

Bank financing for margin trading

DBOD.BP.BC.45/21.04.137 /2001-02

November 15, 2001
Kartika 24, 1923

All scheduled commercial banks
(excluding RRBs and LABs)

Dear Sir,

Bank financing for margin trading

Please refer to our circular DBOD.BP.BC.27/21.04.137-2001 dated September 22, 2001 in terms of which banks were permitted, on an experimental basis, to extend finance to stockbrokers for margin trading within the overall ceiling of 5% prescribed for exposure of banks to capital market, for a period of 60 days (i.e. up to November 22, 2001). As indicated therein, the guidelines have been reviewed by the RBI in consultation with major commercial banks.

2. It has been decided to continue the scheme of extending finance by banks to stockbrokers for margin trading until further notice. It has been further decided that the Board of each bank should formulate detailed guidelines for lending for margin trading, subject to the following parameters:

- (i) The finance extended for margin trading should be within the overall ceiling of 5% prescribed for exposure to capital market,
- (ii) A minimum margin of 40 per cent should be maintained on the funds lent for margin trading.
- (iii) The shares purchased with margin trading should be in dematerialised mode, under pledge to the lending bank. The bank should put in place an appropriate system for monitoring and maintaining the margin of 40% on a regular basis.
- (iv) The Bank's Board should prescribe necessary safeguards to ensure that no "nexus" develops between inter-connected stock broking entities / stockbrokers and the bank in respect of margin trading. Margin trading should be spread out by a bank among a reasonable number of stockbrokers and stock broking entities.

3. The Audit Committee of the Board should monitor periodically the bank's exposure by way of financing for margin trading and ensure that the guidelines formulated by the bank's Board, subject to the above parameters, are complied with. Banks should disclose the total finance extended for margin trading in the "Notes on Account" to their Balance Sheets.

4. A copy of the policy on financing of margin trading approved by the bank's Board may be forwarded to the RBI, in due course.

5. The earlier guidelines issued by the RBI on September 22, 2001 will remain in operation until fresh guidelines are issued by the bank's Board as per this circular.

6. The RBI-SEBI Technical Committee will again review the guidelines in June 2002 in the light of experience.

Please acknowledge receipt.

Yours faithfully,

(M.R. Srinivasan)
Chief General Manager-in-Charge