Table V.19: Range of Deposits held by Non-Banking Financial Companies

(Amount in Rs. crore)

Deposit range	As at end-March					
	No. of NBFCs			Amount of deposits		
	2003	2004	2005	2003	2004	2005
1	2	3	4	5	6	7
1. Less than Rs.0.5 crore	491	428	287	65 (1.3)	53 (1.2)	37 (1.0)
2. More than Rs.0.5 crore and up to Rs.2 crore	233	210	168	225 (4.5)	206 (4.8)	164 (4.5)
3. More than Rs.2 crore and up to Rs.10 crore	90	82	70	360 (7.1)	352 (8.2)	320 (8.8)
4. More than Rs.10 crore and up to Rs.20 crore	21	18	16	284 (5.6)	242 (5.6)	250 (6.9)
5. More than Rs.20 crore and up to Rs.50 crore	12	17	14	364 (7.2)	569 (13.2)	507 (13.9)
6. Rs.50 crore and above	23	19	15	3,737 (74.3)	2,895 (67.0)	2,368 (64.9)
Total	**870**	**774**	**570**	**5,035 (100.0)**	**4,317 (100.0)**	**3,646 (100.0)**

Note: Figures in parentheses are percentages to total deposit.

'more than Rs.20 crore and up to Rs.50 crore', which increased sharply during 2003-04. Fifteen companies in the deposit size of 'Rs.50 crore and above' held 64.9 per cent of total public deposits held by all NBFCs at end-March 2005. Twenty nine NBFCs with deposit size of 'Rs.20 crore and above', held more than 78.8 per cent of total deposits, while remaining 541 companies held little more than 21.2 per cent of total public deposits (Table V.19).

Region-wise Composition of Deposits held by NBFCs

5.58 Deposits held by NBFCs across all the regions declined during 2003-04 and 2004-05. The Southern region accounted for the largest share of deposits (75.9 per cent) held by NBFCs at end-March 2005, followed distantly by other regions. This was on account of largest share of deposits (71.1 per cent) held by Chennai (Table V.20).

Table V.20: Public Deposits held by Registered and Unregistered NBFCs - Region-wise

(Amount in Rs. crore)

Region	2002-03		2003-04		2004-05	
	No. of NBFCs	Amount	No. of NBFCs	Amount	No. of NBFCs	Amount
1	2	3	4	5	6	7
Northern	271	543 (10.8)	248	442 (10.2)	195	351 (9.6)
North-Eastern	1	2 (0.0)	1	1 (0.0)	–	–
Eastern	18	212 (4.2)	17	204 (4.7)	13	158 (4.3)
Central	82	112 (2.2)	75	101 (2.3)	66	92 (2.5)
Western	63	687 (13.6)	41	365 (8.5)	27	280 (7.7)
Southern	435	3,479 (69.1)	392	3,205 (74.2)	269	2,765 (75.9)
Total	**870**	**5,035**	**774**	**4,318**	**570**	**3,646**
Metropolitan cities:						
Mumbai	45	672	23	351	14	268
Chennai	318	3,162	304	2,879	217	2,591
Kolkata	15	203	14	187	11	158
New Delhi	108	443	98	345	71	266
Total	**486**	**4,480**	**439**	**3,762**	**313**	**3,283**

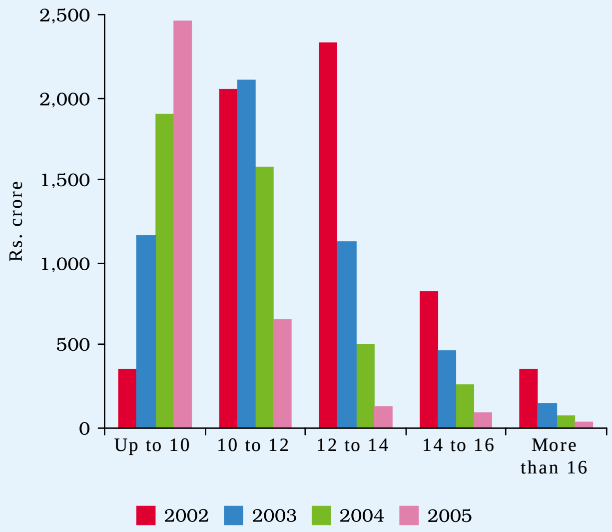
– : Nil/Negligible.
Note: Figures in parentheses are percentages to total.

Interest Rate and Maturity Pattern of Public Deposits with NBFCs

5.59 Deposits contracted by NBFCs at interest rates up to 10 per cent increased sharply during the year ended March 2004 as well as March 2005, while deposits contracted at all other interest rates declined significantly. However, some portion of the deposits accepted by NBFCs was at interest rate of above 14 per cent or even 16 per cent. About 71 per cent of the deposits contracted at end-March 2005 were at interest rate up to 10 per cent (Table V.21).

5.60 In line with the general decline in the interest rate over the years, interest rates paid by NBFCs on deposits have also declined steadily over the years, which was reflected in the increase in the share of deposits contracted at interest rate of up to 10 per cent and decline in the share of deposits accepted at 12 to 14 per cent (Chart V.3).

Chart V.3: Distribution of Interest Rate Paid on Deposits by NBFCs (end-March)



The Maturity Pattern of Public Deposits

5.61 Deposits contracted by NBFCs in all maturity ranges declined significantly during 2003-04 and 2004-05. Deposits in the maturity range of 'more than 2 and up to 3 years' accounted for the largest share (35.5 per cent) at end-March 2005 (Table V.22).

5.62 The spread between the maximum interest rate on public sector bank deposits of 'one to three year' maturity and the interest rate offered by NBFCs on deposits with the same maturity narrowed down over the years (Table V.23).

Borrowings

5.63 The outstanding borrowings by NBFCs, which declined by 14.8 per cent during the year ended March 2004 on account of decline in the borrowings by equipment leasing companies and

Table V.21: Distribution of Public Deposits of NBFCs According to Rate of Interest

(Amount in Rs. crore)

Interest Range	As at end-March		
	2003	2004	2005
1	2	3	4
Up to 10 per cent	1,174 (23.3)	1,896 (43.9)	2,604 (71.4)
More than 10 per cent and up to 12 per cent	2,101 (41.7)	1,586 (36.7)	726 (19.9)
More than 12 per cent and up to 14 per cent	1,137 (22.6)	505 (11.7)	164 (4.5)
More than 14 per cent and up to 16 per cent	475 (9.4)	254 (5.9)	109 (3.0)
16 per cent and above	148 (3.0)	76 (1.8)	43 (1.2)
Total	**5,035 (100.0)**	**4,317 (100.0)**	**3,646 (100.0)**

Note: Figures in parentheses are percentages to total deposits.

Table V.22: Maturity Pattern of Public Deposits held by NBFCs

(Amount in Rs. crore)

Maturity Period @	As at end-March		
	2003	2004	2005
1	2	3	4
Less than 1 year	1,203 (23.9)	1,176 (27.3)	1,145 (31.4)
More than 1 and up to 2 years	1,241 (24.6)	1,046 (24.2)	862 (23.6)
More than 2 and up to 3 years	1,927 (38.3)	1,573 (36.4)	1,295 (35.5)
More than 3 and up to 5 years	619 (12.3)	492 (11.4)	330 (9.0)
5 years and above	45 (0.9)	30 (0.7)	14 (0.4)
Total	**5,035 (100.0)**	**4,317 (100.0)**	**3,646 (100.0)**

@ : On the basis of residual maturity of outstanding deposits.
Note: Figures in parentheses are percentages to total deposits.

