Income recognition, asset classification, Provisioning and other related matters - Valuation of investments (BP.BC. 28 /21.04.048/98-99)

BP.BC. 28 /21.04.048/98-99

April 15, 1999

All Commercial Banks
(excluding Regional Rural Banks)

Dear Sir,

Income recognition, asset classification,
Provisioning and other related matters -
Valuation of investments

Please refer to our circular DBOD.No.BP.BC.29/21.04.048/98 dated 11 April, 1998 prescribing the method to be adopted by banks and auditors for valuation of Government and other securities while finalising the Balance Sheet as on 31 March, 1998. It has now been decided that banks should adopt the method indicated in the Annexure, for the Balance Sheet as on 31 March, 1999.

2. In this connection we advise that if there is any appreciation in the value of securities on account of the method of valuation as indicated in the Annexure, it should not be booked as income. Further, banks which have adopted a more prudent method of valuation of securities than the one now being suggested, may continue the practice hitherto followed by them.

3.Please acknowledge receipt.

Yours faithfully

(C.R. Muralidharan)
General Manager

Encls: 4

ANNEXURE

Investment Category		Method to be adopted by banks
1. Permanent Investments	(i)	Any gain on sale of securities in the `Permanent' category should be first taken to the Profit and Loss account and thereafter it could be appropriated to "Capital Reserve".
	(ii)	`Permanent' investments should be valued at cost and in case cost price is higher than the face value, the premium should be amortised over the remaining period of maturity of the security. On the other hand, where the cost price is less than the face value, the difference should be ignored and should not be amortised or taken to income account since the amount represents unrealised gain.
2. Current Investments		Valuation of Government Securities in the `Current' category should be done as per market quotations as on 31 March, 1999, wherever available. Where market quotations are not available, valuation of the Government Securities should be made on the following basis : As on 31 March, 1999 the Central Government Securities which were on the RBI list for sale and their prices are given below :

Nomenclature of security	Sale Price (Rs. Ps.)
11.15 % 2002	99.80
11.98 % 2004	101.60
12.40 % 2013	100.60

In respect of other Central Government Securities, other than the 6.00 per cent Capital Indexed Bonds 2002, the following yields as on March 31, 1999 may be applied:

No. of years	YTM (%)
0	7.65
1	10.07
2	11.00
3	11.17
4	11.32
5	11.50
6	11.63
7	11.74
8	11.84
9	11.94
10	12.05
11	12.13
12	12.18

13	12.24
14	12.29
15	12.33
16	12.37
17	12.40
18	12.44
19	12.47
20 and beyond	12.50

The yields as indicated above should also be applied to the State Government Securities and Government Guaranteed Securities.

The 6.00 per cent Capital Indexed Bonds may be valued at `Cost' as defined in Circular DBOD.No.BC.8/12.02.001/97-98 dated January 22, 1998.

It is clarified that the reckoning of number of years for the purpose of deciding upon appropriate YTM Rate be done by rounding off the fractional period of an year to the nearest completed year.

For valuation of **taxable non priority sector PSU bonds**, 2% above the YTM rates of Government Securities stated above should be applied.

For **tax free non priority sector PSU bonds,** 1% below the YTM rates of Government Securities stated above should be applied.

For **tax free priority sector PSU bonds,** 2% below the YTM rates of Government Securities stated above should be applied.

For valuation of **taxable priority sector PSU bonds**, YTM rates of Government Securities stated above should be applied.
As regards valuation of other unquoted securities banks should uniformly follow 'Yield To Maturity' method for arriving at valuation of unquoted securities.

3. Shares

(i) Wherever Stock Exchange quotations are available, the shares should be valued accordingly.

(ii) In the case of shares for which Current quotations are not available or where the shares are not quoted on the Stock Exchanges, the same should be taken at Book Value (without considering Revaluation Reserves, if any) which is to be ascertained from the latest Balance Sheet. In case latest Balance Sheet is not available, the shares are to be taken at Re.1 per company.

(iii) In the case of public sector companies, shares of PSUs should be valued at the break-up value as per the Balance Sheet as on 31 March, 1998. In case the 31 March, 1998 Balance Sheet is not available, the break-up value as per 31 March, 1997 Balance Sheet should be worked out and it should be reduced or discounted by 20%. If 31 March, 1997 Balance Sheet is also not available, the shares of the concerned PSUs should be valued at Re.1 per

		company.
4. Debentures	(i)	Wherever Stock Exchange quotations are available, the debentures should be valued accordingly.
	(ii)	Wherever Current quotations are not available or where the debentures are not quoted on the Stock Exchanges the same should be valued as follows : a) At Carrying Cost (i.e. book value), if interest is serviced regularly. b) Where interest is not serviced regularly and as such, is in arrears, the Depreciation should be made on the same lines as advances classified as sub-standard, doubtful and loss.
5. Mutual Fund Units		Investment in Mutual Fund Units is to be valued based on latest NAV declared by the Mutual Fund in respect of each particular Scheme. However, if market rates are available as per Stock Exchange quotations, market rates should be adopted.
6. Investments in subsidiar-ies and sponsored institutions		Security is to be valued at Carrying Cost (i.e. book value) on a consistent basis.
7. Treasury Bills (All maturities)		Valuation may be based at Carrying Cost (i.e. book value).
8.Commercial Paper		Commercial Paper to be valued at Carrying Cost (i.e. book value).
9.General Issues		
(i) Rounding off (e.g. to nearest 000s)		May be done at bank's discretion on a consistent basis.
(ii) Investment Categories		For the purpose of Balance Sheet, investments are to be classified into the following categories : (a) Government Securities (inclusive of T Bills, Zero Coupon bonds) (b) Other approved securities (c) Shares (d) Debentures and bonds (e) Subsidiaries and Joint Ventures (sponsored institutions)

	(f) Others (CP, Mutual Fund Units, etc.)
(iii) Aggregation	Securities under each category shall be valued scrip-wise as indicated above and Depreciation/ Appreciation shall be aggregated category-wise. Net depreciation, if any, shall be provided for. Net Appreciation, if any, should be ignored. Net Depreciation required to be provided for in any one category should not be reduced on account of Net Appreciation in any other category.
10. Recapitalisation Bonds	Recapitalisation Bonds will not form part of `Permanent’ or `Current’ investments. It will not be necessary to provide for depreciation on the Recapitalisation Bonds received by the nationalised banks from Government. In case, however, banks acquire recapitalisation bonds of other banks for Investment purposes, the Depreciation, if any, will have to be provided for.