

Chapter 4

Timing and Sequencing of Measures for Capital Account Convertibility

- 4.1** The establishment of preconditions/signposts have been outlined in Chapter 3. The timing and sequencing of phasing out of capital controls assumes operational significance in the move towards CAC and these issues are addressed in this Chapter.
- 4.2** Capital account convertibility is at present available for foreign direct investors under the extant FDI policy, portfolio investment for FIIs, NRIs and investment in non resident repatriable deposit schemes with banks in India. The international experience has shown that liberalisation of the capital account induces large capital inflows, which can cause a real appreciation of the exchange rate and erode the effectiveness of certain domestic macro economic policies. The Committee recommends that alongside further measures of liberalisation of capital inflows it is desirable to simultaneously liberalise controls on outflows as a means of contending with capital inflows. An early albeit cautious beginning to allow capital outflows is desirable as the system is attuned to a totally rigid ban on certain outflows and there is a need to develop confidence that some capital outflows, far from being destabilising, would be conducive to the overall efficiency of deployment of resources. Capital outflows, in the context of larger inflows, could relieve pressure on the exchange rate and the foreign exchange reserves and thereby enhance the effectiveness of domestic policies.
- 4.3** The Committee recognises that while the timing and sequencing of CAC proposed in this chapter can be undertaken under the existing laws and regulations relating to foreign exchange, they would be facilitated by the proposed changes in the legislative framework governing foreign exchange transactions. In this regard, Shri. P. Chidambaram, the Union Finance Minister in his speech while presenting the Union Budget for 1997-98 said
- " As we progress towards a more open economy with greater trade and investment linkages with the rest of the world, the regulations governing foreign exchange transactions also needs to be modernised it is generally acknowledged that the Foreign Exchange Regulation Act, 1973 needs to be replaced by a new law consistent with full capital account, convertibility" [Part A - Paragraph 38]
- 4.4** In this Chapter, the timing and sequencing of liberalising both inflows and outflows of capital are set out within the framework of a phased three year road map, classified in relation to various economic agents, viz., resident and non resident corporates, banks, non bank financial institutions and individuals. Concomitant measures for the development of financial markets to handle the enhanced mobility of capital flows are also set out.
- 4.5** The banking system in India has been insulated from overseas markets for decades. Severe restrictions have been placed on banks borrowing funds from overseas or investing/lending abroad. Arbitraging between domestic and overseas markets have been strictly prohibited. The Committee recommends several measures for liberalising capital transfers by banks. Having regard to the fact that large scale short-term borrowings can be destabilising, the Committee recommends limits on such borrowings by the banking system. At the same time, a level playing field is to be ensured and the phased relaxation of controls should be concurrent with measures undertaken to ensure such a level playing field. In the area of foreign direct investment and portfolio investment, the Committee recommends complete elimination of the prior approval process from exchange control for investment/disinvestment.
- 4.6** Having regard to the need to keep external debt within sustainable limits, the Committee has proposed continuance of the policy of ceilings on external commercial borrowings (except for loans with long maturities). The Committee recommends simplification of the procedure for investments overseas in joint ventures/subsidiaries and substantial increase in the value limit for such investments (without prior approval) which is expected to make Indian industry competitive. Moreover, the Committee recommends that the exacting repatriation stipulations for such investments should be totally removed.

4.7 The Committee is of the view that a start should be made to liberalize outflows by individual residents. This will lend credibility to the commitment for CAC and give confidence to both residents and non residents that their genuine requirements for capital transactions are adequately met.

4.8 The various measures for removing capital controls and the timings and sequencing thereof proposed by the Committee are tabulated in Chapter. The rationale for the measures is given in the paragraphs following the tabulated list of measures.

Capital Account Convertibility- Timing and Sequencing of Measures

(\$ indicates US dollars)

Item	Present Position	Phase I 1997-98	Phase II 1998-99	Phase III 1999-2000
1. CORPORATES/BUSINESSES				
A. Corporates/Businesses - Residents				
1. Issuing foreign currency denominated bonds to residents (only rupee settlement) and investing in foreign currency denominated bonds and deposits (only rupee settlement).	Not permitted	To be permitted without any ceiling	Same as Phase I	Same as Phase I
2. Financial capital transfers abroad including for opening current/chequeable accounts.	Not permitted.	\$ 25,000 per annum.	\$ 50,000 per annum.	\$ 100,000 per annum.
3. Accessing capital markets abroad through GDRs & ADRs/ other forms of equity issues.	Permitted individually by Government. Approval under FERA given by RBI.	No approval to be taken from RBI/ Government Reporting within 30 days from close of issue	Same as Phase I	Same as Phase I
4. External Commercial Borrowings(ECBs)	ECBs are subject to overall ceiling with sub-ceilings as indicated below: (i) Import linked short-term loans (Buyers/ Suppliers credit) for less than 3 years (i.e., 35 months) approved by RBI subject to sub- ceiling fixed by Government. ii) Loans beyond 35 months approved by Government. iii) US \$ 3 million for a minimum period of 3 years for business related expenses including financing rupee cost of the project - approved by RBI within sub-ceiling fixed by Government. iv) All other loans are approved by Government (generally for financing requirements of infrastructure projects, etc.).	Queuing for purposes of implementing ceiling on ECB while ensuring that relatively smaller borrowers are not crowded out by a few very large borrowers. No restrictions on end use of funds. Loans for periods with average maturity of 10 years and above to be kept outside the ceiling.	Same as Phase I except for loans with average maturity of 7 years and above to be outside ceiling.	Same as Phase II
5. Foreign Currency Convertible Bonds/Floating Rate Notes	Permitted individually by Government within overall ECB ceiling.	To be within ECB ceiling with same procedure viz. queuing vide item 4.	Same as Phase I	Same as Phase I
6. Loans from non residents	Allowed by RBI on a case-by-case basis for loans from NRIs on non repatriable basis with restrictions on interest payment and end-use.	To be allowed to borrow up to \$ 250,000 per entity with payment of interest not exceeding LIBOR without restriction on period of loan, use of funds and repatriation of loan/interest.	To be allowed to borrow up to \$ 500,000 per entity with payment of interest not exceeding LIBOR without restriction on period of loan, use of funds and repatriation of loan/interest.	To be allowed to borrow up to \$ 1 million per entity with payment of interest not exceeding LIBOR without restriction on period of loan, use of funds and repatriation of loan/ interest.

