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MONETARY AND CREDIT INFORMATION REVIEW

POLICY

Investment Portfolio of Primary Dealers

As per the extant guidelines, the Reserve Bank has permitted standalone Primary Dealers (PDs) to categorise a portion of their government securities portfolio in the Held to Maturity (HTM) category, subject to certain conditions, till March 31, 2010. The said guidelines have been reviewed and it has been decided to permit the PDs to continue holding government securities in HTM category until further advice. All other conditions will continue to apply. Banks undertaking primary dealer activities departmentally may continue to follow the extant guidelines applicable to banks in regard to the classification and valuation of the investment portfolio issued by the Reserve Bank.

Security Features in Cheque Forms

The Reserve Bank has decided to prescribe certain benchmarks towards achieving standardisation of cheques issued by banks across the country. These include provision of mandatory minimum security features on cheque forms like quality of paper, watermark, bank's logo in invisible ink, void pantograph, etc., and standardisation of field placements on cheques. In addition, certain desirable features are also being suggested which could be implemented by banks based on their need and risk perception. The set of minimum security features would not only ensure uniformity across all cheque forms issued by banks in the country but also help presenting banks while scrutinising/recognising cheques of drawee banks in an image-based processing scenario. The homogeneity in security features is expected to act as a deterrent against cheque frauds, while the standardisation of field placements on cheque forms would enable straight-through-processing by use of optical/image character recognition technology. It may be recalled that earlier a working group had been set-up by the Reserve Bank for examining further standardisation of cheque forms and enhancement of security features therein. The working group comprised various stakeholders viz. commercial banks, paper manufacturers, security printers, etc., apart from the Reserve Bank. Recommendations of the working group were discussed internally as also forwarded to Indian Banks' Association (IBA), National Payments Corporation of India (NPCI) and select banks for their views.

Interest on Savings Bank Account

In view of the present level of computerisation, the Reserve Bank has directed to all scheduled commercial banks that payments of interest on savings bank accounts may be made by banks on a daily product basis from April 1, 2010. In order to ensure smooth transition, banks have been advised to work out modalities.

Ceiling Rate on Export Credit

The Reserve Bank has reduced the ceiling rate on export credit in foreign currency by banks to LIBOR plus 200 basis points from the present ceiling rate of LIBOR plus 350 basis points, subject to the express condition that the banks will not levy any other charges viz. service charge, management charge, etc., except for recovery towards out of pocket expenses. Similar changes may be effected in interest rates in cases where EURO LIBOR/EURIBOR has been used as the benchmark. The revision in the rates of interest would be applicable only to fresh

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advances. Further, the ceiling interest rate on the lines of credit with overseas banks has also been reduced from six months LIBOR/EURO LIBOR/EURIBOR plus 150 basis points to six months LIBOR/ EURO LIBOR/EURIBOR plus 100 basis points.

Additional Disclosures by Banks

The Reserve Bank has decided to prescribe the following additional disclosures in the 'Notes to Accounts' in the banks' balance sheets, from the year ending March 2010:

- Concentration of deposits, advances, exposures and Non-Performing Assets (NPAs).
- Sector-wise NPAs.
- Movement of NPAs.
- Overseas assets, NPAs and revenue.
- Off-balance sheet Sepcial Purpose Vehicles (SPVs) sponsored by banks.

FEMA

External Commercial Borrowings (ECB) Policy

As per the extant policy, domestic Rupee denominated structured obligations have been permitted to be credit enhanced by non-resident entities under the approval route. In view of the growing needs of funds in the infrastructure sector, the Reserve Bank has put in place a comprehensive policy framework on credit enhancement to domestic debt. It has since been decided that the facility of credit enhancement by eligible non-resident entities may be extended to domestic debt raised through issue of capital market instruments, such as debentures and bonds, by Indian companies engaged exclusively in the development of infrastructure and by the Infrastructure Finance Companies (IFCs), which have been classified as such by the Reserve Bank subject to the following conditions:

- Credit enhancement will be permitted to be provided by multilateral/regional financial institutions and government owned development financial institutions.
- The underlying debt instrument should have a minimum average maturity of seven years.
- Prepayment and call/put options would not be permissible for such capital market instruments up to an average maturity period of 7 years.
- Guarantee fee and other costs in connection with credit enhancement will be restricted to a maximum 2 per cent of the principal amount involved.
- On invocation of the credit enhancement, if the guarantor meets the liability and if the same is permissible to be repaid in foreign currency to the eligible non-resident entity, the all-in-cost ceilings, as applicable to the relevant maturity period of the Trade Credit/ECBs, would apply to the novated loan.
- In case of default and if the loan is serviced in Indian Rupees, the applicable rate of interest would be the coupon of the bonds or 250 bps over the prevailing secondary market yield of 5 years Government of India security, as on the date of novation, whichever is higher.
- IFCs proposing to avail of the credit enhancement facility should comply with the eligibility criteria and prudential norms laid down in the circular and in case the novated loan is designated in foreign currency, the IFC should hedge the entire foreign currency exposure.
- The reporting arrangements as applicable to the ECBs would be applicable to the novated loans.

