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BANKING

Banks to formulate Own Cheque Collection Policy

The Reserve Bank has advised all scheduled commercial banks to formulate a comprehensive and transparent policy covering issues relating to (i) immediate credit of local/outstation cheques (ii) time frame for collection of local/outstation cheques and (iii) interest payment for delayed collection. Consequently, the Reserve Bank's earlier instructions in this regard now stand withdrawn.

While framing their cheque collection policy, banks have been advised to -

- Take into account their technological capabilities, systems and processes adopted for clearing arrangements and other internal arrangements for collection through correspondents.
- Review their existing arrangements and capabilities and work out a scheme for reduction in collection period.
- Take adequate care to ensure that the interests of the small depositors are fully protected.
- Ensure that the policy is integrated with their deposit policy formulated in line with the Indian Banks' Association's (IBA's) model deposit policy.
- Lay down their liability by way of interest payments due to delays for non-compliance with the standards set by them. Compensation by way of interest payment, where necessary, should be made without any claim from the customer.

Banks should place the policy before their Board alongwith the Reserve Bank's instructions in this regard and the Board's specific approval should be obtained on the reasonableness of the policy.

Banks should give wide publicity to the policy by placing it on the web-site and also displaying it on the notice board in their branches. Banks should clearly apprise their customers of the assurances on the services on these aspects at the time of establishment of the initial relationship be it as a depositor, borrower or otherwise. Further, banks should also take necessary steps to keep the customers duly informed of the changes in the policy formulated by them from time to time.

Banks have been further advised that the Reserve Bank and the Banking Ombudsman would continue to exercise the

prerogative to examine any dispute which may arise between a bank and any of its customer, vis-à-vis their published policies and procedures.

Interest on FCNR (B) Deposits on Monthly Basis

To bring consistency in the procedure of fixing interest rates on non-resident (external) rupee (NRE) and foreign currency non-resident (banks) FCNR (B) deposits, banks have been advised to fix the interest rates on FCNR (B) deposits on the basis of LIBOR/SWAP rates as prevailing on the last working day of the preceding month, effective from November 1, 2004. The ceiling on interest rates would, however, continue to be the LIBOR/SWAP rate minus 25 basis points, as hitherto, except in the case of Yen deposits, where banks have the freedom to set the FCNR (B) deposit rates which may be equal to or less than the LIBOR.

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Mid-term Review of the Annual

Domestic Developments

- GDP growth projection for 2004-05 placed in the range of 6.0-6.5 per cent as against the earlier expectation of 6.5-7.0 per cent.
- Annual inflation, as measured by point-to-point variations in the wholesale price index, rose from 4.6 per cent at end-March to 8.3 per cent in end-August but has since come down to 7.1 per cent by October 9, 2004.
- The point-to-point inflation rate based on WPI for the year 2004-05 is projected at around 6.5 per cent for policy purposes as against of 5.0 per cent projected earlier.
- Money supply (M_3) growth in this fiscal year (up to October 1, 2004) lower at 5.4 per cent as compared with 7.8 per cent in the previous year.
- Projected expansion of money supply (M_3) for 2004-05 retained at 14.0 per cent.
- A robust increase in non-food credit by 11.5 per cent in this fiscal year (up to October 1, 2004) as compared with an increase of 6.0 per cent in the previous year.
- The Central Government has completed gross market borrowings of Rs.75,044 crore in the fiscal year (up to October 21, 2004), which is 49.8 per cent of the budgetary amount.
- The Central Government has completed net market borrowings of 29.0 per cent of the budgeted amount up to October 21, 2004.
- The market borrowing programme in the remaining part of the year needs to be calibrated carefully in view of strong credit demand.
- Financial markets have remained generally stable though the government securities market tended to show some nervousness in recent months.
- The market interest rates have displayed some upward movement, particularly at the longer end.
- Banks advised to prepare themselves to implement the capital charge for market risk as envisaged under Basel II norms in a phased manner by end-March 2006.

