Chapter III

Developments in Commercial Banking

3.1 During the year 2003-04, the strong macroeconomic environment and supporting monetary and financial policies had a favourable impact on business growth and financial performance of commercial banks. The balance sheets of banks witnessed further strengthening due to the robust growth of deposits on the liabilities' side accompanied by strong growth of loans and advances, and investment on the assets side. The record growth in bank credit in the priority sector including agriculture, small industries and other sectors including housing, and also in non-priority sectors including the consumer credit reflected an improvement in access to credit. There was a significant improvement in the asset quality and profitability of commercial banks with a continuing focus on integrated risk management systems to monitor credit, market and operational risks, recovery management and corporate governance practices. The capital to risk-weighted assets ratio (CRAR) showed further improvements across various banks. A notable achievement was that despite the switch over to the 90-day delinquency norm with effect from March 2004, gross non-performing assets declined in absolute terms for a second year in succession. Despite sluggish income growth consequent upon the lower interest rates prevailing, the momentum of the high growth of profits witnessed in recent years was sustained during 2003-04 mainly driven by the substantial increase in non-interest income and a significant containment in the overall expenditure, primarily, interest expenditure (Table III.1).

2. Assets and Liabilities of Scheduled Commercial Banks[1]

3.2 The size of the balance sheet of scheduled commercial banks (SCBs) recorded stronger growth during 2003-04; the growth rate of aggregate assets at 16.2 per cent was higher by nearly 6 percentage points over the growth of 2002-03. The ratio of assets of SCBs to GDP at factor cost at current price increased to 71 per cent, an increase of 2.5 percentage points over 2002-03, implying further deepening of the financial sector. On the liabilities side, deposits continued to account for about four-fifths of banks' total liabilities. On the assets side, the shares of two major components, *i.e.*, loans and advances, and investment, in total assets of SCBs remained more or less similar to the position recorded in 2002-03 (Table III.2). The share of loans and advances in the balance sheet

Table III.1: Changes in the Income Expenditure Profile of Scheduled Commercial Banks

(Amount in Rs. crore)

Indicator	2002-03		2003-04	
	Absolute	Per cent	Absolute	Per cent
1	2	3	4	5
1. Income (a+b)	**21,313**	**14.1**	**11,422**	**6.6**
a) Interest Income	13,785	10.9	3,286	2.3
b) Other Income	7,528	31.3	8,136	25.7
2. Expenditure (a+b+c)	**15,812**	**11.3**	**6,229**	**4.0**
a) Interest Expenses	6,080	6.9	-6,029	-6.4
b) Operating Expenses	4,388	13.0	5,463	14.4
c) Provisions and Contingencies	5,344	29.3	6,795	28.8
3. Operating Profits	**10,845**	**36.3**	**11,989**	**29.5**
4. Net Profits	**5,501**	**47.5**	**5,194**	**30.4**

[1] The assets and liabilities of scheduled commercial banks are analysed primarily on the basis of end-March audited annual accounts. During 2003-04 one private sector bank, *viz.*, Development Credit Bank shifted from old private sector bank to new private sector banks, with statistical implications for the balance sheet and financial performance of new private sector banks and the old private sector banks.

of SCBs increased marginally accompanied by an increase in the share of term loans. The share of investments in total assets of SCBs declined, *albeit*, marginally, while there was an increase in the share of investment in Government securities. The share of investment in non-approved securities witnessed a decline reflecting the stringent norms imposed on non-SLR investments. The investment component of the balance sheet grew at 15.6 per cent during 2003-04, lower by 2.5 percentage points when compared with the record growth of the year 2002-03.

Bank-group wise position

3.3 Among bank groups, public sector banks (PSBs) continued to account for the major component of balance sheet of SCBs though their market share in deposits, advances, and investments was somewhat contained and that of private sector banks increased during 2003-04 (Table III.3). Bank-group wise consolidated balance sheets are provided in Appendix Tables III.1.(A) to III.1(C). All bank groups witnessed double-digit asset growth (Table III.4).

Intra-year Variations[2]

3.4 The trends in major banking aggregates of SCBs indicated a stronger growth of deposits, robust growth of credit particularly non-food credit, and a continued growth in investments during 2003-04 (Table III.5).

Table III.2: Consolidated Balance Sheet of Scheduled Commercial Banks

(As at end-March) (Amount in Rs.crore)

Item	2003		2004	
	Amount	per cent to total	Amount	per cent to total
1	2	3	4	5
Total Liabilities	**16,99,197**	**100.0**	**19,75,020**	**100.0**
1. Capital	21,594	1.3	22,348	1.1
2. Reserves and Surplus	76,288	4.5	94,240	4.8
3. Deposits	13,55,654	79.8	15,75,143	79.8
3.1 Demand Deposits	1,64,366	9.7	2,03,142	10.3
3.2 Savings Bank Deposits	3,02,303	17.8	3,73,677	18.9
3.3 Term Deposits	8,88,984	52.3	9,98,324	50.5
4. Borrowings	87,469	5.1	96,490	4.9
5. Other Liabilities and Provisions	1,58,192	9.3	1,86,798	9.5
Total Assets	**16,99,197**	**100.0**	**19,75,020**	**100.0**
1. Cash and balances with RBI	86,123	5.1	1,13,246	5.7
2. Balances with banks and money at call and short notice	75,113	4.4	82,223	4.2
3. Investments	6,93,753	40.8	8,02,066	40.6
3.1 In Government Securities (a+b)	5,36,214	31.6	6,39,144	32.4
a. In India	5,32,976	31.4	6,36,267	32.2
b. Outside India	3,238	0.2	2,877	0.1
3.2 In other approved Securities	19,281	1.1	18,100	0.9
3.3 In non-approved Securities	1,38,258	8.1	1,44,822	7.3
4. Loans and Advances	7,39,553	43.5	8,64,143	43.8
4.1 Bills purchased & discounted	58,813	3.5	67,231	3.4
4.2 Cash Credit, Overdrafts, *etc.*	3,54,768	20.9	3,71,836	18.8
4.3 Term Loans	3,25,972	19.2	4,25,076	21.5
5. Fixed Assets	20,278	1.2	21,403	1.1
6. Other Assets	84,378	5.0	91,940	4.7

Note : Scheduled commercial banks' data for 2002-03 are as reported in the balance sheets of banks for 2003-04 and hence may not tally with those reported in the *Report on Trend and Progress of Banking in India, 2002-03*, to the extent the figures for 2002-03 have been revised by some banks.

Source : Balance sheets of respective banks.

[2] This sub-section is based on the statutory returns submitted by scheduled commercial banks under Section 42 (2) of the Reserve Bank of India Act, 1934.

Table III.3: Major Components of Balance Sheet - Share of Bank Groups

(As at end-March) (per cent)

Bank-group	Assets		Deposits		Advances		Investment	
	2003	2004	2003	2004	2003	2004	2003	2004
1	2	3	4	5	6	7	8	9
Scheduled Commercial Banks	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Public Sector Banks	75.6	74.5	79.6	77.9	74.2	73.2	78.6	78.0
Nationalised Banks	46.5	46.7	50.8	50.4	48.6	47.7	46.5	47.1
State Bank Group	29.1	27.8	28.8	27.5	25.6	25.5	32.2	30.9
Private Sector Banks	17.5	18.6	15.3	17.0	18.8	19.8	15.5	16.8
Old Private Sector Banks	6.2	6.1	6.7	6.7	6.7	6.5	5.8	5.9
New Private Sector Banks	11.3	12.5	8.5	10.4	12.1	13.3	9.7	10.9
Foreign Banks	6.9	6.9	5.1	5.1	7.1	7.0	5.9	5.2

Deposits

3.5 Aggregate deposits of SCBs increased by 17.5 per cent in 2003-04, which was higher than the growth rate of 13.4 per cent (adjusted for the merger effect) recorded in 2002-03 (Appendix Table III.2). The greater requirement for transaction balances due to buoyant economic conditions, growth of non-food credit during the later part of the year and various other developments in financial markets pertaining *inter alia*, to developments in mutual funds segment and increased activity in capital market including disinvestments and FII inflows, had induced a high growth of demand deposits during 2003-04. Demand deposits of SCBs increased substantially by 32.1 per cent during the year as against an increase of 11.3 per cent in 2002-03, while time deposits grew by 15.2 per cent during 2003-04 compared with 13.7 per cent growth rate (adjusted for merger effect) in 2002-03 (Chart III.1).

