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Continuity or Change: Leadership Discourse and Policy Analysis at the Helm of Reserve Bank of India

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Abstract

Understanding the evolution of policy over long horizons is an interesting exercise. While it is possible to look at a policy approach ex-ante, many of the decisions of the policy makers are undertaken in response to an emerging situation and several times, there could be initiatives that seemingly have internal contradictions. Additionally, institutions like the Reserve Bank of India would have approaches institutionalised that shape the policy making and thoughts of the leaders at the helm of affairs. Understanding this process through chronological insights and seeing patterns is an exercise that this paper attempts. The paper looks at the speeches delivered by the Governors (and one Deputy Governor) of the RBI to find a pattern and meaning into the series of policy initiatives that the institution is undertaking. In looking at the patterns, the paper tries to build a narrative of an overarching concern that the leaders might have during their tenure. The paper picks up the speeches delivered by leaders at the helm of RBI from 2004 till 2018 and examines the policy discourse to understand the elements of continuity and change.

Keywords: Monetary Policy Decisions, RBI Governors, Policy Discourse

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I. Introduction

How does one examine the evolution of the policy and regulatory approach of a Central Bank over a period of time? This is an intriguing question. One way to look at the issue is to document chronologically the list of circulars, notifications and policy statements and try and read a pattern into it. By doing so, it would be possible to understand the actions of the policy maker, break up the larger policy stance into actionable parts and superimpose an intellectual logic.

Are there alternative ways of trying to understand the policy narrative, and is it possible to associate some of the initiatives to the leadership at that time? Would we be able to understand how the leadership steered the policy primarily according to their own personalities and orientations? How much of it is guidance from the technical and practical imperatives and whether something could be attributed to the leadership and vision of the Governor. Any of these would have to factor the limitations of implementation. It would also be important to factor in the short and tactical reversals in a larger narrative. It is possible to carry out an exercise to get a deeper insight into the policy making process.

An attempt was made in the past, to understand the evolution of policy with regard to financial inclusion through a series of detailed interviews of the Governors of the Reserve Bank of India (RBI). This was done by examining the events during the terms of the Governors with the intellectual logic being provided them in the long-form interview, where they could look back at the actions and provide a greater logic, with the benefit of hindsight (Sriram, 2018). In this paper, we try to look at how the leadership of the RBI shaped the discourse through a review of the speeches delivered by the Governors during their tenure, largely by reviewing the collection of speeches of recent Governors.

We have the benefit of the speeches being made available in the form of books. Governors YV Reddy, Raghuram G Rajan and Urjit Patel have published the speeches delivered during their tenure in the form of books. The advantage of getting the speeches in the form of a book is that there is a logic and prior classification by the author which gives an indication about the broader thematic context. D Subbarao (Governor during 2008 to 2013) published his memoirs during his stint at the RBI but not his speeches (Subbarao, 2016). However, all the speeches delivered from 1990 onwards by the senior functionaries of RBI are available on the website and we have reviewed Governor Subbarao's speeches from that repository. Urjit Patel's book (2019) is a bit narrow as he did not deliver many speeches and was known to be reticent. However, in addition to him, we have a book of speeches delivered by Deputy Governor Viral Acharya(2020) – whose tenure significantly overlapped with that of Urjit Patel.

It is also possible to do a longer and deeper comparative analysis of the speeches of the Governors at the international level given that a repository of the speeches is available at the Bank for International Settlements[1]. However, for the purpose of this paper, we have restricted the review only to the four books of speeches that were published and dipped into Subbarao's speeches available on the RBI website, largely to fill the chronological gaps.

Reddy: The leader who insulated rather than integrated

Reddy's book (2009) titled "India and the Global Financial Crisis" was published in the aftermath of the 2008 Global Financial Crisis (GFC). However, it does not quite deal with the crisis as such. The book

[1] See for instance, https://www.bis.org/list/cbspeeches/

has a well-balanced set of speeches that look at the role, functions and concerns of a central bank – economic growth and development and locating monetary policy in the rubric; price stability and inflation; financial sector regulation, risks and measures to avoid volatility; changing contours of the function of financial institutions – particularly banking; external sector, foreign exchange, managing capital flows and the difficult topic of global balances between emerging market economies and the evolved markets.

The timeline of Reddy's book was between 2003 and 2008. The concerns of the Governor were on issues of India integrating with the global economy and the insulation that should be made available. It dealt with multiple transitions that were happening in the world where he appeared to be juggling with many balls in the air.

