



भारतीय रिज़र्व बैंक  
RESERVE BANK OF INDIA

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## RBI Bulletin - February 2021

The Reserve Bank of India today released the [February 2021](#) issue of its monthly Bulletin. The Bulletin includes Monetary Policy Statement, 2020-21: Resolution of the Monetary Policy Committee (MPC) February 3-5, 2021, one Speech, four Articles and Current Statistics.

The four articles are: I. State of the Economy; II. Sectoral Deployment of Bank Credit in India: Recent Developments; III. Assessing the Future Path of Monetary Policy from Overnight Indexed Swap (OIS) Rates; IV. Do Markets Know More? India's Banking Sector through the Lens of PBR.

### I. State of the Economy

#### Highlights

- In India, economic activity is gaining steam as COVID-19 incidence recedes and the ongoing vaccine rollout releases pent-up optimism.
- All engines of aggregate demand are starting to fire; only private investment is missing in action and the time is apposite for it to come alive.
- Broader measures of liquidity reflect easing of monetary and financial conditions in the system.

### II. Sectoral Deployment of Bank Credit in India: Recent Developments

The analysis of sectoral credit data provides insights into the flow of credit to various important sectors of the economy. This article analyses the developments in sectoral deployment of bank credit during the period preceding the COVID-19 pandemic and compares them with developments during the COVID-19 period, *i.e.*, during April-November 2020-21.

#### Highlights

- Bank credit growth, which witnessed a slowdown in 2019-20, experienced a further setback in 2020-21 in the wake of COVID-19-induced lockdown but with the gradual resumption of economic activity, credit to agriculture and services sectors has registered accelerated growth in the recent period.
- Public Sector Banks (PSBs) have been primarily responsible for an accelerated growth in credit to agriculture and services sectors in the recent period.
- Even in the industrial sector, credit growth to medium industries has accelerated indicating positive impact of several measures taken by the Government and the Reserve Bank.
- Empirical estimates indicate that non-food credit is sensitive to interest rate changes with a lag, with industry and services sectors exhibiting greater sensitivity.

### **III. Assessing the Future Path of Monetary Policy from Overnight Indexed Swap (OIS) Rates**

The use of the overnight indexed swap (OIS) rate as a measure of monetary policy expectation is gaining popularity in the literature. This article, by adopting the methodology of Lloyd (2018), empirically tests whether onshore OIS trades in India of different tenors (ranging from 1 month to 10 years) for the period from August 03, 1999 to May 31, 2019 are efficient measures of market participants' expectation of short-term interest rates.

#### **Highlights:**

- The article computes *ex post* "excess return" as the difference between the OIS fixed rate and the floating overnight reference rate.
- The excess returns of the OIS trades of tenors of up to one year were low ranging between 2 basis points (bps) and 20 bps indicating that these OIS rates were, on average, a fair indication of the direction of future course of monetary policy.
- Specifically, the OIS rates of tenors 1, 9 and 12 months appear to more accurately measure the expectations of future short-term interest rates with the excess returns of these tenors, on average, being not significantly different from zero.
- Based on the findings of the study, the OIS rates in India are found to be credible predictors of the direction of monetary policy, if not the exact timing of policy changes.

### **IV. Do Markets Know More? India's Banking Sector through the Lens of PBR**

What is an appropriate measure of bank value? This article argues that price-to-book ratio (PBR) of banks may be considered as an alternative measure of bank value to better understand their health and stability in the Indian context.

#### **Highlights:**

- While there are several indicators such as capital adequacy ratios, Z-scores, and profitability, none of them comprehensively capture the viability of the underlying business models of banks. Moreover, such standard indicators often change due to shifts in the regulatory environment without necessarily reflecting a fundamental change in the health of banks.
- Through credit intermediation, banks generate valuable intangible assets, such as private information on borrowers' worth and develop long-term banking relationships with them. Since banking business is subject to stringent entry requirements and regulations, incumbent banks have greater access to market profits. These factors contribute to a bank's franchise value, which can be captured by its price-to-book ratio.
- The article finds that variations in PBR have linkages with financial and economic cycles. PBR also shares a close correlation with indicators relating to profitability and viability of banks. As it is available on a high-frequency basis, unlike the balance sheet data, PBR of banks promises to be a useful metric for policy purposes.