

Leadership Style of Dr. Raghuram G. Rajan in the Field of Monetary Policy: A Case Study

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INTRODUCTION

Dr. Raghuram Rajan will always be remembered as a great leader, visionary and person with deep intellectual knowledge. In spite of global slowdown across world, he navigated India smoothly by keeping the rupee stable against dollar. As a futurist, he forecasted the US recession of 2008 in the year 2005. Very courageously, he resisted the political pressure of lowering down the interest rates, He was always very vocal, and his heart, mind spoke the same language. He has farsighted vision to connect and relate the economic, political and social events at macro level.

BACKGROUND OF RAGHURAM RAJAN

In August 2013, Rajan joined as RBI governor. He was born on February 3, 1963 known as an Indian economist who served as the 23rd Governor of the Reserve Bank of India, and having served as Vice-Chairman of the Bank for International Settlements for 2015-16. He was chief economist at the International Monetary Fund from 2003 to 2007, the youngest to occupy the position. He was a Distinguished Service Professor of Finance at the University of Chicago Booth School from 1991 to 2013, when he went on public service leave¹. At present, he has joined academics after serving India as governor of RBI serving as distinguished Service Professor of Finance, University of Chicago Booth School.

LEADERSHIP TRAITS

Raghuram Rajan has various traits of being a true leader, He is combination of wisdom, will, wit and zeal. Blend of accomplished academician and visionary economist, he has reputation of being an uncompromised leader at RBI. He was innovative on

reforms and conservative on stability. As leader he demonstrated, passion is required for innovations in financial products, process and financial institutions. Some of his other qualities include his ability to communicate. Being expert in his field, he has reputation which is built on his professional integrity.

As reformist, he has done various reforms at RBI like restructuring recruitments, he made recruitments domain-expertise based and focused strongly on RBI on performing function as training institution i.e. imparting training on capital markets, economy, finance etc. He brought some of key changes in RBI as institution like positioning RBI as a knowledge institution. A strong protagonist of Monetary policy committee. He resisted with full courage and wisdom, the pressure mounting against his second term, rather than responding to his critics, he remained calm and composed. Further, to demonstrate the quality of decision making process, he made some key organizational changes in the RBI.

He worked fearlessly and dragged the NPA issue to Supreme Court. Also, he had the courage to share the list of defaulters in open. He has done a deep surgery on banks and forced the banks to disclose NPA by following the full disclosure norms and made them make provide for bad loans, though the change in norms resulted in very high losses by public sector banks.

In any Economy, the distribution of resources should be fair. Rajan's view of keeping currency stable and inflation under control, he had pro-poor policy in mind, it was converge by RBI in order to fulfill the agenda of Financial Inclusion. It was important to check the credit flow in order to keep the debt level of financial institutions under control, and in order to save India from US like recession. After all, all the policy-making requires vision, deep study and

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¹ https://en.wikipedia.org/wiki/Raghuram_Rajan

intellectual horse power and courage is required to implement it. He demonstrated all these qualities in him.

FLASH BACK

When Raghuram Rajan resumed his office in 2013 the situation was very crucial. Long back in the year 2008, in order to boost the economy during crises, under the UPA regime, the bankers lend money blindly to corporate sector and to the big projects especially infrastructural projects without considering the exposure limits. Corporate sector too has taken loans without much requirement particularly steel, power, telecom and infrastructure. From then to 2012-13 large economic slowdown had set in, and therefore the overambitious projects requiring large capital were not able to do well. The Global commodity collapse and China's slowdown added fuel to the fire. This crisis began to unfold when corporate started defaulting on interest payout. This was reason of increasing amount in NPA among public sector banks. Now, because of this burden of corporate lending the banks are facing severe problem of NPA and are in losses specially public sector banks and vice a versa these corporate's are unable to pay back interest and as well as principal amount. After 2013, Rajan made banks to disclose all the actual position of NPA's and list of defaulters in public.²