Our commitments to international trade treaties with the World Trade Organisation, required us make our markets available to the international community. We had to do this without causing turmoil or distress to the domestic players. At the same time, the economy was moving towards the market-based principles. This meant an aggressive growth of private sector with reduced significance of public sector enterprises; family businesses turning more professional; a change in the relationship between labour and management; increase in productivity and efficiency leading to growth, but without a concomitant increase in jobs; need for greater regulation to ensure fair competition and the debate on whether our policies are pro-market or pro-business – indicating a structural approach in the former and a crony approach in the latter. There were attempts at consolidation of the banking sector through the reverse merger of development financial institutions with banks, the increasing importance of capital and prudential norms in the banking sector following the Basel recommendations and the concerns of customer service and financial inclusion.

In the run up to this period, the economic administration had also changed. Automatic monetisation was phased out after the agreement between the Union Ministry of Finance and the RBI Governor in 1997 and the move was towards the Fiscal Responsibility and Budgetary Management Act (FRBM).

How did Reddy respond to all these dynamics? The answer could be provided in two words – integration and insulation. His speeches broadly indicated a commitment to the common person which was evident in his speech about the approach of RBI towards microfinance. Here, he recognised the importance of informality inherent in the operations and why this sector had to have light regulation. The approach was to encourage innovation and unshackle the sector from stringent banking norms.

For a regulator who had the dual role of market development and universalisation of formal financial services and at the same time interested in maintaining systemic stability and customer protection, there was a dilemma: Is it okay to allow these institutions to accept deposits, as the poor needed savings services badly? How did that square up with legacy issues in the co-operative sector where there was a general belief that governance norms were not stringent; fit-and-proper norms were compromised because of the essential nature of informality and the principle of mutuality? Were there some warning bells ringing in the co-operative sector? So, was it desirable to have a separate legislation for the inclusive finance sector? Given that these services were offered both in the for-profit format, Reddy had hard choices on the regulatory framework, including on the role of foreign capital, particularly from the private equity players who had significantly high hurdle rates of profits, valuation and stringent time horizons for exit.

Reddy was able to place the debate relating the rural finance in the larger perspective of what he called the four deficits: public investment and credit deficit; infrastructure deficit; market economy deficit and the knowledge deficit. He also asked the difficult question for a central banker – whether farmers needed loans at a lower interest rate, or they needed better access. While the paper on rural credit did not provide the answer, it was effectively answered by the microfinance sector, which had put the need for access above the benefits of a low interest rate.

On both monetary policy and inflation targeting, Reddy was a man unto his own. However, the thought that monetary policy had to be a decision based on widespread consultation was institutionalised during his time. He formed a technical advisory committee that gave inputs to the Governor. Between inflation led growth and control of inflation, it appeared that Reddy's preference was towards the latter – a belief that inflation was a penalty on the poor.

There is a notion that Reddy was a conservative at heart – a reason why we were insulated from the GFC was because of his conservatism which prevented any innovation in the financial markets. His speeches expressed these concerns about derivatives and exotic instruments. This did not mean that he was anti-reform. Reddy's speeches indicated that he was pro-reform, but in an insulated atmosphere. He believed that there was merit in integration with the global markets only after internal strengths were acquired in an insulated environment. Therefore, he was open and encouraging about prudential norms, increasing capital adequacy, making the public sector banks more market-oriented, while there was reluctance on allowing foreign banks to come in. He recognised that the forex markets should be open for retail customers and on the current account, but not on the capital flows.

Reddy's speeches were even more important because he used the speeches as an instrumentality of intervention in the market. This is what he called open mouth operations (rather than open market operations) – influencing the markets through signalling through the speeches.

The last two sections of the book of speeches were possibly a prelude to an impending crisis. They talked about liberalisation of capital account and the global imbalances, an area where Reddy had significant reservations with the government of the day. An area where Reddy preferred insulation rather than integration. History tells us that this approach of insulation was a wise one. There are enough insights in the speeches to understand his justifications.

Subbarao: Managing the crisis and its aftermath

There were multiple initiatives taken up during Subbarao's time. The memoirs "Who Moved my Interest Rate?" provided a well-rounded picture of his tenure covering multiple functions of a leader of the central bank. The book continued an objective he had set for himself when he entered the RBI: demystifying the Central Bank. While the book did a good and well-rounded job of defining the functions and tensions of the central bank, his speeches (not brought out as a book but listed on the RBI website) were overly skewed towards the issues pertaining to the GFC and its management, the question of integration with the global economy and insulation from the crisis. In one sense, Reddy's theoretical questions about integration were starkly visible with international experiences. The independent think tanks and agencies like the International Monetary Fund were revisiting the integration question as well as the regulatory framework that was market-friendly.

