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Demonetisation: Does Urjit Patel's silence hint at government's sidelining of RBI's role?

By *Atmadip Ray* & *Saikat Das*, ET Bureau | Updated: Nov 26, 2016, 08.26 AM IST

Urjit Patel, who is known for his taciturn nature, interacted with the press only once after assuming charge in the first week of September for about half an hour after announcing a 25 basis point repo rate cut in his first monetary policy.

US Federal Reserve chairman Alan Greenspan once said: “Since I’ve become a central banker, I’ve learned to mumble with great incoherence. If I seem unduly clear to you, you must have misunderstood what I said.” He was being facetious… probably.

Reserve Bank of India Governor Urjit Patel never mumbles, nor has he ever been incoherent, but he’s been notably reticent amid the turmoil sparked by the withdrawal of Rs 500 and Rs 1,000 notes on November 8, according to traders and other market watchers.

Anytime a central bank chief speaks, it’s news, even if he or she spouts banalities. Some argue that even silence conveys a message, especially when the circumstances are such that banks are running out of currency notes and a sense of panic appears to be taking hold among some sections of the population at least. The government has said the concerns are overblown and that the situation has eased up considerably.

RBI governors from Bimal Jalan to Raghuram Rajan have used their position to communicate with the market and the wider world. Whatever the approach, it was intended to calm stakeholders without the need for frequent central bank intervention, experts said. One market veteran suggested that the credibility of a venerable institution could be called into question.

“Over the past few years, RBI had earned considerable credibility from global investors,” said Jamal Mecklai, CEO of Mecklai Financial.

“However, today, as a result of the botched demonetisation, the central bank may begin to be seen as either inefficient or, worse, a ‘non-independent arm’ of the government. This would reduce its credibility, which would make foreign portfolio investors more wary of investing in India.”

The RBI has been working overtime to push new notes to the banks with 86% of the country’s currency rendered invalid and combating a slide in the rupee, which tumbled to a low on Thursday before rebounding.

“While in general I don’t think central banks should be continuously communicating with markets, when there is a crisis, whether as a result of demonetisation or sudden rupee volatility, the RBI should be there to calm the markets,” Mecklai said.

To be sure, the central bank has been intervening in the market to smooth out volatility in the currency markets, according to traders. That in itself is a form of communication, said some market experts.

“The market is always expecting RBI to say something, which becomes self-fulfilling. If the RBI is quiet, it assumes that it is okay with the rate or depreciation and the rupee falls further,” said CARE Ratings chief economist Madan Sabnavis.

The preamble of the Reserve Bank of India describes its basic functions as regulating the issue of bank notes and keeping of reserves with a view to securing monetary stability in India and generally to operate the currency and credit system of the country to its advantage.

Patel was last seen on national television on November 8 evening after Prime Minister Narendra Modi made this surprise announcement.

Most of the public statements on demonetisation have been made by economic affairs secretary Shaktikanta Das.

“The PM announced it and the political apparatus of the BJP has supported it,” said SP Kothari, deputy dean at the Massachusetts Institute of Technology. “Under these circumstances, the central bank’s role gets sidelined from the strategic and policy-oriented dimensions to execution.”

Power minister Piyush Goyal directly credited Patel and the 10-member RBI board for taking the demonetisation decision when speaking in the Rajya Sabha on November 16.

Patel, who is known for his taciturn nature, interacted with the press only once after assuming charge in the first week of September for about half an hour after announcing a 25 basis point repo rate cut in his first monetary policy. The rupee weakened 3.2% since November 8 to touch a low of 68.86 per dollar on Thursday.

The All India Bank Officers Confederation has demanded that Patel resign taking the moral responsibility for the current crisis and the deaths of more than 50 people, including 11 bank officials. The next monetary policy will be announced in the second week of December.