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# MONETARY AND CREDIT INFORMATION REVIEW

**POLICY**

## Opening of Administrative/Controlling Offices

With a view to further increasing the operational flexibility of banks, domestic scheduled commercial banks (other than RRBs) have now been permitted to open offices exclusively performing administrative and controlling functions (regional offices/ zonal offices) in Tier 1 centres without needing to obtain the Reserve Bank's prior permission in each case, subject to reporting.

This general permission would, however, be subject to regulatory/supervisory comfort in respect of the bank concerned and the Reserve Bank would have the option to withhold the general permissions now being granted, on a case-to-case basis, taking into account all relevant factors.

Opening of branches including central processing centres (CPCs)/service branches by domestic scheduled commercial banks (other than RRBs) in Tier 1 centres (centres with population of 100,000 and above as per census 2001) will continue to require the Reserve Bank's prior permission.

Banks should report to the Reserve Bank details of administrative offices opened under general permission.

## Acquisition of Accommodation on Lease/Rental Basis

The Reserve Bank has reiterated that banks should strictly adhere to the policy and operational guidelines formulated by their board of directors for hiring of premises on lease/rental basis in metropolitan, urban, semi-urban and rural areas. While acquiring premises for opening a branch, banks should also ensure that the location of the branch complies with the local norms/laws of the municipal corporation/nagar palika/town area authority/village panchayat or any other competent authority.

## Definition of Infrastructure Lending

It has been decided to harmonise the definition of 'infrastructure lending for the purpose of financing of infrastructure by banks and financial institutions' with that of the master list of infrastructure sub-sectors notified by the Government of India on March 27, 2012. The revised definition of 'infrastructure lending' will be effective from November 20, 2012. The exposure of banks to projects under sub-sectors which were included under the previous definition of infrastructure, but not included under the revised definition, will continue to get the benefits under 'infrastructure lending' for such exposures till the completion of the projects. Any fresh lending to those sub-sectors from November 20, 2012 will not qualify as 'infrastructure lending'. For the revised definition of 'infrastructure lending' please see box on page 2.

## CRR Reduced

The average cash reserve ratio (CRR) required to be maintained by scheduled commercial banks has been reduced by 25 basis points from 4.50 per cent to 4.25 per cent of their net demand and time liabilities (NDTL) from the fortnight beginning November 3, 2012.

## NPAs and Restructuring of Advances

The Reserve Bank has advised banks that -

- They should strictly adhere to the instructions regarding sharing of information relating to credit, derivatives and unhedged foreign currency exposures among themselves and put in place an effective mechanism for information sharing by end-December 2012.

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- Any sanction of fresh loans/*ad hoc* loans/renewal of loans to new/existing borrowers from January 1, 2013 should be done only after obtaining/sharing necessary information.
- Non-adherence to these instructions would be viewed seriously by the Reserve Bank and banks would be liable to action, including imposition of penalty, wherever considered appropriate.

## Bank Finance for Purchase of Gold

The Reserve Bank has advised banks not to grant any advances for purchase of gold in any form, including primary gold, gold bullion, gold jewellery, gold coins, units of gold exchange traded funds and units of gold mutual funds. Banks may, however, provide finance for genuine working capital requirements of jewellers. The scheme of gold (metal) loan detailed in the Reserve Bank's circular of December 31, 1998 as amended from time to time, will continue to be in force.

## Liquidity Risk Management

Based on the documents *Principles for Sound Liquidity Risk Management and Supervision* as well as *Basel III:International Framework for Liquidity Risk Measurement, Standards and Monitoring,* published by the Basel Committee on Banking Supervision (BCBS) in September 2008 and December 2010 respectively, the Reserve Bank had placed the draft guidelines on liquidity risk management and Basel III framework on liquidity standards on its website in February 2012 for comments and feedback.

Taking into account the comments and feedback received, the guidelines on liquidity risk management have been finalised and placed on the Reserve Bank's website. The guidelines consolidate the various instructions/guidance on liquidity risk management that the Reserve Bank has issued from time to time in the past, and where appropriate, harmonise and enhance these instructions/guidance in line with the BCBS's *Principles for Sound Liquidity Risk Management and Supervision*. They include, enhanced guidance on liquidity risk governance, measurement, monitoring and reporting to the Reserve Bank on liquidity positions. Banks have been advised to immediately implement the enhanced liquidity risk management measures.

The Reserve Bank has further advised that the Basel III liquidity standards are currently subject to an observation period/ revision by the BCBS with a view to addressing any unintended consequences that the standard may have for financial market, credit extension and economic growth. The final guidelines on Basel III liquidity framework will, therefore, be issued once BCBS revises the framework.

