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MONETARY AND CREDIT INFORMATION REVIEW

FLOOD RELIEF

Banks to Provide Relief to Flood Affected

The Reserve Bank has advised banks to liberally extend its relief package for the state of Maharashtra which witnessed unprecedented rains leading to floods and destruction of life and property. Bank branches have been directed to initiate the package of measures immediately after the district/state authorities declare the district/state as calamity affected area. Banks have been advised to provide financial assistance to agriculturists, small scale industrial units, artisans, small businesses and trading establishments affected by the calamity. Banks have also been advised to provide financial assistance for repairs/reconstruction of dwelling units and also to small road transport operators including taxi, auto rickshaw operators affected by the calamity, keeping in view the viability of the proposals.

The measures include consumption loans to persons affected by calamities for sustenance, waiver of margin requirements or considering as margin the grants, subsidies provided by state governments, provision of credit not only to existing borrowers but also to other eligible persons as also conversion and rescheduling/restructuring of existing loans. The package also includes providing to affected persons term loans for developmental purposes. Further, banks while using their discretion on charging of interest are required to view such cases sympathetically and consider waiving of penal interest to be charged for default of current dues and deferment of compounding of interest. Banks have also been advised to increase the limit of consumption loan to be provided to the affected persons in the State up to Rs 5,000 without any collateral. The limit may be enhanced to Rs.10,000 at the discretion of the branch manager, depending on the repaying capacity of the borrower. Further, banks have been asked to expeditiously restore banking services in the affected areas.

The Reserve Bank has asked the convenor bank for the state of Maharashtra to immediately convene a special state level bankers' committee (SLBC) meeting to discuss the situation and to consider and recommend any special measures that might be required to be taken in the affected areas in addition to the Reserve Bank's relief package.

Opening of Bank Accounts for Flood Affected Persons

The state government has arranged to issue cheques ranging from Rs.50,000 to Rs.2 lakh to persons affected by unprecedented floods in Maharashtra. These persons may or may not be having bank accounts and would need to quickly open bank accounts. The Reserve Bank has, therefore, advised banks to observe minimum formalities for enabling such persons to open a bank account quickly. The accounts may be opened with –

(a) introduction from another account holder, or

(b) documents of identity, such as, voter's identity card or a driving licence, identity card issued by an office, company, school, college, etc., along with a document indicating the address, such as, electricity bill, ration card etc., or

(c) introduction by two neighbours who have the documents as indicated above, or

(d) in the absence of the above, any other evidence to the bank's satisfaction.

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POLICY

Risk Weights on Banks' Exposures

The Reserve Bank has decided to increase the risk weights on banks' exposures as indicated below :

Commercial Real Estate

The risk weight for all outstanding commercial real estate exposure of banks has been increased from 100 per cent to 125 per cent and would be applicable on an on-going basis.

Commercial real estate exposure is defined as (a) fund based and non-fund based exposures secured by mortgages on commercial real estates (office buildings, retail space, multi-purpose commercial premises, multi-family residential buildings, multi-tenanted commercial premises, industrial or warehouse space, hotels, land acquisition, development and construction, etc.) and (b) investments in mortgage backed securities (MBS) and other securitised exposures backed by exposures as at (a) above.

Capital Market Exposure

The risk weight for credit risk on capital market exposures has been increased from 100 per cent to 125 per cent with immediate effect. Capital market exposures cover the following -

(a) direct investment by a bank in equity shares, convertible bonds and debentures and units of equity oriented mutual funds,

(b) advances against shares to individuals for investment in equity shares (including initial public offerings (IPOs)/ employee stock options (ESOPs), bonds and debentures, units of equity oriented mutual funds, etc. and

(c) secured and unsecured advances to stock brokers and guarantees issued on behalf of stock brokers and market makers.