External Developments

- Although global economic recovery is gaining strength, there is some increase in downside risk primarily on account of persistence of uptrend in global oil prices.
- The exchange rate of the rupee depreciated vis-à-vis US dollar, Euro, Pound sterling and Japanese yen by October 21, 2004.
- Foreign exchange reserves increased by US \$ 7.6 billion from US \$ 113.0 billion at end-March 2004 to US \$ 120.6 billion as on October 21, 2004.
- India's exports during April-September 2004 increased by 24.4 per cent in US dollar terms, while imports rose faster by 34.3 per cent. The higher trade deficit reflects high oil imports bill as also the growth in overall import demand.
- The current account remained in surplus consecutively over the past three years, the current account in the first quarter of 2004-05 also posting a surplus of US \$ 1.9 billion.

Overall Assessment

- The pick-up in investment activity and significant growth in non-food credit appear to be broad based and are not temporary phenomena.

- As the magnitude and persistence of supply shock was partly unanticipated, demand management seems to invite closer attention, particularly for stabilising inflationary expectations in a credible manner.
- While the Reserve Bank will continue to pursue stability, the markets should be prepared for the uncertainties.
- Challenges for the rest of the year would broadly remain the same as in the first half of the year with equal weight being given to maintaining growth momentum and stabilizing inflationary expectations.

Stance

- The overall stance of monetary policy for 2004-05 will be provision of appropriate liquidity to meet credit growth and support investment and export demand in the economy, while placing equal emphasis on price stability.
- RBI to pursue an interest rate environment that is conducive to macroeconomic and price stability, and maintaining the momentum of growth.
- RBI to consider measures in a calibrated manner, in response to evolving circumstances with a view to stabilising inflationary expectations.

Reforms and Measures

- Bank Rate kept unchanged at 6.0 per cent.
- Repo Rate increased by 25 basis points to 4.75 per cent.
- Revised liquidity adjustment facility to operate with overnight fixed rate repo and reverse repo (circular issued).
- Ceiling on interest rates on NRE deposits raised by 50 basis points over US dollar LIBOR/SWAP rates of corresponding maturities (circular issued).
- Ceiling on interest rates on FCNR(B) deposits to be fixed on monthly basis (circular issued).
- Minimum tenor of retail domestic term deposits reduced to 7 days (circular issued).
- Limit on advances under priority sector enhanced for improving credit delivery to the agriculture sector (circular issued).
- Restrictive provisions of service area approach to be dispensed with except for government sponsored programme.
- Banks to increase their disbursements to small and marginal farmers under special agricultural credit plans (SACP) by March 2007 (circular issued).
- Private sector banks urged to formulate SACP's from the year 2005-06, targeting an annual growth rate of at least 20-25 per cent (circular issued).
- Composite loan limit for SSI entrepreneurs enhanced from Rs.50 lakh to Rs.1 crore (circular issued).
- Banks' Investment in securitised assets pertaining to SSI sector to be treated under priority sector (circular issued).
- Banks may now extend direct finance to housing sector up to Rs.15 lakh under priority sector lending (circular issued).
- Banks may finance distressed urban poor to prepay their debt to non-institutional lenders (circular issued).
- IBA to look into the suggestions made by NCAER for the kisan credit card scheme and take remedial action.

