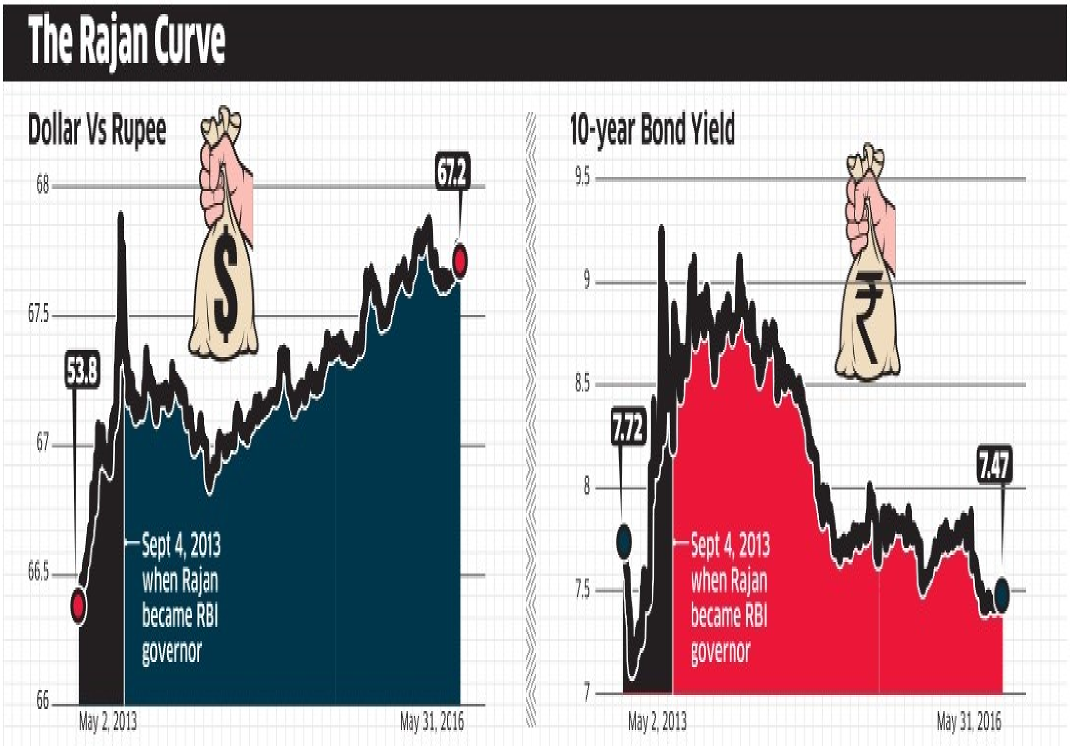
The Rajan Curve
Dollar Vs Rupee
68
67.5
67
66.5
66
53.8
67.2
Sept 4, 2013 when Rajan became RBI governor
May 2, 2013
May 31, 2016
10-year Bond Yield
9.5
9
8.5
8
7.5
7
7.72
7.47
Sept 4, 2013 when Rajan became RBI governor
May 2, 2013
May 31, 2016