Non-SLR Investments of Banks

State and district central co-operative banks have now been permitted to invest their genuine surplus funds in non-SLR securities without taking the Reserve Bank's prior approval on a case-to-case basis provided -

(i) the non-overdue cover (NODC) discipline stipulated by National Bank for Agriculture and Rural Development (NABARD) is complied with;

(ii) all legitimate credit needs of the co-operatives in the state/ district have been fully met;

(iii) there has been no default in repayment of dues to NABARD;

(iv) the stipulated CRR and SLR are maintained;

(v) the State Act has a provision for the proposed investment and the Registrar of Co-operative Societies has no objection to banks making such an investment;

(vi) section 11(1) of the Banking Regulation (BR) Act, 1949 (AACS) is complied with; and

(vii) the bank has not been placed under Directions under Section 35 A of the B.R.Act, 1949 (AACS)

(viii) the bank has not been issued a show cause notice under any Section of the B.R.Act, 1949 (AACS).

Banks which do not comply with the above conditions, should obtain the Reserve Bank's prior approval for non-SLR investment on a case-to-case basis as hitherto.

Banks' total investment in non-SLR securities, viz., bonds of public sector undertakings (PSUs) and bonds/equity of all India financial institutions (AFIs) should, however, not exceed 10 per cent of their total deposits as on March 31 of the previous year, with a sub-ceiling of 5 per cent for investments in bonds of PSUs.

Stepping up Credit to Small and Medium Enterprises

The Hon'ble Finance Minister, Government of India has announced certain measures for stepping up credit to small and medium enterprises. Accordingly, banks have been advised to take action as under:

Presently, a small scale industrial (SSI) unit is an industrial undertaking in which investment in plant and machinery, does not exceed Rs.1 crore, except in respect of certain specified items, viz., hosiery, hand tools, drugs and pharmaceuticals, stationery items and sports goods where this investment limit has been enhanced to Rs.5 crore. A comprehensive legislation which would enable the paradigm shift from small scale industry to small and medium enterprises is under consideration of the Parliament. Pending enactment of this legislation, the current definition of SSI/tiny industries would continue. Units with investment in plant and machinery in excess of the SSI limit and up to Rs.10 crore should be treated as medium enterprises (ME). Only SSI financing would be included in priority sector.

Measures for improving Credit Flow

- Banks should fix self-targets for financing the small and medium enterprises (SME) sector so as to reflect a higher disbursement over the immediately preceding year, while the sub-targets for financing tiny units and smaller units to the extent of 40 per cent and 20 per cent respectively, would continue.

- Banks should initiate necessary steps to rationalise the cost of loans to the SME sector by adopting a transparent rating system with cost of credit being linked to the credit rating of the enterprise. The Small Industries Development Bank of India (SIDBI) has developed a Credit Appraisal and Rating Tool (CART) as well as a Risk Assessment Model (RAM) and a comprehensive rating model for risk assessment of proposals for SMEs. Banks should consider taking advantage of these models to reduce their transaction costs. The National Small Industries Corporation has recently introduced a credit rating scheme for encouraging SSI units to get themselves credit rated by reputed credit rating agencies. Banks should consider these ratings and wherever appropriate, structure their interest rates depending on the ratings assigned to the borrowing SME units.

- Banks, including regional rural banks, should make concerted efforts to provide credit cover on an average to at least 5 new small/medium enterprises at each of their semi- urban/urban branches per year.

- Banks' boards should formulate a comprehensive and liberal policy for loans to the SME sector based on the Reserve Bank's Master Circular on Lending to SSI Sector dated July 1, 2005. Till such a policy is formulated, the Reserve Bank's current instructions would be applicable to advances granted/to be granted by banks to SME units.
- Cluster based approach for financing SME sector offers possibilities of reduction in transaction costs, mitigation of risk and also provides an appropriate scale for improvement in infrastructure. Banks should adopt the cluster based approach for financing the SME sector. SIDBI in association with the Indian Banks' Association (IBA) is initiating necessary steps to collect and pool common data on risks in each identified cluster and will develop an IT-enabled application, appraisal and monitoring system for small (including tiny) enterprises. SIDBI has also initiated the process of establishing small enterprises financial centres (SEFCs) in select clusters. The risk profile of each cluster would be studied by a professional credit rating agency and would be made available to commercial banks. Each lead bank of a district should consider adoption of at least one cluster.
- A debt restructuring mechanism for nursing sick units in the SME sector and a one time settlement (OTS) scheme for small scale non-performing accounts as on March 31, 2004 are being introduced.