Policy for 2004-05 - Highlights

- RIDF X established with a corpus of Rs.8,000 crore (as announced in the Union Budget for 2004-05).
- Report of the Special Group on Debt Restructuring Mechanism for Medium Enterprises to be placed in public domain (Report placed on website on November 9, 2004).
- RBI has constituted Empowered Committees to focus on operational issues related to better functioning of regional rural banks and to provide clarifications on regulatory issues.
- Report of the Task Force for reviving rural co-operative banking institutions expected shortly.
- Banks urged to keep up the momentum of lending to agriculture.
- Bank finance to NBFCs for second hand assets (circular issued).
- Many banks announced gold card scheme for exporters.
- Report of Working Group on Credit Enhancement by State Governments expected shortly.
- Further move towards pure inter-bank call/notice money market.
- The minimum maturity period of CP reduced to 7 days (circular issued).
- IPAs to report issuance of CP on the NDS platform by the end of the day.
- Group to suggest rationalisation and standardisation of processing, settlement and documentation of CP issuance.
- Automated value-free transfer of securities between market participants and the CCIL facilitated.
- The Report of the Group on Negotiated Dealing System (NDS) to be placed in the public domain (Report placed on website on November 4, 2004).
- Capital Indexed Bonds to be introduced during the year 2005-06 in consultation with the Government.
- The Report of the Working Group on Primary Dealers to be placed before the TAC.
- Settlement of OTC Derivatives through CCIL expected to be operationalised by March 2005.
- Group on Corporate Debt expected to submit its Report in January 2005.
- The ceiling on MSS raised from Rs.60,000 to Rs.80,000 crore.
- A study Group to be constituted for strengthening OMO framework.
- Guarantee by ADs for trade credit liberalised (circular issued).
- Time limit for export realisation relaxed for EOUs (circular issued).
- Booking of forward contracts by exporters/importers relaxed (circular issued).
- An internal Group on forex market constituted.
- RBI to undertake fresh survey on impact of trade related measures.
- RBI to prepare draft guidelines for implementation of Basel II norms and place them in the public domain.
- A second Draft Guidelines on Ownership and Governance to be put in public domain soon.
- Necessary instructions on "Fit and Proper" criteria issued to private sector banks.
- All cases of penalty imposed by RBI as also strictures/directions arising out of inspection to be placed in the public domain (circular issued).
- Temporary risk containment measures prescribed on housing and consumer loans.
- Banks to comply with prudential guidelines on non-SLR securities.
- Prudential norms for classification of doubtful assets for FIs announced (circular issued).
- Approaches for supervision of DFIs and large NBFCs proposed.
- Dissemination of credit information by CIBIL for improving asset quality of banks (circular issued).
- To constitute a Working Group on conflicts of interest in the Indian financial services sector.
- A vision document for the future role of UCBs to be evolved.
- The Standing Advisory Committee on UCBs chaired by Deputy Governor, RBI would meet on a quarterly basis in future.
- Detailed guidelines on road map for RNBCs would be issued.
- Non-banking finance companies encouraged to consider phasing out their public deposits consistent with international practice.
- Enhancement of capital base for asset reconstruction companies to 15 per cent of assets acquired or Rs. 100 crore, whichever is less.
- The Report of the Technical Group on Refinancing Institutions is expected by December 2004.
- The first lot of the data series under CDBMS to be released on November 1, 2004. (Data can now be accessed on RBI website through Data Base on Indian Economy).
- The draft vision document on Payment and Settlement System be placed in the public domain for feedback and discussions.
- The draft regulation to set up the Board for Payment and Settlement Systems submitted to the Government for notification in the Gazette.
- The national settlement system is expected to be operationalised in early 2005.
- The Working Group on Risk Mitigation for Indian Retail Payment System to submit its Report by November 2004.
- Existing per transaction limits for ECS and EFT being dispensed with effective November 1, 2004.
- Working Group for Regulatory Mechanism for Cards to be constituted.
- CBDT to grant refunds up to Rs.25,000 through Electronic Clearing System (ECS) facility at select centres.
- A High Powered Committee constituted for streamlining the systems and procedures for transmission of data on excise duty and service tax.
- A revised draft report on International Financial Standards and Codes is being placed in the public domain.

Interest Rate Ceiling on NRE Deposits raised

It has been decided that until further notice, the interest rates on NRE deposits for one to three years maturity contracted with effect from November 1, 2004 should not exceed the LIBOR/SWAP rates, as on the last working day of the previous month, for US dollar of corresponding maturity plus 50 basis points. The revised interest rates for three year deposits would also be applicable in case the maturity period exceeds three years and to NRE deposits renewed after their present maturity period.

