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RBI Announces Further Measures for Liquidity Management and Improving Credit Flow

1. In its Mid-Term Review of Monetary Policy on October 24, 2008, the Reserve Bank of India indicated that it will closely and continuously monitor the liquidity and monetary situation and respond swiftly and effectively to the impact of the global developments on Indian financial markets. The Reserve Bank also indicated that the challenge for the conduct of monetary policy is to strike an optimal balance among preserving financial stability, maintaining price stability and sustaining the growth momentum.

2. In response to emerging global developments, the Reserve Bank has taken a number of measures since mid-September 2008. The aim of these measures was to augment domestic and forex liquidity and to enable banks to continue to lend for productive purpose while maintaining credit quality so as to sustain the growth momentum. The following is a synopsis of the important measures taken:

Monetary Measures

- The repo rate under the liquidity adjustment facility (LAF) has been reduced by a cumulative 150 basis points since October 20, 2008. Accordingly, the repo rate has been brought down from 9.0 per cent to 7.5 per cent.

Rupee Liquidity

- In order to enhance rupee liquidity, the cash reserve ratio (CRR) has been reduced by a cumulative 3.5 percentage points of net demand and time liabilities (NDTL) since October 11, 2008. Accordingly, the CRR has been brought down from 9.0 per cent to 5.5 per cent of NDTL.

- The statutory liquidity ratio (SLR) has been reduced by one percentage points, that is, from 25 per cent of NDTL to 24 per cent.

- A term repo facility for an amount of Rs.60,000 crore has been instituted under the LAF to enable banks to ease liquidity stress faced by mutual funds (MFs) and non-banking financial companies (NBFCs) with associated SLR exemption of 1.5 per cent of NDTL.

- The Reserve Bank provided an advance of Rs.25,000 crore to financial institutions under the Agricultural Debt Waiver and Debt Relief Scheme pending release of money by the Government.

- A special refinance facility has been introduced for scheduled commercial banks (excluding regional rural banks or RRBs) with a limit of 1.0 per cent of each bank's NDTL as on October 24, 2008 at the LAF repo rate up to a maximum period of 90 days. During this period, refinance can be flexibly drawn and repaid.

- The Reserve Bank has put in place a mechanism to buy back dated securities issued under the market stabilisation scheme (MSS) so as to provide another avenue for injecting liquidity of a more durable nature into the system.

Forex Liquidity

- The Reserve Bank announced that it would continue to sell foreign exchange (US dollars) through agent banks to augment supply in the domestic foreign exchange market or intervene directly to meet any demand-supply gaps.
- The Reserve Bank announced that it would institute special market operations to meet the foreign exchange requirements of public sector oil marketing companies against oil bonds when they become available.
- The interest rate ceilings on FCNR (B) and NR(E)RA term deposits were increased by 100 basis points each.
- External commercial borrowings (ECBs) up to US $ 500 million per borrower per financial year were permitted for rupee expenditure and/or foreign currency expenditure for permissible end-uses under the automatic route.
- The all-in-cost ceiling for ECBs for average maturity period of three years and up to five years was enhanced to 300 basis points above LIBOR and to 500 basis points above LIBOR for ECBs over five years.
- The all-in-cost ceiling for trade credit less than 3 years was enhanced to 6 months LIBOR plus 200 basis points.
- Systemically Important Non-Deposit taking NBFCs have been temporarily permitted to raise short-term foreign currency borrowings under the approval route, subject to their complying with the prudential requirements of capital adequacy and exposure norms.

3. Global financial conditions continue to be uncertain and unsettled with ripple effects on domestic money, forex and credit markets. There are indications that the global slowdown is deepening with a larger than originally expected impact on the domestic economy, particularly for the demand conditions in the medium and small industry sector and export-oriented sectors. In the context of these developments, further augmenting rupee and forex liquidity, strengthening credit delivery mechanisms and improving credit delivery are imperative for sustaining the growth momentum. Particular attention needs to be paid to maintaining the viability of sectors that contribute significantly to employment and exports.

4. On a further review of the evolving developments, the Reserve Bank has decided to take the following measures:

Enhancing Rupee Liquidity

(i) The special term repo facility, introduced for the purpose of meeting the liquidity requirements of MFs and NBFCs will continue till end-March 2009. Banks can avail of this facility either on incremental or on rollover basis within their entitlement of up to 1.5 per cent of NDTL.

Enhancing Forex Liquidity

Foreign Currency Non-Resident (Banks) [FCNR(B)] Scheme

(ii) Currently, the interest rate ceiling on FCNR(B) deposits is fixed at Libor/Swap rates plus 25 basis points for the respective currency/ corresponding maturities. In view of the prevailing market conditions, it has been decided to increase the interest rate ceiling on FCNR (B) deposits by a further 75 basis points, *i.e.*, to Libor/Swap rates plus 100 basis points with immediate effect.

Non-Resident (External) Rupee Accounts [NR(E)RA]

(iii) Currently, the interest rate ceiling on NR(E)RA is set at Libor/Swap rates plus 100 basis points for US dollar of corresponding maturities. It has now been decided to increase the interest rate ceiling on NR(E)RA deposits by a further 75 basis points, *i.e.*, to Libor/Swap rates plus 175 basis points with immediate effect.

Housing Finance Companies

(iv) It has been decided to allow, as a temporary measure, housing finance companies (HFCs) registered with the National Housing Bank (NHB) to raise short-term foreign currency borrowings under the approval route, subject to their complying with prudential norms laid down by the NHB. Details in this regard are being notified separately.