Monitoring/Review

- The existing institutional arrangements for review of credit to the SSI sector like the Reserve Bank's Standing Advisory Committee and cells at banks' head offices as also at important regional centres would periodically review flow of credit to SME, including the tiny sector.
- The Reserve Bank is constituting empowered committees at the regional offices with Regional Director of the Reserve Bank as the Chairman to review the progress in SME financing and rehabilitation of sick SSI and medium enterprise units. The committees would also co-ordinate with other banks/financial institutions and the state government in removing bottlenecks, if any, to ensure smooth flow of credit to the sector. These regional level committees would decide the need to have similar committees at cluster/district levels.

Banks should ensure specialised SME branches in identified clusters/centres with preponderance of medium enterprises to enable SME entrepreneurs to have easy access to bank credit and to equip bank personnel to develop requisite expertise. The existing specialised SSI branches should also be re-designated as SME branches. Though the core competence would be utilised for extending finance and other services to the SME sector, they would have operational flexibility to extend finance/ render other services to other sectors/borrowers.

For wider dissemination and easy accessibility, the policy guidelines formulated by banks' boards as well as instructions/ guidelines issued by the Reserve Bank should be displayed by banks and SIDBI on their respective web sites. Banks should also prominently display all the facilities/schemes offered by them to small entrepreneurs at each of their branches.

BANKING

KYC Procedure for Low Income Group Relaxed

With a view to enabling persons belonging to the low income group to have access to banking services, it has been decided to further simplify the 'know your customer' (KYC) procedure. The flexibility in procedure for opening accounts would, however, be applicable to those persons who intend to keep balances not exceeding Rs. 50,000 in all their accounts taken together and the total credit in all the accounts taken together is not expected to exceed Rs. one lakh in a year.

The Reserve Bank has advised that if persons desirous of opening an account are not able to produce documents in proof of identity and address, banks may open the account by adopting the procedure indicated below -

a) obtain introduction from another account holder who has been subjected to full KYC procedure. The introducer's account with the bank should be at least six months' old and should show satisfactory transactions. The introducer should certify the photograph and address of the customer who proposes to open the account; or

b) obtain any other evidence relating to the identity and address of the customer to the bank's satisfaction.

While opening such accounts, banks should make the customer aware that if at any point of time, the balances in all his/her accounts with the bank (taken together) exceed Rs. 50,000 or total credit in the account exceeds Rs. one lakh, no further transactions would be permitted until the full KYC procedure is completed. When the balance reaches Rs. 40,000 or the total credit in a year reaches Rs. 80,000, banks should notify the customer that appropriate documents for conducting the KYC must be submitted otherwise the operations in the account would be stopped when the total balance in all the accounts taken together exceeds Rs. 50,000 or the total credit in the accounts exceeds Rs. one lakh in a year.

Banks have also been advised that accounts opened with reduced KYC standards in respect of persons affected by floods, to enable them to credit the grant received from the government, should be treated at par with the accounts opened as indicated above. The maximum balance in such accounts should, however, be permitted up to the amount of grant received from the government or Rs. 50,000, whichever is more. The initial credit of the grant amount should not be counted towards the total credit.

It may be recalled that in November 2004, banks were advised to formulate a customer acceptance policy and customer identification procedure to be followed while opening an account. Banks were also advised to categorize customers into low, medium and high risk, according to risk perceived. The KYC guidelines also require banks to verify the identity and address of the customer through documents. It was brought to the notice of the Reserve Bank that, although flexibility in the requirement of documents of identity and proof of address has been provided for, yet a large number of persons, especially, those belonging to the low income group, both in urban and rural areas, are not able to produce such documents to the satisfaction of banks.