Table V.23: Maximum/Ceiling Interest Rates on Banks and NBFC Deposits

(Per cent)

Interest Rate	As at end-March					
	2000	2001	2002	2003	2004	2005
1	2	3	4	5	6	7
1. Maximum interest rate on public sector bank deposits of 1-3 year maturity	10.5	9.5	8.5	6.75	6.75	7.00
2. Ceiling interest rate for NBFCs	16.0	14.0	12.5	11.0	11.0	11.0
3. Spread (2-1)	5.5	4.5	4.0	4.25	4.25	4.00

hire purchase companies, increased marginally during the year ended March 2005. Hire purchase companies continued to account for the largest share (59.6 per cent) of total borrowings by all NBFCs (Table V.24).

5.64 Borrowings by NBFCs from banks and FIs and external sources declined, while those by way of debentures increased during 2003-04 and 2004-05. Borrowings from the Government, which had increased marginally during the year ended March 2004, declined sharply in the following year. Borrowings from the Government relate mostly to one State-owned NBFC operating in the Southern region. Hire purchase companies have been the most active in raising resources from banks/FIs and the debt market. Borrowings from banks and financial institutions by equipment leasing and hire purchase companies, which declined sharply during 2003-04, increased marginally in 2004-05. On the other hand, borrowings by loan companies from banks and FIs after increasing sharply in 2003-04, declined in 2004-05 (Table V.25). Debentures emerged as the most important source of funds for NBFCs during the year ended March 2005, relegating the borrowings from banks and FIs to the second position. Between end-March 2003 and end-March 2005, while the share of borrowings by way of debentures increased from 21.9 per cent to 30.6 per cent, that of borrowings from banks and FIs declined from 36.6 per cent to 27.1 per cent.

Assets of NBFCs

5.65 Advances constitute the main assets of NBFCs. Reflecting the decline in deposits and borrowings, advances extended by all NBFCs declined during the year, barring those by loan companies during the year ended March 2004. While advances by equipment leasing companies and hire

Table V.24: Borrowings by NBFCs –Group-wise

(Amount in Rs. crore)

NBFC Group	As at end-March						Percentage Variation	
	No. of NBFCs			Total Borrowings				
	2003	2004	2005	2003	2004	2005	2003-04	2004-05
1	2	3	4	5	6	7	8	9
Equipment Leasing	58	46	38	6,472 (26.4)	2,811 (13.5)	3,112 (14.2)	-56.6	10.7
Hire Purchase	439	396	316	13,650 (55.8)	12,141 (58.2)	13,008 (59.6)	-11.1	7.1
Investment	19	11	5	1,613 (6.6)	1,718 (8.2)	1,092 (5.0)	6.5	-36.4
Loan	122	87	54	2,600 (10.6)	3,775 (18.1)	3,679 (16.8)	45.2	-2.5
Others	232	234	157	145 (0.6)	407 (2.0)	950 (4.4)	180.7	133.4
Total	**870**	**774**	**570**	**24,480 (100.0)**	**20,852 (100.0)**	**21,841 (100.0)**	**-14.8**	**4.7**

Note: Figures in parentheses are percentages to total borrowings.

Table V.25: Sources of Borrowings of NBFCs

(Amount in Rs. crore)

NBFC Group	As at end-March														
	Government			External			Banks and Financial Institutions			Debentures			Others		
	2003	2004	2005	2003	2004	2005	2003	2004	2005	2003	2004	2005	2003	2004	2005
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16
Equipment Leasing	61	21	–	571	291	190	3,080	1,141	1,252	1,639	893	1219	1,121	465	452
		(-65.6)	(-100.0)		(-49.0)	(-34.7)		(-63.0)	(9.7)		(-45.5)	(36.5)		(-58.5)	(-2.8)
Hire Purchase	85	91	–	124	332	327	5,613	4,114	4,223	2,721	3,919	4,425	5,107	3,684	4,033
		(7.1)	(-100.0)		(167.7)	(-1.5)		(-26.7)	(2.6)		(44.0)	(12.9)		(-27.9)	(9.5)
Investment	1,423	1,467	885	–	–	–	14	14	10	–	42	12	176	196	185
		(3.1)	(-39.7)						(-28.6)		(-)	(-71.4)		(11.4)	(-5.6)
Loan	–	–	86	–	–	–	245	1,132	413	992	1,065	1,037	1,363	1,579	2,142
								(362.0)	(-63.5)		(7.4)	(-2.6)		(15.8)	(35.7)
Others	–	–	–	–	–	–	7	13	31	–	–	–	138	394	920
								(85.7)	(138.5)					(185.5)	(133.5)
Total	**1,570**	**1,579**	**971**	**695**	**623**	**517**	**8,959**	**6,413**	**5,929**	**5,352**	**5,919**	**6,693**	**7,905**	**6,318**	**7,732**
		(0.6)	**(-38.5)**		**(-10.2)**	**(-17.0)**		**(-28.4)**	**(-7.5)**		**(10.6)**	**(13.1)**		**(-20.1)**	**(22.4)**

– : Nil/Negligible.
Note: Figures in parentheses are percentage change over the previous year.

purchase companies increased during the year ended March 2005, those by investment and loan companies declined. Investment by NBFCs also declined during the years ended March 2004 and March 2005, reflecting mainly the impact of decline in investment by two major groups, *i.e.*, equipment leasing and hire purchase companies (Table V.26).

Distribution of NBFCs According to Asset Size

5.66 The asset size of NBFCs varies significantly from less than Rs.25 lakh to above Rs.500 crore. Most of the companies were in the asset range of more than Rs.50 lakh and up to Rs.10 crore. However, bulk of the assets were held by NBFCs in the large asset size. Sixteen companies with asset size of above Rs.500 crore held 79.4 per cent of total assets of all NBFCs as at end-March 2005 (Table V.27).

Distribution of Assets of NBFCs – Type of Activity

5.67 Assets held by NBFCs in loans and inter-corporate deposits, investments, and equipment and

Table V.26: Major Components of Assets of NBFCs – Group-wise

(Amount in Rs. crore)

NBFC Group	As at end-March								
	Assets			Advances			Investment		
	2003	2004	2005	2003	2004	2005	2003	2004	2005
1	2	3	4	5	6	7	8	9	10
Equipment Leasing	7,996	3,744	4,721	7,087	3,020	3,875	1,028	348	331
	(21.2)	(11.4)	(13.9)	(22.8)	(11.3)	(13.9)	(23.7)	(9.1)	(9.4)
Hire Purchase	22,163	19,929	20,039	18,849	17,114	18,312	1,909	1,805	1,202
	(58.8)	(60.8)	(59.2)	(60.7)	(64.1)	(65.8)	(44.0)	(47.3)	(34.3)
Investment	2,208	2,422	1,890	1,520	1,617	1,061	629	750	788
	(5.9)	(7.4)	(5.6)	(4.9)	(6.1)	(3.8)	(14.5)	(19.6)	(22.5)
Loan	4,109	5,485	5,319	2,763	4,208	3,456	527	604	657
	(10.9)	(16.7)	(15.7)	(8.9)	(15.8)	(12.4)	(12.1)	(15.8)	(18.7)
Others	1,233	1,173	1,874	818	745	1,129	245	311	530
	(3.3)	(3.6)	(5.5)	(2.6)	(2.8)	(4.1)	(5.6)	(8.1)	(15.1)
Total	**37,709**	**32,753**	**33,843**	**31,037**	**26,704**	**27,833**	**4,338**	**3,818**	**3,508**
	(100.0)	**(100.0)**	**(100.0)**	**(100.0)**	**(100.0)**	**(100.0)**	**(100.0)**	**(100.0)**	**(100.0)**

Note: Figures in parentheses represent percentage share in total.