7.	Joint ventures/wholly owned subsidiaries abroad	Proposals for investments up to \$ 4 million are cleared by the RBI. The extent of outflow is dependent upon the export performance of the Indian promoter and capability for repatriation by way of dividend, etc., within a period of five years. Cases not covered by these criteria are cleared by a Special Committee. Recently, an announcement has been made in the Budget that balances in EEFC accounts can be used for investments upto \$ 15 million without the specific approval of RBI.	Direct investments abroad to be allowed for ventures up to \$ 50 million by ADs subject to transparent guidelines to be laid down by the RBI. Above \$ 50 million through Special Committee. The current stipulation on repatriation of earnings by way of dividend etc. within a specified time period should be removed. JVs/WOSs can be set up by all parties and not restricted only to exporters/exchange earners.	Same as Phase I	Same as Phase I
8.	Project Exports	Indian project exporters are required to approach the RBI for prior approval for variety of purposes while executing the projects abroad	Requirement of prior approval by the RBI may be dispensed with subject, to reporting to the RBI.	Same as Phase I	Same Phase I
9.	Establishment of offices abroad	Powers given to ADs to allow remittances for exporters with an average annual export turnover of Rs. 150 lakhs and above to open representative/non-trading offices. Further, EEFC account holders have been permitted to utilise their EEFC balances without any restriction for establishing any type of offices. Other cases require RBI approval.	Any corporate entity may open offices abroad without the need for prior approval from RBI. Capital expenditure towards opening of the offices and current expenditure for maintenance could be subject to overall value limits to be allowed by ADs.	Same as Phase I	Same as Phase I
10.	EEFC accounts for exporters and exchange earners	50 per cent for EOUs and 25 percent for others- restrictions on use of funds for current account and permitted capital account transactions.	100 per cent of earnings for all exporters/exchange earners to be allowed to be held in EEFC accounts in India. Use of funds allowed for current and permitted capital account transactions with cheque writing facility.	Same as Phase I	Same as Phase I with additional provision that EEFC ac counts can be held with banks outside India at the option of the exporter and the exchange earners.
B. Corporates - Non Residents (including OCBs)					
1.	Foreign Direct Investment (FDI)	Currently OCBs are allowed facilities similar to NRIs. Other corporates are allowed to invest up to various proportions with RBI/Government approval under the FDI policy of the Government.	Prior approval of RBI not required for FDI. Reporting by ADs to the RBI.	Same as Phase I	Same as Phase I
2.	Portfolio Investment in India through stock exchanges in shares/debentures.	Allowed within the 24 per cent limit (can be increased to 30 per cent at the option of the company) which includes portfolio investment by NRIs, FIs & OCBs subject to approval by the RBI which is valid for a period of five years. The investment restricted to	To be allowed to all non-residents without prior approval by RBI. Designated ADs should be required to report to the RBI.	Same as Phase I	Same as Phase I

		1 per cent by individual NRIs/OCBs and 10 per cent by individual FIIs. Corporates, other than OCBs and FIIs, are not permitted.			
3.	Disinvestment	Disinvestment as approved by the RBI except where sales are made through stock exchange under portfolio investment scheme.	RBI approval to be dispensed with.	Same as Phase I	Same as Phase I
II. BANKS					
A. Banks - Residents					
1.	Loans and borrowings from overseas banks and correspondents including overdrafts in nostro account	ADs are permitted to borrow up to \$ 10 million from their overseas offices/ correspondents without any conditions on end use and repayment of such borrowings.	(i) Each bank may be allowed to borrow from overseas markets, short-term (up to one year) and long-term (over one year), to the extent of 50 per cent of the unimpaired Tier I capital with a sub limit of one third (i.e., 16.67 per cent of unimpaired Tier I capital) for short-term borrowings. (ii) No restrictions on use of funds and repayment. Prudential norms regarding open position and gap limits to continue.	Same as Phase I except that the ceiling will be 75 per cent of unimpaired Tier I capital with a sub-limit of one third (i.e., 25 per cent of unimpaired Tier I capital) for short-term borrowings.	Same as Phase I except that the ceiling will be 100 per cent of unimpaired Tier I capital with a sub-limit of one third (i.e., 33.33 per cent of unimpaired Tier I capital) for short-term borrowings.
2.	Investments in overseas markets	Banks allowed to invest in overseas money markets up to \$ 10 million.	Investments may be in overseas money markets, mutual funds and foreign securities. To be allowed subject only to (i) requirements of Section 25 of BR Act 1949* (ii) open position/gap limits.	Same as Phase I	Same as Phase I
3.	Fund based /non fund based facilities to Indian joint ventures and wholly owned subsidiaries abroad	Cleared by RBI/ Special Committee.	To be left to banks' discretion - only restriction to be Section 25 of BR Act.	Same as Phase I	Same as Phase I
4.	Buyers' credit/acceptance for financing importer/their bankers for buying goods and services from India (including financing of overseas projects)	Depending on amount cleared by ADs/EXIM Bank/ Working Group. FERA approval required from RBI.	To be allowed subject only to Section 25 of BR Act.	Same as Phase I	Same as Phase I
* Note : Section 25 of the Banking, Regulation Act, 1949 stipulates that the assets in India of every bank at the close of business on the last Friday of every quarter shall not be less than 75 per cent of its demand and time liabilities in India.					
5.	Accept deposits and extend loans denominated in foreign currencies from /to individuals (only rupee settlement)	Not allowed other than under existing foreign currency deposit schemes.	To be allowed without any ceilings - assets/ liabilities mismatch to be taken into overall open position /gap limits	Same as Phase I	Same as Phase I
6.	Forfaiting	Exim Bank alone has been permitted by RBI to do forfaiting	All ADs should be permitted to undertake forfaiting.	Same as Phase I	Same as Phase I
B. Banks - Non Residents					
1.	Rupee Accounts of non resident banks	Used only for merchant based transactions - investments not allowed. Overdrafts allowed upto Rs. 150 lakhs for normal business requirements for temporary periods.	Forward cover to be allowed to the extent of balances. Cancelling/ rebooking to be allowed. The present overdraft limit could be increased and limited investments may be allowed in rupee accounts	Same as Phase I	Non resident banks may be allowed to freely open rupee accounts with banks in India without any restrictions on their operations.

III. NON BANKS - FINANCIAL

A. Non Banks - Financial - Residents

1.	SEB I registered Indian investors (including Mutual Funds) investments overseas	Not allowed	Overall ceiling of \$ 500 million and the ceiling should be so operated that a few large funds do not pre-empt the overall amount.	Overall ceiling of \$ 1 billion.	Overall ceiling of \$ 2 billion.
2.	All India Financial Institutions	Borrowings from overseas markets or investments abroad subject to RBI/ Government prior approval	(i) Borrowings more than one year to continue within ECB ceiling with Government approval. (ii) Short-term borrowings to be allowed subject to limits. Investments in short term instruments to be permitted within limits up to the extent of liabilities maturing within one month.	(i) Same as Phase I (ii) Short-term borrowings to be allowed subject to limits. Investments in short term instruments to be permitted within limits up to the extent of liabilities maturing within 3 months	(i) Same as Phase I (ii) Short-term borrowings to be allowed subject to limits. Investments in short term instruments to be permitted within limits up to the extent of liabilities maturing within 6 months.

