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Monetary and Credit Information Review

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Monetary Policy

Fourth Bi-monthly Monetary Policy Statement, 2018-19

Resolution of the MPC

On the basis of an assessment of the current and evolving macroeconomic situation, Monetary Policy Committee (MPC) at its meeting held on October 5, 2018, decided to keep the policy repo rate unchanged at 6.5 per cent under the liquidity adjustment facility (LAF). Consequently, the reverse repo rate under the LAF remains at 6.25 per cent, and the marginal standing facility (MSF) rate and the Bank Rate at 6.75 per cent.

The decision of the MPC is consistent with the stance of calibrated tightening of monetary policy in consonance with the objective of achieving the medium-term target for consumer price index (CPI) inflation of 4 per cent within a band of +/- 2 per cent while supporting growth. (https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=45152)

Developmental and Regulatory Policies

This Statement sets out various developmental and regulatory policy measures for developing and strengthening financial markets.

Voluntary Retention Route for Investment by FPIs

The regulatory framework for Foreign Portfolio Investors (FPIs) investment in debt has evolved over the years, influenced by trade-offs in encouraging capital flows and attendant macro-prudential considerations. Several measures have been undertaken in recent times to facilitate FPI investment in debt. To encourage FPIs willing to undertake long-term investments, a special route called 'Voluntary Retention Route' (VRR) is being proposed. Under the proposed route, FPIs will have more operational flexibility in terms of instrument choices as well as exemptions from regulatory provisions, such as, the cap on short-term investments (less than one year) at 20 per cent of portfolio size, concentration limits, and caps on exposure to a corporate group (20 per cent of portfolio size and 50 per cent of a single issue). To be eligible to invest under this route, FPIs would need to voluntarily commit to retaining in India a minimum required percentage of their investments for a period of their choice. FPIs would apply for investment limits under the route through an auction process.

Regulation of Financial Benchmarks

The robustness and reliability of financial benchmarks are critical for efficient pricing and valuation of financial instruments. Ensuring the credibility of benchmarks promotes their wider adoption which, in turn, facilitates efficient transmission of price signals in the financial system. Following the controversy surrounding the London Inter-Bank Offer Rate (LIBOR) fixing, the International Organisation of Securities Commissions (IOSCO) laid down principles of financial benchmarks that provide the overarching framework to ensure robust and credible benchmarks in financial markets. Many regulators across jurisdictions have come up with regulations for financial benchmarks based on these principles. In India, the Report of the Committee on Financial Benchmarks had recommended, among other things, regulatory oversight of benchmark administrators. Accordingly, to improve the governance of the benchmark processes, it is proposed to introduce a regulatory framework for financial benchmarks which shall apply, initially, to benchmarks issued by the Financial Benchmarks of India Ltd. (FBIL). (https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=45153)

Banking Regulation

LCR, FALLCR against Credit to NBFCs and HFCs

The Reserve Bank on October 19, 2018 permitted banks, with immediate effect, to reckon Government securities held by them up to an amount equal to their incremental outstanding credit to NBFCs and Housing Finance Companies (HFCs), over and above the amount of credit to NBFCs and HFCs outstanding on their books as on October 19, 2018, as Level 1 High Quality Liquid Assets (HQLA) under Facility to Avail Liquidity for Liquidity Coverage Ratio (FALLCR) within the mandatory Statutory Liquidity Ratio (SLR) requirement. This will be in addition to the existing FALLCR of 13 per cent of Net Demand and Time Liabilities (NDTL) and limited to 0.5 per cent of the bank's NDTL.

The single borrower exposure limit for NBFCs which do not finance infrastructure stands increased from 10 per cent to 15 per cent of capital funds, up to December 31, 2018. (https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11396&Mode=0)

Banking Supervision

ECB Policy - Liberalisation

The Reserve Bank on October 3, 2018 in consultation with the Government of India, liberalised the External Commercial Borrowings (ECB) policy and permitted public sector oil marketing companies (OMCs) to raise ECB for working capital purposes with a minimum average maturity period of 3/5 years from all recognised lenders under the automatic route.

Further, the individual limit of USD 750 million or equivalent and mandatory hedging requirements as per the ECB framework have also been waived for borrowings under this dispensation. However, OMCs should have a Board approved forex mark to market procedure and prudent risk management policy, for such ECBs. The overall ceiling for such ECBs shall be USD 10 billion equivalent and the said facility will come into effect from October 3, 2018. All other provisions of the ECB policy shall remain unchanged.