Table III.4: Growth of Balance Sheet: Bank Group-wise

(As at end-March) (per cent)

Items	2003			2004		
	Public Sector Banks	Private Sector Banks	Foreign Banks	Public Sector Banks	Private Sector Banks	Foreign Banks
1	2	3	4	5	6	7
1. Capital	0.6	-6.6	25.8	3.8	3.7	3.3
2. Reserves and Surplus	21.7	21.6	28.4	29.1	22.0	14.5
3. Deposits	12.4	11.4	2.1	15.4	29.6	15.1
3.1 Demand Deposits	7.6	6.6	7.1	11.0	72.4	50.8
3.2 Savings Bank Deposits	18.3	17.1	22.2	19.6	53.3	40.1
3.3 Term Deposits	11.5	10.3	-2.4	14.4	19.4	-1.1
4. Borrowings	-14.4	15.8	-12.8	28.5	-4.2	10.8
5. Other Liabilities and Provisions	9.4	7.2	24.5	26.7	23.9	47.9
Total Liabilities/ Assets	**11.2**	**11.0**	**2.7**	**16.6**	**23.6**	**16.8**
1. Cash and balances with RBI	-8.7	45.0	12.6	26.1	32.5	59.7
2. Balances with banks and money at call and short notice	-28.1	-52.7	-59.7	32.1	37.0	52.2
3. Investments	20.1	9.9	16.2	17.3	25.6	1.9
3.1 In Government Securities	25.4	16.5	27.6	21.2	31.5	6.1
3.2 In other approved Securities	-11.2	-14.7	-8.8	-4.7	-17.7	11.0
3.3 In non-approved Securities	6.6	-1.5	-8.9	6.6	13.8	-11.1
4. Loans and Advances	14.4	18.9	7.6	14.8	23.0	16.0
Of which : Term Loans	22.8	26.1	6.0	31.9	26.0	25.3
5. Fixed Assets	1.5	1.3	-2.9	6.7	5.7	-10.8
6. Other Assets	-3.6	44.4	34.0	8.5	5.6	44.5

Source: Balance Sheets of respective banks.

Table III.5: Select Banking Indicators

(Amount in Rs. crore)

Indicator	Outstanding as on March 19, 2004	Financial Year Flows (per cent)	
		2002-03	2003-04
1	2	3	4
1. Aggregate Deposits (a+b)	15,04,416	16.1 (13.4)	17.5
a) Demand Deposits	2,25,022	11.3	32.1
b) Time Deposits	12,79,394	16.9 (13.7)	15.2
2. Bank Credit (a+b)	8,40,785	23.7 (16.1)	15.3
a) Food Credit	35,961	-8.3	-27.3
b) Non-food Credit	8,04,824	26.9 (18.6)	18.4
3. Investments in Government securities	6,54,758	27.3	25.1

Note : Figures in bracket exclude the impact of mergers since May 3, 2002.
Source : Section 42(2) Returns of commercial banks.

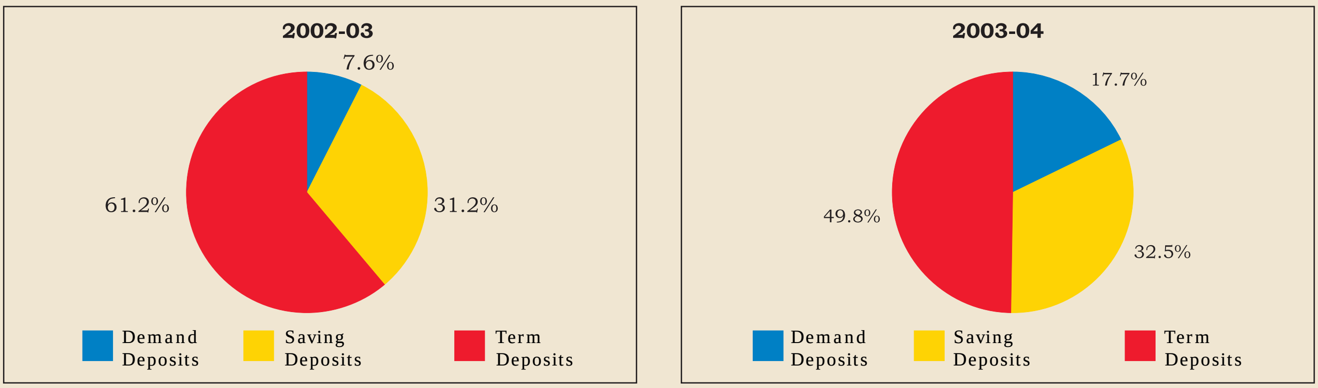
3.6 Across bank groups, the expansion of deposits in 2003-04 was highest at 29.6 per cent for private sector banks followed by 15.4 per cent for PSBs, and 15.1 per cent for foreign banks. The rate of expansion in demand and saving deposits was highest for private sector banks followed by foreign banks and PSBs. Regarding term deposits too, the private sector banks recorded the highest growth followed by the PSBs. For foreign banks, however, there was a decline in the growth of term deposits due to payouts of maturing deposits.

Bank Credit

3.7 Bank credit recorded robust growth during 2003-04 amidst the contraction in food credit owing to lower procurement and higher off-take and a sustained growth of non-food credit due to the turnaround in the macroeconomic environment and increase in foreign currency credit demand reflecting relatively lower cost of funds *vis-à-vis* Rupee loans. The initial sluggishness in non-food credit demand during the year was reversed by an upsurge from mid-August 2003, backed mainly by growth of priority sector loans, housing, retail and industrial credit. Gross bank credit increased by 15.3 per cent during 2003-04 compared with an increase of 16.1 per cent (net of merger effect) recorded in 2002-03. The growth of bank credit was supported by sustained increase in non-food credit, which increased by 18.4 per cent during 2003-04, almost similar to the growth rate of 18.6 per cent (adjusted for the merger effect) recorded in 2002-03.

3.8 In 2003-04, the balance sheet of SCBs showed that term loans accounted for a major share of 79 per cent of increase in outstanding loans and advances. The improvement in asset-liability management was evident from the fact that the expansion in term loans accounted for about 90 per cent of expansion in term-deposits.

Chart III.1: Component-wise Accretion in Deposits of Scheduled Commercial Banks



The bank group-wise analysis indicated that the expansion in loans and advances component of banks' assets registered an almost stable growth for PSBs but recorded sharp increases for private sector banks and foreign banks. The growth of term loans was high for all bank groups. Reflecting the improvement in asset-liability management, PSBs and private sector banks had expanded term loans consistent with the expansion of term deposits. For foreign banks, however, the expansion in term loans was met by expansion of demand and saving deposits.