Minimum Tenor of Domestic/NRO Term Deposits reduced

In order to provide uniformity in the tenor of term deposits, banks have been permitted to reduce the minimum tenor of domestic/ordinary non-resident (NRO) term deposits, even those below Rs.15 lakh, from 15 days to 7 days. Banks would, however, continue to have the freedom to offer differential rates of interest on term deposits of Rs.15 lakh and above. The revised instructions are effective from November 1, 2004.

Earlier, banks could accept term deposits of Rs.15 lakh and above for a minimum maturity period of 7 days. In the case of term deposits of less than Rs.15 lakh, the minimum maturity period was 15 days.

Time Limit For Export Realisation relaxed

Units set up in electronics hardware technology parks (EHTPs), software technology parks (STPs) and bio-technology parks (BTPs) and 100 per cent export oriented units (EOUs) are now allowed to realise and repatriate the full value of export proceeds within a period of twelve months from the date of export. This relaxation would be available for exports made on or after September 1, 2004. The existing guidelines regarding crediting 100 per cent of the foreign exchange earnings to the exchange earners' foreign currency (EEFC) account would, however, continue.

Minimum Maturity Period of CPs reduced

With a view to providing an option to issuers to raise short-term resources through commercial paper (CP) as also an avenue to investors to invest in quality short-term papers, the minimum maturity period of CP has been reduced from 15 days to 7 days with immediate effect.

Bank Finance for Second Hand Assets

The Reserve Bank has advised banks that they may extend finance to non-banking finance companies (NBFCs) against second hand assets financed by them. Banks may also extend financial assistance to customers directly for purchase of second hand assets.

Banks have been further advised to formulate suitable loan policies with their board of directors' approval to finance second hand assets, both directly and through NBFCs.

Earlier, banks were precluded from granting finance against existing assets whether by way of term loans for purchase of such assets or by way of finance to leasing companies for purchase and re-lease of such assets.

Financing of Distressed Urban Poor

With a view to bringing in the urban poor into the formal financial system, it has been decided that banks may advance loans to distressed urban poor to prepay their debt to non-institutional lenders, against appropriate collateral or group security. Banks may formulate suitable guidelines in this regard with their board of directors' approval. Urban poor in this case would include families in the urban areas who are below the poverty line.

Further, banks may classify such loans to the urban poor, as loans to weaker sections, within the priority sector. Such loans may, however, be reported under a separate sub-head, "loans to urban poor indebted to non-institutional lenders" under the broad head "other priority sector" in the returns submitted to the Reserve Bank.

Composite Loan Limits for SSIs enhanced

In order to facilitate smooth flow of credit to small scale industries (SSIs), the composite loan limit for SSI entrepreneurs has been enhanced from Rs.50 lakh to Rs.1 crore.

Banks' Investments in Securitised SSI Assets under Priority Sector

To encourage securitisation of loans to SSI sector, banks' investments in securitised assets representing direct lending to the SSI sector, would now be treated as their direct lending to SSI sector under priority sector, provided -

- the pooled assets represent direct loans to SSI sector which are reckoned under priority sector; and
- the securitised loans are originated by banks/financial institutions.

Housing Loan Ceiling Under Priority Sector enhanced

In order to further improve flow of credit to the housing sector, banks may, with the approval of their boards, extend direct finance to housing sector up to Rs. 15 lakh irrespective of location, as part of their priority sector lending.

Lending to Small and Marginal Farmers

Banks have been advised to make efforts to increase their disbursements to small and marginal farmers to 40 per cent of their direct advances under special agricultural credit plans (SACP) by March 2007. Banks have also been advised to separately furnish data in respect of their lending to small and marginal farmers in the half-yearly statements on disbursements under SACP.

Lending for Agricultural Machinery and Distribution of Inputs

With a view to further improving credit delivery to the agriculture sector, it has been decided to increase the limit on advances under priority sector for dealers in agricultural machinery including drip/sprinkler irrigation systems from Rs. 20 lakh to Rs.30 lakh and for distribution of inputs for allied activities from Rs.25 lakh to Rs.40 lakh.