Definition of Infrastructure Sector

Definition of infrastructure sector has been expanded to include "cold storage or cold room facility, including for farm level pre-cooling, for preservation or storage of agricultural and allied produce, marine products and meat" for the purpose of availing of ECB. Accordingly, the infrastructure sector would henceforth be defined to include (i) power, (ii) telecommunication, (iii) railways, (iv) road including bridges, (v) sea port and airport, (vi) industrial parks, (vii) urban infrastructure (water supply, sanitation and sewage projects), (viii) mining, exploration and refining and (ix) cold storage or cold room facility, including for farm level pre-cooling, for preservation or storage of agricultural and allied produce, marine products and meat. 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, average maturity period, prepayment, refinancing of existing ECB, reporting arrangements and terms and conditions remain unchanged.

Reporting of Overseas Direct Investment

Revising the reporting package on Overseas Direct Investment (ODI) by the Indian parties, the Reserve Bank has decided to operationalise the on-line reporting system in a phased manner from March 2, 2010. Some of the major highlights of new system are as follows:

- The new system would enable on-line generation of the Unique Identification Number (UIN), acknowledgment of remittances and filing of the Annual Performance Reports (APRs) and easy accessibility to data at the Authorised Dealer (AD) level for reference purposes.
- As per the plan, initially, Part I (Sections A to D), II and III of form ODI should be filed on-line in the Overseas Investment Application (OIA) for allotment of UIN, reporting of subsequent remittances, filing of APRs, etc. Authorised Dealer Category–I banks (AD Category–I banks) would continue to receive the ODI forms in physical form which should be preserved, UIN wise, for onward submission to the Reserve Bank, if specifically required.
- Transactions in respect of mutual funds, Portfolio Investment Scheme (PIS) and Employees Stock Options Scheme (ESOPS) are also required to be reported on-line in the OIA.

- The on-line reporting would be required to be made by the centralised unit/nodal office of AD Category–I banks.
- AD Category–I banks would be responsible for the validity of the information reported on-line. The application for overseas investment under the approval route would continue to be submitted to the Reserve Bank in physical form as hitherto, in addition to the on-line reporting of Part I as contemplated above, for approval purposes.
- Transactions relating to closure/disinvestment/ winding up/ voluntary liquidation of the overseas Joint Ventures/Wholly Owned Subsidiaries (JVs/WOSs) under the automatic and approval routes (Part IV of form ODI) would continue to be submitted to the Reserve Bank in physical form as is being done at present. As per the new reporting system, AD Category–I banks would be able to generate the UIN on-line under the automatic route. However, subsequent remittances under the automatic route and remittances under the approval route should be made and reported on-line in Part II, only after receipt of the letter, confirming the UIN from the Reserve Bank.

CO-OPERATIVE BANKING

Loan against Security of Gold

State and Central Co-operative Banks grant loans for various purposes against the security of gold and gold ornaments as part of their lending policy. As per the extant instructions banks charge interest at monthly rests on loans and advances granted for purposes other than agricultural and allied activities. On a review, the Reserve Bank has decided to permit bullet repayment of gold loans up to Rupees one lakh as an additional option subject to the following guidelines:

- The amount of gold loan sanctioned should not exceed Rs.1 lakh at any point of time.
- The period of loan shall not exceed 12 months from the date of sanction.
- Interest will be charged to the account at monthly rests, but will become due for payment along with repayment of principal only at the end of 12 months from the date of sanction.
- The bank should prescribe a minimum margin to be maintained in case of such loans and accordingly, fix the loan limit taking into account the market value of the security (gold/gold ornament), expected price fluctuations, interest that will accrue during the tenure of the loan, etc.
- Such loans shall be governed by the extant income recognition, asset classification and provisioning norms which shall be applicable once the principal and interest become overdue.
- The account would also be classified as non-performing asset (sub standard category) even before the due date of repayment, if the prescribed margin is not maintained.

Crop loans sanctioned against the collateral security of gold/gold ornaments shall continue to be governed by the extant income recognition, asset classification and provisioning norms for such loans.