B. Non Banks - Non Residents

1.	FII's				
(a)	Portfolio Investment	(a) Investments in secondary market allowed once FII is registered with SEBI subject to 24 per cent ceiling (can be increased to 30 per cent at the option of the company) which includes portfolio investment by NRIs, FIIs and OCBs with a 10 per cent limit for individual FIIs and 1 per cent by individual NRIs/ OCBs. FERA approval is given by RBI which is valid for a period of five years.	To be allowed without RBI prior approval. Designated ADs would be required to report to RBI	Same as Phase I	Same as Phase I
(b)	Primary market investment/private	Primary market offering/private placement allowed with RBI approval up to 15 per cent of the new issue/ capital.	RBI approval not required. Designated ADs to report to the RBI.	Same as Phase I	Same as Phase I
(c)	Disinvestment	(i) Disinvestment through stock exchange allowed freely. (ii) Other routes of disinvestment require RBI approval	RBI approval for disinvestment to be dispensed with.	Same as Phase I	Same as Phase I
(d)	Investments in debt instruments	Permitted to invest in dated Government securities of Central and State Governments (excluding Treasury Bills) both in primary and secondary markets. ECB ceiling includes FII investment in rupee debt instruments. The Debt Funds of FIIs are also allowed to invest in corporate	Maturity restrictions on investments in debt instruments (including, treasury bills) to be removed. FII investments in rupee debt securities to be kept outside ECB ceiling but could be part of a separate ceiling	Same as Phase I	Same as Phase I

debt securities
(NCDs, Bonds, etc.)
listed or to be listed.

FII's can invest in
equity and debt
(NCDs, Bonds, etc.)
in the ratio of 70:30,
Debt Funds of FII's
can invest upto 100
per cent in debt
instruments subject
to a ceiling,
prescribed by SEB1.

IV INDIVIDUALS

A Individuals -Residents

1.	Foreign currency denominated deposits with banks/corporates in India (only-rupee settlement)	Not permitted	To be permitted without ceiling	Same as Phase I	Same as Phase I
2.	Financial capital transfers including for opening current/chequeable accounts	Not permitted	\$ 25,000 per annum	\$ 50,000 per annum	\$ 100,000 per annum
3.	Loans from non residents	Residents are allowed to obtain interest free loans on non repatriation basis from non resident relatives for personal and business purposes other than investment. Other cases need RBI approval.	Residents to be allowed to take loans from non residents up to \$ 250,000 per individual with payment of interest not exceeding LIBOR, without restrictions on period of loan, repatriation of principal/interest and use of funds.	Residents to be allowed to take loans from non residents up to \$ 500,000 per individual with payment of interest not exceeding LIBOR, without restrictions on period of loan, repatriation of principal/ interest and use of funds.	Residents to be allowed to take loans from non residents up to \$ 1 million per individual with payment of interest not exceeding LIBOR, without restrictions on period of loan, repatriation of principal/ interest and use of funds.

B Individuals : Non Residents

1.	Capital transfers from non repatriable assets held in India (including NRO and NRNR RD accounts)	Not allowed; however, a few cases allowed on sympathetic grounds.	\$ 25,000 per year*	\$ 50,000 per year*	\$ 100,000 per year*
2.	Foreign Direct Investment in India (FDI) (other than in real estate)	(a) FDI for NRIs with repatriation benefits are to be cleared by RBI/ Government under FDI policy. (b) FDI for other non resident individuals are to be cleared by Government and RBI.	No RBI permission for FDI subject to reporting by ADs.	Same as Phase I	Same as Phase I

* No fresh **NRNRD** accounts from 1997-98. On maturity the balances in the accounts get merged with other non repatriable funds or depositors can shift the maturity proceeds to a special 3 year NRE account with full repatriation benefit on maturity. If prematurely withdrawn from special NRE account, funds will get merged with other non repatriable funds of the non resident. In case of investments permitted on non repatriation basis on maturity or on disinvestment, the proceeds will be merged with other non repatriable assets.

3.	Portfolio Investment in India through stock exchanges.	Allowed to NRIs within the 24 per cent ceiling (can be increased to 30 per cent at the option of the company) which includes portfolio investment by NRIs, FIIs and OCBs subject to approval by the Reserve Bank which is given for a period of five years. The investment restricted to 1 per cent by individual NRIs/OCBs and 10 per cent by individual FIIs.	Allowed to all non residents without RBI prior approval. Designated ADs would be required to report to RBI.	Same as Phase I	Same as Phase I
4.	Disinvestment	Disinvestment to be approved by RBI except where sales	RBI approval to be dispensed with.	Same as Phase I	Same as Phase I

are made through stock exchange under portfolio investment scheme.

V. FINANCIAL MARKETS

1. Foreign Exchange Market

(a) Forward contracts

Forward contracts are allowed to be booked on the basis of business projections in respect of exporters and importers. Also forward cover allowed for non residents for limited purposes such as dividend remittance and freight/passage collections.

To allow all participants in the spot market to participate in the forward market; FIIs, non residents and non resident banks having rupee assets can be allowed forward cover to the extent of their assets in India. Banks to be allowed to quote two way in rupee to overseas banks/ correspondents both spot and forward subject to their position/gap limits. Those with economic exposures to be allowed to participate in forward market.

Same as Phase I

Same as Phase I. No restrictions on participants in spot/forward markets i.e., participation allowed without any underlying exposure.

(b) Authorised dealers

Authorised dealers at present are only banks.

All India FIIs which comply with the regulator/prudential requirements and fulfil well defined criteria should be allowed to participate as full-fledged ADs in the forex market.

Same as Phase I

To allow select NBFCs to act as full-fledged authorised dealers on the basis of criteria similar to FIIs.

(c) Products

Currently the only derivative in the rupee \$ market is the forward contract. ADs have been allowed to enter into Rupee/\$ currency swaps with counterparties in India subject to open position and gap limits. Cross currency derivatives and interest rate derivatives allowed for covering underlying exposures - to be routed through ADs

All derivatives including rupee based derivatives to be allowed. Futures in currencies and interest rates to be introduced with the system of screen-based trading and an efficient settlement mechanism.

Direct access to overseas markets by corporates for derivatives without routing through ADs Phase I to continue.