While many initiatives were taken when he was the Governor – like financial inclusion which required institutional village visits; the agenda being institutionalised by mandating all banks to submit board approved financial inclusion plans and allocation of all habitations with a population of more than 2,000 to a bank for having a customer touchpoints – these do not find proportionate representation in his discourse. Even the Andhra Pradesh microfinance crisis that created much news barely finds a mention in his speeches. Interestingly all the speeches pertaining to the financial inclusion were largely delivered by KC Chakrabarty, the then Deputy Governor in charge of that portfolio. On issues of monetary policy and inflation, most of the speeches were delivered by another Deputy Governor Subir Gokarn. It is also telling that none of his deputies spoke about the crisis as much as Subbarao during his tenure.

This broadly indicated that the Governor was overly concerned about restoring stability and minimising the impact of the crisis. The personal priority was to emerge out of the crisis with as little damage. That focus also meant that towards the end of his tenure, inflation went out of control. It is but natural that contextually he would have been invited to speak on the GFC during his tenure as that was the issue bothering the world at large, because of the overwhelming nature of the crisis, it was telling that even on occasion where he could have chosen a different topic, Subbarao generally chose to speak about the crisis. Therefore, it is quite interesting that he did not publish a specialised semi-academic book on the crisis but chose to have a more popular, well-rounded book on the governor's office in the form of memoirs.

Rajan: Exuberance and Enthusiasm

Raghuram Rajan’s leadership at the Central Bank was unusual in many ways. Unlike his predecessors, who did five-year terms, he had a limited term of three years. Rajan seems to have had a dual approach with regard to his role. One was the classic approach of a central banker: looking at the economy, inflation, banking, capital flows, stability and regulation. The other was to look at how RBI was organised. Both from his actions and his speeches, we find that his canvas was vast. The speeches delivered by Rajan were very unusual from all the speeches delivered by any Governor in the past.

His book “I Do What I Do” has the speeches and is organised into multiple sections. One section broadly covers the outward-facing functions of the RBI: managing inflation, competitiveness in banking, deepening of financial markets; financial inclusion; and the resolution of distress. The section titled “RBI Matters” is inward-facing, where the communication to RBI staff and issues pertaining to the structure and functions of RBI are discussed. But beyond these two broad buckets, the part that made news were the speeches that were clubbed under the head “The Economy and Other Issues”. These moved towards a much wider canvas where broader issues of democracy, tolerance and similar issues were picked up, taking the discourse into the remit of a public intellectual. That he delivered a range of speeches that were unusual for a Governor, in itself, became a matter of discussion, and his predecessor Subbarao came to his defence in one of the interviews much later (PTI, 2016).

Rajan’s speeches engaged with the economy as a whole. He had particular interest in talking about inflation. He talked about targeting inflation and using the appropriate index for doing so. He was also concerned about how inflation could be managed, and the concept could be effectively communicated to people at large. While the inflation targeting framework was first recommended by the Financial Sector Legislative Reforms Commission (Srikrishna, 2013), it was not acted upon. Rajan was in favour of transitioning monetary policy formulation to a committee system. The Urjit Patel committee on monetary policy was one of the early committees that was set up during Rajan’s tenure. The RBI Act was also amended to formalise the Monetary Policy Committee system. By the time the first sitting of the newly constituted monetary policy happened, Rajan had demitted office.

We also find that Rajan had an abiding interest in financial inclusion – during his tenure not only did he appoint the Nachiket Mor Committee that went into great detail on aspects of financial inclusion, but he also implemented many recommendations, including licencing a new set of payments banks and small finance banks. The aggression with which new licences were given and the concomitant ability to take the risk of inviting a large number of new players was not seen in any of the former Governors.

While Rajan's term did lay out a larger vision for the role of the RBI in integrating with the global market and embracing reform domestically to prepare for integration, we could say that he had a greater focus on the reform of the banking system. He initiated governance reforms in public sector banks, firstly by setting up the PJ Nayak Committee and later attempting to implement some of the recommendations. While the credit for starting the reform in the governance of state-owned banks by setting up a Bank Boards Bureau was to go to the union government, the foundation and the intellectual argument was laid by Rajan. The reform road map was both from the perspective of changing the banking system structure, incorporating a large number of new and market friendly players, and the deep reform needed with the legacy players – the public sector banks (and the old private sector banks). To this end, he advocated greater competition in banking. He advocated unshackling public sector banks to face up to the competition.

