R.No. MAHENG/2004/14130
Regd. No. MH/MR/South-30/2009-11

Monthly Subscription : Re. 1.

Volume VI ◆ Issue 9
March 2010

MONETARY AND CREDIT INFORMATION REVIEW

POLICY

Infrastructure Finance Companies

In view of the critical role played by systemically important non-deposit taking non-banking finance companies engaged predominantly in infrastructure financing, the Reserve Bank has introduced a new category of non-banking finance companies (NBFCs) to be known as infrastructure finance companies (IFCs). Apart from this new addition, the existing categories of NBFCs are asset finance companies (AFCs), loan companies and investment companies. In terms of the new provisions, to be classified as an IFC, a non-deposit taking NBFC has to fulfil the criteria mentioned below:

i) A minimum of 75 percent of its total asset should be deployed in infrastructure loans as defined in Non-Banking Financial (Non-deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2007.

ii) Net owned funds of Rs. 300 crore or above.

iii) Minimum credit rating of 'A' by an accredited rating agency.

iv) Capital to Risk-Weighted Assets Ratio (CRAR) of 15 percent (with a minimum Tier I capital of 10 percent)

The other main highlights of the provisions in respect to IFCs are as follows:

- Any NBFC classified as an IFC may exceed the concentration of credit norms as provided in the aforesaid prudential directions in lending to any single borrower by ten percent of its owned fund and any single group of borrower by fifteen percent of its owned fund.
- In lending and investing (loans and investments) taken together an IFC may exceed the concentration of credit norms by five percent of its owned fund to a single party and by ten percent of its owned fund to a single group of parties.
- The extant norms for investments for both single party and single group of parties will remain same as provided in the prudential directions referred to above.
- Since the classification for the purpose of income recognition, asset classification and provisioning norms is based on asset specification, the extant prudential norms will continue as hitherto.

Exposure of Banks to NBFCs

The Reserve Bank has laid down risk weights and exposure norms in respect of banks exposure to NBFCs categorised as IFCs. The main highlights of which are as follows:

(i) As per the new norms, banks' exposure to NBFC-IFCs will henceforth be risk weighted as per the ratings assigned to these NBFCs by the rating agencies registered with the Securities & Exchange Board of India and accredited by the Reserve Bank.

(ii) Banks have to assign appropriate risk weights for their exposure to NBFC-IFCs similar to corporates/ corporate bonds, while computing capital for credit risk and specific risk under the market risk as provided in Master Circular dated February 08, 2010 on New Capital Adequacy Framework.

(iii) In respect of exposure of banks to the IFCs, the exposure should not exceed 15 per cent of bank's capital funds as per its last audited balance sheet, with a provision to increase it to 20 per cent if the same is on account of funds on-lent by the IFCs to the infrastructure sector.

(iv) The other provisions of the aforesaid Master Circular would also be applicable.

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Cash Processing Centres

As a part of the clean note policy, the Reserve Bank has decided to encourage banks to set up state of the art cash processing centres (CPCs) with substantial processing and storage capacities. Banks may consider any of the following three types of CPCs:

(i) A CPC established at an existing currency chest branch in the same location.

(ii) A CPC attached to an existing/new currency chest branch in different location.

(iii) A stand alone CPC that provides only fitness, sorting and authentication services (i.e they shall collect mixed notes from the bank branches in the morning and would return the same after processing/authentication checking/sorting in the evening as unfit notes, fit/issuable notes and suspect notes).

To make the CPCs viable and also to take advantage of capacity built up, the CPCs may also serve the branches of other banks which may require its services and charge from them a reasonable fee for the services rendered at mutually agreed rates. The stand alone CPCs could also render services to others such as merchant establishments, petrol pumps, etc., handling large volumes of cash against payment of fees. CPCs shall be subject to inspection by the Reserve Bank.

FEMA

External Commercial Borrowings Policy

As a measure of simplification of the existing procedures, the Reserve Bank has decided to delegate powers to designated authorised dealer category- I (AD category-I) banks to approve the following requests from the borrowers availing External Commercial Borrowings (ECBs), subject to specified conditions:

- Changes/modification in the drawdown/ repayment schedule of the ECBs already availed can be approved by designated AD category-I banks both under the approval and the automatic routes subject to the condition that the average maturity period, as declared while obtaining the Loan Registration Number is maintained.
- The changes in the drawdown/repayment schedule should be promptly reported to the Reserve Bank.
- Any elongation/ rollover in the repayment on expiry of the original maturity of the ECB would require the prior approval of the Reserve Bank.
- Changes in the currency of borrowing can also be allowed by designated AD category-I banks if so desired by the borrower company, in respect of ECB availed of both under the automatic and the approval routes, subject to all other terms and conditions of the ECB remaining unchanged.
- Designated AD category-I banks should ensure that the proposed currency of borrowing is freely convertible.
- Change of the existing designated AD category-I bank may be allowed by another designated AD category-I bank subject to No-Objection Certificate from the existing designated AD Category- I bank and after due diligence.
- Changes in the name of the borrower company may be allowed by designated AD category-I banks subject to production of supporting documents evidencing the change in the name from the Registrar of Companies.