Sectoral Deployment of Gross Bank Credit

3.9 Credit to agriculture and rural sector has been accorded top priority in the Common Minimum Programme of the Government of India. In the Budget 2004-05, Government of India has announced that the flow of credit to agriculture should be doubled in three years. Accordingly, all banks have been advised to step up agricultural credit. In 2003-04, the sectoral deployment of credit was associated with some positive developments. The growth of non-food credit was mainly driven by loans to priority sector, housing and infrastructure (Table III.6, Appendix Table III.3).

3.10 The credit flow to the priority sector from select SCBs (which account for about 90 per cent of gross bank credit) increased by 24.7 per cent, which was higher by about 8 percentage points over the growth rate (adjusted for merger effect) recorded in 2002-03. On an incremental basis, the flow of credit to priority sector accounted for about 55 per cent of the variation in net bank credit during the year, higher by about 20 percentage points when compared with 2002-03. During 2003-04, the growth of credit to the priority sector has been driven by the increase in lending to agriculture sector, small scale industries (SSI) and the other priority sector. The flow of credit to agriculture increased substantially by 23 per cent in 2003-04 as against an increase of 18 per cent in 2002-03. Bank credit to SSI also increased sharply by 9 per cent in 2003-04 as against an increase of 6 per cent in 2002-03. The spurt in other priority sector lending could be attributed to inclusion of investment made by banks in the mortgage backed securities (MBS) under direct lending to housing within the priority sector and the increase in the ceiling for lending for housing to Rs.10 lakhs in rural area. Anecdotal evidence suggests increases in credit lines to small transport operators.

3.11 The flow of credit to medium and large industries recorded lower growth during 2003-04 as compared with 2002-03. Industrial credit decelerated due to greater dependence of large corporates on internal sources as well as alternative sources of external financing. Credit to infrastructure sector, however, increased by 41.6 per cent in 2003-04 on top of a 35.3 per cent increase in 2002-03. Banks' lending to wholesale trade posted a robust growth during the year. Banks' lending to non-bank financial companies showed a decline in 2003-04. The flow of credit to various other sectors including retail loans recorded stronger growth of 23.7 per cent during

Table III.6: Sectoral Deployment of Non-food Gross Bank Credit: Flows

(Variations over the year)

(Amount in Rs. crore)

Sector	2002-03@		2003-04	
	Absolute	Per cent	Absolute	Per cent
1	2	3	4	5
1. Priority sectors	28,540	16.3	52,225	24.7
2. Industry (Medium and Large)	28,011	16.3	12,042	5.1
of which: Infrastructure	5,224	35.3	10,927	41.6
3. Housing	12,308	55.1	15,394	42.1
4. Non-banking financial companies	4,399	45.6	2,675	18.9
5. Wholesale trade (other than food procurement)	1,939	9.5	2,289	10.1
6. Other sectors	9,481	11.5	23,742	23.7
Total (1 to 6)	**84,678**	**17.5**	**1,08,367**	**17.5**
of which: Export Credit	6,424	14.9	8,485	17.2

@ Excluding the impact of merger of ICICI with ICICI Bank.

Note: Data are provisional and relate to select scheduled commercial banks which account for 85-90 per cent of bank credit of all scheduled commercial banks.

2003-04 as compared to growth rate of 11.5 per cent recorded in 2002-03. Thus, retail banking, mainly, in the form of housing and personal loans attracted an increasing share of banks' loan portfolio.

Housing Loans

3.12 Fiscal 2003-04 witnessed an increase in the share of housing loans in non-food gross bank credit to 7.1 per cent in March 2004, higher by a percentage point from 2002-03. Although the growth rate of housing loans at 42 per cent for 2003-04 was substantially high, it was lower by 13 percentage points compared with the growth rate of 55 per cent recorded in 2002-03 (Box III.1).

Consumer Credit

3.13 The retail banking portfolio encompasses deposit and asset linked products as well as other financial services offered to individuals for a variety of personal consumption and investment purposes. Retail banking is increasingly viewed

Box III.1: Housing Finance

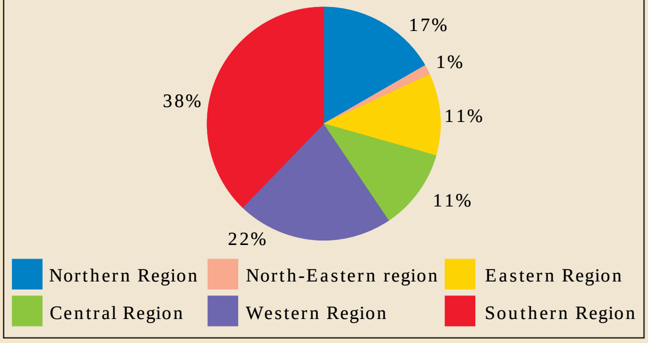
Housing finance in developing countries is a social good in view of its backward and forward linkages with other sectors of the economy. In India, growth of housing finance segment has accelerated in recent years in response to the several supporting policy measures taken and the supervisory incentives instituted. The Reserve Bank has been promoting the housing sector through minimum disbursement targets linked to incremental deposits and also by prescribing lower capital adequacy requirements. Direct finance to the housing sector up to Rs.15 lakh is treated as part of priority sector lending. The limit on housing loans for repairing damaged houses has been raised to Rs.1 lakh in rural and semi-urban areas and to Rs.2 lakh in urban areas. Banks have the freedom to stipulate lending rates without reference to their benchmark prime lending rates in respect of loans extended to individuals for acquiring residential properties.

Government of India too has been according considerable importance to the housing sector in rural areas. Housing in the rural areas, both of agriculturists and non-agriculturists, combines the business as well as dwelling needs and thereby leads to overall rural development. With a view to supplementing the efforts of Government of India, State Governments, National Housing Bank (NHB) and banking sector in augmenting the resources for the rural housing segment, NABARD included rural housing as an eligible activity for extension of refinance (investment credit) to the eligible banks since April 2001. Housing finance is available for construction of new as well as repairs/ renovation of existing houses in rural areas subject to various terms and conditions including *security/margin requirement* as per RBI/NHB guidelines issued from time to time. In case land is acquired, the land cost may be reckoned as margin money. Otherwise cost of land is not included in the project cost.

During the period 1993-2004, outstanding housing loans by scheduled commercial banks and housing finance companies grew at a trend rate of 23 per cent, higher than the trend growth rate of 14.8 per cent recorded in respect of scheduled commercial banks' non-food credit during the same period. The share of housing loans in total non-food credit of scheduled commercial banks has increased from about 3 per cent in 1992-93 to about 7 per cent in 2003-04.

Unlike many other countries, asset impairment on account of housing finance constitutes a very small portion. As at end-March 2004, the impaired credit (*i.e.*, net NPAs) was 1.4 per cent of outstanding advances. However, with growing competition in the housing finance market, there has been a growing concern over its likely impact on the asset quality.

Regional Distribution of Housing Loans 2003-04



Expressing concerns about the high growth witnessed in the housing segment the Reserve Bank has, as a temporary measure, put in place risk containment measures and increased the risk weight from 50 per cent to 75 per cent in the case of housing loans.

Although scheduled commercial banks as well as housing finance companies have led the robust growth in credit to housing sector since the late 1990s, the housing needs of the poor and low income groups have remained unaddressed (EPW, May 2004). As per the 10th Five Year Plan, around 90 per cent of the shortage in housing is experienced by the economically weaker sections of society. One of the reasons for low financing to weaker sections is the clause of margin. Margin is the proportion of the loan to be brought in by the borrowers. The clause is considered to be a constraining factor for the weaker section to access the housing loans. In order to solve this problem, NHB is promoting a separate entity India Mortgage Credit Guarantee Corporation (IMCGC). IMCGC will guarantee the payment of principal and interest by the borrower to lender, *i.e.*, banks, housing finance companies. IMCGC will also mitigate the risk perception of banks and housing finance companies and enable them to expand further credit in housing sector. However, due to non-availability of clear land titles in rural areas, and the difficulties in risk assessment due to irregular income behaviour in rural areas, growth of housing finance in rural areas has been constrained.