As a part of the clean-up exercise, Rajan laid a strong foundation for identifying stressed assets, providing for them and eventually tackling the stressed assets. In a speech in 2016, he comprehensively laid his vision for resolving the stress in the banking system – possibly the most comprehensive speech where he identified the sources of distress and the principles of cleaning up with the role of the regulator clearly charted. He also articulated clearly the approach that RBI took during his tenure.

If we were to look at the speeches of Rajan, we would generally find a couple of speeches on each of the functions of RBI and more than half of the speeches dedicated to either the internal management of RBI or aspects beyond the core functioning of RBI. In case of his predecessors, there was a greater engagement on the thematic issues and some deep connection with thoughts on the evolutionary process of the institution. In Rajan's case we found that the institutional thought process – which lent itself into policy analysis was quite divorced from the individual's intellectual moorings.

Urjit Patel: Brevity and Focus

Urjit Patel was unlike any other Governor in how he took to his job. He rarely made public appearances and had very few speeches. Even during the customary press briefing after an event or after the Monetary Policy Committee meeting, he would usually make a brief statement and let the other officials – Deputy Governors and sometimes Executive Directors do most of the talking. He would routinely pass the questions directed at him to a Deputy in charge of the subject matter.

However, Urjit Patel was known for two aspects – the implementation of his own report on the Monetary Policy Framework through the Monetary Policy Committee and also for trying to clean up the banking system. In this regard, he continued the work of Rajan with greater gusto. We did not find much of an articulation on other matters. His book "Overdraft: Saving the Indian Saver" is not exactly a collection of his speeches but draws from all the speeches during his tenure and a bit beyond. The book essentially made a point about what was wrong with the banking system and how it was intertwined with interests beyond both banks and the regulator.

His tenure looked like a valiant fight at cleaning up the banking system. He had identified 9 'R's: Recognise the reality; Record; Report; Recovery and then Resolution; Reinforced Resolution; Recapitalisation; Reset and Ringfence; and Reform. While there were some speeches about agricultural credit, loan waivers and policies for a financialised world, his focus was completely and narrowly on the clean-up of the banks. We have not found such a single-minded focus from a Governor in his utterances both during and after his tenure.

There were other pressures on Patel during his tenure – he had to preside over a controversial demonetisation exercise in the early part of his tenure and part with a substantial part of the reserves of the RBI as dividend to the government during the later part of his career. Both events put tremendous pressure on his image and his credibility to stand up to the autonomy of the RBI. However, he eventually resigned on the issue of resolution of bad loans.

It would be too simplistic to reduce his resignation too narrowly and attributing it to differences on issues pertaining to resolution of bad loans. The bad loans as an issue had to be elevated to a larger intellectual level of argument. While Patel did not provide that argument explicitly in the book, it was provided by Viral Acharya, his Deputy Governor, whose tenure significantly overlapped with Patel. Acharya argued that Fiscal Dominance trumped the financial sector. While making the argument of trying to restore financial stability, he made this point about the exit of Patel: *"Nevertheless, attempts to alter the governance structure of the RBI to institutionalise such outcomes in future would have meant crossing the Rubicon and had to be foiled. As a result, the RBI lost its Governor on the altar of financial stability"* (Acharya, 2020, pp. xxviii).

Viral Acharya: Articulating the unsaid

The tenure of Viral Acharya, Deputy Governor in charge of monetary policy, significantly overlapped with Governor Patel. Acharya published a book of his speeches, "Quest for Restoring Financial Stability in India" where he articulated many issues with which the RBI was engaged. Interestingly, no other Deputy Governor published their speeches. Acharya, like his Governor Urjit Patel, resigned before his tenure was over. It was a matter of sheer coincidence that the books of Patel and Acharya hit the markets on the same day. The reason why we indicated that Acharya was articulating the unsaid was to highlight the intellectual contribution of Acharya to the discourse as an integral part of the team at the RBI. It is evident in his acknowledgements in the book as well as in a controversial (and famous) AD Shroff Memorial Lecture where he had argued for the autonomy of the Central bank and concluded: "*Governments that do not respect a central bank's independence will sooner or later incur the wrath of the financial markets, ignite economic fire and come to rue the day they undermined an important regulatory institution* (pp.295)" (Acharya, 2020). In this particular speech, Acharya acknowledged Patel for inputs and credited Patel with the very idea of the speech. Therefore, it is important to look at Acharya's speeches in tandem with those of Patel.

Acharya's book discusses issues pertaining to the external sector, the monetary policy and its transmission, and the Central Bank's autonomy. However, the most compulsive arguments in eight of the seventeen speeches collected in the volume related to banking and in particular, they were about resolving the NPA framework.

