CREDIT INFORMATION REVIEW

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BANKING POLICY

Banks to implement SSI Committee Recommendations

The Reserve Bank of India has accepted 35 out of 106 recommendations of the High Level Committee on Credit to Small Scale Industries (SSI) (S.L. Kapur Committee) for immediate implementation by banks. The Reserve Bank has asked banks to :

* introduce tri-lingual loan application forms, i.e., in Hindi, English and local language;

* straightaway use the application form prescribed for facilities up to Rs.2 lakh for facilities up to Rs.10 lakh, that prescribed for facilities up to Rs.15 lakh for such facilities up to Rs.50 lakh and that prescribed for limits up to Rs.1 crore for facilities beyond Rs.50 lakh and up to Rs.2 crore and even beyond;

* adopt committee approach for sanction of applications and to dispose off adopt committee approach for sanction of applications and to dispose off loan applications in a time bound manner. Applications for amounts up to Rs.25,000 within a fortnight and those for amounts above Rs.25,000 within 8 to 9 weeks;

* to get the filled in application forms submitted by the borrowers examined by a bank official having adequate experience in credit operations to facilitate quick disposal of applications; maintain a check list with this official so that he can advise the applicant what additional information is required to be submitted for completion of the application;

* extend necessary help to applicants in filling up the application forms and make available at each branch adequate number of copies of bank's instructions/schemes, RBI instructions and literature prepared by SIDBI, NABARD, State and Central Governments, etc;

* delegate powers to branch managers to grant ad-hoc facilities to the extent of 20 per cent of the limits sanctioned subject to the usual lending discipline;

* lay down, with the approval of their boards, some clear guidelines for computing the working capital limits for various sub-sectors granted to SSI borrowers, particularly those units where fund based working capital requirements exceed Rs.4 crore;

* normally accept, in case of new units, the projections accepted by the term lending institutions, for the first year of operation unless there are specific reasons for not doing so;

* out of the total funds allocated by banks to SSI sector give at least 40 per cent to the units with investment in plant and machinery up to Rs.5 lakh and 20 per cent to the units with investment in plant and machinery between Rs.5 lakh and Rs.25 lakh. As now the flow of credit to SSI would be assessed by using data on disbursement rather than 'outstanding balances' fix disbursement targets for SSI loans along with outstanding balances;

* pay more attention to the backward states such as Bihar, Jammu & Kashmir, Madhya Pradesh and North Eastern States while fixing the lending targets and seek separate progress reports;

* enhance the limit of composite loans from Rs.2 lakh to Rs.5 lakh so that the entire requirement of such units is met by single documentation and security and charge creation process;

* extend this facility to all SSI units requiring loans up to Rs.5 lakh irrespective of their location.

* only banks should entertain projects both for term and working capital loans of borrowers with loan requirement up to and inclusive of Rs.5 lakh and that only one organisation, either State Financial Corporation (SFC) or bank may sanction both, the term loan and working capital loan for projects requiring institutional credit for more than Rs.5 lakh and up to and inclusive of Rs.25 lakh.

* for projects having loan requirement in excess of Rs.25 lakh, arrangements should be made by the Small Industries Development Bank of India (SIDBI) with the public sector banks to have a memorandum of understanding signed between the SFC and selected public sector banks active in different regions of the country for joint financing. Both, term loan as well as working capital loan should be shared along with sharing of securities on pari passu basis. The borrowers in this category who want to avail such facilities from a single agency, i.e., bank or SFC, however, should be allowed to exercise their option.

* the overall interest payable by SSI should remain within the existing parameters fixed by the Reserve Bank, i.e., maximum of Prime Lending Rate (PLR) plus four per cent. Additional spread over the PLR should be used as premium for guaranteeing the repayment of the loan. SSI units, with good track record will thus have to pay lower premium and would derive some advantage out of lower spreads.

* allow SSIs to invest overseas up to US$ 20,000 based on a simple procedure.

The Reserve Bank has also favoured Kapur Committee's recommendations, such as, opening of more specialised branches or converting existing branches into special branches for SSIs and make the customer grievance machinery more effective.

PROPOSED GUIDELINES ON ASSET-LIABILITY MANAGEMENT SYSTEM IN BANKS

The Reserve Bank of India has issued broad draft guidelines for Asset-Liability Management (ALM) System in banks. The guidelines are intended to form the basis for initiating measures for collection, compilation and analysis of data required to support ALM system. The Reserve bank has requested banks to study the guidelines and send in their suggestions and difficulties, if any, that may be encountered in implementation of the system. The Reserve Bank has also stated that it proposes to introduce the ALM system in banks from April 1, 1999 after issuing the final circular in January 1999.