## List of Sub-Sectors for Infrastructure Lending

**Definition**

A credit facility extended by lenders (i.e., banks and select AIFIs) to a borrower for exposure in the following infrastructure sub-sectors will qualify as 'infrastructure lending':

| Category | Infrastructure Sub-sectors |
|---|---|
| Transport | (i) Roads and bridges |
| | (ii) Ports |
| | (iii) Inland waterways |
| | (iv) Airport |
| | (v) Railway track, tunnels, viaducts, bridges*1 |
| | (vi) Urban public transport (except rolling stock in case of urban road transport) |
| Energy | (i) Electricity generation |
| | (ii) Electricity transmission |
| | (iii) Electricity distribution |
| | (iv) Oil pipelines |
| | (v) Oil/gas/liquefied natural gas (LNG) storage facility*2 |
| | (vi) Gas pipelines*3 |
| Water and Sanitation | (i) Solid waste management |
| | (ii) Water supply pipelines |
| | (iii) Water treatment plants |
| | (iv) Sewage collection, treatment and disposal system |
| | (v) Irrigation (dams, channels, embankments, etc) |
| | (vi) Storm water drainage system |
| Communication | (i) Telecommunication (fixed network)*4 |
| | (ii) Telecommunication towers |
| Social and Commercial Infrastructure | (i) Education institutions (capital stock) |
| | (ii) Hospitals (capital stock)*5 |
| | (iii) Three-star or higher category classified hotels located outside cities with population of more than 1 million |
| | (iv) Common infrastructure for industrial parks, special economic zone (SEZ), tourism facilities and agriculture markets |
| | (v) Fertiliser (capital investment) |
| | (vi) Post harvest storage infrastructure for agriculture and horticultural produce including cold storage |
| | (vii) Terminal markets |
| | (viii) Soil-testing laboratories |
| | (ix) Cold chain*6 |

*1. *Includes supporting terminal infrastructure, such as, loading/unloading terminals, stations and buildings*
*2. *Includes strategic storage of crude oil*
*3. *Includes city gas distribution network*
*4. *Includes optic fibre/cable networks which provide broadband/internet*
*5. *Includes medical colleges, para medical training institutes and diagnostics centres*
*6. *Includes cold room facility for farm level pre-cooling, for preservation or storage of agriculture and allied produce, marine products and meat.*

## Monitoring Unhedged Foreign Currency Exposures

Unhedged forex exposure of corporates is a source of risk to them as well as to the financing banks and the financial system. Large unhedged forex exposures have resulted in accounts becoming non-performing assets (NPAs) in some cases. Banks were, therefore, advised in February 2012 that they should rigorously evaluate the risks arising out of unhedged foreign currency exposure of corporates and price them in the credit risk premium while extending fund-based and non fund-based credit facilities. Further, banks were also advised to consider stipulating a limit on unhedged position of corporates on the basis of a policy approved by their board. Despite these instructions, it is observed that unhedged forex exposure risks are not being evaluated rigorously and built into pricing of credit by banks. Banks are, therefore, advised that in accordance with the guidelines of February 2012, they should put in place a proper mechanism to rigorously evaluate the risks arising out of unhedged foreign currency exposure of corporates and price them in the credit risk premium. They should also consider stipulating a limit on the unhedged position of corporates on the basis of the policy approved by their board. Banks have also been advised to furnish compliance/action taken reports to the Reserve Bank before end-December 2012 after obtaining their board's approval.

## Frauds – Classification and Reporting

On a review and as a part of rationalisation of process and procedures, it has been decided to discontinue, from November 15, 2012, the practice of banks reporting attempted fraud cases of Rs.10 million and above to the Reserve Bank's Fraud Monitoring Cell, Department of Banking Supervision.

Banks should, however, continue to place individual cases involving Rs. 10 million and above before the audit committee of its board as hitherto. The report containing attempted frauds which is to be placed before the audit committee of the board should cover the following:

- The modus operandi of the attempted fraud.
- How the attempt did not materialise in a fraud or how the attempt failed/was foiled.
- The measures taken by the bank to strengthen the existing systems and controls.
- New systems and controls put in place in the area where the fraud was attempted.
- Yearly consolidated review of such cases detected during the year containing information, such as, area of operations where such attempts were made, effectiveness of new process and procedures put in place during the year, trend of such cases during the last three years, need for further change in process and procedures, if any, etc., as on March 31 every year, within three months of the end of the relative year. The first such yearly consolidated review should be for the year ending March 31, 2013.

# BRANCH BANKING

## Monitoring end-use of Crop Loans

Banks have been advised to ensure that all crop loans against which they are claiming interest subvention satisfy, *inter alia*, the following criteria:

- The borrower is an agriculturist.
- The rate of interest charged does not exceed the rate stipulated by the Government of India.
- The amount of loan is fixed according to the prescribed scale of finance for agricultural loans and the loan is used for the stated purpose.
- Seasonality is observed in regard to both disbursement and recovery.

Banks have been further advised to strengthen their systems for pre-sanction scrutiny and post-disbursement supervision and also consider carrying out post-disbursement audits to ensure that all crop loans for which interest subvention is being claimed are being used for the stated purpose and that there is no diversion of funds. Banks should not claim any interest subvention for loans not meeting the above criteria as these will not be treated as ‘agricultural’ loans.