References :

Economic and Political Weekly, May 2004

NABARD-Housing Finance for Rural Areas, 2003-04

Reserve Bank of India, Annual Report 2002-03

The Working Group on Housing Finance (Chairman: Shri R.V. Verma), 2002, NHB

by banks as an attractive market segment with opportunities for growth. The expansion of the retail banking segment can be attributed to the growing middle class with high disposable income, wider choices of consumer durables available to be financed by the banks, increased acceptance of credit cards and increased demand for housing loans spurred by attractive tax breaks (Box III.2).

Box III.2: Consumer Credit

Across the globe, retail lending has been the most spectacular innovation in the commercial banking sector in recent years. Retail loans comprise consumer credit for specific purpose and credit for general use. The surge in credit to the retail segment across developing as well as developed economies has occurred due to commercial banks shifting from traditional banking activities to a broad-based lending portfolio. The growth of retail lending, especially, in emerging economies, is attributable to the rapid advances in information technology, the evolving macroeconomic environment owing to financial market reform, and several micro-level demand and supply side factors. Technology induced innovative financial products have facilitated strengthening of balance sheets and income structures of banks. Technology has enabled a significant reduction in cost of external finance for borrowers, while banks have benefited from product innovations, and lower transaction cost associated with collection, processing and use of information. This, in its wake, has offered banks better techniques for risk management and pricing of products.

The surge in retail lending, however, has certain limitations. Retail lending may accentuate indebtedness of households, with implications for sustainability of private consumption and saving in the medium to longer horizon. Rapid increase in retail loans may impinge on bank credit for investment activities with implications for economic growth. Several cross section studies suggest that retail lending may, however, pose various risks with implications for banks' asset quality.

In the Indian context, retail lending has been the mainstay and a key profit driver for banks in the recent times with retail portfolio constituting 21.5 per cent of total outstanding advances as on March 2004. The overall impairment of the retail loan portfolio worked out to 2.5 per cent and compares favourably with the Gross NPA ratio for the entire loan portfolio, which is placed at 7.4 per cent. Within the retail segment, the housing loans, which formed nearly 48 per cent of total retail portfolio, had the least gross asset impairment at 1.9 per cent while consumer durables segment had the highest gross asset impairment at 6.3 per cent. Apart from diversification objective, various factors have influenced banks' lending to the retail sector in India. These relate to falling interest rates, fiscal incentives from the Government, various reform measures pertaining to the Securitisation Act (SARFAESI), the repealing of Urban Land Ceiling Act and the rationalisation of stamp duty structure, low default rate, low credit off-take from the commercial and corporate sector, lowering of costs of housing, consumer durables and automobiles due to competition, and technological innovations relating to increasing use of credit/debit cards[3], ATMs, direct debits and phone banking etc. While retail banking has always been prevalent in various forms (for instance, co-operative banks, some of whom are over a century old, have always had the retail thrust), for the last few years it has become synonymous with mainstream banking for many banks. While new generation private sector banks (ICICI Bank, accounting for nearly 30 per cent of the domestic retail growth) have invested in creating and sustaining a retail brand, their public sector counterparts too, have not lagged behind. Leveraging their vast branch network and outreach, public sector banks like State Bank of India (SBI) whose retail segment constitutes 20 per cent of the total advances have aggressively forayed to garner a larger slice of the retail pie. The retail lending of SBI grew by Rs.8,803 crore in 2003-04 as against an increase of Rs.6,641 in 2002-03. There are, however, various concerns as to whether retail lending has emerged as an efficient channel for improving access to credit and promoting broad-based development. At present, retail lending is largely confined to urban and metropolitan regions. Expressing concerns about the high growth witnessed in the consumer credit segments the Reserve Bank has, as a temporary measure, put in place risk containment measures and increased the risk weight from 100 per cent to 125 per cent in the case of consumer credit including personal loans and credit cards (mid-term Review of annual policy, 2004-05).

Table : Retail Portfolio of Banks
(As at end-March 2004)

Items	Amount Outstanding (Rs. crore)	Impaired Credit as per cent of outstanding Loans	Net NPAs as per cent of out-standing loans
(i) Housing Loan	89,449	1.9	1.4
(ii) Consumer Durables	6,256	6.6	4.0
(iii) Credit Card Receivables	6,167	6.3	2.4
(iv) Other Personal Loans	87,170	2.6	1.6
(v) Total Retail Loans [(i) +(ii)+(iii)+(iv)]	1,89,041	2.5	1.6
(vi) Total Loans & Advances	8,59,092	7.4	2.8

Data pertains to Domestic operations.

Source: RBI's Off-site Supervisory Returns.

References :

Céline G. L., and Erlend N., (2004), 'The Economics of Retail Banking—An Empirical Analysis of the UK Market for Personal Current Accounts', *Financial Stability Report,* 2004, Bank of England,

European Credit Research Institute (2000) 'Consumer Credit in the European Union' *ECRI Research Report* No. 1 February.

Morris, J., (2001), 'Risk Diversification in Credit Portfolio, An Overview of Country Practices', *IMF Working Paper* No. 01/200

Stefanie K., and Harald S., (2002), 'Consumer Credit Rates in the Eurozone: Evidence on the Emergence of a Single Retail Banking Market', *ECRI Research Report* No. 2, January.

Wendy E., (2004), 'Testing for Adverse Selection and Moral Hazard in Consumer Loan Markets', Federal Reserve Board, February 10.

Wightman, J., (1980), 'Consumer Lending', *The Canadian Banker & ICB Review*, Toronto, August, Vol.87, Issue 4; p. 28

[3] Also see Chapter II: Box II.17.

3.14 The typical products offered in the retail banking segment are housing loans, consumption loans for purchase of durables, auto loans, credit cards and educational loans. The loans are marketed under attractive brand names to differentiate the products offered by banks. The loan values typically range between Rs.20,000 to Rs.100 lakh. The loans are generally for duration of five to seven years with housing loans granted for a longer duration of 15 years. Credit cards is another rapidly growing sub segment of this product group.

3.15 An important characteristic of retail banking assets is the comparatively low loan values. In order to appraise such loans, banks are using more refined credit assessment methods. These include credit scoring techniques, automated application processing, behavioral scoring models and income surrogate models (Box III.3). In addition, banks are also using data sharing as a means of improving the selection of customers and reduction of credit losses. In the absence of full fledged Credit Bureaus, the negative data sharing extends to sharing of data on hot listed credit cards besides using banks' own internal black lists.

Export Credit

3.16 In 2003-04, export credit grew by 17 per cent as against an increase of 15 per cent in 2002-03. The share of export credit in net-bank credit improved only marginally to 7.6 per cent in 2003-04 as against 7.4 per cent in 2002-03 notwithstanding higher export growth during the year (Chart III.2). The export credit refinance limit showed a declining trend during May-November, 2003 (Appendix Table III.4). The outstanding export credit refinance availed remained negligible during 2003-04.

