Rationalisation of Back-stop Facility Rate

REF: No. MPD. BC.233/07.01.279/ 2002-03

April 29, 2003
Vaishakha 9, 1925(S)

To:
All Scheduled Banks (excluding Regional Rural Banks (RRBs))
and Primary Dealers

Dear Sirs,

<u>Rationalisation of Back-stop Facility Rate</u>

Please refer to Paragraphs 77 through 79 of the Governor's statement on Monetary and Credit Policy for the year 2003-04 enclosed with his letter No. MPD. BC.230/07.01.279/2002-03 dated April 29, 2003 (copy of the paragraphs enclosed).

2. It may be indicated that at present, standing liquidity facilities comprising collateralised liquidity support to PDs and export credit refinance facility available to scheduled banks are available from RBI upto certain limits. These limits are split into a "normal" facility (constituting one-half of the standing facility), which is available at the Bank Rate, and a "back-stop" facility (constituting the remaining half of the standing facility) available at a variable daily rate determined by RBI from time to time. At present, the "back-stop" interest rate is higher than the repo/reverse repo/ NSE-MIBOR rates.

3. In order to increase the efficacy of liquidity adjustment facility (LAF) operations, and in view of rationalising the multiplicity of rates at which liquidity is injected, it has been decided that:

(i) The "back-stop" interest rate will be at the reverse repo cut-off rate at which funds were injected earlier during the day in the regular LAF auctions.
(ii) Where no reverse repo bid is accepted as part of LAF auction, the "back-stop" interest rate will generally be 2.0 percentage points over the repo cut-off rate of the day under LAF.
(iii) On the days when no bids for repo or reverse repo auctions are received/accepted, the "back-stop" interest rate will be decided by RBI on an *ad hoc* basis.

The normal facility would continue to be provided at the Bank Rate.

4. Back-stop facility would be operated till close of the banking hours.

5. Back-stop facility would come into effect from the close of business of April 29, 2003.

Kindly acknowledge receipt.

Yours faithfully

(D. Anjaneyulu)
Principal Monetary Policy Adviser

Encl.: as above

Extract from Governor's Statement on Monetary and Credit Policy for the year 2003-04

Back-stop Facility

77. Banks are eligible for standing facilities (export credit eligible for refinance) and PDs are eligible for collateralised liquidity support from RBI subject to certain limits. These limits are split into a “normal” facility (constituting one-half of the total standing facility), which is available at the Bank Rate, and a “back-stop” facility (constituting the remaining half of the standing facility) available at a variable rate determined by RBI from time to time. At present, the “back-stop” interest rate is higher than the repo/reverse repo/ NSE-MIBOR rates.

78. In order to increase the efficacy of liquidity adjustment facility (LAF) operations, it is desirable to rationalise the multiplicity of rates at which liquidity is absorbed/injected. Accordingly, it is proposed that:

- The “back-stop” interest rate will be at the reverse repo cut-off rate at which funds were injected earlier during the day in the regular LAF auctions.
- Where no reverse repo bid is accepted as part of LAF auction, the “back-stop” interest rate will generally be 2.0 percentage points over the repo cut-off rate of the day under LAF.
- On the days when no bids for repo or reverse repo auctions are received/accepted, the “back-stop” interest rate will be decided by RBI on an *ad hoc* basis.

79. With the above changes, it is expected that the “back-stop” interest rate will be lower by 1.0 percentage point over the present “back-stop” rate. This should benefit banks (as well as borrowers) using this facility.