“To add further, when Raghuram Rajan took office as the 23rd governor of the Reserve Bank of India (RBI) on September 4, 2013, it was a time when foreign investors had fast been losing faith in the Indian economy. Indeed, the country was facing its worst crisis in confidence in two decades. The rupee had fallen more than 20% since the start of the year and over 40% within a two-year period. By the summer of 2013, panic had spread among investors in India, and, with an election less than a year away, the minds of India's minority government had firmly focused on the task at hand. The government realized it needed Rajan's credibility as an internationally recognised economist – one who had held the top economics post at the IMF and who predicted the global financial crisis – to help restore confidence and handed the chief economic adviser to the finance ministry the governorship of the RBI. The RBI governor attributed

much of the loss of confidence at the time as stemming from concerns over India's balance of payments, particularly after Indians made “extraordinarily high” purchases of gold in April and May 2013. This widened the country's current account deficit just as then Federal Reserve chairman Ben Bernanke said he planned to start tapering the Fed's latest programme of quantitative easing. India was wrong-footed and while the sense of fragility “was probably overstated”, according to Rajan, “there was a clear need to restore confidence quickly to the financial markets as well as some stability to the exchange rate”.

With more than \$275 billion in foreign exchange reserves, Rajan could have instructed the RBI to continue to intervene heavily in the forex markets in a bid to stabilise the rupee as it had been doing in previous months (with a burn rate sometimes in excess of \$5 billion a week). But this could only be a short-term measure, should economic fundamentals remained weak. India already had the lowest total value of reserves compared with peers such as Brazil, China and Russia, and could cover its import payments for around seven months – much less than some of its emerging market rivals. Instead, Rajan determined the best way to reassure investors about the longer-term value of the rupee was to address India's runaway inflation, which by a number of measures was well in excess of 10%. “As we tackled inflation, other things would fall into place,” Rajan said. In September 2013, the RBI opened a special concessional window to allow banks to swap foreign currency non-residential dollar funds until November 30, with the aim to help Indian banks bring in “safe” money to help fund the country's current account deficit. Another confidence-boosting measure was the decision by Rajan to reverse the RBI's earlier opposition to the issuance of sovereign bonds whose proceeds were immediately taken to reserves. The idea was to show that India still had the capacity to raise money should the need arise. “There was no urgent need for it and we took it directly into reserves,” said Rajan. “But it was good to show the world that we had the capacity to tap markets.” Unveiling his first monetary policy action in September 2013, Rajan immediately demonstrated his hawkish credentials by hiking the repo rate by 25 basis points to 7.5%, contrary to the wishes of the

² <http://www.thehindu.com/business/Economy/financial-stability-report-released/article8784187.ece>

country's business community, which in the main wanted a cut. Rajan took the decision in recognition that "inflationary pressures are mounting" and to show the RBI's determination to "establish a nominal anchor that will allow us to preserve the internal value of the rupee". Rajan's efforts to bring macroeconomic stability to the Indian economy, initiate structural reform, promote financial inclusion and ensure financial stability, combined with his forthright views on reforming the global monetary system, make him an inspirational force for change in the central banking community."³

Governor of the year- Raghuram Rajan

Due to his exceptional work, farsightedness, in-depth knowledge and ability to handle monetary policy made him receive different awards and recognitions worldwide, some of his achievements are: "Raghuram Rajan has been felicitated with the Central Banker of the Year Award (Global and Asia Pacific) for 2016 by *The Banker*, the Financial Times Group's monthly publication." RBI's focus on taming inflation - India is set to hit its 6 per cent target in 2016 - was key to this performance and reinforced foreign investors' confidence in India's currency and rupee-denominated assets," the magazine said

Some other International awards conferred upon him are as follows:

In January 2015, *British magazine Central Banking*, named Rajan as the 'Governor of the Year'. The magazine said: "Rajan's disciplined and focused approach in leading the Reserve Bank during his first year as governor was remarkably impressive." The award was presented in March, 2015, in London. Sharp analytical skills, decisive policy action, powerful communication and impressive leadership skills have enabled RBI governor Raghuram Rajan to lead the Indian economy onto firmer ground

In October, 2014, Rajan was conferred with the Best *Central Bank Governor award* for 2014 by *Euromoney* magazine. According to the magazine, Rajan's tough monetary medicine mitigated the storm

ravaging the deficit-ridden economy in the recent emerging market crisis.