Industry-wise Deployment of Credit

3.17 In 2003-04, industrial credit expanded by 5.9 per cent, which was lower than 13.6 per cent growth recorded in 2002-03. The credit off-take by the industrial sector remained relatively subdued amidst buoyancy in industrial activity and stronger corporate balance sheet reflecting, *inter alia*, increased recourse of the corporate sector to internal sources of financing as well as external commercial borrowings. The demand for credit for financing fixed investments remained lower on account of existing excess

Box III.3: Credit Scoring

The rapid advancement in information technology has enabled banks to adopt various sophisticated tools for processing of information and financial engineering in order to better manage risks of their credit portfolios. Credit scoring is one such technique, which is being increasingly utilised by banks for assessing informationally opaque borrowers. Some cross country evidence shows that over 75 per cent of mortgage lenders and over 90 per cent of credit card lenders in United States use credit scores when making their lending decisions. In developing economies, banks have started using the credit scoring technique in a big way, especially for retail lending including housing loans and credit cards.

A credit score is essentially a statistical number that indicates the level of risk associated with the borrowers. Higher/lower credit score reflects lower/higher level of risks of borrowers. Banks use credit score for risk based pricing strategy, which entails differential interest rates and other lending terms based on the risk profile and creditworthiness of borrowers.

Banks and financial institutions use a variety of credit scoring models for analysis of borrowers' creditworthiness. Credit Reporting Agencies (CRA) use different scoring models for different purposes. For instance, housing finance and car loans could employ a model different from that used for credit cards and other retail loans including personal consumption. There is still no general legal obligation on CRAs to provide credit scores to individuals. However, some credit service companies sell credit scores and advice for improving these for a fee.

Credit scoring models use complex formula taking into account a variety of information culled out from borrowers' credit report, payment history, and credit applications, and collections, foreclosures, lawsuits, and other collection items. Typically, information pertaining to borrowers' occupation, length of employment, asset ownership including home and car, amount of credit or debt, types of credit, new credit, and the number of credit checks, and runs among several others are used by scoring models.

Credit scoring models have long been shrouded in secrecy pertaining to types of information used and measurement of borrowers' risks. From lenders' perspective, there are various concerns relating to limits to disclosure and transparency. On the other hand, from borrowers' perspective there are legal concerns relating to data protection.

References:

Berger, A.N., Frame, W.S., and Miller, N.H., (2002) 'Credit Scoring and the Availability , Price and Risk of Small Business Credit', Federal Reserve Bank of Atlanta, *Working Paper*, 2002-6, April..

Frame, W.S., Srinivasan, A., and Wooskey, L., (2002), 'The Effect of Credit Scoring on Small Business Lending', *Journal of Money, Credit and Banking*, Vo.33 (3).

Hand, D.J., and Henkey, W.E., (1997), 'Statistical Classification Methods in Consumer Credit Scoring: A Review', *Journal of Royal Statistical Society*, Vol.160.

Mester, L., (1997), 'What is the Point of Credit Scoring?', *Federal Reserve Bank of Philadelphia Business Review*, September/October.

Chart III.2: India's Exports and Export Credit

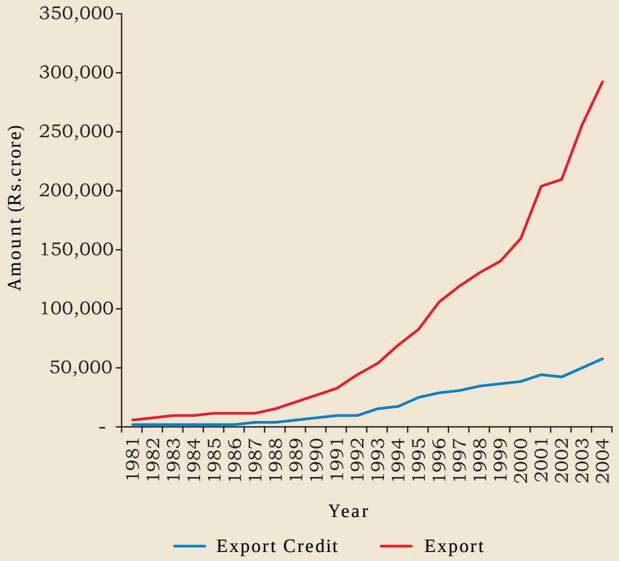
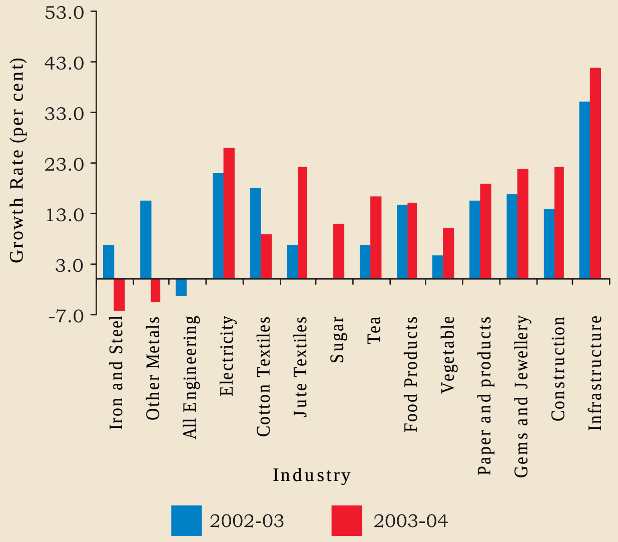


Chart III.3: Industry-wise deployment of Gross Bank Credit



capacities. However, there was a distinct change in the pattern of growth of non-food credit across various industries. The industry-wise deployment of bank credit was induced by loans to infrastructure sector, agro-based industries, exports, wholesale trade and tourism. The increase in credit flow was highest for infrastructure sectors including power, telecommunications, roads and ports. In 2003-04, the flow of credit to the infrastructure sector recorded an expansion of 41.6 per cent with large increments in all the three infrastructure segments - power, telecom and 'roads and ports'. There was increase in credit flow to agro-based industries such as sugar, tea, vegetable oil, paper and food processing. Other industries which recorded increase in credit flow in 2003-04 were electricity, tobacco products, 'gems and jewellery' and construction (Chart III.3, Appendix Table III.5).

Bank Credit to Sick/Weak Industries

3.18 There has been a decline in the number of SSI-sick and non-SSI sick / weak industrial units financed by SCBs in recent years. The quantum of bank loans locked up in sick / weak industries increased from Rs.26,065 crore as at end-March 2002 to Rs 34,816 crore as at end-March 2003, recording an increase of 33.6 per cent. The share of bank loans to sick units in total bank loans increased from 4.4 per cent as at end-March 2002 to 4.8 per cent as at end-March 2003. Across broad category of sick units, non-SSI sick units accounted for a major share of total sick loans, followed by sick SSI and non-SSI weak units (Appendix Table III.6).

Lending to Sensitive Sectors

3.19 During 2003-04, banks' lending to capital market, real estate and commodities sector increased in absolute terms. However, the exposure of SCBs to sensitive sectors accounted for only 3 per cent of aggregate bank loans and advances. Banks' lending to capital market remained negligible at 0.4 per cent of outstanding loans and advances. The share of credit to real estate and commodities sectors in outstanding loans and advances of SCBs was 1.6 per cent and 1.2 per cent, respectively. Real estate sector accounted for the major share of 51.6 per cent of total loans to sensitive sectors followed by commodities and capital markets segments, respectively (Table III.7 and Appendix Table III.7). Among bank groups, PSBs continued to account for about 60 per cent of the total exposure of SCBs to sensitive sectors.

