Report of the Central Board of Directors on the working of the Reserve Bank of India for the year ended June 30, 2015 submitted to the Central Government in terms of Section 53(2) of the Reserve Bank of India Act, 1934

RESERVE BANK OF INDIA ANNUAL REPORT 2014-15

भारतीय रिज़र्व बैंक
RESERVE BANK OF INDIA
www.rbi.org.in

LETTER OF TRANSMITTAL

Ref. No.SYD.720/02.16.001/2015-16

August 27, 2015
Bhadra 5, 1937 (Saka)

The Finance Secretary
Government of India
Ministry of Finance
New Delhi – 110 001

Dear Sir,

In pursuance of Section 53(2) of the Reserve Bank of India Act, 1934, I have the pleasure in transmitting the following documents:

(i) A copy of the Annual Accounts for the year ended June 30, 2015 signed by me, the Deputy Governors and the Chief General Manager, and certified by the Bank's Auditors; and

(ii) Two copies of the Annual Report of the Central Board on the working of the Bank during the year ended June 30, 2015.

Yours faithfully

Sd/-

(Raghuram G. Rajan)

CENTRAL BOARD / LOCAL BOARDS

GOVERNOR

Raghuram G. Rajan

DEPUTY GOVERNORS

Harun R. Khan

Urjit R. Patel

R. Gandhi

S.S. Mundra

DIRECTORS NOMINATED UNDER SECTION 8 (1) (b) OF THE RBI ACT, 1934

Anil Kakodkar

Kiran S. Karnik

Nachiket M. Mor

DIRECTORS NOMINATED UNDER SECTION 8 (1) (c) OF THE RBI ACT, 1934

Y. H. Malegam

Dipankar Gupta

G. M. Rao

Ela Bhatt

Indira Rajaraman

Y.C. Deveshwar

Damodar Acharya

DIRECTORS NOMINATED UNDER SECTION 8 (1) (d) OF THE RBI ACT, 1934

Hasmukh Adhia

Ajay Tyagi

MEMBERS OF LOCAL BOARDS

WESTERN AREA

Kiran S. Karnik

EASTERN AREA

Nachiket M. Mor

Anila Kumari

Sharif Uz-zaman Laskar

NORTHERN AREA

Anil Kakodkar

A. Naveen Bhandary

SOUTHERN AREA

K. Selvaraj

Kiran Pandurang

PRINCIPAL OFFICERS

(As on August 13, 2015)