Background

Under the extant policy, ECBs can be raised under tracks I and III for working capital purposes if such ECB is raised from direct and indirect equity holders or from a group company, provided the loan is for a minimum average maturity of five years. (https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11384&Mode=0)

Inspection of Banks-Sets of Specimen Signatures

The Reserve Bank on October 19, 2018 advised banks/ financial institutions (FIs) about the appointment of senior supervisory managers (SSMs), by Department of Banking Supervision, Central Office, RBI.

Consequent to the introduction of risk-based supervision framework, SSMs have been acting as a single and focal point of contact for all communications/interfaces between the bank and the Reserve Bank. Regional offices of the Reserve Bank were required to provide every year latest set of specimen signatures of senior officials of the Reserve Bank authorised to issue letters of introduction to inspecting officers to the head/ controlling offices of banks/ FIs within their jurisdiction. (https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11398&Mode=0)

Payment and Settlement System

PPIs – Guidelines for Interoperability

In order to prepare better for implementation of interoperability, consolidated guidelines for enabling all phases have been issued by the Reserve Bank on October 16, 2018. Participating Prepaid Payment Instruments (PPIs) issuers, who choose to adopt interoperability shall ensure adherence to the guidelines, in addition to the instructions on Know Your Customer (KYC), security for transactions and application life cycle, cybersecurity, fraud prevention and risk management.

Furthermore, all participating PPI issuers shall be guided by the technical specifications/standards/requirements for achieving interoperability through Unified Payment Interface (UPI) and card networks as per the requirements of National Payments Corporation of India (NPCI) and the respective card networks. NPCI and card networks shall facilitate participation by PPI issuers in UPI and card networks.

Background

- As per the road-map laid down therein, interoperability of all KYC-compliant PPIs was to be enabled in three phases – Interoperability of PPIs issued in the form of wallets through Unified Payments Interface (UPI),
- Interoperability between wallets and bank accounts through UPI, and
- Interoperability for PPIs issued in the form of cards through card networks. (https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11393&Mode=0)

Co-operative Bank Supervision

Basic Cybersecurity Framework for Primary UCBs

The Reserve Bank on October 19, 2018 issued basic cyber security guidelines applicable to all urban co-operative banks (UCBs). However, any UCB, depending on its self-risk assessment, complexity of its information technology (IT)/ information security (IS) systems, nature of digital products offered, and others, is free to adopt advanced cyber security norms as decided by their Boards. It is observed that the level of technology adoption is also different across the banks in this sector – some banks offering state of the art digital products to its customers and some banks maintaining their books of account in a standalone computer and using e-mail for communicating with its customers/supervisors/ other banks.

Need for a Board approved Cybersecurity Policy

All UCBs should immediately put in place a cyber security policy, duly approved by their Board/Administrator, giving a framework and the strategy containing a suitable approach to check cyber threats depending on the level of complexity of business and acceptable levels of risk. On completion of the process of policy formulation by the Board, a confirmation shall be sent to Department of Co-operative Bank Supervision, Central Office, Bandra Kurla Complex, Mumbai by email within three months from the date of circular. It shall be ensured that the cyber security policy deals with the following broad aspects, keeping in view the level of technology adoption and digital products offered to the customers:

Cybersecurity Policy to be distinct from the IT policy/IS Policy

The cyber security policy should be distinct from the IT/IS policy of the UCB so that it highlights the risks from cyber threats and the measures to address/reduce these risks. While identifying and assessing the inherent risks, UCBs should keep in view the technologies adopted, delivery channels, digital products being offered, internal and external threats etc., and rate each of these risks as low, medium, high and very high.

IT Architecture/Framework should be security compliant

The IT architecture/ framework which includes network, server, database and application, end-user systems, and others, should take care of security measures at all times and this should be reviewed by the Board or IT Sub-committee of the Board periodically. For this purpose, UCBs may carry out the following steps:

- Identify weak/vulnerable areas in IT systems and processes,
- Allow restricted access to networks, databases and applications wherever permitted, through well-defined processes and approvals including rationale for permitting such access,
- Assess the cost of impact in case of breaches/failures in these areas and,
- Put in place suitable cybersecurity system to address them,
- Specify and document clearly the responsibility for each of above steps.

A proper record should be kept of the entire process to enable supervisory assessment.