Other Investments

3.20 Besides loans and advances, banks provide financial support to the corporate sector in the form of non-SLR investments, which includes commercial paper, shares, bonds, and debentures issued by the private corporate sector and public sector undertakings (PSUs)

Table III.7 : Lending to Sensitive Sectors by Scheduled Commercial Banks
(As at end-March)

(Amount in Rs. crore)

Advances to	2003	2004
	1	2
1. Capital market	2,484 (10.5)	3,333 (12.2)
2. Real Estate	12,464 (52.6)	14,170 (51.6)
3. Commodities	8,735 (36.9)	9,952 (36.2)
Total (1+2+3)	**23,683** **(100.0)**	**27,455** **(100.0)**

Note : Figures in brackets are percentage to total.

(Table III.8). The investment in bonds and debentures continued to be the major component of banks' non-SLR investments, though its share in total non-SLR investments declined during the year. In absolute terms, there was a sharp increase in banks' finance to mutual funds. The share of banks' investment in mutual funds in total non-SLR investments increased to 8.6 per cent in 2003-04 from 4.7 per cent in 2002-03.

Certificates of Deposit (CDs)

3.21 The outstanding amount of CDs issued by SCBs increased from Rs.1,188 crore on April 4, 2003 to Rs.4,461 crore by mid-March 2004 (Appendix Table III.8). The typical discount rate for CDs with a 3-month maturity declined from 7.2 per cent at mid-April 2003 to 5.5 per cent at end-August 2003 and further to 5.0 per cent by mid-March 2004. During 2004-05 (upto October 15, 2004), it further softened to 4.75 per cent. The outstanding amount of CDs continued to increase to Rs.4,837 crore upto October 15, 2004. The growth of CDs has been on account of a number of factors including the issuance of guidelines by the Reserve Bank on investments by banks in non-SLR debt securities, reduction in stamp duty on CDs effective March 1, 2004, ban on premature closure of CDs and greater opportunity for secondary market trading. These developments have led to greater demand for investment in CDs by mutual funds particularly in the wake of their improved funds position. An encouraging development that ensued has been that some of the top rated banks have been getting their CDs rated for better access to the market even when such ratings are not mandatory under the extant guidelines.

Table III.8: Scheduled Commercial Banks' Select Non-SLR Investments
(As at end-March)

(Rs. crore)

	Instrument	2003	2004
	1	2	3
1.	Commercial Paper	4,007 (3.0)	3,770 (2.7)
2.	Units of UTI and other Mutual Funds	6,317 (4.7)	11,808 (8.6)
3.	Investment in shares issued by	10,206 (7.6)	9,696 (7.0)
	of which :		
	a) Public sector undertakings	1,430 (1.1)	1,272 (0.9)
	b) Private corporate sector	7,589 (5.7)	7,395 (5.4)
4.	Investments in bonds/debentures issued by	1,13,169 (84.6)	1,12,370 (81.6)
	of Which :		
	a) Public sector undertakings	46,854 (35.0)	48,646 (35.3)
	b) Private corporate sector	32,973 (24.7)	27,903 (20.3)
Total (1+2+3)		**1,33,699** **(100.0)**	**1,37,644** **(100.0)**

Notes: 1. Figures in brackets are percentages to total.
2. Data excludes RRBs. Data are based on statutory Section 42 (2) returns submitted by scheduled commercial banks.

Commercial Paper

3.22 Easy liquidity conditions prompted companies to mobilise funds through commercial papers (CPs). The issuance of CPs picked up from mid-November 2003 on account of increased interest by mutual funds and banks in the wake of the guidelines by the Reserve Bank barring investments in non-SLR debt securities with original maturity upto one year with the exception of CDs and CPs. Furthermore, the reduction in stamp duty on CPs also buoyed up the market. The discount rates on CP eased from a range of 5.25-8.15 per cent in April 2003 to 4.70-6.50 per cent in March 2004. During 2004-05 (upto mid-November 2004), the discount rates ranged in between 5.10-6.23 per cent. The weighted average discount rate (WADR) also declined from 6.20 per cent in April 2003 to 5.11 per cent in March 2004 before increasing to 5.54 per cent in mid-November 2004. The spread of the WADR between the prime-rated and medium-rated companies narrowed from 162 basis points in April 2003 to 73 basis points in March 2004. As on mid-November 2004, the spread has further declined to 30 basis points. During the current financial year upto mid-November 2004 the most preferred maturities of CPs were 'up to 90 days' and '181 days & above'. During the current financial year (up to mid-November 2004), the share of manufacturing and other companies in the amount of CPs raised stood lower at 40 per cent (44 per cent in 2003-04), while finance/leasing companies and financial institutions accounted for 55 per cent and 5 per cent respectively, from 38 per cent and 18 per cent in 2003-04.

Forward Rate Agreements (FRAs) / Interest Rate Swaps (IRS)

3.23 There has been a sharp increase in the volume in FRAs/IRS market during the current financial year so far. FRAs/IRS transactions, both in terms of number of contracts and outstanding notional principal amount, rose from 9,363 contracts amounting to Rs.2,42,983 crore as on April 4, 2003 to 19,867 contracts for Rs.5,18,260 crore as on March 19, 2004. During the current financial year up to the fortnight ended October 15, 2004, the number of contracts and notional amount have increased to 30,101 and Rs.7,99,032 crore, respectively. There has been a significant increase in the number and amount of contracts. Also, the participation in the market has been broad based and include select PSBs, PDs, foreign and private sector banks. In a majority of these contracts, NSE-MIBOR, LIBOR and MIFOR were used as the benchmark rates. The other benchmark rates used were secondary market yields of Government of India securities having residual maturity of 1 year, primary cut-off yield on 364-day Treasury Bills, *etc*.

Credit to Government

3.24 In recent years, scheduled commercial banks' investment in government and other approved securities has been much in excess of the required statutory liquidity ratio (SLR) of 25 per cent. As at end-March 2004, investments in SLR securities constituted 41.3 per cent of net demand and time liabilities (NDTL) of banks as against 41.5 per cent as at end-March 2003.

3.25 The rate of expansion of investment in Government securities for PSBs was 21.2 per cent for 2003-04, lower by about 4 percentage points over 2002-03. Private sector banks' investments in Government securities increased sharply by 31.5 per cent in 2003-04 as against an increase of 16.5 per cent recorded in 2002-03. The increasing preference of private banks for Government securities reflected their efforts toward improving capital to risk weighted assets ratio. Foreign banks, however, recorded a substantially lower growth of investment at 6 per cent in 2003-04 as compared with an increase of 27.6 per cent in 2002-03.

Credit-Deposit Ratio

3.26 The credit-deposit ratio (C-D ratio) is one of the most widely used banking indicators for analysing the role of banks in promoting productive sectors and contributing to economic growth. In a bank-based financial system, the C-D ratio assumes greater significance as an aggregative measure for gauging the effectiveness of credit delivery system. Higher C-D ratio implies for greater credit orientation of banks. In the Indian context, however, the C-D ratio has shown a downward trend over the years. Although the deployment of credit and the time path of C-D ratio, in general, is influenced by the structural transformation of the economy, the role of credit culture and banks' lending policy have a considerable impact on the size of the ratio (Box III.4).

3.27 According to the data available from the Basic Statistical Returns (BSR), the C-D ratio (as per sanctions) of SCBs at end-March 2004 was 58.7 per cent as against 59.2 per cent at end-March 2003. The total flow of resources, as reflected in the credit *plus* investment to deposit (IC-D) ratio (as per utilisation) had increased to 66.4 per cent at end-March 2003 from 65.6 per cent at end-March 2002. Region-wise, the C-D ratio (as per sanctions) showed an increase for all regions with the exception of Western region (Appendix Table III.9).