It may be recalled that the Reserve Bank had, in October 1997, announced that it will issue broad guidelines for managing liquidity and interest rate risks faced by banks.

In normal course, banks are exposed to credit and market risks in view of the asset-liability transformation. With the gradual liberalisation of the Indian financial system and growing integration of domestic markets with external markets, the risks associated with banks' operations have become complex and large, requiring strategic management. The fast changing financial environment has exposed Indian banks to interest rate risk, forex risk, equity price risk and liquidity risk. Any adverse movements in market interest rates and currency rates would immediately affect the bank's earnings. In the long-term, any change in market rates would impact the economic value or Market Value of Equity (MVE) through significant changes in the market value of the banks assets, liabilities and off-balance sheet positions. Further, imprudent liquidity management can put banks' earning and reputation at risk. It is, therefore, important that banks introduce effective risk management systems that address the issues related to market risks. Against this background the Reserve Bank has issued draft guidelines for operationalisation of ALM system by banks.

In the draft guidelines, the Reserve Bank has advised banks to address market risks in a structured manner by upgrading their risk management skills and adopting more comprehensive ALM practices. As a part of the integrated approach, banks have been advised to set up Asset-Liability Management Committees (ALCO), which should be headed by the Chief Executive Officer/ Chairman and Managing Director or Executive Director of the bank. Banks have also been advised to constitute a professional management and supervisory committee consisting of 3/4 directors on boards to oversee implementation of the system and review its functions periodically.

The guidelines cover the measurement of liquidity and interest rate risks and at this stage, focus on simple easy-to-comprehend methodologies.

Liquidity Risk

Measuring and managing liquidity needs are vital, for effective operation of banks. The importance of liquidity transcends individual institutions, as liquidity shortfall in one institution can have repercussions on the entire system. Thus, banks should not only measure liquidity positions on an ongoing basis but also examine how liquidity requirements are likely to evolve under different assumptions. The draft guidelines suggest the use of maturity ladder and calculation of cumulative surplus or deficit of funds at selected maturity dates. The banks have been advised to prepare a statement of structural liquidity (static basis) by placing all cash inflows and outflows in the maturity ladder according to the expected timing of cash flows. Banks are expected to monitor mismatches in cash flows by establishing internal prudential limits with the approval of the board/management committee. The mismatch during 1-14 days and 15-28 days are sought to be restricted at 20 per cent of the cash outflows during these time buckets. In addition to the structural liquidity, the banks have also been advised to monitor their short-term liquidity for 90 days, on a dynamic basis, on the basis of business projections and other commitments.

Interest Rate Risk

Phased deregulation of interest rates and the operational flexibility given to banks in pricing most of the assets and liabilities imply the need for the banking system to cover the interest rate risk. Considering the problems associated with availability of data, simple traditional gap analysis, under assumption of a parallel shift in yield curve has been suggested as a suitable method to measure interest rate risk in the first place. It is the intention of the Reserve Bank to move over to more modern techniques like the duration gap analysis, simulation and value at risk over time when banks acquire sufficient expertise and sophistication acquiring and apprehending management information system (MIS). The gap report can be prepared by grouping rate sensitive liabilities, assets and off-balance sheet positions into time buckets according to residual maturity or next repricing period, whichever is earlier. Banks have been advised to set prudential limits on individual gaps, having a bearing on total assets, earning assets or equity. Banks have also been advised to work out earnings at risk based on their views on interest rate movements.

Currency Risk

Presently, the banks are free to set gap limits with the Reserve Bank's approval and are required to adopt value at risk approach to measure the risk associated with forward exposures. Thus, the open position limits together with the gap limits continue to be the risk management approach to forex operations. The Reserve Bank had already issued detailed guidelines to banks in this area in December 1997.

Considering the inadequate MIS in the Indian banking system and that the Reserve Bank is prescribing guidelines in ALM for the first time, the banks have been advised to study the guidelines and forward to the Reserve Bank suggestions and difficulties, if any, that may be encountered in implementation of the system. Banks have also been advised to set up a small group under the charge of the General Manager (Funds Management/Treasury) for implementation of the ALM system.