In September, 2013, Rajan was awarded the *Fifth Deutsche Bank Prize for Financial Economics 2013*. He was conferred with the award in recognition of his research work which influenced financial and macro-economic policies around the world.

Rajan's book *How Hidden Cracks Still Threaten the World Economy* won the *Financial Times Business Book of the Year* award in 2010. Raghuram Rajan won the *Fischer Black Prize* in 2003. The prize, established in 2002, honours individual financial research."⁴

While receiving some of prestigious awards, when he received applaud worldwide, very modestly he passed the credit of his success to his peers and acknowledged the important role of government (at Governor of the year award function by Central banking magazine – London, March 2015) In accepting the award, Rajan said, "I am honored to be named governor of the year by the magazine. This is a recognition of the part the Reserve Bank and its staff have been playing in bringing macroeconomic stability to our economy, in creating more competition and new growth opportunities in the banking and financial markets, as well as in expanding financial inclusion, he added of course, no central bank works alone. The important role played by the government in maintaining fiscal discipline, in initiating growth-friendly structural reforms and in launching ambitious new financial sector programmes such as rolling out bank accounts for all, has been critical to any success the economy has had, and is likely to have. Moreover, all our collective efforts should be seen as work in progress "But I am convinced we are moving in the right direction and believe developments will affirm this," Rajan said.⁵

Numbers speaks louder than words

His regime was not only awarded at various platforms but his work was exceptional during his tenure, the data below conferred the same story. Rajan was able to tame inflation, his policies were pro- poor, Inflation

³ <http://www.centralbanking.com/central-banking-journal/feature/2389636/governor-of-the-year-raghuram-rajan>

⁴ http://www.business-standard.com/article/finance/awards-won-by-rbi-governor-raghuram-rajan-116010800288_1.html

⁵ <http://www.thehindu.com/business/raghuram-rajan-conferred-central-banker-of-the-year-award/article6785093.ece>

came down from 10.5% to 5.8%, Currency remain stable and he was able to boost the confidence of the foreign investors and fetched good amount of foreign exchange reserves. He was successful in awarding two banking license to IDFC and Bandhan bank. Though the Gross NPA increased but that was because of disclosure norms and he made banks to make provisions, he has also suggested various constructive measures like early warning system for banks to detect stressed assets. He took mobile banking a step forward by launching unified payment interface which is a mobile to mobile payment platform; it will help users to pay all utility bills on mobile.

During Rajan's tenure		
Indicator/Period	Sep-13	Jun-16
Consumer price Inflation	10.50%	5.80%
Repository Rate	7.50%	6.50%
Statutory liquidity Ratio	23%	21.25%
Credit off take	15.50%	8.70%
Gross Non performing Assets	4.20%	5.20%
Rupee vs. Dollar	Rs 65	Rs 67
Forex Reserves (in Billions)	276	363

Source: RBI, Market, Unfinished agenda, Business today, July 2016 Issue,⁶

Appointment of Urjit Patel as RBI Governor

Dr. Urjit R Patel appointed as the 24th RBI governor in September 2016. Government decided not extends the second term to Raghuram Rajan and instead choose Urjit Patel who was positioned as Deputy Governor and close aide to Raghuram Rajan. The ideology shared by Raghuram Rajan and Urjit Patel is same. It is the difference in the personalities, which lead to this difference of choice by the government.

