Public Spat between RBI and Government

Why in news?

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The differences between the Finance Ministry of the government and the RBI over certain issues have resulted in a public spat.

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What are the issues between RBI and the government?

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- There are essentially five issues which are debated on by both the sides.
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- These are - \n
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  - Issues in handling NPAs (non-performing assets),
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  - Tweaking with PCA (prompt corrective action) norms,
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  - Providing liquidity to NBFCs,
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  - Increase lending to the SMEs,
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  - Deploying the RBI reserves to fund the Budget.
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- From a purely economic standpoint, all these issues are quite fundamental in nature and can provide solutions if there is agreement between the two parties.
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What is the matter of contention in these issues?

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- **Issues in handling NPAs –** Insolvency and Bankruptcy Code (IBC) reform was brought to address the issue of NPAs and the RBI made is stronger by mandating a resolution process for 180 days, even if there is default by a single day.
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- The arguments rose between RBI and Finance Ministry as the Power sector pleaded for exclusion in the resolution process.
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- This can't be approved by the RBI because, if the RBI provides exemption for Power sector, other sectors will also demand for exemption.
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- And if RBI approves exemption based on corporate debt restructuring, then the exempted amount would almost equal the total NPAs.
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- **Tweaking with PCA norms** – RBI had defined banks which are weak and placed lending restrictions for a certain period until they revive.
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- In this scenario, the argument to allow 11 banks under PCA to get some exemptions, especially when liquidity is an issue, is not feasible.
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- **Providing liquidity to NBFCs** – The RBI provides funds to banks which are on-lent to others including the NBFCs.
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- And the Central bank's role can be to the extent of ensuring liquidity in banks through repo, OMO (open market operations) and possibly CRR cuts which are being done continuously.
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- A separate window for NBFC is an option, but it would call other sectors for similar allowances.
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- **Increase lending to the SMEs** – When demonetisation happened, the RBI made an allowance for NPA recognition to SMEs.
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- The RBI doesn't lend directly to SMEs but has created an enabling framework for them and the Priority Sector Lending guidelines defines how SMEs get its share.
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- Should the banks be pushed to lend more for this sector because it's important for the economy or should they take into account the NPAs in this sector and decide accordingly is an issue.

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- **Deploying the RBI reserves to fund the Budget** – In legislative terms the government may have the right but this is not a good idea as it is a one-time transfer like disinvestment, once exhausted the problems resurface.
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- Using reserves can be for specific purposes but not for balancing the Budget.
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What are the suggestions for solving their differences?

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- The present situation definitely calls for introspection and the need to reformulate the premises of the both their respective stands.
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- Provisions that enable the government to issue directions to the RBI has to be used only after the consultations with the RBI Governor.
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- And in the absence of declaration by the Court on the finality of decisions taken by the government, this issue would become messy.
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- Any differences has to be handled with dignity, grace and an air of maturity, instead of such spats in front of public eye.
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- In long term, the relationship between the RBI and Finance Ministry ought to strive for an “appropriate” relationship in terms of doing their respective tasks under the Constitution.
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Source: Business Line, Business Standard

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