All other aspects of the ECB policy, such as USD 500 million limit per company per financial year under the automatic route, eligible borrower, recognised lender, end-use, all-in-cost ceiling, average maturity period, refinancing of existing ECB and reporting arrangements remain unchanged.

Export and Import of Currency

Any person resident in India may take outside India or having gone out of India on a temporary visit, may bring into India (other than to and from Nepal and Bhutan) currency notes of Government of India and Reserve Bank of India notes upto Rs. 7,500 as per the amended provisions of Foreign Exchange Management (Export and Import of Currency) Regulations, 2000. Earlier the permissible limit was Rs. 5000 per person. The Reserve Bank through a recent circular has directed all authorised persons in foreign exchange to bring the changes to the notice of their constituents, customers and foreign counter parties concerned.

Transactions through Asian Clearing Union

The Reserve Bank has laid down detailed procedure for channelling transactions through Asian Clearing Union (ACU) to be followed by authorised dealer category- I (AD category-I) banks. Some of the major highlights of the said procedures are as follows:

- All transactions to be handled in same manner as other normal foreign exchange transactions.
- All instruments of payment shall be denominated in Asian Monetary Units (AMUs). Settlement of such instruments may be made by AD category-I banks through operation on ACU dollar and ACU euro accounts.
- The essence of the procedure for settlement is that a large part of the transactions, as possible, should be settled directly through the accounts maintained by AD category-I banks with banks in other participating countries and vice versa; only the spill-overs in either direction being required to be settled by the central banks in the countries concerned through the clearing union.
- AD category-I banks may repatriate the excess liquidity in their ACU dollar and ACU Euro accounts maintained with their branches/correspondents in other participating countries.
- The hours for receiving applications for funding of ACU dollar and ACU Euro accounts in overseas participant countries or surrendering of surplus liquidity in the ACU dollar and ACU euro accounts of their overseas correspondents maintained in India will be the regular business hours of the Reserve Bank.

- AD category-I banks should ensure that at all times the balances maintained in the ACU dollar and ACU Euro accounts are commensurate with the requirements of their normal exchange business and funds rendered surplus should be repatriated to India regularly.
- Operations conducted in and through the ACU dollar and ACU euro accounts will be subject to compliance with all the FEMA regulations and specific provisions of the ACU memorandum.
- Under the revised procedure, the Reserve Bank will receive and pay US dollar and euro from/to AD category-I banks and there will be no corresponding payment/receipt of Indian rupee.

Regional Rural Banks

Opening of Regional Offices

The Reserve Bank has now permitted all Regional Rural Banks (RRBs) (both amalgamated and stand alone) to open one Regional Office for every 50 branches. It may be recalled that as per the earlier policy amalgamated RRBs having 75 or more branches were allowed to open one Regional Office (RO) for every 50 branches, and RRBs, which had not undergone amalgamation (stand alone) and having 50 or more branches, were allowed to open one RO for every 25 branches. The distinction between amalgamated and stand alone RRBs in regard to opening of ROs has now been removed.

Electronic Banking

National Electronic Funds Transfer System

National Electronic Funds Transfer (NEFT) system which was launched in November 2005 is becoming a very popular mode for nationwide transfer of money from one branch to any other bank branch participating in the NEFT system. In the month of January 2010 alone, more than 6 million transactions were processed through the NEFT system. The coverage has also increased substantially with participation of over 63,000 bank branches spread across the length and breadth of the country. With a view to further strengthen the NEFT system in terms of availability, convenience, efficiency and speed, the Reserve Bank has introduced following measures for refinement of process flow and enhancement of operational features:

- All transactions under the NEFT system are required to be processed under different batches throughout the available time. However it was being observed that transactions were being processed by the destination branches only at the end of the day and not batch wise. The destination banks would now be required to afford credit to the beneficiary accounts immediately upon completion of a batch.
- The destination bank is required to return the transactions within two hours of completion of the batch settlement, if credits are unable to be afforded for any reason. This will ensure movement of money on a near-real-time basis.
- The operating hours for NEFT have been increased. The new operating hours would be from 9 am to 7 pm on weekdays and from 9 am to 1 pm on Saturdays. The previous operating hours was 9 am to 5 pm on week days and from 9 am to 12 noon on Saturdays.
- With a view to evenly space out transactions across batches, as also to make the system near-real-time, it has been decided to introduce the concept of hourly settlements with eleven hourly settlements starting from 9 am to 7 pm on all week days and five hourly settlements from 9 am to 1 pm on Saturdays.
- The current system of settlement in six batches at 9 am, 11 am, 12 noon, 1 pm, 3 pm and 5 pm on weekdays and the system of settlement in three batches at 9am, 11am, and 12 noon on Saturdays would be dispensed with.
- Originator of a NEFT transaction would now be receiving through a mobile SMS or an e-mail a positive confirmation in the form of an acknowledgement containing the date and time of credit, immediately after the credit is afforded to the beneficiary account.

