Autonomy of regulators: the central bank

This column, now continuing for more than 30 years, has often been critical of the Reserve Bank in relation to its exchange rate policy, regulation of derivatives in particular and banks in general, and, sometimes, also its monetary policy. It is time perhaps to balance the books in a longer perspective.

One way or another, I have been dealing personally with the Reserve Bank and its policies since the mid-1960s, i.e. for the last 45 years (I was employed by its subsidiary, SBI, since 1957). My connection with the bank thus goes back longer than perhaps any of its existing employees! Over the period, I have also had the privilege of working on various committees appointed by the central bank. For many years now, one has also had the privilege of being invited, along with economists and commentators, to share our views on policy issues at the highest level of the bank. Such formal meetings apart, informal discussions keep taking place at various levels. Many of my colleagues are pleasantly surprised at the cordial personal and institutional relationships continuing despite the persistent criticism of specific policies in my columns.

In fact, this is the great strength of the organisation – it is open to views different than its own and takes them into consideration while framing policies. (As one former executive director mentioned to me only half in joke: "while we may not do anything about your arguments and suggestions, one thing I can assure you is that a file gets started"!) More seriously, compared to most central banks in the developing world, its record on inflation control, the management of the exchange rate and the external account, the safety of the banking system, has been far superior – clearly a manifestation of its professionalism. One reason for this professional culture could well be – and I confess to Mumbai-chauvinism on this point – its location away from Delhi, away from the often feudal culture in Delhi.

One should also mention another factor: unlike most other public institutions, there has never been a whiff of corruption or mal-practice about its functioning even when it had huge discretionary powers under exchange control, the credit authorisation scheme, etc; few other public institutions in India could make such a claim.

One would have thought that the government would be anxious to preserve the autonomy, powers and culture of such an institution. But one smells from several recent moves an unmistakable trend of taking power away from Mumbai to Delhi. At one level was the purchase of SBI's shares from RBI; now, it seems, there is a move to do the same about the National Housing Bank, NABARD, etc. There is also the proposal to take public debt management away from RBI, to a unit under the Ministry. I am sure that individually each move has some plausible justification but, collectively, the intention is clear.

Is the last point (debt management) aimed at getting an even greater say in monetary policy? To be sure, in a socio-political economy like India's, a central bank cannot have a single point agenda of inflation control, whatever the monetary purists may say. It will need to have a broader developmental agenda – and this means coordinating monetary policy with the fiscal. But the fact remains that one can hardly remember a time when so many Delhi bureaucrats have been making public statements on inflation and the specifics of interest rate policies – the Finance Secretary, the Economic Adviser, the Secretary, Ministry of Statistics and Programme Implementation, the Commerce Secretary, the Finance Minister himself, etc. Does this help in framing of policies to manage inflation expectations, which is what the central bank is supposed to do? Even on banking regulation one sometimes wonders whether Delhi is driving the agenda on issues like credit derivatives for example, in the name of financial sector reforms and encouraging innovation.

The provocation for these thoughts is the move to convert the ordinance on regulatory coordination into an act, instead of allowing it to lapse, as the RBI Governor has suggested, perhaps with some cosmetic changes. One can add little to the substance of the argument on the issue to what the Governor has so brilliantly articulated in his letter to the Finance Minister – see Tamal Bandopadhyay's column in Mint (July 13) which quotes some extracts.

Overall, it would be a sad day if the independence and autonomy of the monetary authority and banking regulator are curbed – or a vehicle created which could be used for the purpose later.

Tailpiece: Toyota has had major and well-publicised manufacturing defect problems on some of its models and has had to recall a large number of cars for correcting the defects. The U.S. Department of Transportation has analysed dozens of accidents involving Toyotas and come to the conclusion that most of the accidents were due to driver failures and not car defects. Can one imagine an Indian regulator, or even the media, coming to such a conclusion where a foreign MNC is involved?

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