Table V.27: Non-Banking Financial Companies According to Asset Size

(Amount in Rs. crore)

Asset size	As at end-March					
	2003	2004	2005	2003	2004	2005
	No. of reporting companies			Assets		
1	2	3	4	5	6	7
1. Less than 0.25	62	59	34	6 (0.0)	6 (0.0)	4 (0.0)
2. More than 0.25 and up to 0.50	77	73	41	28 (0.1)	27 (0.1)	15 (0.1)
3. More than 0.50 and 2	354	317	209	388 (1.0)	352 (1.0)	232 (0.7)
4. More than 2 and up to 10	245	209	164	1,131 (3.0)	964 (2.9)	724 (2.1)
5. More than 10 and up to 50	68	69	71	1,399 (3.7)	1,593 (4.9)	1,765 (5.2)
6. More than 50 and up to 100	19	13	18	1,315 (3.5)	850 (2.6)	1,216 (3.6)
7. More than 100 and up to 500	28	17	17	6,492 (17.2)	3,819 (11.7)	3,007 (8.9)
8. Above 500	17	17	16	26,950 (71.5)	25,143 (76.8)	26,880 (79.4)
Total	**870**	**774**	**570**	**37,709 (100.0)**	**32,754 (100.0)**	**33,843 (100.0)**

Note: Figures in parentheses are percentages to total.

leasing declined during 2003-04 and 2004-05. However, assets in hire purchase, which declined during 2003-04, increased sharply in the following year. As a result, assets held in hire purchase activity accounted for the largest share (42.0 per cent) of total assets of NBFCs, followed by loans, including inter-corporate deposits (33.4 per cent) (Table V.28).

Table V.28: Distribution of Assets of NBFCs - Activity-wise

(Amount in Rs. crore)

Activity	As at end-March			Percentage Variation		
	2003	2004	2005	2002-03	2003-04	2004-05
1	2	3	4	5	6	7
1. Loans and Inter-corporate deposits	13,398 (35.4)	12,363 (37.7)	11,301 (33.4)	-2.3	-7.7	-8.6
2. Investments	4,338 (11.5)	3,818 (11.7)	3,508 (10.4)	0.1	-12.0	-8.1
3. Hire Purchase	13,031 (34.5)	11,649 (35.6)	14,200 (42.0)	-1.3	-10.6	21.9
4. Equipment and Leasing	2,011 (5.3)	1,115 (3.4)	778 (2.3)	-35.4	-44.6	-30.2
5. Bills	450 (1.2)	436 (1.3)	464 (1.4)	-33.1	-3.2	6.4
6. Other assets	4,581 (12.1)	3,375 (10.3)	3,592 (10.6)	-4.6	-26.3	6.4
Total	**37,809 (100.0)**	**32,756 (100.0)**	**33,843 (100.0)**	**-5.3**	**-13.4**	**3.3**

Note: Figures in parentheses are percentages to total.

Financial Performance of NBFCs

5.68 Financial performance of NBFCs improved during 2003-04 and 2004-05 due mainly to containment of expenditure. Both fund-based and fee-based income of NBFCs declined during the year ended March 2004. During 2004-05, fund-based income and fee-based income improved marginally. Financial and operating expenditure declined during 2003-04 and 2004-05, resulting in improvement in the operating profit and net profit. Increase in net profit for the year ended March 2004, to an extent, was also due to decline in tax provisions. Improvement in net profit combined with decline in total assets led to an improvement in the net profit to asset ratio in 2003-04 and further in 2004-05 (Table V.29 and Chart V.4).

Interest Cost to Total Income

5.69 Interest cost as per cent to total income which increased marginally during 2003-04, declined sharply in the following year. Non-interest costs relative to total income declined in both the years. As a result, cost to income ratio declined significantly from 88.3 per cent in 2002-03 to 83.8 per cent in 2003-04 and further to 78.8 per cent during 2004-05 (Table V.30).

Chart V.4: Financial Performance of NBFCs

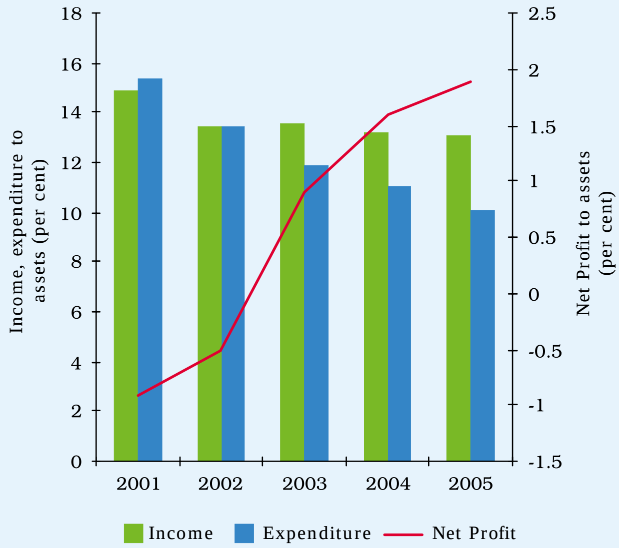


Table V.29: Financial Performance of NBFCs

(Amount in Rs. crore)

Item		2002-03	2003-04	2004-05	Percentage Variation 2002-03	Percentage Variation 2003-04	Percentage Variation 2004-05
1		2	3	4	5	6	7
A.	**Income (i+ii)**	**5,084 (100.0)**	**4,332 (100.0)**	**4,435 (100.0)**	**-5.1**	**-14.8**	**2.4**
	(i) Fund-based	4,709 (92.6)	4,005 (92.5)	4,062 (91.6)	-5.9	-15.0	1.4
	(ii) Fee-based	375 (7.4)	327 (7.5)	373 (8.4)	6.5	-12.8	14.1
B.	**Expenditure (i+ii)**	**4,491 (100.0)**	**3,621 (100.0)**	**3,495 (100.0)**	**-15.6**	**-19.4**	**-3.5**
	(i) Financial	2,757 (61.4)	2,099 (58.0)	2,054 (58.8)	-16.4	-23.9	-2.1
	(ii) Operating	1,734 (38.6)	1,522 (42.0)	1,441 (41.2)	-14.3	-12.2	-5.3
C.	**Tax Provisions**	**254**	**180**	**349**	**2.4**	**-29.1**	**93.9**
D.	**Operating Profit (PBT)**	**593**	**711**	**940**	**1,547.2**	**19.9**	**32.2**
E.	**Net Profit (PAT)**	**339**	**531**	**591**	**-259.9**	**56.6**	**11.3**
F.	**Total Assets**	**37,709**	**32,754**	**33,843**	**-5.3**	**-13.1**	**3.3**
G.	**Financial Ratios***						
	(i) Income	13.5	13.2	13.1			
	(ii) Fund Income	12.5	12.2	12.0			
	(iii) Fee Income	1.0	1.0	1.1			
	(iv) Expenditure	11.9	11.0	10.3			
	(v) Financial Expenditure	7.3	6.4	6.1			
	(vi) Operating Expenditure	2.9	3.1	4.2			
	(vii) Tax Provisions	0.7	0.5	1.0			
	(viii) Net Profit	0.9	1.6	1.7			

* : As percentage to total assets.
Note: Figures in parentheses are percentages share to the respective total.

Table V.30: Interest Cost to Total Income

(Amount in Rs. crore)

Year	Total Income	Total Cost	Interest Cost	Non-Interest Cost
1	2	3	4	5
2002-03	5,084	4,491 (88.3)	974 (19.2)	3,517 (69.2)
2003-04	4,322	3,621 (83.8)	888 (20.5)	2,733 (63.2)
2004-05	4,435	3,495 (78.8)	760 (17.1)	2,735 (61.7)

Note: Figures in parentheses indicate percentage to total income.