It has come to the Reserve Bank’s notice that banks in various regions have failed to ensure end-use of funds disbursed ostensibly as crop loans. As a consequence, the expenditure incurred by the Government of India with the intention of helping small and marginal farmers has not, to a significant extent, reached the intended beneficiaries. There have been some reports that the ‘borrowers’ of these ‘crop loans’ have diverted the funds and are, to some extent, using the scheme as an arbitrage opportunity by borrowing at a lower rate of interest owing to the subvention available and investing them in fixed deposits and/or in other investment avenues at higher rate(s) of interest.

## Educational Loan Scheme

The Reserve Bank has advised banks not to reject any educational loan application citing the reason that the residence of the borrower does not fall under the bank's service area. Banks have also been advised to issue suitable instructions to their branches/controlling offices for meticulous and strict compliance in this regard.

Banks have been further advised that the service area norms are to be followed only in the case of government sponsored schemes as advised in the Reserve Bank's circular of December 8, 2004 and are not applicable for sanction of educational loans.

# PAYMENT SYSTEM

## National/Regional Electronic Clearing Service

With a view to extending both national electronic clearing service (NECS) and regional electronic clearing service (RECS) facility to the customers of all bank branches, the Reserve Bank has once again advised participating banks to make efforts in bringing all their branches under NECS/RECS. Branches which are on core banking solution (CBS) and already participating in

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national electronic funds transfer (NEFT) should be taken up on a priority basis.

NECS was launched by the Reserve Bank in September 2008 to extend the facility of electronic clearing service (ECS) on a pan-India basis. It was expected that banks will gradually bring all their CBS-enabled branches under NECS, thereby extending the benefits of ECS to all their customers. Subsequently, RECS was also launched in a few states to enable ECS payments/ receipts across all the branches located in a state/group of states from a centralised location.

**FEMA**

## Availing of ECB by SIDBI

On a review of the extant external commercial borrowings (ECB) policy, it has been decided to include the Small Industries Development Bank of India (SIDBI) as an eligible borrower for availing of ECB for on-lending to the micro, small and medium enterprises (MSME) sector, as defined under the MSMED Act, 2006, subject to the terms and conditions indicated below:

(a) such on-lending by SIDBI shall be to the borrowers directly either in Indian rupees or in foreign currency.

  (i) the foreign currency risk shall be hedged by SIDBI in full in case of on-lending to the MSME sector in Indian rupees; and

  (ii) on-lending in foreign currency shall be subject to Regulation 5(5) of FEMA Notification No. 3/2000-RB dated May 03, 2000, as amended from time to time and shall only be to those beneficiaries which have natural hedge by way of foreign exchange earnings.

(b) availment of ECBs, including outstanding ECBs, up to 50 per cent of their owned funds, for on-lending to the MSME sector, will be under the automatic route and beyond 50 per cent of owned funds, will be under the approval route, subject to a ceiling of USD 500 million per financial year.

(c) the proceeds of ECB availed by SIDBI, shall be used for on-lending to the MSME sector only for the permissible end-uses as provided under the extant ECB policy.

All other conditions of ECB, such as, recognised lender, all-in-cost, average maturity, prepayment, refinancing of existing ECB and reporting arrangements shall remain unchanged.

**RRBs**

## Opening of Branches in Unbanked Rural Centres

Regional rural banks (RRBs) have been advised to allocate at least 25 per cent of the total number of branches proposed to be opened during a year in unbanked rural (Tier 5 and Tier 6) centres. An unbanked rural centre would mean a rural (Tier 5 and Tier 6) centre that does not have a brick and mortar structure of any scheduled commercial bank for customer based banking transactions.

## Second Quarter Review of Monetary Policy 2012-13

Dr. D. Subbarao, Governor, Reserve Bank of India, in a meeting with chief executives of major commercial banks presented the Second Quarter Review of Monetary Policy for the year 2012-13 on October 30, 2012. The highlights of the Review are:

**Projections**

- Baseline projection of GDP growth for 2012-13 revised downwards from 6.5 per cent to 5.8 per cent.
- Inflation for March 2013 raised to 7.5 per cent.
- M3 growth for 2012-13 projected at 14 per cent.

**Stance**

- To manage liquidity to ensure adequate flow of credit to the productive sectors of the economy.
- To reinforce the positive impact of government policy actions on growth as inflation risks moderate.
- To maintain an interest rate environment to contain inflation and anchor inflation expectations.

**Monetary Measures**

- Bank Rate retained at 9.0 per cent.
- Cash reserve ratio (CRR) of scheduled banks reduced by 25 basis points from 4.50 per cent to 4.25 per cent of their NDTL.
- Repo rate under the liquidity adjustment facility (LAF) retained at 8.0 per cent.
- Reverse repo rate under the LAF, determined with a spread of 100 basis points below the repo rate, retained at 7.0 per cent.
- Marginal standing facility (MSF) rate, determined with a spread of 100 basis points above the repo rate, retained at 9.0 per cent.

**Expected Outcomes**

The policy actions and the guidance are expected to:

- Facilitate a turnaround in credit growth to productive sectors so as to support growth.
- Reinforce the growth stimulus of the policy actions announced by the government.
- Anchor medium-term inflation expectations on the basis of a credible commitment to low and stable inflation.

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