3.28 The C-D ratio though useful as an aggregate measure provides limited information about the credit orientation of banks and the access of diverse economic agents to bank credit. In this context, the alternative measures of credit market concentration have been explored by several studies for gauging the effectiveness of credit delivery system and thereby providing critical inputs for policy formulation (Box III.5).

Trends in Major Banking Indicators – 2004-05

3.29 During 2004-05 (up to October 29, 2004), aggregate deposits of scheduled commercial banks rose by 7.5 per cent (7.2 per cent, net of conversion of IDBI) as compared with an increase of 9.0 per cent in the corresponding period of the previous year. The lower deposit growth this year could be mainly attributed to reduction in non-resident Indian (NRI) deposits with the banking system. On an annual basis, the growth in aggregate deposits at 15.8 per cent (15.6 per cent, net of conversion of IDBI) was, however, higher than that of 11.8 per cent during 2003-04. During 2004-05 (up to October 29), scheduled commercial banks' credit increased by 17.5 per cent (13.7 per cent, net of conversion of IDBI) which was substantially higher than the increase of 4.5 per cent in the corresponding period of 2003-04. Food credit increased by Rs.3,751 crore as against a decline of Rs.13,459 crore in the previous year reflecting a turn-around of about Rs.17,210 crore. Non-food credit posted a robust increase of 17.9 per cent (13.8 per cent,

Box III.4: Credit Culture

There is growing realisation that though macroeconomic stability is necessary, several sufficient conditions assume importance for achieving sustained and rapid economic progress. Regarding various indicators of sufficient conditions, economists attach critical importance to an effective credit delivery system, which ensures better access to credit for various productive activities. About two decades ago, across countries it was believed that better access to credit could be achieved through a wide network of formal credit institutions. During the 1990s, economists while drawing lessons from the performance of formal credit institutions and the informal credit agencies have recognised that better access to credit can be achieved with an appropriate credit culture.

Conceptually, there are four basic types of credit cultures adopted by banks. These pertain to value driven, immediate-performance driven, production driven, and un-focused credit culture. The key determinants of the credit culture are the management's commitment, credit discipline, priority-based incentives, risk-managed lines of business, as well as a clear, consistent and candid communication strategy. An effective credit delivery process entails a process for ordering and integrating priorities, culture, strategy and controls. This is possible by establishing corporate priorities, choosing a credit culture, determining the credit risk strategy and implementing risk controls (Strischek, 2003). In a competitive environment, such a strategy entails that the credit culture should be dynamic in nature.

In the Indian context, the issue of credit culture has generated an animated discussion (Reddy, 2004 and Mohan, 2003, 2004). An examination of various issues pertaining to banks' lending policy indicated that banks should adopt prudent risk management strategies rather than risk aversion strategies in order to contribute to an effective credit delivery system. Broadly, the discussion on credit culture has surfaced amidst concerns pertaining to the underlying trends in credit-deposit ratio and rural credit, high investments in Government securities, the prevalence of category-wise lending policy, downward inflexibility of lending rates among several other developments. In this context, studies have suggested that banks should devise appropriate lending policies to ensure the success of the gradual deregulation and financial market reforms undertaken.

References:

Mohan, R., (2003), 'Transforming Indian Banking: In Search of a Better Tomorrow', *RBI Bulletin*, January.

Mohan, R., (2004), 'Finance for Industrial Growth', *RBI Bulletin*, March.

- 'Bonds hold attraction for India's lazy bankers', *Times News Network*, November 25, 2003.

Reddy, Y. V., (2004), 'Credit Policy, Systems, and Culture', *RBI Bulletin*, March.

Strischek, D., (2003) 'Credit culture Part II: Types of credit cultures', *The RMA Journal*, Philadelphia, Dec 2002/Jan 2003. Vol. 85, Iss. 4, pg. 35.

net of conversion of IDBI) during 2004-05 (up to October 29) as compared with an increase of 6.8 per cent in the corresponding period of 2003-04. The incremental non-food credit-deposit ratio was as high as 127.8 per cent (102 per cent, net of conversion of IDBI) during 2004-05 (up to October 29) as against 41 per cent in the corresponding period of the 2003-04.

Box III.5: Credit Market Concentration

Finance literature suggests that portfolio diversification is desirable for minimising credit portfolio risk, improving asset quality, and optimising efficiency in allocation of resources for productive activities. From a policy perspective, with increasing concern for financial stability across countries, measures of portfolio diversification of banks have received considerable importance. Applied models of financial stability have integrated alternative measures of credit market concentration pertaining to institutional structure of banking sector, regional and sectoral deployment of credit for evaluating and analysing the underlying nature of market competition and the stability of financial system in various countries. Measures of credit market concentration have been used for gauging the competitive efficiency of credit delivery system.

On an empirical plane, various approaches have been adopted. The extent of competition in the banking industry in a country is analysed in terms of participation of different bank groups such as public sector banks, domestic private banks and foreign banks. Several studies have used Hirschman and Herfindhal Index (HHI)[4] of market concentration for analysing credit market concentration (BOE, Quarterly Bulletin, 2004). The World Bank database on regulation and supervision provides useful information about concentration of banking sector across countries. The study shows that among 121 countries, there were as many as 102 countries, which had five big banks accounting for more than fifty per cent of deposits. On the other hand, there were 112 countries out of 129 countries, which had five big banks accounting for more than fifty per cent of assets (Table A). According to the study, five largest banks in India accounted for about 41 per cent of banks' deposit and 44 per cent of assets. India's position was ranked better than that of Brazil, Chile, Mexico, Malaysia and France (Table B).

Table A: Bank Concentration in World
Share of Five Big Banks in Deposits and Assets
(Cross-country Distribution)

Category Greater or equal to (in per cent)	Deposits	Assets
	No. of Banks	
30	116	125
45	107	113
50	102	112
70	71	75
80	52	58
90	35	38

Source: *World Bank Database on Regulation and Supervision 2003*

Table B: Share of Five Largest Banks

(per cent to total)

Countries	Deposits	Assets
Brazil	63	54
Chile	62	61
France	70	60
Germany	21	20
India	**41**	**44**
Japan	46	46
Malaysia	57	56
Mexico	80	80
Philippines	46	43
United Kingdom	24	23
United States	29	30

Source: *World Bank Database on Regulation and Supervision 2003*

In the Indian context, an empirical analysis of credit market concentration brings forth certain useful insights. The competitive nature of the banking sector has witnessed a significant improvement due to the increasing participation of domestic private sector and foreign banks. The share of public sector banks in aggregate deposits has come down from 92 per cent in 1990-91 to 78 per cent in 2003-04 while the share of domestic private sector banks has improved from four per cent in 1990-91 to 15 per cent in 2003-04. In terms of bank credit, the share of public sector banks has come down from 92 per cent in 1990-91 to 74 per cent in 2003-04. The share of domestic private sector banks in bank credit has increased from three per cent in 1990-91 to 19 per cent in 2003-04 while the share of foreign banks has increased from four per cent in 1990-91 to seven per cent in 2003-04. Greater competition has offered customers a wider range of options both in terms of parking funds with banks as well as borrowing in a cost-effective manner.

The HHI index estimated using industry-wise deployment of credit shows a decline from the range of 1300 in 1991-92 to the range of 800 in 2003-04, thereby, suggesting an improvement in banks' credit portfolio diversification and decline in credit market concentration. The HHI index measure based on sectoral deployment of credit also shows that credit concentration has reduced over the period 1991-92 to 2003-04.

Reference:

Bank of England (2004), 'Banking Concentration in UK', *Financial Stability Review*, June, Article 7.

World Bank Database on Regulation and Supervision 2003.