Same as Phase I & 11

2. Money Market

Banks allowed to lend and borrow freely. FIIs allowed to lend with no limit/ allowed to borrow within small limits. Others allowed to lend to primary dealers for minimum amount of Rs. 10 crores. MFs participate only as lenders. Residual restrictions on deposit rates applicable to public deposits; minimum period for CDs/ MMMFs/ fixed deposits specified.

Market segmentation to be removed. Deposit rates to be deregulated and minimum period restrictions to be removed. Restrictions on participants in the money market to be freed. Level playing field for all banks, FIIs and NBFCs regarding reserve requirements and prudential norms.

Same as Phase I

Same as Phase I

3. Government Securities Market

A number of measures have been taken to strengthen the market for Government securities such as a move towards market related rates of interest introduction of auctions and new instruments and

(i) Access to FIIs in Treasury bill market.
(ii) RBI to develop Treasury bill market offering two-way quotes.
(iii) Government Securities (including Treasury bills) futures to be introduced.
(iv) RBI to provide

(i) The OPD to take up part of issue of dated securities and all Treasury bills. (ii) RBI to discontinue participation in 91 day Treasury bill primary auctions and it

(i) The OPD to take full responsibility for primary issues of all Treasury bills and dated securities.
(ii) Full underwriting of issues by PDs with

	measures to develop the secondary market through Primary Dealers (PDs) and Satellite Dealers (SDs).	Liquidity Adjustment Facility to PDs through Repos and Reverse Repos. (v) Dedicated gilt funds to be given strong and exclusive fiscal incentives to individuals to develop the retail segment. (vi) Number of PDs and SDs to increase. Progressive increase in share of PDs in underwriting. Commission to PDs to be related to underwriting commitment (vii). Government to initiate action for setting up of an Office of Public Debt (OPD) (viii) Delivery Versus Payment (DVP) system to be fully automated for all securities on a real time basis with proper safeguards for ensuring that risks are controlled.	should only participate in the secondary market. (iii) Number of PDs and SDs to be further increase with a quantum jump in share of PDs in underwriting with strong incentives through underwriting commission.	RBI discontinuing participation in primary market for dated securities.
4. Gold	At present, there are restrictions on import of gold. There are only three channels through which import of gold is allowed (1) through channels agencies (ii) through returning NRIs and (iii) through special import licences.	(i) Banks and financial institutions fulfilling well- defined criteria to be allowed to operate freely both in domestic and international markets. (ii) Sale of gold by banks and FIs included under (i) above to be freely allowed to all residents. (iii) Banks to be allowed to offer gold denominated deposits and loans (iv) Banks fulfilling well-defined criteria may be allowed to mobilise household gold and provide working capital gold loans to jewellery manufacturers as also traders. (v) Banks may be allowed to offer deposit schemes akin to GAPs (gold accumulation plans)	Steps to be taken by Government and the RBI for developing, a well regulated market in India for gold and gold derivatives including, forward trading. Both residents and non residents to be allowed to operate in this market.	Same as Phase I and II
5. Participation in international commodity markets	Not allowed	To be allowed	Same as Phase I	Same as Phase I

I. Corporates/Businesses

I.A. Residents

I.A.1. Issuing Foreign Currency Denominated Bonds to Residents and Investing in Foreign Currency Denominated Bonds and Deposits(only Rupee Settlement)

In order to familiarise residents with holding foreign currency denominated assets with banks and corporates and providing them with opportunities to diversify their investments by taking currency risk, the Committee recommends that corporate residents may be permitted. to issue foreign currency denominated deposits/bonds. Simultaneously, corporates get the advantage of lower cost of foreign currency denominated funds while having to bear the exchange risk. No limit on such issuance/investments is recommended as it is expected that the corporates will issue such liabilities only to the extent they are able to or are willing to bear the exchange risk. As there is only rupee settlement, this measure will not result in any outflow of foreign exchange.

I.A.2 Financial Capital Transfers Including Opening Current/Chequeable accounts

The Committee recommends outflows up to US \$ 25,000 per annum in Phase I (with higher limits in subsequent phases) for financial capital outflows for resident individuals ([Paragraph IV.A.2](#)). Analogously, resident corporates could be allowed similar facilities.

I.A.3. Accessing Capital Markets Abroad through GDR/ADRs/ other Form of Equity Issues

At present, access to international capital markets through equity issues like GDRs, ADRs, etc., is permitted on a case by case basis by the Government and clearance is obtained from the RBI under FERA. While timing of the issue is crucial for the success of the issues, the approval process itself involves avoidable delay. The Committee is of the view that since all such issues are handled by merchant/investment bankers taking into account all factors including the rating of the corporate/country, prior approval by Government/ RBI is not necessary. Moreover, most of the international capital markets are regulated by securities regulators for investor protection and minimising systemic risk. The Committee therefore recommends that all restrictions on accessing international capital markets by resident corporates by way of GDRs/ ADRs/ other equity issues be removed subject to reporting such transactions not later than 30 days of the close of the issue.

I.A.4. External Commercial Borrowings (ECBs)

In order to keep the external debt of the country within sustainable limits, the Committee accepts that an overall ceiling on debt, albeit a flexible one, is necessary. The Committee is also aware that in order to implement the ceiling, the process of prior approval of such loans with a principle of queuing is unavoidable. The system of prior approvals should ensure that relatively smaller borrowers are not crowded out by a few very large borrowers. As in the case of equity issues, debt issues are syndicated/managed by international investment banks and the terms of issue, timing of borrowing, etc., are best left to the perception of the manager. The Committee recommends that in Phase 1, loans with average maturity of 10 years and above may be kept outside the ceiling for ECB. In the subsequent phases, the average maturity of loans for which ceiling on ECBs should not be applicable may be reduced to 7 years and above. The Committee recommends that all restrictions on end use of ECB should be removed for all ECBs.

I.A.5. Foreign Currency Convertible Bonds (FCCBs)/Floating Rate Notes (FRNs)

The Committee recommends that the policy governing ECBs should be applicable to FCCBs/FRNs, etc., and the ceiling on ECB should include those debt issues with average maturity below the periods recommended viz., 10 years in the first phase and 7 years thereafter.

I.A.6. Loans from Non Residents

The Committee has elsewhere ([Paragraph IV.A.3](#)) recommended that resident individuals could be allowed to avail of loans from non residents up to an amount of US \$ 250,000 (with increase in subsequent phases) in Phase I on repatriation basis with payment of interest at LIBOR. Analogously, the Committee recommends that corporates/businesses may be freely allowed to avail of loans from non residents up to US \$ 250,000 (with increase in subsequent phases) in Phase I on repatriation basis with payment of interest at LIBOR on similar lines as available to resident individuals.