RELIEF FOR EXPORTERS

The cyclonic storm that hit the Gujarat coast in June, 1998 had adversely affected the export from that region. The Reserve Bank of India has decided that, after confirming the genuineness of the case, banks may give the following concessions to the affected exporters:

(i) extend pre-shipment credit granted for less than 180 days to 180 days at the interest rate applicable for the period upto 180 days (9 per cent per annum effective August 6, 1998);

(ii) may charge the concessional rate applicable for the period beyond 180 days and upto 270 days for the period beyond 180 days and upto 360 days (12 per cent per annum effective August, 6 1998);

(iii) extend credit beyond 360 days when necessary on the basis of the bank's commercial judgement, discretion and with the approval of its Board;

(iv) extend foreign currency credit beyond 180 days as per actual cost of roll-over instead of applying two per cent over the rate charged for the period upto 180 days;

(v) convert the amount of loan required to be recovered from exporters, after the settlement of claim by Export Credit and Guarantee Corporation, into a short term loan waiving penal interest;

(vi) treat the advances as non-performing assets only if the interest or installment remains unpaid for two quarters after it has become overdue taking into the revised due date fixed by the banks after extension of the period or conversion of the pre-shipment credit.

KISAN CREDIT CARDS

The Reserve Bank of India has advised all scheduled commercial banks to introduce a suitable Kisan Credit Card Scheme on the lines of the Model Scheme formulated by National Bank for Agriculture and Rural Development (NABARD). It may be recalled that the Union Finance Minister in his Budget speech for 1998-99 had announced that National Bank for Agriculture and Rural Development (NABARD) would be asked to formulate a model scheme for issue of Kisan Credit Cards to farmers. The scheme would be designed for uniform adoption by banks.

The objective of the Kisan Credit Card is to provide adequate and timely support from the banking system to the farmers for their cultivation needs including purchase of inputs in a flexible and cost effective manner. The scheme would cater to the short term credit requirements of the farmers, including purchase of agricultural inputs, such as seeds, fertilisers, pesticides etc., and draw cash for their production needs. Banks may provide Kisan Credit Cards to farmers who are eligible for sanction of production credit of Rs.5000 and above. Credit would be available to the farmers under the scheme in the form of revolving cash credit normally valid for three years, subject to an annual review. The rate of interest on Kisan Credit Cards should be the same as is applicable to crop loans. The credit card account would be deemed to be a non-performing asset (NPA) if it remains out of order for a period of two crop seasons.

BANK FINANCE AGAINST SHARES AND DEBENTURES

The Reserve Bank of India has issued a master circular containing all existing guidelines on bank finance against shares and debentures. The master circular supersedes all the instructions issued by the Reserve Bank on the subject from time to time. The circular is available on the Reserve Bank of India website on the internet (URL:http://www.rbi.org.in).

EXCHANGE CONTROL

IMPORT OF FILMS

The Reserve Bank of India has permitted all the authorised dealers to allow remittances for import of cinematograph feature films and video films on lease/rental basis on periodical payment terms such as fixed rentals, royalties, service charge, licence fee, profit sharing etc., as agreed upon between the overseas suppliers and the Indian importers. This, however, would be subject to fulfilment of the conditions laid down in the Government of India Public Notice No.4(PN)79-02 dated March 31, 1997. In the case of import on outright purchase basis, remittances can be allowed towards the cost of import of feature/video films under the existing instructions.

INCOME ON NON-REPATRIABLE INVESTMENT

Investment income and rent on immovable property accrued to Non Resident Indians would be eligible for repatriation as part of current income even if the original investment was made on non-repatriation basis.

STOCK OPTION FOR SOFTWARE EMPLOYEES

It has been decided to allow the Indian software companies to offer American Depository Receipts (ADR)/Global Depository Receipts (GDR) linked stock option scheme to their non-resident and resident permanent employees including the Indian and overseas working directors. On exercise of the option, each resident employee/working director will be permitted to remit upto US $ 50,000 in a block of 5 years to acquire the ADRs/GDRs.

FOREIGN INVESTMENTS IN INDIAN COMPANIES

The ceiling on holding of a single Foreign Institutional Investor or Foreign Institutional Investor group in total paid up capital of an Indian company has been raised from 5 per cent to 10 per cent. The aggregate ceiling of 24 per cent for Foreign Institutional Investor investment in primary and secondary markets in the paid up capital of Indian companies applicable to all holdings taken together including conversions out of the fully and partly convertible debentures can be raised to 30 per cent subject to the approval of the board of the company concerned and passing a special resolution by the general body to that effect. The ceiling of 24 per cent to 30 per cent, as the case may be, will not include investments by Non-Resident Indians/Overseas Corporate Bodies under the portfolio investment scheme. Under the portfolio investment scheme for Non-Resident Indians/Overseas Corporate Bodies, the existing ceiling for investment in the equity capital of the company for a single non resident investor has been raised from 1 per cent to 5 per cent and aggregate ceiling of 5 per cent for all Non-Resident Indians/Overseas Corporate Bodies has been raised from 5 per cent to 10 per cent. The overall ceiling of 10 per cent can be raised upto 24 per cent by passing a resolution in the General Body. This ceiling will be in addition to FII investment of 24 per cent to 30 per cent.