Buy-back/Pre-payment of Foreign Currency Convertible Bonds (FCCBs)

(v) On account of the global developments, FCCBs issued by Indian corporates are currently trading at a discount. There is a benefit to the company concerned as well as to the economy if corporates buy back the FCCB at the prevailing discounted rates. In view of these potential benefits, Reserve Bank of India will consider proposals from Indian companies to prematurely buy back their FCCBs. The buy back should be financed by the company's foreign currency resources held in India or abroad and/or out of fresh external commercial borrowing (ECB) raised in conformity with the current norms for ECBs. Proposals in this regard will be considered under the approval route. Extension of FCCBs will also be permitted at the current all-in cost for the relative maturity.

Credit Delivery

(vi) In view of the difficulties being faced by exporters on account of the weakening of external demand, it has been decided to extend the period of entitlement of the first slab of pre-shipment rupee export credit, currently available at a concessional interest rate ceiling of the benchmark prime lending rate (BPLR) minus 2.5 percentage points from 180 days to 270 days with immediate effect.

(vii) At present, the ECR limit is fixed at 15 per cent of the outstanding rupee export credit eligible for refinance as at the end of the second preceding fortnight. The aggregate limit of ECR is currently around Rs.9,500 crore. It has now been decided to enhance the eligible limit of the ECR facility for scheduled banks (excluding RRBs) to 50 per cent of the outstanding export credit eligible for refinance. This will provide additional liquidity support to banks of an amount of about Rs.22,000 crore. The rate of interest charged on the ECR facility will continue to be the prevailing repo rate under the LAF which is currently 7.5 per cent.

(viii) Taking into account the need to ensure the growth momentum in the employment-intensive sectors of micro and small enterprises and housing, it has been decided to immediately allocate amounts, in advance, from scheduled commercial banks for contribution to the SIDBI and the NHB to the extent of Rs.2,000 crore and Rs.1,000 crore, respectively, against banks' estimated shortfall in priority sector lending in March 2009. The allocation now made in respect of SIDBI and NHB will be adjusted against the banks' actual achievement of the target/sub targets for priority sector lending as at the end of March 2009. The bank-wise allocations are being notified separately.

(ix) In order to provide further comfort on liquidity and to impart flexibility in liquidity management to banks, on November 1, 2008, the Reserve Bank introduced a special refinance facility under Section 17(3B) of the Reserve Bank of India Act, 1934 under which all scheduled commercial banks (excluding RRBs) are provided refinance from the Reserve Bank equivalent to up to 1.0 per cent of each bank's NDTL as on October 24, 2008 at the LAF repo rate up to a maximum period of 90 days. Banks are encouraged to use this facility for the purpose of extending finance to micro and small enterprises.

(x) As a counter-cyclical prudential measure, the general provisioning requirement on standard advances for residential housing loan beyond Rs.20 lakh has been progressively increased from 0.25 per cent to 1.0 per cent, while that on standard advances in the commercial real estate sector, personal loans including outstanding credit card receivables, loans and advances qualifying as capital market exposure and non-deposit taking systemically important NBFCs has been progressively increased from 0.25 per cent to 2.0 per cent. In view of the current macroeconomic, monetary and credit conditions, it has been decided, consistent with the practice of dynamic provisioning, that the provisioning requirements for all types of standard assets will stand reduced to a uniform level of 0.40 per cent except in case of direct advances to agricultural and SME sector which shall continue to attract provisioning of 0.25 per cent, as hitherto. The revised norms will be effective prospectively, but the provisions held at present should not be reversed.

(xi) Similarly, risk weights on banks' exposures to certain sectors, which had been increased counter cyclically, are also being revised downward in view of the current macroeconomic, monetary and credit conditions. All unrated claims on corporates shall attract a uniform risk weight of 100 per cent as against the risk weight of 150 per cent for such exposures prescribed earlier which was applicable for exposures above Rs 50 crore from April 1, 2008 and for exposures above Rs 10 crore from April 1, 2009. Claims secured by commercial real estate shall attract a risk weight of 100 per cent as against the earlier risk weight of 150 per cent. Claims on rated as well as unrated non-deposit taking systemically important non-banking financial companies (NBFC-ND-SI) shall be uniformly risk weighted at 100 per cent. As regards the claims on asset financing companies (AFCs), there is no change in the risk weights, which would continue to be governed by the credit rating of the AFCs, except the claims that attract a risk weight of 150 per cent under the new capital adequacy framework, stands reduced to a level of 100 per cent.

5. The Reserve Bank will continue to closely monitor the developments in the global and domestic financial markets and will take swift and effective action as appropriate.

Alpana Killawala
Chief General Manager

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Related Press Releases/Notifications:

1. RBI announces Further Measures for Monetary and Liquidity Management
2. Special Fixed Rate Repo Under Liquidity Adjustment Facility
3. Temporary liquidity support for financing agricultural operations
4. Special Refinance Facility (SRF) under Section 17(3B) of the Reserve Bank of India Act, 1934
5. Trade Credits for Imports into India – Review of all-in-cost ceiling
6. Enhancement of NBFCs' capital raising option for capital adequacy purposes
7. Interest Rates on Non-Resident (External) Rupee (NRE) Deposits and FCNR(B) deposits
8. Short-term Foreign Currency Borrowings by Housing Finance Companies
9. Export Credit Refinance Facility: Relaxation
10. Review of Prudential Norms – Provisioning for Standard Assets and Risk Weights for Exposures to Corporates, Commercial Real Estate and NBFC- ND-SI