I.A.7. Joint Ventures/Wholly Owned Subsidiaries(JV/WOS) Abroad

With the globalisation of the Indian economy, Indian enterprise should be encouraged to invest in joint ventures/wholly owned subsidiaries (JVs/ WOSs) abroad. At present, proposals involving Indian investment not exceeding US \$ 4 million fulfilling conditions relating to past export turnover accompanied by an undertaking for repatriation are cleared by RBI under the Fast Track Route within a period of 21 days. All other proposals which do not qualify for the Fast Track Route are cleared by a Special Committee constituted for this purpose by the RBI. An announcement was made in the recent Budget that funds in Exchange Earners Foreign Currency (EEFC) account can be used for making investment in overseas JVs/WOSs up to a limit of US \$ 15 million without reference to the RBI. The limits mentioned above include remittance from

India, capitalisation of export proceeds towards equity and giving loans/corporate guarantees to/on behalf of the Indian JVs/WOSs.

The Committee is of the view that in order that Indian industry is able to exploit opportunities on a global scale, there should be a substantial step up in the limit for investment by Indian industry in overseas businesses.

The Committee recommends that overseas investment up to US \$ 50 million could be cleared at the level of the ADs based on transparent and comprehensive guidelines set out by the RBI. Projects involving investment of over US \$ 50 million may go through a screening to be done by the Special Committee. The Committee recommends that the existing requirement of repatriation of the amount of the investment by way of dividend, technical know-how fee, etc., within a period of five years may be removed. Furthermore, JVs/WOSs could be allowed to be set up by all parties and not restricted only to exporters/exchange earners.

I.A.8. Project Exports

Indian project exporters are required to approach RBI for prior approval for a variety of purposes while executing projects abroad such as executing corporate guarantee at the bid or post award stage instead of providing bank guarantee, advance payment of commission instead of pro rata payment, inter-project transfer of funds, etc. The Committee recommends that requirement of RBI approval for various purposes while executing projects abroad should be dispensed with, subject to project exporters reporting the transactions to the RBI.

I.A.9. Establishment of Offices Abroad

Indian corporate entities may open offices/branches abroad without the need for prior approval from RBI. The published balance sheet of the company should reflect the operations of these branches/offices separately. The Committee recommends that the necessary amendments towards this end in the legislation be made expeditiously. Capital expenditure towards opening of the offices and current expenditure for maintenance could be subject to suitable overall value limits to be allowed by ADs.

I.A.10. EEFC accounts for Exporters/Exchange Earners

Under the present exchange control restrictions, exporters/exchange earners are allowed to retain their foreign exchange earnings not exceeding 25 per cent of such remittances. In the case of 100 per cent export oriented units or EPZ units, etc., amounts up to 50 per cent of the remittance can be credited to EEFC accounts. RBI permits individual exporters having good track records to credit a higher percentage of inward remittances i.e., in excess of 25 per cent/50 per cent as the case may be, to EEFC accounts to meet their foreign exchange requirements for imports. As long as the exchange earnings are retained in accounts in India to be used flexibly by the exchange earner/ exporter for all current/permitted capital transactions, the Committee recommends 100 per cent retention of exchange earnings in EEFC accounts for all exporters/exchange earners. The Committee recommends complete flexibility in the operation of these accounts including having cheque writing facility. It is essential to put in place a system of contemporaneous reporting to the RBI of the operations in the EEFC accounts. At a later phase of CAC, the restriction on maintaining EEFC accounts in India could be removed and exporters/exchange earners could be allowed to maintain such accounts with banks abroad. One of the members (Shri AN. Rajwade) was of the view that 100 per cent retention of earnings by exporters/exchange earners could be allowed only after the Phase I preconditions are met fully.

I.B. Corporates - Non Residents (including OCBs)

I.B.1. Foreign Direct Investment (FDI)

The Committee recognises that FDI is an engine of growth. In the context of a move towards CAC the Committee recommends that no prior RBI approval should be necessary for foreign direct investment/disinvestment. The Committee recommends that to encourage foreign direct investment, the guidelines for investment/disinvestment should be made transparent without complicated administrative clearances and without any requirement of any form of RBI

intervention. Towards this end, the Committee recommends that investors should be provided comprehensive and transparent guidelines for foreign direct investment in India.

I.B.2. Portfolio Investment in India through Stock Exchanges in Shares/Debentures

Currently, foreign equity holding in a company through the portfolio investment route is available for approved NRIs, OCBs & FIIs and should not exceed 24 per cent (can be increased to 30 per cent at the option of the company) of the equity of the company. This limit is monitored through a system of reporting by designated ADs and when such portfolio investments are moving towards the limit, a brake is applied. The sub-limits of holding by any individual FII, NRI or OCB are also monitored through this system. The Committee recommends that the portfolio investment route could be made available to all non residents through designated ADs without the need for prior approval of RBI. The designated ADs would continue to report to the RBI. The comprehensive and transparent guidelines referred to under I.B.1 above could also cover portfolio investment.

I.B.3. Disinvestment

Approval of disinvestment by the RBI could be dispensed with and there should only be reporting by the ADs. The Committee recommends that the guidelines on foreign direct investment and portfolio investment should also cover guidelines for disinvestment.

II. BANKS

II. A. Banks-Residents

II.A. 1. Loans and Borrowings from Overseas Banks and Correspondents Including Overdrafts in Nostro Accounts

At present each bank is permitted to borrow up to US \$ 10 million without any restriction on the use of such funds in India or its repayment. With a view to providing the banking system with greater opportunities to access/intermediate funds from abroad and bring about integration between overseas and domestic markets, the Committee recommends that banks may be allowed to borrow, both short-term (upto one year) and long-term (over one year), from the overseas markets to the extent of 50 per cent of their unimpaired Tier I capital in Phase I (with increase in subsequent phases) with a sub-limit of one-third of the overall limit for short term borrowings. In Phase II the overall limit may be increased to 75 per cent and in Phase III to 100 per cent of the unimpaired Tier I capital. While the prudential norms regarding open position and gap limits will also govern such borrowings, there should be no restrictions on the end-use and repayment of funds.

II.A.2 Investments in Overseas Markets

The Committee notes that Section 25 of the Banking Regulation Act, 1949 restricts the deployment of assets by way of loans or investments outside India to 25 per cent of a bank's demand and time liabilities. The Committee is of the view that other than this legal restriction, no restrictions need be placed on deployment of banks' funds outside India either by way of investments or loans. Investments may be made in overseas money markets, mutual funds and foreign securities. The ceiling under Section 25 would include investment in overseas markets made from foreign currency accounts maintained in their books in India. The bank's management may formulate a policy in this regard keeping in view the credit risk and prudential regulations relating to currency exposure and maturity mismatches. The policy should enunciate in detail the systems in place for managing various types of risks including credit risk, market risk, settlement risk, etc., so that the bank's management is aware of the likely loss that will devolve on the bank in a worst case scenario. As at present the open position and gap limit fixed by bank's management may be approved by RBI. Capital adequacy guidelines for cash and derivative instruments may be reviewed in keeping with international standards.