100 PER CENT NRI/OCB SCHEMES

Indian companies seeking Non-Resident Indian/Overseas Corporate Body investment under 100 per cent scheme have been granted general permission to issue and export equity shares subject to the conditions stipulated in Notification No.FERA.180/98-RB dated January 13, 1998 by which general permission has been granted for issue and export of shares to foreign investors in respect of cases of foreign direct investment eligible under the automatic route.

EXPORT FACTORING

Authorised dealers have been allowed to provide export factoring services to exporters on "with recourse" basis subject to guidelines issued by the Reserve Bank’s Department of Banking Operations and Development.

RESURGENT INDIA BONDS (RIBs)

The State Bank of India had recently floated the Resurgent India Bonds (RIBs) with a maturity period of 5 years for subscription by Non-Resident Indians/Overseas Corporate Bodies by way of inward remittance in foreign exchange from abroad or out of funds held in their NRE/FCNR

(B) accounts with banks in India. The bonds are to be redeemed on maturity in the currency of subscription and the principal amount and the interest earned on that will be fully repatriable.

Authorised dealers have been asked not to grant loans in India against the security of Resurgent India Bonds (RIBs). They could, however grant loans in non-repatriable rupees in India to the holders of Resurgent India Bonds for purposes other than investment in India, subject to the following conditions:

(i) The loans should be fully secured by the value of bonds and accrued interest;

(ii) The regulations relating to normal margin, rate of interest etc., as stipulated by the Reserve Bank from time to time are complied with;

(iii) The period of loan should not exceed the unexpired period of maturity of the bonds and

(iv) The loan should be repaid out of inward remittance from abroad or maturity proceeds of the bonds or out of funds held in NRO account of the bondholder.

Authorised dealers may also grant loans to the account holders for the purpose of making direct investment in India on non-repatriation basis by way of contribution to the capital of Indian firms/companies engaged in manufacturing/industrial activities, export oriented trading activities, hospitals, hotels of 3 star or higher grades, shipping, development of computer software and oil exploration services subject to the conditions as stated above and the conditions as under:

(i) The loan amount should be disbursed to the investee firm/company on behalf of the bondholder;

(ii) The investment made out of the loan should not be allowed to be repatriated abroad at any time;

(iii) The concerned investee company intending to issue shares to NRIs/OCBs on non-repatriation basis should adhere to the other conditions stipulated in Reserve Bank's Notification No.FERA.114/92-RB dated April 27, 1992.

Authorised dealers may also grant loans to the non-resident bondholders of Indian nationality/origin (and not to OCBs) for the purpose of acquisition of flats/houses in India for their own residential use of subject to further conditions as stated below:

(i) the period of loan does not exceed the unexpired maturity of bonds,

(ii) the house/flat to be acquired/constructed should be for residential use of the bondholder and not for commercial purposes,

(iii) sale proceeds of flat/house will not be allowed to be repatriated abroad at any time,

(iv) acquisition of property by foreign citizens of Indian origin will be subject to the Reserve Bank's approval.

Authorised dealers may grant loans/overdrafts to resident individuals/firms/ companies in India against the collateral of Resurgent India Bonds (RIBs), subject to the following conditions:

(i) there should be no direct or indirect foreign exchange consideration for the non-resident depositor to pledge his deposits to enable the resident to obtain the loan,

(ii) the period of loan should not exceed the unexpired maturity of bonds,

(iii) regulations relating to normal margin, interest rates, purpose of loan as stipulated by the Reserve Bank from time to time should be complied with,

(iv) the loan should be utilised for personal purposes/for carrying on business activities other than agricultural/plantation activities,

(v) the loan should be granted only against a special mandate from the NRI bondholder.

Authorised dealers should apply the usual norms as in the case of advances to trade, industry etc., and satisfy themselves as to the acceptability of the purpose, genuineness of credit needs and end use of funds etc., and need not be guided solely by the availability of the security.

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