EXECUTIVE DIRECTORS	Deepak Mohanty
	P. Vijaya Bhaskar
	Jasbir Singh
	Deepali Pant Joshi
	N.S. Vishwanathan
	U.S. Paliwal
	Chandan Sinha
	Michael D. Patra
	K.K. Vohra
	G. Mahalingam
	Meena Hemchandra
CENTRAL OFFICE	
Central Vigilance Cell	Surekha Marandi, Chief Vigilance Officer
Consumer Education and Protection Department	Arun Pasricha, Chief General Manager
Corporate Strategy and Budget Department	Saurav Sinha, Chief General Manager
Department of Banking Regulation	Sudarshan Sen, Principal Chief General Manager
Department of Banking Supervision	Parvathy Sundaram, Chief General Manager-in-Charge
Department of Communication	Alpana Killawala, Principal Press Relations Officer
Department of Co-operative Bank Regulation	Suma Varma, Principal Chief General Manager
Department of Co-operative Bank Supervision	Malvika Sinha, Principal Chief General Manager
Department of Corporate Services	J.L. Negi, Chief General Manager
Department of Currency Management	Uma Shankar, Principal Chief General Manager
Department of Economic and Policy Research	B.M. Misra, Principal Adviser
Department of External Investments and Operations	S.K. Bal, Chief General Manager-in-Charge
Department of Government and Bank Accounts	M. Sarkar Deb, Chief General Manager-in-Charge
Department of Information Technology	S. Ganeshkumar, Chief General Manager-in-Charge
Department of Non-Banking Regulation	C.D. Srinivasan, Chief General Manager
Department of Non-Banking Supervision	Sathyan David, Chief General Manager
Department of Payment and Settlement Systems	Nanda Dave, Chief General Manager
Department of Statistics and Information Management	G. Chatterjee, Officer-in-Charge
Financial Inclusion and Development Department	A. Udgata, Principal Chief General Manager
Financial Markets Operations Department	M. Rajeshwar Rao, Chief General Manager
Financial Markets Regulation Department	R. Subramanian, Chief General Manager
Foreign Exchange Department	B.P. Kanungo, Principal Chief General Manager
Financial Stability Unit	S. Rajagopal, Chief General Manager
Human Resource Management Department	R.L. Das, Chief General Manager-in-Charge
Inspection Department	B.P. Vijayendra, Principal Chief General Manager
Internal Debt Management Department	R.G. Warriar, Chief General Manager
International Department	M.K. Saggar, Adviser
Legal Department	Mona Anand, Legal Adviser-in-Charge
Monetary Policy Department	B.K. Bhoi, Principal Adviser
Premises Department	Arvind Sharma, Chief General Manager-in-Charge
Rajbhasha Department	Ramakant Gupta, General Manager
Risk Monitoring Department	A.K. Misra, Chief General Manager
Secretary's Department	S.K. Maheshwari, Chief General Manager
COLLEGES	**PRINCIPALS**
College of Agricultural Banking, Pune	P.K. Panda
Reserve Bank Staff College, Chennai	Uma Subramaniam
OFFICES	**REGIONAL DIRECTORS**
Chennai	J. Sadakkadulla
Kolkata	R.N. Kar
Mumbai	S. Ramaswamy
New Delhi	Deepak Singhal
BRANCHES	
Ahmedabad	P.C. Sahoo
Bengaluru	E.E. Karthak
Bhopal	Ajay Michyari
Bhubaneswar	P.K. Jena
Chandigarh	Rashmi Fauzdar
Dehradun	R.L. Sharma
Guwahati	S.S. Barik
Hyderabad	R.N. Dash
Jaipur	Arnab Roy
Jammu	D. Sethy
Kanpur	Shekhar Bhatnagar
Lucknow	Supriya Pattnaik
Nagpur	J.M. Jivani
Patna	M.K. Verma
Raipur	Saraswati Shyamaprasad
Shimla	I.S. Negi
Thiruvananthapuram	Nirmal Chand
	OFFICERS-IN-CHARGE
Agartala	N.P. Topno, General Manager (O-i-C)
Belapur	S.N. Panda, Chief General Manager
Gangtok	Manabendra Misra, General Manager (O-i-C)
Kochi	U. Chiranjeevi, General Manager (O-i-C)
Panaji	Jaikish, General Manager (O-i-C)
Ranchi	Patric Barla, General Manager (O-i-C)
Shillong	Amar Nath, General Manager (O-i-C)
Srinagar	Satish Sharma, Assistant General Manager (O-i-C)