Background of Dr. Urjit R. Patel

Urjit Patel's educational background is very impressive. He has been to the best places of learning from both the sides of Atlantic. Patel assumed charge after serving as Deputy Governor since January 2013

to 2016. He was re-appointed as Deputy Governor on January 11, 2016 after completion of his first three-year term of office. Patel has also served at the International Monetary Fund (IMF). He was on deputation from the IMF to the Reserve Bank during 1996-1997, and in that capacity he provided advice on development of the debt market, banking sector reforms, pension fund reforms, and evolution of the foreign exchange market. He was a Consultant to the Ministry of Finance (Department of Economic Affairs), Government of India, from 1998 to 2001. He has also had other assignments in the public and private sectors. Patel has worked closely with several central and state governments at high level committees. Patel has a Ph.D in economics from Yale University, an M. Phil from University of Oxford and a B. Sc. from the University of London.⁷

Challenge for Urjit Patel

Governor's job is tough and requires deep knowledge on micro economics, macro economics, international economics, banking and finance. Governor should be having exposure to markets. Though, technically both Raghuram Rajan and Urjit Patel are equally competent. The bad weather seems to be over and the time is less challenging for Urjit Patel, it was more challenging for his predecessor Rajan in the year 2013.

Times are far less challenging for Patel than they were for his predecessor Raghuram in 2013. Urjit Patel comes with the glorious past and experiential learning with him, he attained Indian citizenship in year 2013. His biggest challenge is to carry forward the legacy of predecessor Raghuram Rajan, ultimately it is not glamour which matters, and it is result which speaks itself. Now Raghuram Rajan has gone it's on new governor to nurture his ideas.

Retail inflation, which has been rising since April and was 6.07% in July, is expected to be around 5% in August, September 4.3%, and by January 2017 it could come down to below 4%. Similarly food inflation also came down and prices of food items improved.

“Retail inflation moderated to a 13-month low in September as prices of vegetables and pulses softened, opening the door for a possible interest rate cut when

⁶ <http://www.businesstoday.in/magazine/cover-story/the-unfinished-agenda-of-raghuram-rajan/story/234229.html>

⁷ https://rbi.org.in/scripts/BS_PressReleaseDisplay.aspx?prid=37969

RBI reviews monetary policy in December. Data released by the Central Statistics Office (CSO) on Thursday showed inflation, as measured by the consumer price index, slowed to 4.3% in September, lower than previous month's 5.1%. Inflation in rural areas was close to 5% while in urban area it was 3.6%. The food price index also slowed to 3.9% from previous month's 5.9% as prices of vegetables fell and supplies improved."⁸

Overall the economy is stable, inflation is under control, good rainfall placed in this season likely to improve agriculture sector, and Seventh pay commission is also expected to boost the demand for all sectors. GDP forecast at 7.7% by economic outlook for FY 2016-17, implementation of GST will also have positive impact on economy. Overall the domestic situation is better for Urjit Patel

His comparison with predecessor

While addressing at RBI press meet, Urjit Patel was everything Rajan wasn't: The man PM Modi always wanted, It wasn't the 0.25 percent rate cut, but the way governor Urjit Patel presented himself that caught the attention of many who watched the Reserve Bank of India (RBI) monetary policy press conference, at the central bank's Mumbai headquarters." Patel appeared not too keen to go into the details of the underlying thought process that went into the monetary policy assessment. Journalists, who were waiting to see the new RBI governor make a new personality statement, were clearly disappointed. Ever since Patel took over charge from Raghuram Rajan in the first week of September, he has never met the press or public, a marked difference from RBI governors of the past. Unlike most of his predecessors at the post, often, he was seen restricting his words to the specifics — the macroeconomic rationale that led to the unanimous decision of the newly formed six-member Monetary Policy Committee (MPC) to the rate cut." To some, even the rate cut was a surprise, given that Patel, in the capacity of Rajan's deputy, was always seen as an extremely cautious, more 'hawkish' than Rajan himself when it comes to

lowering the guard on central bank's long fight on inflation. But, contrary to expectations, Patel announced a rate cut on Tuesday, even while stating the persistent upside risks to inflation and seemingly reflecting the Narendra Modi-government's view that inflation is easing and, hence, growth is the primary economic priority now.⁹ As the newly appointed Governor, Urjit Patel is expected to talk especially when he is heading the institution. But he unlike his predecessor he preferred not to give his opinions in public but simply read out the MPC statement.