Soundness Indicators

Asset Quality of NBFCs

5.70 Gross and net non-performing assets of the reporting NBFCs, as a group, registered a steady decline between end-March 2001 and end-March 2004. While gross NPAs continued to decline during the year ended March 2005, net NPAs increased significantly (Table V.31).

Table V.31: Non-Performing Assets of NBFCs*

(per cent of credit exposure)

End-March	Gross NPAs	Net NPAs
1	2	3
2001	11.5	5.6
2002	10.6	3.9
2003	8.8	2.7
2004	8.2	2.4
2005	7.0	3.4

* : Excluding MBFCs, MBCs and MNBCs.

5.71 Asset quality of different NBFC groups showed a divergent trend. Gross NPAs as a percentage to total assets of equipment leasing companies, hire purchase companies and investment companies increased during 2003-04, but declined during 2004-05. Gross NPAs of loan companies, however, declined in both the years. More or less the same trend was discernable in respect of net NPAs. Investment companies had the lowest gross NPA ratio at end-March 2005 (1.8 per cent), followed by loan companies (3.7 per cent), hire purchase companies (4.6 per cent) and equipment leasing companies (12.3 per cent) (Table V.32).

Table V.32: NPAs of NBFCs - Group-wise

(Amount in Rs. crore)

NBFC Group/ End-March	Gross Advances	Gross NPAs			Net Advances	Net NPAs		
		Amount	Per cent to Gross Advances	Per cent to Assets		Amount	Per cent to Net Advances	Per cent to Assets
1	2	3	4	5	6	7	8	9
Equipment Leasing								
2001	4,118	304	7.4	6.1	3,826	12	0.3	0.2
2002	1,625	646	39.7	28.0	1,330	351	26.3	15.2
2003	5,969	932	15.6	11.1	5,506	469	8.5	5.6
2004	3,306	582	17.6	13.3	3,067	344	11.2	7.8
2005	5,611	718	12.8	12.3	5,310	418	7.9	7.1
Hire Purchase								
2001	8,296	1,324	16.0	12.3	7,604	631	8.3	5.9
2002	6,825	1,167	17.1	14.8	6,068	410	6.8	5.2
2003	16,489	1,288	7.8	6.8	15,305	104	0.7	0.5
2004	10,437	942	9.0	7.3	9,748	253	2.6	2.0
2005	12,812	619	4.8	4.6	12,498	306	2.4	2.3
Investment								
2001	232	53	22.9	5.1	223	45	20.0	4.3
2002	149	2	1.6	0.1	147	1	0.4	0.0
2003	93	11	11.9	2.1	90	8	8.9	1.5
2004	63	15	24.2	2.6	55	7	12.7	1.2
2005	58	10	17.2	1.8	58	10	17.2	1.8
Loan								
2001	7,414	595	8.0	5.9	7,118	299	4.2	3.0
2002	3,986	549	13.8	10.1	3,615	177	4.9	3.3
2003	2,707	144	5.3	4.8	2,503	–	–	–
2004	2,038	142	7.0	4.1	1,833	–	–	–
2005	1,906	83	4.4	3.7	1,780	–	–	–
Others								
2001	1,394	493	35.4	24.2	1,308	407	31.1	20.0
2002	175	9	5.1	3.0	165	–	–	–
2003	294	2	0.6	0.5	294	1	0.5	0.4
2004	–	–	–	–	–	–	–	–
2005	–	–	–	–	–	–	–	–

– : Nil/Negligible.

Table V.33: Classification of Assets of NBFCs – Group-wise

(Amount in Rs. crore)

Item/End of the Period	Standard Asset		Sub-Standard Asset		Doubtful Asset		Loss Asset		Gross NPAs		Total Assets
	Amount	per cent	Amount	per cent	Amount	per cent	Amount	per cent	Amount	per cent	
1	2	3	4	5	6	7	8	9	10	11	12
Equipment Leasing											
Mar-03	5,037	84.4	520	8.7	205	3.4	207	3.5	932	15.6	5,969
Sep-03	2,986	77.9	502	13.1	194	5.1	154	4.0	850	22.1	3,836
Mar-04	2,724	82.4	396	12.0	84	2.5	102	3.1	582	17.6	3,306
Sep-04	3,389	87.2	365	9.4	19	0.5	114	2.9	498	12.8	3,887
Mar-05	4,893	87.2	393	7.0	98	1.7	227	4.1	718	12.8	5,611
Hire Purchase											
Mar-03	15,201	92.2	746	4.5	273	1.7	269	1.6	1,288	7.8	16,489
Sep-03	15,621	92.4	758	4.5	245	1.5	283	1.7	1,286	7.6	16,907
Mar-04	9,495	91.0	613	5.9	103	1.0	226	2.2	942	9.0	10,437
Sep-04	11,420	91.5	730	5.9	118	0.9	213	1.7	1,061	8.5	12,481
Mar-05	12,193	95.2	401	3.1	128	1.0	90	0.7	619	4.8	12,812
Investment											
Mar-03	82	88.1	9	9.3	2	2.4	–	0.2	11	11.9	93
Sep-03	43	80.6	9	16.9	1	2.4	–	0.1	10	19.4	54
Mar-04	48	75.8	–	–	10	15.3	6	8.9	15	24.2	63
Sep-04	71	86.4	1	1.4	10	12.1	–	–	11	13.6	82
Mar-05	48	82.0	1	1.1	10	16.7	–	0.2	10	18.0	58
Loan											
Mar-03	2,563	94.7	37	1.3	20	0.7	88	3.2	145	5.3	2,708
Sep-03	5,693	95.8	81	1.4	59	1.0	112	1.9	252	4.2	5,945
Mar-04	1,896	93.0	40	2.0	20	1.0	82	4.0	142	7.0	2,038
Sep-04	1,697	93.9	28	1.6	9	0.5	73	4.0	110	6.1	1,807
Mar-05	1,823	95.6	14	0.7	41	2.1	28	1.5	83	4.4	1,906
Others											
Mar-03	293	99.4	1	0.4	1	0.2	–	–	2	0.6	295
Sep-03	1	55.0	–	25.9	–	19.0	–	–	1	45.0	2
Mar-04	–	–	–	–	–	–	–	–	–	–	–
Sep-04	–	–	–	–	–	–	–	–	–	–	–
Mar-05	–	–	–	–	–	–	–	–	–	–	–

– : Nil/Negligible.

5.72 Composition of NPAs of NBFC groups also showed divergent trends during 2003-04 and 2004-05. Composition of NPAs of equipment leasing companies, after showing improvement during the year ended March 2004, deteriorated in the following year. Composition of NPAs of hire purchase companies, investment companies and loan companies deteriorated during 2003-04, but improved in the following year (Table V.33).

Capital Adequacy Ratio

5.73 Capital to risk-weighted assets ratio (CRAR) norms were made applicable to NBFCs in 1998, in terms of which every deposit-taking NBFC is required to maintain a minimum capital consisting of Tier-I and Tier-II capital of not less than 12 per cent (15 per cent in the case of unrated deposit-taking loan/investment companies) of its aggregate risk-weighted assets and of risk-adjusted value of off-balance sheet items. Total of Tier-II capital, at any point of time, is required not to exceed 100 per cent of Tier-I capital. The number of NBFCs with CRAR less than 12 per cent, which constituted 6.4 per cent of all NBFCs at end-March 2003, declined to 5.2 per cent at end-March 2004, but increased to 19.8 per cent at end-March 2005. On the other hand, number of NBFCs with more than 20 per cent CRAR increased from 85.3 per cent at end-March 2003 to 89.7 per cent at end-March 2004, but declined sharply to 73.5 per cent at end-March 2005 (Table V.34).

