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RBI Makes External Benchmark Based Interest Rate mandatory for certain categories of loans from October 1, 2019

The Reserve Bank of India has been examining the feasibility of mandating the use of external benchmark for determining interest rate on floating rate loans. In August 2017 the RBI constituted an Internal Study Group (ISG) to examine the working of the Marginal Cost of Fund Based Lending Rate (MCLR) system that was put in place in April 2016. The report of the ISG, which recommended the move over to an External Benchmark based Lending rate system, was placed in public domain in [October 2017](#). The comments of the Study Group on the responses to the report were also placed in public domain as an addendum thereto in [February 2018](#).

2 The RBI, in the [Statement on Developmental and Regulatory Policies dated December 5, 2018](#) announced its intention to make it mandatory for banks to link all new floating rate personal or retail loans and floating rate loans to MSMEs to an external benchmark. As it was felt that the matter required further stakeholder consultations, it was announced in the [Statement on Developmental and Regulatory Policies dated April 4, 2019](#), that RBI would hold further deliberations before taking a final decision in the matter.

3. It has been observed that due to various reasons, the transmission of policy rate changes to the lending rate of banks under the current MCLR framework has not been satisfactory. The RBI therefore has today issued a [circular](#) making it mandatory for banks to link all new floating rate personal or retail loans and floating rate loans to MSMEs to an external benchmark effective October 1, 2019. The banks are free to choose one of the several benchmarks indicated in the circular. The banks are also free to choose their spread over the benchmark rate, subject to the condition that the credit risk premium may undergo change only when borrower's credit assessment undergoes a substantial change, as agreed upon in the loan contract.