The above modifications will be implemented in NEFT from March 1, 2010.

Information

Base Rate for Banks

The Reserve Bank has issued a draft circular on Base Rate for comments and feedback. The Circular aims to bring transparency in the pricing of lending products following the recommendations of a working group on Benchmark Prime Lending Rate (BPLR) which had submitted its report on October 20, 2009.

Co-operative Banks

Bilateral clearing arrangements

The Reserve Bank has directed all state and central-co-operative banks to immediately discontinue all bilateral clearing arrangements arising out of normal banking transactions. Bilateral agreements include correspondent banking arrangements, arrangements under cash management services or any arrangement that envisages routine clearing of cheques drawn on either or both banks without routing them through the clearing house infrastructure. It may be pointed out that the bilateral arrangements between banks being inter-bank in nature fall within the ambit of payments system and require authorisation from the Reserve Bank.

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Third Quarter Review of Monetary Policy 2009-10

Dr. D. Subbarao, Governor, Reserve Bank of India, in a meeting with chief executives of major commercial banks presented the Third Quarter Review of the Monetary Policy Statement for 2009-10 on January 29, 2010. The highlights are:

Projections

- The growth projection for Gross Domestic Product (GDP) growth for 2009-10 now revised to 7.5 percent as against 6.0 per cent projected earlier.
- Wholesale Price Index (WPI) inflation projection for end March 2010 revised to 8.5 per cent as against 6.5 per cent projected earlier.
- Money supply (M3) growth for 2009-10 now projected to be 16.5 as against 17 percent projected earlier.

Policy Stance

On the basis of the overall assessment, the stance of the monetary policy for the remaining period of 2009-10 will be to:

- Anchor inflation expectations and keep a vigil on the trends in inflation through policy adjustments as warranted.
- Actively manage liquidity to ensure that credit demands of productive sectors are adequately met consistent with price stability.
- Maintain an interest rate environment consistent with price stability and financial stability, and in support of the growth process.

Financial Markets

Financial markets continued to remain orderly and overnight money market rates remained below or close to the lower bound of the liquidity adjustment facility rate corridor as liquidity conditions remained comfortable. Despite large government borrowings, yields remained contained due to lower credit demand, open market operations and active liquidity management by the Reserve Bank.

Risk Factors

A number of downside risks to growth and upside risks to inflation need to be recognized:

- There is still uncertainty about the pace and shape of global recovery. There are concerns that it is too dependent on public spending and will unravel if governments around the world withdraw their fiscal stimuli prematurely.
- A downturn in global sentiment will affect our external sector and also our domestic investment.
- Any sharp increase in oil prices will affect all commodities which could stoke inflationary pressure even as growth remains below potential.
- Performance of the south-west monsoon in 2010 to have considerable effect on inflation.
- Sharp increase in capital inflows, above the absorptive capacity of the economy may complicate exchange rate and monetary management.
- As growth accelerates and the output gap closes, excess liquidity, if allowed to persist, may exacerbate inflation expectations.
- As the recovery gains momentum, it is important that there is co-ordination in the fiscal and monetary exits.

Considerations for Policy Stance

There are three important considerations behind the policy stance:

- It is necessary to carry forward the process of exit from expansionary stance adopted earlier with focus now shifting from ‘managing the crisis’ to ‘managing the recovery’.
- To prevent supply side inflation from spilling over into a wider inflationary process. If the growth momentum turns out to be as expected, pressures on capacities in an increasing number of sectors are likely to strengthen the transmission of higher input and wage costs into product prices.
- The recovery is yet to fully take hold. Strong anti-inflationary measures, while addressing one problem, may precipitate another by undermining the recovery, particularly by deterring private investment and consumer spending.

Monetary Measures

- Bank Rate retained at 6.0 per cent.
- Repo rate and reverse repo rate under the Liquidity Adjustment Facility (LAF) retained at 4.75 per cent and 3.25 per cent respectively.
- Cash reserve ratio (CRR) of scheduled banks increased by 75 basis points from 5.0 per cent to 5.75 per cent of their net demand and time liabilities (NDTL) in two stages. The first stage of 50 basis points increase to be effective from fortnight beginning February 13, 2010 followed by 25 basis increase effective from fortnight beginning February 27, 2010.

Edited and published by **Alpana Killawala** for the **Reserve Bank of India,** Department of Communication, Central Office, Shahid Bhagat Singh Marg, Mumbai - 400 001 and printed by her at **Onlooker Press,** 16, Sassoon Dock, Colaba, Mumbai - 400 005.
For renewal and change of address please write to the Chief General Manager, Department of Communication, Reserve Bank of India, Central Office Building, 12th floor, Fort, Mumbai - 400 001 without enclosing DD/cheque. MCIR is also available on Internet at www.mcir.rbi.org.in