During the tenure of Patel and Acharya, they picked up the baton from Rajan, who had laid the larger argument and framework for reform of the banking system. They focused on one significant sticky issue of NPAs and a framework for resolution in the banking system. The larger objective was in insulating the banking system from the fiscal ill effects. That they chose to do this using something as mundane as NPAs was interesting. However, this was a vital part that looked like an internal management reform, but that reform could not happen unless there were some systemic changes about the resolution mechanism – particularly pertaining to the bankruptcy code. A stringent implementation of the norms would put the banks under the Prompt Corrective Action framework freezing incremental lending, thereby insulating the banks from what is now famously termed as "phone banking".

Putting the stressed corporations through the bankruptcy code and preventing ex-ante promoters from the bidding process addressed the more significant issue of cronyism; and setting up a "bad bank" would clean up the balance sheets of the host banks and give a focus to the resolution of the stressed assets. This would naturally lead to questions of (a) autonomy of the state-owned banks; (b) governance reform through fit-and-proper boards, and (c) adequate capitalisation based on merit, forcing the State to either disinvest or find resources to be compliant with the internationally determined capital norms. So, the evangelical approach to stressed asset resolution possibly anticipated a much larger impact.

All the eight speeches delivered by Acharya are broadly on this theme: looking at resolving the stressed assets, restoring the health of public sector banks, creating a public credit registry, and talking about prompt corrective action. The speeches not only contain a good diagnosis of what is wrong with the Indian financial system and in particular, banking, but also has a robust framework for resolving these.

That there was a larger plan operating in this alternative route to the banking sector, and financial sector reform is evident in both Patel's presentation (2019) and in Acharya's preface to his book (2020), where they argue the creep of fiscal matters into the commercial banking and how it affects the overall ecosystem when the Chinese walls between the fiscal and monetary issues are broken down. Acharya's Preface about Fiscal Dominance gives a theoretical argument in the larger scenario of the political economy why getting an autonomous and commercially oriented – market-facing banking system and an autonomous central bank is increasingly difficult in the context of the fiscal situation which is largely under stress.

In conclusion

If we were to look at the journey of policy making at the central bank, from Reddy to Patel, we find the discourse getting more inward-looking and narrow. Reddy's leadership mostly articulated and laid out the issues and challenges at hand. His leadership was all about preparing for the eventuality – that eventuality could be the GFC as it happened, or if not, preparing for the eventuality of globalisation and opening up. Reddy's long experience in the government and the fact that he saw the balance of payments crisis first hand – possibly gave a certain amount of cautiousness. Therefore, Reddy's regime, hawkish as it was described then, prepared a solid ground for the eventual response that Subbarao could provide from a relative position of strength. In Subbarao's public discourse, we see that there is somewhat a sense of specialisation by the Governor in largely articulating the crisis and response. While the leadership provided by Subbarao also significantly focussed on financial inclusion and reform, his intellectual articulation was taken up by the crisis. The other agenda of monetary policy, inflation was largely being articulated by the Deputy Governor Gokarn and on inclusion by Deputy Governor Chakrabarty.

Rajan provided a significant change, and his brief tenure was marked by multiple initiatives. Unlike in all other regimes, one would find a lot of dynamism in the central bank and also an element of cautious risk-taking. His book of speeches is also equally diverse. While Rajan was not aggressive on reform and integration into the global economy but was happy to move towards that objective cautiously – largely on the foundation laid by Reddy and the consolidation of Subbarao, his appetite for risk and experimentation internally was quite good. In order to achieve his objectives, Rajan also saw the reason for internal reform and re-organisation. Having had the legacy of heading a committee on financial sector reform, Rajan was also keen to implement several of his recommendations and saw banking and financial institutions as integral to his reform agenda. His speeches tried to locate RBI on a much larger canvas and he pushed the frontiers.

It appears that Patel picked one agenda from Rajan, which was about the reform of the banking sector, by addressing one significant issue of stressed assets and used that as a lever for larger reforms. He, like Subbarao, allowed his Deputy Governor Viral Acharya to do most of the articulation both on reform and monetary policy.

We look at institutions and institutional history as a continuum. Systems, procedure and hierarchy ensure continuity and provide institutional memory. However, we also see some breaks in the pattern, a different articulation and worldview that comes out of the same institution when the leadership changes. Each leader defines the role they out to perform and chooses the priorities. Each leader also chooses a medium to communicate messages to the world at large. When we look at the institution from this perspective, we realise that it has not been a continuum after all.

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