II.A.3. Fund Based/Non Fund Based Facilities to Indian Joint Ventures and Wholly Owned Subsidiaries Abroad

The Committee has proposed considerable liberalisation of the approval process for setting up

JVs/WOSs and is of the view that banks in India should be free to assist such ventures/ subsidiaries on the basis of their commercial judgment subject to only the restriction imposed under Section 25 of the Banking Regulation Act, 1949 as stated under paragraph II.A.2.

II.A.4. Buyers Credit/Acceptance for Financing Importer/their Bankers for Buying Goods and Services from India (including Financing of Overseas Projects)

Consistent with measures to provide sufficient flexibility to banks to intermediate forex flows, the Committee recommends that banks should be free to exercise their commercial judgment in providing buyers' credit/ acceptance facilities to importers/their banks for facilitating exports of goods and services from India (including financing of project exports). Banks should be free to extend such credit without approval from any authority subject only to the provisions of Section 25 of the Banking Regulation Act, 1949.

II.A.5. Accept Deposits and Extend Loans Denominated in Foreign Currencies from/to Individuals (only Rupee Settlement)

The Committee's proposal is analogous to the recommendation at paragraph I.A.1 viz., permitting corporates to issue/invest in foreign currency denominated assets where the settlement takes place in rupees. The Committee recommends that banks may be permitted to accept deposits from residents denominated in foreign currency as also to make advances to residents by way of foreign currency denominated loans for any purpose for which the banks normally give rupee loans. While no ceiling need be fixed for lending or for deposits, the currency/maturity mismatches will be taken into account for overall open position/gap limits.

II.A.6 Forfaiting

At present RBI has accorded approval only to EXIM Bank for forfaiting. The Committee recommends that all AD s should be freely permitted to undertake forfaiting.

II.B. Banks - Non Residents

II.B.1. Rupee Accounts of non resident banks

The Committee recommends a cautious approach in allowing non-resident banks to open accounts in India and invest/borrow in these accounts for arbitraging between markets. In Phase I, while the existing restrictions on opening/operating on such accounts to support merchant based activities may continue, the Committee recommends that the existing restrictions on forward cover to non resident banks could be removed and forward cover provided to the extent of the balances in these accounts. Furthermore, the present limit of Rs. 150 lakhs on overdrafts in such accounts could be increased commensurate with the business and investment facilities may also be provided to non resident banks in such accounts. In Phase III, non resident banks may be allowed to freely open rupee accounts with banks in India without any restrictions on their operations.

III. NON BANKS

III.A. Non Banks - Residents

III.A.1. SEBI registered Indian Investors(including Mutual Funds) Investments Overseas

In order to diversify the investment opportunities for residents, the Committee recommends that SEBI approved investors in India (including mutual funds) could be allowed to set up funds part/whole of which can be invested in overseas markets. Such funds could be open for subscription by all residents and may be subject to an overall ceiling of US \$ 500 million in Phase I with higher overall ceilings of US \$ 1 billion for Phase II and US \$ 2 billion for Phase III. The overall ceiling should be so operated that a few large funds do not pre-empt the overall amount. Individual fund clearances from the exchange control should be only for purposes of implementing the overall ceiling.

III.A.2. All India Financial Institutions (FIs)

At present long term borrowings by FIs have to be cleared by the Government. External commercial borrowings by FIs are also subject to the ceiling for ECB. The Committee recommends that the existing process may continue. To facilitate efficient funds management, the Committee recommends that the All India FIs may be allowed, without prior clearance from Government/RBI, to avail of overseas short term borrowings subject to certain limits and also be permitted to invest in short term instruments in overseas markets to the extent of liabilities maturing within one month in Phase I, three months in Phase II and six months in Phase III.

III.B. Non Banks - Non Residents

III.B.I. FIIs

(a) Portfolio Investment

Currently, approved FIIs are permitted portfolio investment provided such investment in any one company for all FIIs, NRIs and OCBs taken together does not exceed 24 per cent, the limit can be increased to 30 per cent at the option of the company. Consistent with the Committee's recommendation at I.B.2 above, the Committee recommends that the portfolio investment route could be made available freely to all non residents (including FIIs) through designated ADs without the requirement of prior approval from RBI, subject to reporting by the ADs.

(b) Primary Market Investment/Private Placement

At present FIIs who want to make private placement or enter the primary market are allowed to do so on a case by case approval by RBI subject to the 24 per cent limit for overall foreign equity holding (including NRIs, OCBs) in any company and specific limit of 15 per cent of each issue in case of private placement. Consistent with the Committee's recommendation for portfolio investment, the Committee recommends that prior RBI approval for FIIs' private placement/primary market investment may be dispensed with subject to reporting by the company.

(c) Disinvestment

The Committee recognises that although there is CAC on inflows by FIIs, prior approval from RBI is required for portfolio disinvestment where such disinvestment is not on the basis of the quoted prices for listed shares. The Committee recommends that disinvestment may be undertaken on the basis of comprehensive and transparent disinvestment guidelines referred to earlier subject to reporting by ADs and the requirement of exchange control approval for disinvestment should be dispensed with.

(d) Investment in Debt Instruments

FIIs in general can invest in equity and debt in the ratio of 70:30. In 1996-97, approved FIIs were allowed to set up funds to be invested exclusively in debt instruments listed on the stock exchange. Recently, approved debt funds of FIIs have also been permitted to invest in Government dated securities. The total of such investments is, however, subject to the overall ceiling for ECB and therefore specific approvals are given for such investments, not exceeding certain limits. Moreover, there are restrictions placed on investments in Treasury bills.- The Committee recommends that all maturity restrictions on debt instruments including Treasury bills be removed and furthermore that while FII investment in- rupee debt instruments could be subject to an overall ceiling, such a ceiling should be distinct and separate from the ECB ceiling.