Table V.34: Capital Adequacy Ratio of NBFCs *

Range	As at end-March											
	2003				2004				2005			
	EL	HP	LC/IC	Total	EL	HP	LC/IC	Total	EL	HP	LC/IC	Total
1	2	3	4	5	6	7	8	9	10	11	12	13
Less than 12 per cent	10	17	15	42	5	12	8	25	4	55	5	64
More than 12 and up to 15 per cent	1	8	1	10	1	4	1	6	–	–	1	1
More than 15 and up to 20 per cent	4	32	9	45	2	15	2	19	2	15	4	21
More than 20 and up to 30 per cent	9	54	11	74	6	38	7	51	5	26	1	32
Above 30 per cent	32	334	121	487	28	300	55	383	25	153	28	206
Total	**56**	**445**	**157**	**658**	**42**	**369**	**73**	**484**	**36**	**249**	**39**	**324**

– : Nil/Negligible.
* : Excluding MBFCs, MBCs and MNBCs.
Note : 1. EL - Equipment Leasing.
2. HP - Hire Purchase.
3. LC/IC - Loan Companies /Investment Companies.

Net Owned Fund vis-à-vis Public Deposits of NBFCs

5.74 Net owned fund (NOF) of NBFCs is the aggregate of paid-up capital and free reserves, netted by (i) the amount of accumulated balance of loss, (ii) deferred revenue expenditure and other intangible assets, if any, and adjusted by investments in shares and loans and advances to (a) subsidiaries, (b) companies in the same group and (c) other NBFCs (in excess of 10 per cent of owned fund). Information of NOFs can complement the information on CRAR. The ratio of public deposits to NOF in respect of almost all NBFC groups except loan companies, after increasing marginally during the year ended March 2004, declined during the year ended March 2005 (Table V.35).

5.75 Net owned funds of NBFCs range from less than Rs.25 lakh to over Rs.500 crore. The number of companies in nearly all NOF ranges declined during 2003-04 and 2004-05. NOF of NBFCs, which declined marginally during 2003-04, increased during 2004-05. NBFCs in the NOF range of 'up to Rs.25 lakh' continued to have negative NOF. One NBFC had NOF above Rs.500 crore at end-March 2005 as against two at end-March 2004. The ratio of public deposits to NOF maintained by NBFCs declined from 1.2 at end-March 2003 to 1.1 at end-March 2004 and further to 0.8 per cent at end-March 2005. NBFCs in the NOF range of Rs.100 crore to Rs.500 crore held the largest share (29.3 per cent) of public deposits (Table V.36).

Residuary Non-Banking Companies (RNBCs)

5.76 Three RNBCs were operating in the country at end-March 2004 and end-March 2005 as against five at end-March 2003. Assets of RNBCs

Table V.35: Net Owned Fund *vis-à-vis* Public deposits of NBFCs* – Group-wise

(Amount in Rs. crore)

NBFC Group	Net Owned Fund			Public Deposits			Public Deposits to Net Owned Fund		
	2003	2004	2005	2003	2004	2005	2003	2004	2005
1	2	3	4	5	6	7	8	9	10
Equipment Leasing	154	96	427	511	344	343	3.3	3.6	0.8
Hire Purchase	2,979	2,235	2,597	3,539	2,963	2,315	1.2	1.3	0.9
Investment	553	607	662	125	106	93	0.2	0.2	0.1
Loan	367	893	428	177	178	157	0.5	0.2	0.4
Others	88	265	331	683	727	738	7.8	2.7	2.2
Total	**4,141**	**4,096**	**4,445**	**5,035**	**4,317**	**3,646**	**1.2**	**1.1**	**0.8**

* : Including MBFCs, MBCs and MNBCs.

Table V.36: Range of Net Owned Funds *vis-à-vis* Public Deposits of NBFCs*

(Amount in Rs. crore)

Range of NOF	As at end-March											
	2003				2004				2005			
	No. of reporting companies	Net Owned Funds	Public Deposits	Public Deposits as multiple of NOFs	No. of reporting companies	Net Owned Funds	Public Deposits	Public Deposits as multiple of NOFs	No. of reporting companies	Net Owned Funds	Public Deposits	Public Deposits as multiple of NOFs
1	2	3	4	5	6	7	8	9	10	11	12	13
1. Up to 0.25	208	-1,356	843	–	175	-881	667	–	93	-591	456	–
2. More than 0.25 and up to 2	497	309	369	1.2	451	289	430	1.5	332	228	372	1.6
3. More than 2 and up to 10	110	461	467	1	92	394	384	1	97	428	392	0.9
4. More than 10 and up to 50	30	677	447	0.7	35	683	577	0.8	29	661	470	0.7
5. More than 50 and up to 100	10	639	255	0.4	7	478	204	0.4	6	456	158	0.3
6. More than 100 and up to 500	15	3,411	2,654	0.8	12	2,039	1,342	0.7	12	2,595	1,067	0.4
7. Above 500	–	–	–	–	2	1,094	713	0.7	1	669	731	1.1
Total	**870**	**4,141**	**5,035**	**1.2**	**774**	**4,096**	**4,317**	**1.1**	**570**	**4,446**	**3,646**	**0.8**

– : Nil/Negligible.
* : Including MBFCs, MBCs and MNBCs

declined by 3.5 per cent during the year ended March 2004 and 6.4 per cent during the year ended March 2005. Fixed deposits with banks, bonds/debentures and other fixed income investments, however, increased sharply during 2004-05. Net owned funds of RNBCs increased during 2003-04 and 2004-05.

5.77 Financial performance of RNBCs was lacklustre during 2003-04 and 2004-05. Despite increase in income, their operating profit and net profit declined during 2003-04 due mainly to increase in expenditure. A sharp decline in income of RNBCs during 2004-05 resulted in a further decline in their net profit (Table V.37).

Table V.37: Profile of Residuary Non-Banking Companies (RNBCs)

(Amount in Rs. crore)

Item	As at end-March			Percentage Variation	
	2003	2004	2005	2003-04	2004-05
1	2	3	4	5	6
A. Assets (i to v)	**21,104**	**20,362**	**19,057**	**-3.5**	**-6.4**
(i) Unencumbered approved securities	6,129	5,824	2,037	-5.0	-65.0
(ii) Fixed deposits with banks	1,470	2,033	4,859	38.3	139.0
(iii) Bonds or debentures or commercial papers of Govt. companies/ public sector banks/ public financial institutions/ corporations	6,553	6,048	9,225	-7.7	52.5
(iv) Other investments	912	2,059	1,639	125.8	-20.4
(v) Other Assets	6,040	4,398	1,297	-27.2	-70.5
B. Net Owned Funds	**809**	**1,002**	**1,065**	**23.9**	**6.3**
C. Total Income (i+ii)	**1,801**	**2,055**	**1,532**	**14.1**	**-25.5**
(i) Fund Income	1,801	2,055	1,530	14.1	-25.5
(ii) Fee Income	–	–	2	–	–
D. Total Expenses (i+ii+iii)	**1,435**	**1,813**	**1,396**	**26.3**	**-23.0**
(i) Financial Cost	1,212	1,368	1,196	12.9	-12.6
(ii) Operating Cost	105	129	146	22.9	13.2
(iii) Other cost	118	316	74	167.8	-76.6
E. Taxation	**134**	**32**	**48**	**-76.1**	**50.0**
F. Operating Profit (PBT)	**366**	**242**	**136**	**-33.9**	**-43.8**
G. Net profit (PAT)	**232**	**210**	**88**	**-9.5**	**-58.1**

– : Nil/Negligible.
* : Comprising only fund-based income.
Note : 1. PBT - Profit before tax
2. PAT - Profit after tax

Regional Pattern of Deposits of RNBCs

5.78 Of the three RNBCs, two are based in the Eastern region and one in the Central region. While deposits held by RNBCs in the Eastern region declined during the year ended March 2004 and March 2005, those held by RNBCs in the Central region increased in both the years. The RNBCs together held a sizeable portion (82.0 per cent) of total deposits held by all NBFCs at end-March 2005 (Table V.38).