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APPENDIX TABLES

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LIST OF ABBREVIATIONS

AAY - Antyodaya Anna Yojana

ABCI - Association of Business Communications of India

ACB - Audit Committee of Board

AD - Authorised Dealer

ADF - Asset Development Fund

ADF - Automated Data Flow

ADR - American Depository Receipts

AEs - Advanced Economies

AFA - Additional Factor of Authentication

AFCs - Asset Finance Companies

AIFIs - All India Financial Institutions

AMS - Audit Management System

ANBC - Adjusted Net Bank Credit

APL - Above Poverty Line

APMC - Agricultural Produce Marketing Committee

APMS - Asset Price Monitoring System

ARCs - Asset Restructuring Companies

ARMS - Audit and Risk Management Sub-Committee

ATBs - Auction Treasury Bills

ATM - Automated Teller Machine

BAs - Business Areas

BBPCU - Bharat Bill Payment Central Unit

BBPOU - Bharat Bill Payment Operating Unit

BBPS - Bharat Bill Payment System

BC - Business Correspondent

BCBS - Basel Committee on Banking Supervision

BCM - Bank for Currency Management

BCM - Business Continuity Management

BCSBI - Banking Codes and Standards Board of India

BE - Budget Estimates

BFS - Board for Financial Supervision

BIS - Bank for International Settlements

BLRC - Bankruptcy Law Reform Committee

BO - Banking Ombudsman

BoJ - Bank of Japan

BoP - Balance of Payments

BPL - Below Poverty Line

BPLR - Benchmark Prime Lending Rate

BPR - Business Process Re-engineering

bps - Basis Points

BPSS - Board for Regulation and Supervision of Payment and Settlement Systems

BRBNMPL - Bharatiya Reserve Bank Note Mudran Private Ltd.

BRICS - Brazil, Russia, India, China and South Africa

BSBD - Basic Savings Banking Deposit

BSBDAs - Basic Savings Bank Deposit Accounts

BSR - Basic Statistical Return

CAB - College of Agricultural Banking

CAD - Current Account Deficit

CAFRAL - Centre for Advanced Financial Research and Learning

CAMELS - Capital Adequacy, Asset Quality, Management, Earnings, Liquidity, Systems and Control

CAP - Corrective Action Plan

CARG - Compound Annual Rate of Growth

CBLO - Collateralised Borrowing and Lending Obligation

LIST OF ABBREVIATIONS

CBS - Core Banking Solution
CBSE - Central Board of Secondary Education
CBSL - Central Bank of Sri Lanka
CCB - Committee of the Central Board
CCC - Central Complaints Committee
CCCB - Counter-Cyclical Capital Buffer
CCIL - Clearing Corporation of India Ltd
CCP - Central Counter Party
CCS - Credit Condition Survey
CCSO - Chief Customer Service Officer
CD - Certificate of Deposit
C-D - Credit-Deposit
CDR - Corporate Debt Restructuring
CDS - Credit Default Swaps
CEOBE - Credit Equivalent Amount of Off-Balance Sheet Exposure
CEPD - Consumer Education and Protection Department
CERSAI - Central Registry of Securitisation Asset Reconstruction and Security Interest of India
CES - Consumer Expenditure Survey
CFs - Capital Funds
CGFs - Committee of Global Financial System
CGRA - Currency and Gold Revaluation Account
CGTMSE - Credit Guarantee Trust for Micro and Small Enterprises
CHRS - Comprehensive Human Resource System
CICs - Credit Information Companies
CICs - Core Investment Companies
CIL - Coal India Limited
CIS - Collective Investment Schemes
CISO - Chief Information Security Officer
CIT - Cash in Transit
CLSS - Credit Linked Subsidy Scheme
CMBs - Cash Management Bills
CMD - Chairman and Managing Director
CODs - Central Office Departments
CP - Commercial Paper
CPC - Cash Processing Centre
CPC - Cheque Processing Centre
CPI - Consumer Price Index
CPI-AL - Consumer Price Index-Agricultural Labourers
CPI-C - Consumer Price Index - Combined
CPIS - Co-ordinated Portfolio Investment Survey
CPMI - Committee on Payments and Market Infrastructure
CRA - Contingent Reserve Arrangement
CRAR - Capital to Risk-Weighted Assets Ratio
CRILC - Central Repository of Information on Large Credits
CRR - Cash Reserve Ratio
CS - Currency Swaps
CSBD - Corporate Strategy and Budget Department
CSF - Consolidated Sinking Fund
CSO - Central Statistics Office
CTS - Cheque Truncation System
CVA - Credit Valuation Adjustment
CVMs - Coin Vending Machines
DBIE - Database on Indian Economy
DBR - Department of Banking Regulation
DBS - Department of Banking Supervision