IV. INDIVIDUALS

IV.A. Individuals - Residents

IV.A.1. Foreign Currency Denominated Deposits with Banks/ Corporates in India (only Rupee Settlement)

As indicated under I.A. 1 and II.A.5, in order to familiarise residents with having foreign currency denominated assets/liabilities, the Committee recommends the introduction. of foreign currency denominated deposits with banks and corporates and obtaining foreign currency denominated

loans from banks. Since the settlement takes place in rupees, the Committee is of the view that no limit on such deposits is necessary. The facility would enable residents to take a view on the future movement of currencies vis-a-vis interest rates

IV.A.2 All Other Financial Capital Transfers including for Opening, Current/Chequeable Accounts

The Committee recommends that in Phase 1, individual residents be permitted to invest in assets in financial markets abroad up to US \$ 25,000 per annum (with higher limits in subsequent phases), thus providing them the freedom of an additional avenue- for their personal savings. This will send a salutary signal regarding the country's commitment to CAC. One of the members of the Committee, Shri A.V. Rajwade, was not in favour of permitting financial outflows by resident individuals, resident corporates ([Paragraph I.A.2](#)) and non resident individuals out of their non repatriable assets ([Paragraph IV.B. 1](#)) until the preconditions set out for the first phase of CAC are met. Furthermore, he stressed that significant improvements need to be effected in the collection of data to allow a proper assessment of market conditions. Another member, Dr. S.S. Bhalla, held a contrary view and in his assessment the macro economic situation was unprecedentedly strong. In fact he felt that as the country is likely to continue to experience large capital inflows better macro and exchange rate management would be facilitated if individual residents were allowed outflows with significantly larger limits. Taking into account the divergent viewpoints the Committee recommends that such outflows by resident individuals should be permitted, up to US \$ 25,000 per annum in Phase I and with the progressive entrenchment of preconditions/signposts recommended by it, these limits could be gradually increased to US \$ 50,000 per annum in Phase II and to US \$ 100,000 in Phase III.

IV.A.3 Loans from Non Residents

At present, individual residents are permitted to obtain loans from non resident relatives for personal or business purposes on an interest free non repatriation basis. Such loans cannot be used for purposes of investments by the resident. In the context of CAC, such conditions are too restrictive and the Committee recommends that resident individuals should be free to obtain loans up to US \$ 250,000 in Phase I (with increase in subsequent phases) from non resident individuals on repatriation basis at LIBOR without any restriction on the use of funds and without any prior approval from RBI.

IV.B. Individuals : Non Residents

IV.B.1. Capital Transfers from Non Repatriable Assets held in India (including NRO & NRNRD Accounts)

Currently, non residents are not allowed any capital transfers out of their assets in India other than out of investments made by them on repatriation basis. The Committee considered the question of permitting non resident individuals to effect capital transfers out of their non repatriable assets in India. Consistent with the view taken by it in regard to capital outflows for resident individuals ([Paragraph IV.A.2](#)) the Committee recommends that capital outflows up to identical annual limits may be allowed out of non repatriable assets of non residents.

At present, under the Non Resident Non Repatriable Rupee Deposit Account (NRNRD) scheme the principal is non repatriable, but with the introduction of current account convertibility interest is freely repatriable. The continuation of such a scheme is incongruous with CAC and the Committee recommends this scheme should be terminated in Phase 1. The funds under the existing NRNRD scheme would get merged with other non repatriable assets on maturity. In order to give an incentive to NRNRD. account holders, the Committee recommends that in case the maturity proceeds of the NRNRD accounts are placed in a special three year NRE account (without facility of premature withdrawal) the non resident may be allowed to repatriate the full amount of such deposits on maturity.

IV.B.2. Foreign Direct Investment (FDI) in India(other than in Real Estate)

As in the case of FDI by non resident corporates, FDI by non resident individuals should be without prior RBI approval but subject only to reporting by ADs. The Committee is of the view

that in the matter of FDI no distinction need be made between non resident Indians and other non residents. It, therefore, recommends that all direct investments/disinvestments by non resident individuals may be governed by the comprehensive and transparent guidelines on foreign investment (direct and portfolio) and may be freed of all restrictions from exchange control, subject to reporting through ADs.

IV.B.3. Portfolio Investment in India through Stock Exchanges

The recommendations made by the Committee in regard to portfolio investments in India by non resident OCBs ([Paragraph I.B.2](#)) and FIIs ([Paragraph III.B.1](#)) should be applicable to non resident individuals as well and be governed by the comprehensive guidelines referred to elsewhere.

IV.B.4. Disinvestment

Consistent with the recommendations made that all foreign investments/ disinvestments in India be freed from exchange control, the Committee recommends that disinvestment by non resident individuals need not be subject to approval by RBI/exchange control and can be freely allowed in terms of the comprehensive guidelines referred to above.

V. FINANCIAL MARKETS

The role of the financial markets in the context of CAC has been elaborated in Chapter 111. Well developed financial markets are essential to provide efficient transmission mechanisms for monetary and exchange rate policies and to even out varying market sentiment enabling the arbitrageurs to play their full role in stabilising the volatility arising out of internal/external shocks. Development of deep and liquid financial markets also enable the development of the derivatives market based on the underlying cash market. Towards developing financial markets, the Committee recommends the following specific measures:

V.1. Foreign Exchange Market

(a) Forward Markets

The Committee recommends that in Phase I, all participants in the spot market should be permitted to operate in the forward market; FIIs, non residents and non resident banks having rupee assets may be allowed forward cover (with right of cancelling and rebooking) to the extent of their assets in India. This measure will facilitate two-way expectations to emerge in the market, reducing the need for RBI intervention. Allowing banks in India to make two-way quotes in rupees to overseas branches/banks/ correspondents will signal a step towards CAC. Those having economic exposures may be allowed to participate in the forward market. Restrictions on participation in spot/forward markets, i.e., in terms of underlying actual or economic exposure may be removed in Phase III.

(b) Authorised Dealers

Currently, only banks are allowed to operate as full-fledged ADs. In order to have larger number of market makers who actively give two way quotes and correct the present skewed market, the Committee recommends that All India FIs which comply with well defined criteria and fulfill prescribed prudential/regulatory requirements should be allowed to participate in the forex market as full-fledged ADs even in Phase I. In Phase III, other non bank entities fulfilling criteria similar to those prescribed for FIs could be permitted to become full-fledged ADs.

(c) Products

For long, the forward contract was the only hedging instrument available to cover exchange risk. Even this product is available in the Indian market only for periods up to six months. The monetary and credit policy of April 15, 1997 has announced several measures to facilitate development of the money market and long-term forward market. In view of this and concomitant with other measures for evolving a smooth yield curve, there is scope for introduction of rupee based derivatives. The Committee, recognising the fact that the market will evolve a variety of hedging products, recommends that proper risk management systems should be in place before

allowing ADs to start trading in derivatives. Simultaneously, capital requirements for market risk for derivatives on the lines of internationally accepted principles should be introduced by the RBI. In this connection, the recommendations made by the Expert Group on Foreign Exchange Markets (Chairman: Shri O.P.Sodhani) may be reviewed and implemented. Currently, corporates are allowed to use derivatives for hedging their currency/interest rate exposures through ADs in India and are not allowed to access overseas markets directly. The Committee recommends that in Phase 11, corporates may be allowed to access overseas markets directly for derivatives without routing such transactions through ADs in India. Reporting requirement should, however, continue.