Investment Pattern of RNBCs

5.79 Directions for investments by RNBCs were rationalised in June 2004 with a view to reducing the overall systemic risk in the financial sector and safeguarding the interests of depositors. In this regard, the following road map was prescribed: (a) from the quarter ended June 2005 and onwards, RNBCs were permitted to invest only to the extent of 10 per cent of the aggregated liabilities to the depositors (ALDs) at the second preceding quarter or one time of their net owned fund, whichever is lower, in the manner which in the opinion of the company is safe as per the approval of its Board of Directors; (b) from the quarter ended June 2006 and onwards, this limit would stand abolished and RNBCs would not be permitted to invest any amount out of the ALDs at the second preceding quarter as per their discretion. Thus, from the quarter ended June 2006 and onwards, RNBCs would be required to invest the entire amount of ALDs at the second preceding quarter in the directed investments.

5.80 Further, the requirement of AA+ rating and listing on the stock exchanges was introduced for bonds/debentures which qualify towards directed investments. These measures are expected to impart greater liquidity and safety to the investments of RNBCs and thus enhance protection available to depositors.

5.81 Aggregated liabilities to depositors (ALDs) increased during the year ended March 2004 and March 2005. Investments in unencumbered approved securities declined sharply, while fixed deposits with banks as also investments in bonds/debentures increased. As a result, unencumbered approved securities as a percentage of ALDs declined significantly at end-March 2005 from end-March 2003 (Table V.39).

Table V.38: Public Deposits held by Registered and Unregistered RNBCs - Region-wise

(Amount in Rs. crore)

Region	2003		2004		2005	
	No.	Amount	No.	Amount	No.	Amount
1	2	3	4	5	4	5
Northern	–	–	–	–	–	–
North-Eastern	–	–	–	–	–	–
Eastern	3	7,422 (49.3)	2	6,523 (42.6)	2	5,070 (30.5)
Central	1	7,640 (50.7)	1	8,804 (57.4)	1	11,530 (69.5)
Western	–	–	–	–	–	–
Southern	1	3 (0.0)	–	–	–	–
Total	**5**	**15,065**	**3**	**15,327**	**3**	**16,600**
Metropolitan cities						
Mumbai	–	–	–	–	–	–
Chennai	–	–	–	–	–	–
Kolkata	3	7,422	2	6,523	2	5,070
New Delhi	–	–	–	–	–	–
Total	**3**	**7,422**	**2**	**6,523**	**2**	**5,070**

– Nil/Negligible.
Note : Figures are as at end-March.

Table V.39: Investment Pattern of Residuary Non-Banking Companies

(Amount in Rs. crore)

Item	End-March			Per cent to ALDs		
	2003	2004	2005	2003	2004	2005
1	2	3	4	5	6	7
Aggregated Liabilities to the Depositors (ALDs):	**15,065**	**15,327**	**16,600**	**100**	**100**	**100**
a) Unencumbered approved securities	6,129	3,702	2,036	40.7	24.2	12.3
b) Fixed deposits with banks	1,470	2,431	4,859	9.8	15.9	29.3
c) Bonds or debentures or commercial papers of Government companies/ public sector banks/ public financial institutions/ corporations	6,553	8,319	9,225	43.5	54.3	55.6
d) Other investments	913	2,059	1,639	6.1	13.4	9.9

NBFCs not Accepting Public Deposits and With Assets Size of Rs.500 crore and Above

5.82 In terms of Section 45IA of the RBI Act, 1934 as amended on January 8, 1997, the companies carrying on NBFI activities are required to obtain a Certificate of Registration (CoR) from the Reserve Bank. Further, companies accepting public deposits are required to submit regulatory returns such as Annual Return on public deposits (NBS-1), Half-yearly Return on Prudential Norms (NBS-2) and Quarterly Return on Statutory Liquidity Ratio (NBS-3) as per the NBFC Directions issued on January 31, 1998.

5.83 The Reserve Bank issued CoR to 13,261 NBFCs as on June 30, 2005, out of which only 507 NBFCs are accepting public deposits and submitting the regulatory returns prescribed under the Directions. In order to assess the operations of large non-deposit taking companies, a quarterly return was introduced with effect from September 2004. To begin with, NBFCs with asset size of Rs.500 crore and above were advised to submit quarterly return covering information on their sources and applications of funds as also on their exposures to the capital market, NPAs and profitability.

5.84 Information based on the returns received from nearly 50 NBFCs with asset size of Rs.500 crore and above for the quarters ended March and June 2005 suggests a marginal increase in their assets/liabilities. Unsecured loans constituted the single largest source of funds for NBFCs, followed by secured loans (Table V.40).

Borrowings

5.85 Borrowings constitute the single most important source of funds (74.2 per cent) for large sized NBFCs. Total borrowing (secured and unsecured) by NBFCs for the quarter ended March and June 2005 were placed at Rs.1,26,823 crore

Table V.40: Liabilities of Large Sized NBFCs*

(Amount in Rs. crore)

Item	Quarter Ended			
	March 2005		June 2005	
	Amount	Per cent to total Assets	Amount	Per cent to total Assets
1	2	3	4	5
Total Liabilities	**1,70,957**	**100.0**	**1,79,311**	**100.0**
of which :				
a) Paid up Capital	11,233	6.6	11,294	6.3
b) Preference Shares	689	0.4	689	0.4
c) Reserve & Surplus	22,827	13.4	22,976	12.8
d) Secured Loans	52,774	30.9	56,233	31.4
e) Unsecured Loans	74,049	43.3	76,758	42.8

* : NBFCs not accepting public deposits with asset size of Rs.500 crore and above.

Table V.41: Borrowings by Large Sized NBFCs*

(Amount in Rs. crore)

Item	Quarter Ended			
	March 2005		June 2005	
	Amount	Per cent to total Borrowings	Amount	Per cent to total Borrowings
1	2	3	4	5
A) Secured Borrowings (i to vi)	**52,774**	**41.6**	**56,233**	**42.3**
i) Debentures	30,777	24.3	31,914	24.0
ii) Deferred Credit	–	–	–	–
iii) Term Loans from Banks	11,043	8.7	11,893	8.9
iv) Term Loans from FIs	4,411	3.5	6,574	4.9
v) Others	5,433	4.3	5,169	3.9
vi) Interest accrued	1,110	0.8	683	0.6
B) Unsecured Borrowings (i to viii)	**74,049**	**58.4**	**76,758**	**57.7**
i) Loans from Relatives	1,310	1.0	1,221	0.9
ii) ICDs	7,993	6.3	7,866	5.9
iii) Loans from Banks	19,717	15.5	21,661	16.3
iv) Loans from FIs	2,326	1.8	2,723	2.0
v) Commercial Papers	12,487	9.8	13,382	10.1
vi) Debentures	13,769	10.9	14,256	10.7
vii) Others	15,419	12.3	14,512	10.9
viii) Loans Interest accrued	1,028	0.8	1,137	0.9
Total Borrowings	**1,26,823**	**100.0**	**1,32,991**	**100.0**

– : Nil/Negligible.

* : NBFCs not accepting public deposits with asset size of Rs.500 crore and above.

and Rs.1,32,991 crore, respectively. Secured borrowings by way of debentures and term loans from banks/FIs increased significantly during the quarter ended June 2005. Unsecured borrowings in the form of loans from banks, debentures and commercial papers also increased during the quarter. Increased borrowings enabled large NBFCs to expand their operations on the asset side (Table V.41).