[4] HFI index = $\sum_{i=1}^{n} S^2$, where S is the share of bank credit of an industry/activity in total bank credit during time period t. Higher value of HFI over the years suggests increasing concentration and conversely lower value of HFI over the years shows improvement in credit allocations to different sectors.

3.30 In recent years, the impetus to credit growth has emanated from non-agriculture non-industrial sectors, particularly, housing, small transport operators and retail loans. The detailed information on sectoral deployment of credit available from banks reveals that over two-thirds of credit flow during the current financial year (up to August 2004) have been on account of retail, housing and other priority sector loans. More recent information available points to a revival of industrial credit. Among industries, discernible increase is observed in petroleum, infrastructure, electricity, construction, metal & metal products, drugs & pharmaceuticals, gems & jewellery and automobiles.

3.31 While credit expanded, scheduled commercial banks' investments in bonds/ debentures/shares of public sector undertakings and private corporate sector, commercial paper *etc.*, increased by 2.9 per cent up to October 29, 2004 as compared with a decline of 0.6 per cent. The total flow of resources from scheduled commercial banks to the commercial sector increased substantially by 16.4 per cent (12.7 per cent, net of conversion of IDBI) up to October 29, 2004 as compared with the increase of 5.9 per cent in the corresponding period of the previous year. The year-on-year growth in resource flow was also higher at 27.1 per cent (23.1 per cent, net of conversion of IDBI) as against 13.8 per cent a year ago. Scheduled commercial banks' investments in instruments issued by financial institutions (FIs) and mutual funds this year increased by Rs.154 crore as against an increase of Rs.7,570 crore in October 2003. The total flow of resources to the commercial sector including capital issues, global depository receipts (GDRs)/American depository receipts (ADRs) and borrowings from banks and FIs increased by Rs.1,65,809 crore up to October 29, 2004 as compared with Rs.66,857 crore in the corresponding period of 2003-04.

3.32 During 2004-05 (up to October 29, 2004), scheduled commercial banks' investment in government and other approved securities at Rs.28,955 crore (Rs 16,762 crore, net of conversion of IDBI) was lower than that of Rs.84,031 crore in the corresponding period of 2003-04 partly on account of pick-up in credit demand. Consequently, commercial banks' excess holding of SLR securities was reduced to Rs.2,59,083 crore or 14.5 per cent of net demand and time liabilities(NDTL). Notwithstanding this reduction, the effective SLR investment at 39.5 per cent of NDTL for the banking system as a whole, continues to be high relative to the statutory minimum of 25 per cent. As credit demand is expected to remain buoyant during 2004-05, lower demand by banks for Government securities has implications for government market borrowings programme.

3.33 On an assessment of macro economic and monetary aggregates, the mid-term Review of annual policy Statement for the year 2004-05 indicated that the growth in aggregate deposits would be Rs.2,18,000 crore as projected in the annual policy Statement 2004-05 while non-food bank credit including investments in bonds/ debentures/shares of public sector undertakings and private corporate sector, commercial paper (CP) *etc.*, is expected to increase by around 19.0 per cent, higher than 16.0-16.5 per cent projected earlier; the higher credit expansion could be accommodated without putting undue pressure on money supply because of lower borrowing of the Government from the banking sector; in the eventuality of Government borrowings being larger, unwinding of MSS would facilitate such borrowings.

Role of Banks as Authorised Dealers

3.34 In 2003-04, the total turnover including purchase and sale of foreign exchange by authorised dealers declined by 1.5 per cent. In the inter-bank segment, both purchase and sale operations remained subdued due to a stronger Indian rupee. The merchant segment witnessed an increase in purchase operations and a decline in sale operations in tandem with the movements in the imports and exports. (Table III.9). The inter-bank to merchant turnover ratio hovered in the range of 2.9 per cent to 3.9 during the year, indicating orderly market conditions.

International Banking Statistics

3.35 International banking statistics (IBS) assume critical importance as they provide information about the integration of a country's financial sector with rest of the world. The Reserve Bank has been compiling and disseminating IBS on the lines of the reporting system devised by the Bank for International Settlements (BIS). The data on IBS of India, presented under locational banking statistics (LBS) and consolidated banking statistics (CBS),

Table III.9: Composition of Foreign Exchange Turnover of Authorised Dealers

(Amount in US $ million, ratios in per cent)

Year	Merchant		Inter-Bank		Total	
	Purchase	Sale	Purchase	Sale	Purchase	Sale
1	2	3	4	5	6	7
1997-98	97,937 (14.9)	1,11,989 (17.2)	5,58,019 (85.1)	5,38,103 (82.8)	6,55,956 (100.0)	6,50,091 (100.0)
1998-99	1,18,097 (17.9)	1,34,587 (20.1)	5,40,752 (82.1)	5,34,294 (79.9)	6,58,849 (100.0)	6,68,881 (100.0)
1999-2000	1,23,747 (21.0)	1,28,294 (21.6)	4,66,042 (79.0)	4,65,844 (78.4)	5,89,789 (100.0)	5,94,139 (100.0)
2000-01	1,33,214 (18.4)	1,48,018 (20.8)	5,90,638 (81.6)	5,62,379 (79.2)	7,23,852 (100.0)	7,10,397 (100.0)
2001-02	1,34,966 (18.2)	1,37,420 (18.4)	6,04,678 (81.8)	6,10,295 (81.6)	7,39,644 (100.0)	7,47,715 (100.0)
2002-03	1,65,544 (21.0)	1,63,664 (20.6)	6,24,151 (79.0)	6,31,380 (79.4)	7,89,695 (100.0)	7,95,044 (100.0)
2003-04	1,96,553 (24.6)	1,53,961 (20.2)	6,01,993 (75.4)	6,08,833 (79.8)	7,98,546 (100.0)	7,62,794 (100.0)

Note: Figures in brackets are shares in total turnover.

are supplied to the BIS, which are included in their quarterly publications.

3.36 During 2003-04, international liabilities of banks increased by 10 per cent, as against an increase of 17 per cent in 2002-03 driven by the accretion to non-resident external rupee (NRE) deposits and sizeable foreign currency borrowings. The foreign currency borrowings witnessed a sharp growth of 82 per cent during the year (Table III.10). The surge in NRE accounts recorded in 2002-03 also continued in 2003-04. The foreign currency borrowing showed a sizeable expansion due to various liberalisation measures relating to the capital account for facilitating residents' foreign currency requirement for productive purposes. In particular, the surge in foreign currency

Table III.10: International Liabilities of Banks Classified According to Type

(Amount in Rs. crore)

Liability type	Amount outstanding as at end-March		
	2002	2003	2004
1	2	3	4
1. Deposits and Loans	1,20,604	1,45,930	1,78,994
of which:			
Foreign Currency Non-Resident Bank [FCNR (B)] scheme	39,636	43,989	45,386
Foreign currency Borrowings*	5,514	18,411	33,598
Non-resident External Rupee (NRE) Account	33,233	53,124	75,938
Non-Resident Non Repatriable (NRNR) Rupee Deposits	27,181	15,207	7,335
2. Own Issues of Securities Bonds (including IMD/RIBs)	43,582	44,087	27,720
3. Other Liabilities	7,150	10,475	14,017
of which:			
ADRs/GDRs	1,862	3,833	6,396
Equities of banks held by non-residents	547	556	1,379
Capital/remittable profits of foreign banks in India and other unclassified international liabilities	4,741	6,086	6,242
Total International Liabilities	**1,71,336**	**2,00,493**	**2,20,730**

* Inter-bank borrowings in India and from abroad, external and commercial borrowings of banks.