The Committee is of the view that the time is ripe for introduction of futures in currencies and interest rates to facilitate various users to have access to a wide spectrum of cost efficient hedge mechanism. Alongside the introduction of futures, the Committee is of the view that it may be worthwhile to institute a system of trading in futures which is more transparent and cost efficient than the existing system of trading in forex markets. An ideal system of trading in futures would be one which permits greater transparency by displaying on the screen the demand and supply at various rates to all participants at any given moment, but at the same time, preserving the anonymity of the counterparties. A trader who intends to enter the market enters his quote/quantum after having a look at the ongoing display of quotes. The computer then proceeds to match the quotes and orders and finalises the deal. Such a system is employed by the National Stock Exchange for equity/ debt trading. A trading system of this kind needs the support of an efficient clearing and payment settlement mechanism. The Committee, therefore, recommends that futures trading should be introduced on a screen-based system with back-up support of an efficient settlement system.

V.2. Money Market

The money market, in its existing form, suffers from a considerable degree of segmentation. The banks, FIs and mutual funds are subjected to different norms regarding borrowing and lending. In the interest of developing greater depth and liquidity in money markets, the Committee recommends that such segmentation should be given up simultaneous with introduction of uniform reserve requirement prescriptions for banks and non banks. The financial institutions and non bank entities may be permitted entry in the money market subject to exacting prudential regulations. The RBI should issue prudential guidelines in regard to asset liability mismatches in rupee books of banks and non banks. Various market regulators should jointly examine the feasibility of introducing transparent and cost efficient trading systems. As a further measure of development of the money market, all interest rates should be totally deregulated, minimum period restrictions removed and restriction on entry of participants should be totally removed. Participants in the money market at the wholesale and retail level should be distinguished only by the size of transactions.

V.3 Government Securities Markets

The Committee is of the view that in India, the development of a deep and liquid securities market across all maturities is a *sine qua non* for development of a consistent yield curve. Without development of a well defined rupee yield curve, with sufficient liquidity across maturities, the development of derivatives markets in forex and rupees would be constrained. Several measures have been announced in the monetary and credit policy of April 15, 1997 for development of the money, forex and securities markets. The Committee's recommendations for development of the securities market as indicated in the tabulated list of measures are based on (i) increasing role of primary dealers and satellite dealers, (ii) the RBI withdrawing from the primary market in stages with active presence in the secondary market, (iii) setting up of an Office of the Public Debt (OPD) by Government which will eventually assume full responsibility for the management of public debt including timing and amount of primary issue of all Government securities, (iv) the RBI providing a Liquidity Adjustment Facility to Primary Dealers (PDs) through repos/reverse repos. The Liquidity Adjustment Facility would provide for a corridor within which market rates would be able to move without undue volatility and would facilitate formation of a consistent yield curve, (v) strong and exclusive fiscal incentives for dedicated gilt funds to encourage effective retailing of government securities, (vi) totally automated real time gross settlement through the DVP system for government securities, (vii) allowing FIIs in the Treasury bill market and (viii) introduction of futures in all Government securities.

V.4 Development of the Gold Market

It is essential to liberalise the policy on gold while simultaneously taking steps to develop a transparent and well regulated gold market with integrated links with other financial markets to ensure a successful move towards CAC. The main ingredients of the change in policy on gold could be :

- (i) Removal of restrictions on imports/exports of gold, which *inter alia* would diminish hoarding by ready availability of gold in India.
- (ii) Development of gold related products/financial instruments.
- (iii) Development of markets in physical as well as financial gold in India which could be made use of by both residents and non-residents.
- (iv) Encouragement for the active role of banks and other non bank financial entities in the gold market.

The Committee recognises that the recommendations imply a major change in the policy in relation to gold and that full operative details would need to be worked out for implementation of these recommendations. In this context, the Committee is of the view that it would be useful to study the gold financing schemes and measures for fostering markets in Italy, Turkey and Malaysia.

The Committee recommends that in Phase I banks and financial institutions fulfilling well-defined criteria may be allowed to operate freely both in the domestic and the international markets in gold. Sale of gold by banks and financial institutions should be allowed freely to all residents. The Committee also recommends that all banks may be allowed to offer gold-linked deposits and loans on the lines of foreign currency linked rupee deposits and loans for residents recommended in [Paragraph II.A.5](#). Banks fulfilling certain well-defined criteria may be allowed to mobilise household gold for providing working capital gold loans to jewellery manufacturers as also traders. Banks may also be encouraged to grant loans against gold denominated deposits.

In Phase II, steps should be taken by Government of India and RBI for developing a well-regulated market in India for gold and gold derivatives including forward trading. Both residents and non residents may be allowed to operate in this market, subject to adherence to certain well-defined guidelines.

V.5 Participation in International Commodity Markets

At present residents are not permitted to participate in International Commodity Exchanges. In the context of globalisation, it is necessary to provide residents the same facility as that enjoyed by non residents. Participation in Commodity Exchanges helps participants to hedge their price risk as also provide a mechanism for "price discovery". Allowing such facilities to residents will reduce the volatility of prices.

Concluding Observations

4.9 The Committee underscores the critical importance of monitoring information on various types of capital flows and stocks. The establishment of a comprehensive database encompassing regular reporting of accurate information on capital transactions by ADs as well as by other entities dealing in foreign exchange for capital transactions should be accorded the highest priority by the RBI and in this context an expeditious revamping of the statistical information system should be undertaken.

4.10 While CAC to some extent privatises decisions relating to foreign assets, in order to ensure tax compliance, it is necessary for India to institute arrangements with other countries for sharing tax information on a multilateral basis, akin to the agreement negotiated by the OECD countries.

4.11 Taking into account the sizeable adjustments in terms of the preconditions which would be required in various sectors, principally the fisc and the financial sector, the Committee recommends a phased approach to CAC in India. With a view to implementing the opening up of the capital account without deleterious consequences and erosion of credibility because of any backtracking on the timing and sequencing of measures set out in this Chapter, the Committee recommends that the RBI should ensure ongoing monitoring of policies undertaken to entrench the preconditions/signposts and also ensure that measures on the phased move towards CAC are carefully implemented. The phased programme outlined here could be accelerated or decelerated depending on the performance vis-a-vis the preconditions/ signposts.

4.12 The Committee recognises that even after the third phase is completed, capital controls on a number of items would continue to be necessary. The Committee recommends that at the end of the three year phasing, a stock taking of the progress on the preconditions/signposts as well as the impact of the measures outlined by the Committee should be undertaken. CAC is a continuous process and further measures could be undertaken in the light of the experience gained.