Application of Funds

5.86 Loans (both secured and unsecured) by NBFCs, which is the single largest item on the asset side, increased by 4.6 per cent during the quarter ended June 2005. A sharp increase (23.7 per cent) was also noticed in their current investment. Long-term investments and hire purchase financing declined marginally. Capital market exposure of large NBFCs also declined marginally (Table V.42).

Table V.42: Select Indicators on Application of Funds by Large Sized NBFCs*

(Amount in Rs. crore)

Item	Quarter Ended			
	March 2005		June 2005	
	Amount	Per cent to total application of funds	Amount	Per cent to total application of funds
1	2	3	4	5
1. Secured Loan	42,552	28.4	44,502	28.5
2. Unsecured Loan	60,855	40.6	63,669	40.7
3. Hire Purchase	20,763	13.9	19,982	12.8
4. Long-term Investment	14,847	9.9	14,689	9.4
5. Current Investment	10,883	7.2	13,466	8.6
Total	**1,49,900**	**100.0**	**1,56,308**	**100.0**
Memo Item:				
Capital Market Exposure	17,874	11.9	17,132	11.0
of which: in Equity	12,242	8.2	11,817	7.6

* : NBFCs not accepting public deposits with asset size of Rs.500 crore and above.

Table V.43: Financial Performance of Large Sized NBFCs*

(Amount in Rs. crore)

Item	Quarter Ended			
	March 2005		June 2005	
	Amount	Per cent to total Assets	Amount	Per cent to total Assets
1	2	3	4	5
Total Income	12,954	7.6	4,225	2.4
Total Expenses	9,612	5.6	2,753	1.5
Net Profit	2,255	1.3	1,059	0.6
Total Assets	1,70,957	100.0	1,79,311	100.0

* : NBFCs not accepting public deposits with asset size of Rs.500 crore and above.

Financial Performance

5.87 Total income and expenditure of large NBFCs worked out to 7.6 per cent and 5.6 per cent of total assets, respectively, for the year ended March 2005. Net profit to asset ratio was 1.3 per cent during the year ended March 2005. Large NBFCs earned a sizeable profit of Rs.1,059 crore during the quarter ended June 2005, which was little less than 50 per cent of the total profit earned during the year ended March 2005 (Table V.43).

Asset Quality

5.88 While gross NPAs/total assets ratio remained unchanged, gross NPAs/credit exposure ratio increased significantly during the quarter ended June 2005. Net NPAs relative to both total assets and credit exposure declined during the quarter ended June 2005 (Table V.44).

Table V.44: Gross and Net NPAs of Large Sized NBFCs*

(Per cent)

Item	End-March 2005	End-June 2005
1	2	3
1. Gross NPAs to Total Assets	2.3	2.3
2. Gross NPAs to Total Credit Exposure	6.3	7.9
3. Net NPAs to Total Assets	1.2	1.1
4. Net NPAs to Total Credit Exposure	3.4	2.5

* : NBFCs not accepting public deposits with asset size of Rs.500 crore and above.

4. PRIMARY DEALERS

5.89 The primary dealer (PD) system, created in 1996 continues to be important from the perspective of successful completion of the Government borrowing programme, the size of which is substantial, and the need to further develop the debt markets in India. PDs (at present 17 in number) deal largely in Government securities and other interest rate products and support the borrowing programme of the Central and the State Governments. A number of measures were initiated during 2004-05 to further strengthen the role of PDs in the Government securities market.

Policy Developments

5.90 Prudential guidelines were issued to PDs in June 2004 on dividend distribution policy with focus on pay-out ratio and capital adequacy ratio. Dividend pay-out ratio for PDs, having capital to risk-weighted assets ratio (CRAR) at 20.0 per cent or above in all the four quarters of the previous year, was capped at 50.0 per cent and at 33.3 per cent for PDs not fulfilling the above conditions. A primary dealer cannot declare dividend if the CRAR in any of the four quarters is below the minimum prescribed CRAR of 15 per cent.

5.91 PDs were advised to hold all their equity investments only in dematerialised form by the end of December 2004 and make all fresh investments only in dematerialised form thereafter.

5.92 Guidelines allowing PDs to issue subordinated debt instruments for Tier-II capital and Tier-III capital were issued in October 2004. The guidelines provided for the amount of subordinated debt to be decided by the Board of Directors, ceiling on interest rate spread, restrictions on the type of instrument, mandatory credit rating, compliance with SEBI guidelines, obtaining permission from the Reserve Bank for issuing instruments to NRIs/FIIs, assignment of 100 per cent risk weight for investments in other PDs/ banks and disclosure requirements.

5.93 Since the Reserve Bank would no longer play the role of an underwriter of the last resort from 2006-07, PDs would need to be adequately prepared to ensure success of the market borrowing programme.

5.94 An Internal Technical Group in the Reserve Bank, which examined primary issuance process under the FRBM period, recommended that PDs must underwrite the entire issuance amount of each auction. Given this significantly higher responsibility for PDs, the Group proposed adoption of risk mitigating measures such as short-selling, introduction of 'when-issued' market and exclusivity in primary auctions. In consonance with the proposed incentives, the Group recommended certain market-making obligations for PDs, particularly in the mid-segment. Earlier, another Group (Chairman: Dr. R.H. Patil) had examined the role of PDs in the Government securities market. Both the Reports were discussed in the Technical Advisory Committee (TAC) and certain recommendations were accepted by the Reserve Bank for implementation. Accordingly, several measures were proposed in the Annual Policy Statement for 2005-06. These included: (i) permitted structures of PD business to be expanded to include banks which fulfill certain minimum criteria subject to safeguards and in consultation with banks, PDs and the Government; (ii) to consider the recommendations of the Technical Group on restructuring the underwriting obligations of PDs, allowing exclusivity to PDs in primary auctions, introduction of 'when issued' market and limited short-selling in Government securities in consultation with the Government.

5.95 The operationalisation of these proposed measures is being examined by the TAC and the Reserve Bank/Government of India. The role of PDs in the Government securities market in the post-implementation of FRBM Act, 2003 is envisaged to be more important not only from the debt management perspective, but also from the viewpoint of market development (Box V.2). The risk mitigation tools that are being contemplated by the Reserve Bank and the proposal to expand permitted structures of PD business to include banks might require changes in the regulatory guidelines.

Box V.2: Role of Primary Dealers (PDs) under the FRBM Environment

The primary dealer system, with its current underwriting and bidding commitments, ensured to a great extent the smooth execution of Government borrowing programmes. However, there have been a few instances when some auctions of Government securities remained undersubscribed and devolved on the Reserve Bank. The Reserve Bank's participation in the primary auction process so far, *albeit* at the margin, has ensured that (i) the Government borrows as and when it requires funds; and (ii) irrational bidding behavior is avoided.

Under the FRBM Act, 2003, the Reserve Bank with effect from April 1, 2006, will not be allowed to participate in primary auctions. As such the current institutional mechanism requires a relook to ensure that debt management objectives are met and the Government is able to borrow under all market conditions without exacerbating market volatility.

The Internal Technical Group on Central Government Securities Market, which deliberated on various issues concerning Government securities market, suggested that the Reserve Bank's role in the primary market be replaced by a more active and dynamic participation by PDs. This has necessitated some restructuring of current institutional processes.