Ideological differences

The first difference is to understand the power i.e. the Power of governor to determine interest rate structure was not completely adopted, therefore instead of governor, the power shifted to committee finalized by government. Secondly, the agenda of credit growth vs. inflation are contradictory. Third difference is treatment for NPA i.e. to what extent banks can follow the full disclosure norm and also for corporate it was difficult to digest the shock treatment by disclosing their names in public.

Expectation and Responsibility of Government

Silence is gold, Speak only when approved to speak, Use intelligence and wisdom to promote, project and defend the government, never speak anything which undermines the authority of government. Besides being very much technical competent, cordial relationship with government is required to run central bank and trust is the principal criterion required for holding such top positions and to work in liaison with the government, Therefore, though Rajan was appointed by UPA, and he could not maintain the trust of NDA Government.

It is commonly said that history repeats itself, in past, earlier five RBI governors have been asked to leave in unpleasant circumstances. "Raghuram Rajan has done the right thing. By opting out of seeking an extension as Reserve Bank Governor when his term expired in September, he has protected the institution from further politicization. Those who think this is

⁸ <http://timesofindia.indiatimes.com/business/india-business/Retail-inflation-hits-13-mth-low-as-food-prices-ease/articleshow/54840251.cms>

⁹ As quoted October 4, 2016, First post.com <http://www.firstpost.com/business/at-rbi-presser-urjit-patel-was-everything-rajan-wasnt-the-kind-pm-modi-always-wanted-3034932.html>

the first time this has happened, some delving into history is useful. TCA Srinivasa-Raghavan, who edited some volumes of the RBI's history, wrote in *Business Standard* last year that at least five governors were asked to go."¹⁰

On the other hand, role that the central bank plays in country is huge. The preamble of the Reserve Bank of India describes its main functions as: to regulate 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.¹¹ Therefore, decisions taken by central banks should be accepted, respected and implemented by government. In democracy, government by electing governor should keep some respect, faith, and confidence on the person holding the position.

CONCLUSION

Rajan outlined the RBI approach to tackle inflation, importance of financial inclusion, worked on banking sector reforms, market reforms, and distressed debt; also he fought for independence of the central bank. To maintain confidence of the foreign investor he wanted the inflation to be low. In his regime, in order to give stability to the rupee, the monetary regime was inflation focused. By taking various key initiatives, he ensured financial stability in the country and as a caution, he placed more safeguards. Besides his qualification, experience and knowledge, the best thing about Raghuram Rajan was that he had a vivid understanding of his job, at the same time he was very vocal about the issues related to monetary policy.

The mistake which led to muffle between him and government was that Raghuram Rajan spoke outwardly at national and at international forums on various issues which were beyond RBI. Though Rajan's insights were always same as shared by Prime Minister Narendra Modi i.e. minimal government and maximum governance, but his outspokenness was not

appreciated especially as he was appointed by UPA, and therefore, NDA government always took that as criticism. Being from teaching background, Rajan used his intellectual freedom to express himself which caused discomfort to politicians.

Whenever there is contradiction between protecting the value of rupee by Mint Road and politically correct agenda of growth by North Block, it is the Mint Road which has to bend down. Raghuram Rajan was appropriate person to hold the pitch for the longer period than three years. Had he not been so outspoken, we wouldn't have lost a good governor in the process.

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¹⁰ <http://www.firstpost.com/business/lessons-from-raghuram-rajana-exit-stop-painting-rbi-governor-as-superman-2843184.html>

¹¹ https://en.wikipedia.org/wiki/Reserve_Bank_of_India:_Working_and_Functions