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FEMA

External Commercial Borrowings

Keeping in view the current macroeconomic situation, the experience gained by the Reserve Bank in administering the external commercial borrowings (ECB) policy and requests received from certain sectors, the ECB guidelines have been reviewed.

Accordingly, the ECB policy has been liberalised/modified as indicated below -

- ECB with minimum average maturity of 5 years by non-banking financial companies (NBFCs) from multilateral financial institutions, reputed regional financial institutions, official export credit agencies and international banks to finance import of infrastructure equipment for leasing to infrastructure projects would be considered by the Reserve Bank under the approval route.
- Foreign currency convertible bonds (FCCBs) by housing finance companies satisfying specific criteria would be considered by the Reserve Bank under the approval route.
- Minimum holding of equity by the foreign equity holder in the borrower's company (which would qualify the foreign equity holder as a recognised lender for ECB) has been clarified.
- Authorised dealers (ADs) may allow pre-payment of ECB up to USD 200 million without the Reserve Bank's prior approval, subject to compliance of applicable minimum average maturity period for the loan. Pre-payment of ECB for amounts exceeding USD 200 million would be considered by the Reserve Bank under the approval route.
- Applications for credit enhancement of domestic rupee denominated structured obligations by international banks/ international financial institutions/joint venture partners, would henceforth be considered by the Reserve Bank under the approval route. Earlier, such permissions were granted by the Government of India

The amended ECB policy would come into force with immediate effect and is subject to review.

Foreign Direct Investment

The Government of India has decided to permit foreign direct investment (FDI) in certain sectors as indicated below -

Print Media

FDI and portfolio investment is permitted within the composite ceiling of 26 per cent of the paid-up capital of an Indian company publishing newspapers and periodicals dealing with news and current affairs. The Indian company accepting FDI would, however, have to comply with the Ministry of Information and Broadcasting's guidelines issued on July 13, 2005. The guidelines are available on the Ministry's website at http://mib.nic.in/informationb/CODES/FDI2130705.htm .

Accordingly, the Reserve Bank has withdrawn the earlier prohibition placed on foreign institutional investors (FIIs), non-resident Indians (NRIs) and foreign venture capital investors (FVCIs) from purchasing shares of an Indian company engaged in print media sector.

Construction Development

FDI up to 100 per cent under the automatic route, has been permitted in townships, housing, built-up infrastructure and construction development projects (which would include, but not be restricted to, housing, commercial premises, hotels, resorts, hospitals, educational institutions, recreational facilities, city and regional level infrastructure).

Petroleum Sector

FDI up to 100 per cent has been permitted under the automatic route in petroleum product marketing, oil exploration in both small and medium sized fields and petroleum product pipelines.

Air Transport Services

FDI up to 100 per cent has been permitted under the automatic route in air transport services (domestic airlines) by non-resident Indians (NRIs) and up to 49 per cent by others. Direct or indirect equity participation by foreign airlines would, however, not be allowed.

Foreign Nationals on Indian Companies' Board

It has been clarified that, under the Foreign Exchange Management Act, 1999, appointment of a foreign national as a director on the board of directors of an Indian company does not require the Reserve Bank's approval.

The Reserve Bank has also clarified that general powers have been granted to Indian companies to make payment in rupees towards sitting fees, commission, remuneration and travel expenses to and from and within India to its non-whole time director who is resident outside India and is on a visit to India for the company's work.

FCNR (B) Deposits

Based on a review of the recommendations made by the Technical Committee on Forex markets and feed back received, it has been decided to allow banks to accept foreign currency non-resident (bank) {FCNR (B)} deposits denominated in Canadian dollars and Australian dollars in addition to the existing four currencies viz., US dollar, Pound Sterling, Euro and Yen. Banks would also be allowed to accept FCNR (B) deposits up to a maximum maturity period of five years.

All other terms and conditions applicable to the FCNR (B) deposit scheme would remain unchanged.

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