Cyber Crisis Management Plan

Since cyber risk is different from many other risks, the traditional BCP/DR (Business Continuity Plan/Disaster Recovery) arrangements may not be adequate and hence need to be revisited keeping in view the nature of cyber risk. A Government of India organisation, CERT-In (Computer Emergency Response Team – India, a Government entity) has been taking important initiatives in strengthening cyber security by providing proactive/reactive services and guidelines, threat intelligence and assessment of preparedness of various agencies in different sectors, including the financial sector. CERT-In also has come out with National Cyber Crisis Management Plan and Cyber Security Assessment Framework. UCBs may refer to CERT-In/ National Critical Information Infrastructure Protection Centre (NCIIPC)/RBI/Institute for Development and Research in Banking Technology (IDRBT) guidelines as reference material for their guidance.

UCBs should promptly detect any cyber intrusions (unauthorised entries) so as to respond/recover/contain the impact of cyber-attacks. Among other things, UCBs, especially those offering services, such as, internet banking, mobile banking, mobile wallet, Real Time Gross Settlement (RTGS)/ National Electronic Funds Transfer (NEFT)/ Immediate Payment Service (IMPS), Society for Worldwide Interbank Financial Telecommunications (SWIFT) , debit cards, credit cards and others, should take necessary detective and corrective measures/steps to address various types of cyber threats, such as, denial of service (DoS), distributed denial of services (DDoS), ransomware/crypto ware, destructive malware, business email frauds including spam, email phishing, spear phishing, whaling, vishing frauds, drive-by downloads, browser gateway fraud, ghost administrator exploits, identity frauds, memory update frauds, password related frauds, and others.

Organisational arrangements

UCBs should review the organisational arrangements so that the security concerns are brought to the notice of suitable/concerned officials to enable quick action.

Cybersecurity awareness

Managing cyber risk requires the commitment of the entire organisation to create a cyber-safe environment. This will require a high level of awareness/familiarisation among staff at all levels including Board and Top Management. UCBs should actively promote among their customers, vendors, service providers and other concerned parties an understanding of its cyber security objectives. Security awareness among customers, employees, vendors, service providers about the potential impact of cyber-attacks helps in cyber security preparedness of UCBs.

Ensuring protection of customer information

UCBs, as owners of customer sensitive data, should take appropriate steps in preserving the confidentiality, integrity and availability of the same, irrespective of whether the data is stored/in transit within themselves or with the third-party vendors; the confidentiality of such custodial information should not be compromised in any situation. To achieve this, suitable systems and processes across the data/information lifecycle need to be put in place by UCBs. As regards customers, UCBs may educate and create awareness among them with regard to cybersecurity risks.

Supervisory reporting framework

UCBs should report immediately all unusual cyber security incidents (whether they were successful or mere attempts) to Department of Co-operative Bank Supervision, Central Office, C-9, 1st Floor, Bandra Kurla Complex, Mumbai by email, giving full details of the incident. A 'NIL' report shall be submitted on a quarterly basis in case of no cyber security incidents.

Background

Use of Information Technology by banks has grown rapidly and is now an important part of the operational strategy of banks. The number, frequency and impact of cyber incidents/attacks have increased manifold in the recent past, more so in the case of financial sector including banks. There is an urgent need to put in place a robust cybersecurity/ resilience framework at UCBs to ensure adequate security of their assets on a continuous basis. It has, therefore, become essential to enhance the security of the UCBs from cyber threats by improving the current defences in addressing cyber risks. (https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11397&Mode=0)

Currency Management

Fire Audit of Currency Chests - Clarification

The Reserve Bank has been receiving references from various banks about non-availability of staff in State/ District Fire Departments for getting the periodical fire audit conducted in their respective currency chests. The matter has been examined and it is decided on October 25, 2018 that in case of non-availability of officials of the District Fire Department, the fire audit can also be conducted by the agencies approved by the respective State/District Fire Departments.

Background

All chest-maintaining banks were advised to ensure that fire audits of currency chests are conducted once in two years by the officials from the District Fire Department. (https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11401&Mode=0)

Financial Markets Regulation

Payments Banks and Small Finance Banks– access to Call/Notice/Term Money Market

The Reserve Bank on October 29, 2018 clarified that Payments Banks and Small Finance Banks are eligible to participate in the Call/Notice/Term money market (hereafter referred to as call money market) both as borrowers and lenders. Such eligibility is valid even prior to the completion of the process to get themselves included in the Second Schedule of Reserve Bank of India Act, 1934.

The prudential limits and other guidelines on Call money market for Payments Banks and Small Finance Banks will be the same as those applicable to Scheduled Commercial Banks.

