RBI/2007-2008/179
DBOD.BP.No. 48/ 21.04.048 /2007-08

November 06, 2007

All Commercial Banks
(excluding RRBs)

Dear Sir,

<u>Project Finance Portfolio of banks</u>

At the time of financing projects banks generally adopt one of the following methodologies as far as determining the level of promoters' equity is concerned.

1) Promoters bring their entire contribution upfront before the bank starts disbursing its commitment.
2) Promoters bring certain percentage of their equity (40% – 50%) upfront and balance is brought in stages.
3) Promoters agree, ab initio, that they will bring in equity funds proportionately as the banks finance the debt portion.

While it is appreciated that such decisions are to be taken by the boards of the respective banks, it has been observed that the last method has greater equity-funding risk.

2. To contain this risk, banks are advised in their own interest to have a clear policy regarding the Debt Equity Ratio (DER) and to ensure that the infusion of equity/fund by promoters should be such that the stipulated level of DER is maintained at all times. Further they may adopt funding sequences so that possibility of equity funding by banks is obviated.

Yours faithfully

[Prashant Saran]
Chief General Manager-in-Charge