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- Yet Another Major Setback
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- Some Contemporary and Classical Issues of Money and Finance
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CURRENT STATISTICS

Money, Banking & Finance

Eight papers discuss and explore classical and contemporary issues related to money and finance. Specifically, these papers assess issues related to money and inflation, banking and financial stability, retail investment in the Indian equity market, and the rating methodologies of the three big credit rating agencies. pages 21–104

Ajit Kumar Ghose (1947–2023)
A prominent labour economist, Ajit Kumar Ghose analysed the complex interactions between dual economies and structural transformation. page 13

Credit Risk Management
Banks can benefit from adopting the Basel III internal ratings-based approach to assess the risk involved in their business more accurately. page 10

Media and the Political
Intricate interactions of media infrastructures, networks, and technologies together structure the political sphere of heavily mediatised societies. page 17
Some Contemporary and Classical Issues of Money and Finance

PARTHA RAY

Post the pandemic, the world seems to be back on a high-inflation path, and many geographies in the advanced world have started witnessing inflation rates that were prevalent in the early 1970s. Admittedly, the ongoing war between Russia and Ukraine and the associated supply shocks have had their role in this phenomenon of high inflation. Thus, in a marked departure of the period of the “great moderation,” inflation and its nature have emerged as key issues in the contemporary policy discourse. Along with this, stability concerns in the banks seemed to have surfaced across the United States (US). Coinciding with the near-synchronised rate hikes by the central banks in the developed world, the equity market in these countries have shown some symptoms of dampened exuberance.

It is in this context that this special issue on Money, Banking and Finance brings together a wide bouquet of papers on some contemporary and some age-old, classical issues of money and finance.

Money and Inflation

The paper by C Rangarajan, Dilip Nachane and Partha Ray, titled “Monetary Growth, Financial Structure, and Inflation: The Post-Pandemic New Normal,” delves into the classical issue of money and financial structure in monetary policy. The paper argues that the role of money cannot be neglected. Particularly in the context of the recent spurt in global inflation, the authors claim that the easy monetary and liquidity conditions could have played a role in worldwide inflation. In the context of the role of financial structure, the paper argues that issues of monetary stability, price stability and financial stability are intimately interlinked.

Sitikantha Pattanaik, G V Nadhaneel and Silu Muduli, in their paper titled “Taming Inflation by Anchoring Inflation Expectations,” probe into the Indian experience of flexible inflation targeting using the lens of inflation expectation surveys. However, using the raw inflation expectation surveys is fraught with limitations. Hence, in an innovative way, the authors try to correct for the bias that is typically present in the household inflation expectations data and constructed a bias-adjusted inflation expectations series before generating an inflation expectation anchoring index. Their evidence indicates “the performance on anchoring inflation expectations in India has improved following the adoption of the flexible inflation targeting (ftr) framework.”

On the contrary, given India’s structural specificities, Zico Dasgupta and Indranil Chowdhury, in their paper “Monetary Policy in the Midst of Cost-push Inflation,” question the paradigm of the “New Consensus Macroeconomics,” whose distinguishing feature, in their opinion, is that “it puts the burden of controlling the inflation rate exclusively on monetary policy.” Their empirical investigation for the standard three-equation New Consensus Macroeconomics indicates that the Phillips curve seems to be flat and the inflation rate tends to respond to cost-push factors like terms of trade and oil prices in India. They, thus, question the efficacy of flexible inflation targeting for India.

Issues in Banking and Financial Stability

Richa Verma Bajaj, Sagarika Rastogi and Rhythm Kumar probe into the credit portfolio of domestic-systemically important banks in India during 2009–10 and 2019–20 through an industry-wise analysis. Their estimated default correlation (using equity returns correlations, weighted by diversifiable risk factors) allows the inclusion of both systematic factor as well as industry-specific factors in risk estimation. Their empirical analysis suggests that the macroeconomic factors tend to drive the default correlation in-between the industries. They find some distinct heterogeneity in industry-specific effects. Towards migrating to the newer versions of Basel norms, when an economic capital approach of a bank is related to the internal capital adequacy assessment process, such an empirical assessment for the Indian banks could be quite helpful.

The paper by Pradyot Kumar Das, titled “Do Foreign Banks Affect Market Power, Efficiency, or Stability in India?” is on a relatively less-researched segment of banks in India. Using a sample of 103 commercial banks in India for 1999–2020, Das examines the effects of ownership status (foreign or domestic) on individual banks’ market power, efficiency, and stability. Besides, he looks into the effects of foreign bank presence on individual banks’ market power, efficiency, and stability (spillover effects). His main result indicates, “Foreign banks have greater market power, lower marginal cost of the production of bank output, greater price–cost margin, and higher insolvency risk than domestic banks.” But, “there are no differences between foreign and domestic banks in terms of price of bank output, inefficiency, net non-performing loan ratio, gross default correlation in-between the industries. They find some distinct heterogeneity in industry-specific effects. Towards migrating to the newer versions of Basel norms, when an economic capital approach of a bank is related to the internal capital adequacy assessment process, such an empirical assessment for the Indian banks could be quite helpful.

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This special issue has been put together by Partha Ray who oversaw the commissioning, refereeing, and the final selection of the papers. EPW is grateful to him for being the Advisory Editor for this issue. —Ed.
non-performing loan ratio, or return on assets.” Interestingly, however, foreign bank presence does not seem to affect the price of bank output, gross non-performing loan ratio, or return on assets of an individual bank.

Amulya Neelam’s paper is a commentary on “RBI’s ‘Financial Stability Reports’ and Stress Testing Methodologies: A Commentary.” While complimenting the RBI for its detailed analysis, and for the utility and information content of financial stability reports, Neelam flags the need for more micro details for the sake of transparency. Of course, such calls can, ultimately, be a function of the regulatory concerns and could be taken against the possible impact of revealing market-sensitive bank-specific information.

Retail Investment in Equity Market
Tirthankar Patnaik, in his paper titled “Retail Investment in India: During and after the Pandemic,” highlights the stylised facts of retail stock market investment in India. Interestingly, over the various episodes, retail investment in the Indian equity markets continues to rise steadily. More recently, in an atmosphere of rising inflation, rising monetary policy rates, and the Russia–Ukraine war, “while global equities tanked, Indian markets stayed afloat due to domestic inflows.” Insofar as the retail investment is concerned, Patnaik’s chronicle and analysis show the presence of: (i) “high variability” and (ii) “behavioural finance traits like exuberance and buyers’ remorse.” Notwithstanding a rise in uncertainty, retail participation in India remains significantly higher than the pre-pandemic levels.

Questioning Sovereign Credit Ratings
Finally, Rahul S Chauhan, Ilisa Goenka, Kaushalendra Kishore, Nirupama Kulkarni, Kavya Ravindranath and Gautham Udupa, in their paper titled, “Understanding Sovereign Ratings and Their Implications for Emerging Economies,” assess the rating methodologies of the big three credit rating agencies: S&P, Moody’s, and Fitch. They look into the factors driving sovereign ratings “using a regression framework and machine learning techniques with a panel of 162 countries covering ratings from 2000 to 2018.” Interestingly, across all the models, institutional quality emerges as the most significant factor driving sovereign ratings. However, the rating performance of a country is seen to be a poor predictor of sovereign defaults. Using machine learning techniques, they show that ratings are poor predictors of future defaults.

Views are personal.
Partha Ray (pray@nibmindia.org) is the director of the National Institute of Bank Management, Pune.