

Rajan OK with No Veto for RBI Guv on Rates

Says panels are less likely to make errors than individuals; bats for policy continuity

Reserve Bank of India (RBI) Governor Raghuram Rajan sought to squelch speculation about a rift with the finance ministry, suggesting that his veto over interest rates was an issue for legitimate debate. In a forceful intervention, Rajan said committees were less prone to making mistakes than personalities and would hold up better against pressure. He added that continuity was another critical element when it came to monetary policy.

“Currently, the situation is, the governor has the veto,” Rajan said on Tuesday after announcing a monetary policy that kept policy rates unchanged. “Effectively, all advice is only advice. Ultimately, the decision is the governor's. If it continues to retain the veto, it does not change the current situation, it maintains the status quo. That is something to keep in mind.” Rajan's views on the veto should put to rest talk of the finance ministry and central bank bickering about proposals to reduce governor's powers.

“The difficulty in the current system is it personalises the policy,” Rajan said. “Policy is dependent on one person, which means you can make mistakes. Committees would be less prone to mistakes because there is a discussion among people of different hues. Committees are less susceptible to pressure, both internal as well as external pressure. It is harder to push a committee. But I think what is also important is continuity.” The agreement on the Monetary Policy Committee (MPC) between the government and RBI may provide for a sound independent panel that is insulated from external influence or the central bank's internal views, he indicated.

The aim of future monetary policymaking is to ensure continuity so that investors and industry aren't kept guessing about the future course of monetary action even if the governor left.

Although Rajan did not disclose the details of the nature of the agreement with the government, he signalled that there may be no veto power for the governor as even RBI wants to move away from the current process.

Debate has been raging over the governor's veto power and the government nominating a majority four of the seven-member MPC, since the revised Indian Financial Code draft released last week appeared to recommend the latter. The government has since said this was only a proposal and that it wasn't seeking to clip the governor's wings.

DRAWING A DISTINCTION

Rajan, however, sought to draw a distinction between an often-used overriding vote and one that's rarely cast.

“If you undermine the policy committee by insisting that the governor has a veto... places have a veto for the governor, but have been rarely used,” said Rajan. “If that's the kind of veto, then it is

not a bad thing. If it is a kind of veto which is often used, then we are no different from the current system.“

Finance Secretary Rajiv Mehrishi disclosed on Monday that an agreement had been reached with RBI on MPC and that the details would be unveiled in Parliament.

“We are in discussions with RBI governor on the form and manner of MPC,“ said Mehrishi. “And, in fact, we now have a position which is actually agreed.“

Even though the proposed MPC is likely to be more neutral than what was proposed in the draft IFC, there could be a transitory mechanism in which the RBI governor has an upper hand on decisions.

“What is important is that the segue from the current system into the new system is such that it doesn't create any surprises,“ said Rajan. “The committee structure that is agreed with the government is along those lines. What is important for MPC is that the committee itself coalesces into a body which wants to maintain its reputation for meeting its objective. That is what is going to be the ultimate protection.“

(Economic Times)