Since the current system of annual bidding commitments does not guarantee the success of notified amount being sold at each auction, the Group felt that a system of bidding commitments for each auction is preferable, whereby all PDs put together must commit to bid 100 per cent of each auction, ensuring that the notified amount is sold at each auction. However, since 100 per cent bidding commitments by PDs *per se* do not ensure that the cost of issuance is minimised or is in line with price discovery, the Group felt that instead of bidding commitments, PDs could be required to underwrite the entire notified amount of an auction. The methodology for such arrangement was also broadly suggested by the Group.

Recognising that the envisaged system casts a much larger responsibility on the PDs than under the current arrangements, it was suggested by the Group to compensate PDs with appropriate incentives over and above those already available such as access to the call market, cash and securities account with the Reserve Bank, refinance facility and access to the Liquidity Adjustment Facility (LAF). The Group also suggested that the possibility of providing PDs with a facility to repo their auctioned stock with the Reserve Bank for a limited period after the auction allotment, be examined to help them tide over temporary funding risk.

The Group suggested that the participation in the PD system be expanded to include banks to undertake PD activity departmentally. In almost all countries, the concept of primary dealers is limited to an activity and not an entity. That is, institutions such as commercial banks and investment banks, financial institutions and broker-dealers are designated as primary dealers, and no separate entity is required to be formed for this purpose. The Group, therefore, recommended that in addition to current eligibility norms, permitted structures for PD business be expanded to include banks directly undertaking PD activity as a department with independent subsidiary books of account. The operations of the bank may be kept scrupulously distinct from the PD activities. The Group, therefore, recommended that appropriate restructuring of the PD system be encouraged, with smaller PDs either raising the capital base or merging with parent banks, where there are bank subsidiaries.

The Group further suggested that the primary dealers be granted exclusivity in primary auctions and such exclusivity be granted in phases commencing with Treasury Bills and a few auctions of dated securities.

Operations and Performance of the PDs

5.96 PDs continued to be important players in the Government securities market during 2004-05. The liquidity support limits for PDs for 2004-05 were fixed at Rs.3,000 crore as against Rs.4,500 crore for the previous year. The liquidity support was made available at the Reserve Bank's Repo Rate.

5.97 Bidding commitments in Treasury Bill auctions for all PDs taken together for 2004-05 were fixed at 123 per cent of the issue amount. Total bids received at Rs.1,10,112 crore amounted to 205.8 per cent of the total Treasury Bill issues of Rs.53,500 crore and 74.1 per cent of the total Treasury Bill issues of Rs.1,48,500 crore (inclusive of Market Stabilisation Scheme). For dated securities auctions, the bidding commitments for all PDs taken together were originally fixed at Rs.1,20,300 crore. Subsequently, the bidding commitments were reduced to Rs.77,900 crore on account of reduction in the market-borrowing programme of the Government. The actual bids tendered by the PDs were for Rs.85,474 crore. PDs offered to underwrite the primary issues to the tune of Rs.58,335 crore during the year, out of which bids for Rs.34,720 crore were accepted by the Reserve Bank. The shares of total primary purchases by PDs for Treasury Bills and dated securities at 63 per cent and 47 per cent, respectively, during the year were marginally lower than those of 67 per cent and 50 per cent, respectively, in the preceding year.

5.98 The turnover of transactions by PDs (both outright and repo) in the secondary market for Treasury Bills and Government dated securities at Rs.4,66,242 crore and Rs.12,69,454 crore, respectively, constituted 28.0 per cent and 18.6 per cent, respectively, of the total market turnover of Rs.16,66,020 crore and Rs.68,23,054 crore, respectively.

Sources and Application of Funds

5.99 The investments by PDs in Government securities and corporate bonds declined sharply. Among sources of funds unsecured loans declined sharply (Table V.45).

5.100 The share of Government securities in total assets of PDs declined sharply from 82.3 per cent at end-March 2004 to 69.3 per cent at end-March 2005. Capital funds of the PDs declined to Rs.5,603 crore at end-March 2005 from Rs.6,015 crore at end-March 2004 (Table V.46). Despite this decline, however, PDs were able to maintain capital to risk weighted assets ratios far in excess of the minimum requirement of 15 per cent (Table V.46 and Appendix Table V.7).

Table V.45: Sources and Application of Funds of Primary Dealers

(Amount in Rs. crore)

Item	2003-04	2004-05#	Percentage Variation	
			2003-04	2004-05
1	2	3	4	5
Sources of Funds	**17,135**	**11,911**	**2.2**	**-30.5**
1. Capital	2,354	2,332	17.5	-0.9
2. Reserves and Surplus	3,675	3,334	32.3	-9.3
3. Loans (a+b)	11,106	6,245	-7.4	-43.8
a) Secured	1,654	2,445	-70.2	47.8
b) Unsecured	9,452	3,800	47.0	-59.8
Application of Funds	**17,135**	**11,911**	**2.2**	**-30.5**
1. Fixed Assets	71	75	6.0	5.6
2. Investments (a to d)	16,436	10,224	3.6	-37.8
a) Government Securities	14,094	8,255	-2.2	-41.4
b) Commercial papers	123	443	16.0	260.2
c) Corporate Bonds	2,055	1,176	75.9	-42.8
d) Others	164	350	–	113.4
3. Loans and Advances	2,567	2,322	41.8	-9.5
4. Non Current Assets	–	–	–	–
5. Others*	-1,939	-710	100.8	-63.4

– : Nil/Negligible.
: Figures are unaudited.
* : Including cash bank balance, accrued interest, deferred tax, less current liabilities and provisions.

Table V.46: Select Indicators of Primary Dealers

(Amount in Rs. crore)

Item	End-March	
	2004	2005 #
1	2	3
Total Assets*	17,135	11,911
Of which: Government securities	14,094	8,255
Government securities as percentage of total assets	82.3	69.3
Total Capital Funds	6,015	5,603
CRAR	42.7	54.3
Liquidity Support Limit	2,250 (normal) 2,250 (backstop)	3,000 (normal)

* : Net of current liabilities and provisions.
# : Unaudited.
Note : Figures for 2004 and 2005 do not include SBI Gilts.

Table V.47: Financial Performance of Primary Dealers

(Amount in Rs. crore)

Item	2003-04	2004-05#	Percentage Variation	
			2003-04	2004-05
1	2	3	4	5
A. Income (i to iv)	2,845	574	5.4	-79.8
i) Interest	1,132	778	1.8	-31.3
ii) Discount	174	44	-4.4	-74.7
iii) Trading Profit	1,131	-700	-1.4	-161.9
iv) Others	408	452	57.5	10.8
B. Expenses (i+ii)	977	769	-2.6	-21.3
i) Interest	655	459	-9.3	-29.9
ii) Administrative Costs	322	310	14.6	-3.7
C. Profit Before Tax	**1,868**	**-195**	10.1	-110.4
D. Net Profit	**1,229**	**-250**	14.8	-120.3

: Unaudited.

Financial Performance of PDs

5.101 Net interest income of PDs declined during 2004-05. This combined with trading losses incurred during the year due to hardening of interest rates resulted in net losses before and after taxes (Table V.47). Ten PDs out of 17 posted net profits during the year (Appendix Table V.8).

Table V.48: Financial Indicators of Primary Dealers

(Amount in Rs. crore)

	Indicator	2003-04	2004-05
	1	2	3
i)	Net Profit	1,229	-250
ii)	Average Assets	18,860	15,228
iii)	Return on Average Assets (per cent)	6.5	-1.6
iv)	Net Worth	5,998	5,592

Note : 1. Average net worth is the average of opening and closing net worth of the financial year.
2. Average assets are average of the month-end balances.

5.102 The return on average assets of PDs was negative during the year, reflecting the impact of net losses. The losses suffered by PDs eroded their net worth which declined to Rs.5,592 crore at end-March 2005 from 5,998 crore in the previous year (Table V.48).