These Directions have been issued by the Reserve Bank in exercise of the powers conferred under section 45W of the Reserve Bank of India Act, 1934 and of all the powers enabling it in this behalf.

These directions are applicable with immediate effect. (https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11405&Mode=0)

Non-Banking Regulation

Master Direction - Fit and Proper Criteria for Sponsors

The Reserve Bank on October 25, 2018 issued the Directions on Fit and Proper Criteria for Sponsors of Asset Reconstruction Companies (ARCs) registered under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (the Act).

The provisions of these Directions shall apply to the existing and proposed sponsors of the ARCs.

Determinants of fit and proper status of sponsors of ARCs

In determining whether the sponsor is fit and proper, the Bank shall take into account all relevant factors, as appropriate, including, but not limited to, the following:

- The sponsor's integrity, reputation, track record and compliance with applicable laws and regulations;
- The sponsor's track record and reputation for operating business in a manner that is consistent with the standards of good corporate governance, integrity, in addition to the similar assessment of individuals and other entities associated with the sponsor;
- The business record and experience of the sponsor;
- Sources and stability of funds for acquisition and the ability to access financial markets;
- Shareholding agreements and their impact on control and management of the ARC.

Continuous monitoring arrangements for due diligence in case of existing sponsors

For the purpose of ensuring that all its sponsors are fit and proper, every ARC shall:

- obtain within one month of the close of financial year a declaration from all its sponsors;
- furnish a certificate, by the end of May every year, to the Reserve Bank on the changes in the status of the sponsor.
- Every ARC shall examine any information on the sponsors which may come to its notice that may render such persons not fit and proper to hold such shares and shall immediately furnish a report on the same to the Bank.

Compliance with prior approval requirement

- The ARCs shall make an application as specified in the schedule to these Directions, for the Bank's prior approval for change in shareholding of the ARCs.
- The Bank shall, inter alia, seek feedback on the persons from other domestic as well as foreign regulators and enforcement and investigative agencies as deemed appropriate to make an assessment whether a sponsor is fit and proper. (https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11402&Mode=0)

Releases

All-India HPI Annual Growth decreased in Q1

The Reserve Bank on October 17, 2018 released the quarterly house price index (HPI) (base: 2010-11=100) for Q1:2018-19, based on transactions data received from housing registration authorities in ten major cities (viz., Mumbai, Delhi, Chennai, Kolkata, Bengaluru, Lucknow, Ahmedabad, Jaipur, Kanpur and Kochi). Time series data on All-India and city-wise HPI are available in the Database of Indian Economy (DBIE) portal (https://dbie.rbi.org.in/DBIE/dbie.rbi?site=statistics > RealSector > Price&Wages > Quarterly).

Highlights:

- The All-India HPI recorded a sequential increase of 2.5 per cent in Q1:2018-19 over Q4:2017-18.
- City-wise, large variance was observed in sequential terms, with Delhi recording the highest rise (5.3 per cent) and Kanpur recording the maximum contraction [(-)2.4 per cent].
- On a year-on-year basis, the all-India HPI recorded a growth of 5.3 per cent in Q1:2018-19 as against 6.7 per cent in the previous quarter and 8.7 per cent a year ago.
- Except Delhi, all other cities recorded a rise in housing price on an annual basis.
- In terms of annual growth rates, large divergences can be observed in city-wise house price movements. (https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=45268)

RBI Working on Paper No. India's Investment Cycle

The Reserve Bank on October 16, 2018 placed on its website a Working Paper titled "India's Investment Cycle: An Empirical Investigation" under the Reserve Bank of India Working Paper Series. The Paper is authored by Janak Raj, Satyananda Sahoo and Shiv Shankar.

This paper estimates the duration of the investment cycle and examines the determinants of investment activity in India. As per the findings of the paper, the real investment rate in India followed a three-year cycle during the period from 1950-51 to 2017-18. There were broadly nine episodes of contraction/upturn of two years and above. The decline in investment activity from 2011-12 to 2015-16 was caused by both trend and cyclical components. Decomposition of investment activity suggests that while the trend component has consistently moderated from 2011-12 onwards, the cycle component has turned from 2016-17. The current upturn in the investment cycle is estimated to last up to 2022-23 when the investment rate could rise to 33 per cent from the current rate of 31.4 per cent. The study also finds that GDP growth, real interest rate and bank credit are the major determinants of investment activity in India. The gross fiscal deficit crowds out investment activity. (https://rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=45250)

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