INFORMATION

Review of Credit Guarantee Scheme

A working group set up to review the Credit Guarantee Scheme (CGS) of the Credit Guarantee Fund Trust for Medium and Small Enterprises (CGTMSE) has made several recommendations to further enhance the usage and facilitate increased flow of collateral free loans to Micro and Small Enterprises (MSEs). Some of the main recommendations of the group are highlighted below:

- The limit for collateral free loans to the MSEs sector to be increased from the present level of Rs.5 lakh to Rs.10 lakh and it be made mandatory for banks.
- Consistent with the recommendation for enhancement of the collateral free loan limit from Rs.5 lakh to Rs.10 lakh, the guarantee cover upto 85% of the amount in default to be made applicable to credit facilities upto Rs.10 lakh. However, the extent of guarantee cover for credit facilities above Rs.10 lakh upto Rs.50 lakh will be 75% and for credit facilities in excess of Rs.50 lakh upto Rs.1 crore will be 75% upto Rs.50 lakh and 50% of the amount in excess of Rs.50 lakh, as per the extant provisions.
- The guarantee fee for collateral free loans upto Rs.10 lakh to be absorbed by the CGTMSE subject to the proviso that the Trust be free to adjust the guarantee fee both downwards and upwards based on the modelling of the dynamically evolving distribution of claims. This will ensure that the CGTMSE remains self-financing and self-sustaining in the long-term.
- CGTMSE may charge composite, all-in guarantee fee of 1% p.a. and appropriately realign downwards the guarantee fees chargeable to women entrepreneurs, micro enterprises and units located in north-eastern region including Sikkim.
- With a view to simplifying the procedure for filing claims in respect of small loan accounts, initiation of legal proceedings as a pre-condition for invoking of guarantees to be waived for credit facilities upto Rs.50,000.
- Member Lending Institutions (MLIs) may be allowed to invoke guarantee within a period of two years from the date of classification of the account as non-performing asset instead of the present prescription of within one year.
- The final claim to be paid after three years of obtention of decree of recovery instead of the present procedure of releasing the final claim only after the decree of recovery becomes time barred i.e. 12 years after obtaining decree.
- The chief executive officers of banks should assume complete and total ownership in the matter of strongly encouraging the branch level functionaries to avail of the CGS cover, including making performance in this regard a criterion in the evaluation of their field staff.

The implementation of the recommendations of the working group would result in enhanced usage of the CGS and facilitate increase in quality and quantity of credit to the presently included, as well as excluded, MSEs, leading eventually, to sustainable inclusive growth.

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Regulation of Credit Rating Agencies

A committee constituted by the ministry of finance at the instance of high level coordination committee on financial markets to revisit the legal and policy framework for regulating the activities of Credit Rating Agencies (CRAs) has made several recommendations to strengthen the existing regulations. The committee has taken note of international action in this regard and, inter alia, has recommended that there is a need for enhanced disclosure, continuation of the issuer-pays model, strengthened process and compliance audit, reporting of ownership changes, disclosure of default and transition statistics and strengthening of the regulation of the CRAs in tune with these suggestions.

Review of Lead Bank Scheme

A high level committee constituted by the Reserve Bank to review the Lead Bank Scheme (LBS) has made several recommendations to make it more effective in the changed economic scenario with sharper focus on financial inclusion and recent developments in the banking sector. Some of the major highlights of the recommendations are as follows:

- The State Level Bankers Committee (SLBC) meetings may be held regularly at quarterly intervals and they should be chaired by the Chairman & Managing Director (CMD) of the convenor bank. Additionally, the SLBC meetings may be co-chaired by additional chief secretary or development commissioner of the state concerned.
- In view of the large membership of the SLBC, it would be desirable for the SLBC to constitute sub-committees for specific tasks.
- The secretariat/offices of SLBC should be sufficiently strengthened to enable the SLBC convenor bank to effectively discharge its functions.
- SLBC convenor banks/lead banks are advised to focus attention on the urgent need for achieving 100% financial inclusion through penetration of banking services in the rural areas.
- Lead banks should ensure that private sector banks are more closely involved in the LBS.
- The zonal/controlling offices of banks, while finalising their business plans for the year, should take into account the commitments made in the Annual Credit Plan (ACP) which should be ready well in time before the performance budgets are finalised.
- The Lead District Manager (LDM) may convene a quarterly public meeting at various locations in the district, in coordination with banks having a presence in the area and other stakeholders to generate awareness of the various banking facilities, policies and regulations which impact the common person, obtain feedback from the public and provide grievance redressal to the extent possible at such meetings or facilitation for approaching the appropriate machinery for grievance redressal.
- There is a need for sensitising the district collector and CEOs of zilla parishads on banks and banking in general as also on the specific scope and role of the LBS.
- Staffs at the operational level of banks and government agencies associated with implementation of the LBS need to be aware of the latest developments and emerging opportunities. There is need for staff sensitisation/training/seminars, etc. at periodic intervals on an ongoing basis.
- Several institutions and academicians are engaged in research and studies that have implications for sustainable development in agriculture and micro, small and medium enterprises sector. Engaging with such research institutions and academicians would be useful in bringing in new ideas for furthering the objectives of the LBS. The SLBC/DCC may, therefore, identify such academicians and researchers and invite them as ‘special invitees’ to attend SLBC/DCC meetings.

The Reserve Bank has advised banks to initiate actions for speedy implementation of the recommendations and also to closely monitor the progress made in this regard.

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