LIST OF ABBREVIATIONS

DBT - Direct Benefit Transfer
DCBR - Department of Co-operative Bank Regulation
DCBS - Department of Co-operative Bank Supervision
DCC - Dynamic Currency Conversion
DCCBs - District Central Co-operative Banks
DCCO - Date of Commencement of Commercial Operations
DCM - Department of Currency Management
DCs - Data Centres
DCS - Department of Corporate Services
DEA - Depositor's Education and Awareness
DEIO - Department of External Investments and Operations
DEPR - Department of Economic and Policy Research
DGBA - Department of Government and Bank Accounts
DGCIS - Directorate General of Commercial Intelligence and Statistics
DICGC - Deposit Insurance and Credit Guarantee Corporation
DIF - Deposit Insurance Fund
DIMU - Data and Information Management Unit
DIT - Department of Information Technology
DNBR - Department of Non-Banking Regulation
DNBS - Department of Non-Banking Supervision
DoC - Date of Commissioning
DoC - Department of Communication
DOLS - Dynamic Ordinary Least Square
DPSS - Department of Payment and Settlement Systems
DRG - Development Research Group
DRHP - Draft Red Herring Prospectus
DRTs - Debt Recovery Tribunals
D-SIBs - Domestic Systemically Important Banks
DSIM - Department of Statistics and Information Management
EBT - Electronic Benefit Transfer
ECA - Essential Commodities Act
ECB - European Central Bank
ECB - External Commercial Borrowing
ECCS - Express Cheque Clearing System
ECF - Economic Capital Framework
ECR - Export Credit Refinance
ECS - Electronic Clearing Service
EDMS - Electronic Data Management System
EDPMS - Export Data Processing and Monitoring System
EKP - Enterprise Knowledge Portal
email - Electronic mail
EMDEs - Emerging Market and Developing Economies
EME - Emerging Market Economy
EMV - Europay, MasterCard and Visa
EOI - Expression of Interest
EPC - Engineering, Procurement and Construction
ERE - Exchange Rate Elasticity
ERM - Enterprise-wide Risk Management
ETCD - Exchange Traded Currency Derivatives
EU - European Union

LIST OF ABBREVIATIONS

EWS - Early Warning System
EXIM Bank - Export Import Bank
FAO - Food and Agriculture Organisation
FAQs - Frequently Asked Questions
FBIL - Financial Benchmarks India Pvt. Ltd
FCA - Foreign Currency Assets
FCCBs - Foreign Currency Convertible Bonds
FCI - Food Corporation of India
FCNR(B) - Foreign Currency Non Resident (Bank) Account
FCRA - Foreign Currency Revaluation Account
FCs - Financial Conglomerates
FCVA - Forward Contracts Valuation Account
FCY - Foreign Currency
FDI - Foreign Direct Investment
FDIC - Federal Deposit Insurance Corporation
FED - Foreign Exchange Department
FEDAI - Foreign Exchange Dealers' Association of India
FEMA - Foreign Exchange Management Act
FI - Financial Institution
FIAC - Financial Inclusion Advisory Committee
FICN - Fake Indian Currency Notes
FIDD - Financial Inclusion and Development Department
FII - Foreign Institutional Investor
FIMMDA - Fixed Income Money Market and Derivatives Association of India
FIP - Financial Inclusion Plan
FIPB - Foreign Investment Promotion Board
FIT - Flexible Inflation Targeting
FLCs - Financial Literacy Centers
FMCG - Fast-Moving Consumer Goods
FMD - Financial Markets Department
FMIs - Financial Market Infrastructures
FMOD - Financial Markets Operations Department
FMRD - Financial Markets Regulation Department
FOREX - Foreign Exchange
FPAS - Forecasting and Policy Analysis System
FPI - Foreign Portfolio Investment
FPOs - Follow on Public Offers
FRA - Financial Resolution Authority
FRA - Forward Rate Agreement
FRBM Act - Fiscal Responsibility and Budget Management Act
FSAP - Financial Sector Assessment Programme
FSB - Financial Stability Board
FSDC - Financial Stability and Development Council
FSLRC - Financial Sector Legislative Reforms Commission
FSR - Financial Stability Report
FSU - Financial Stability Unit
FSWM - Financially Sound and Well Managed
FTP - Foreign Trade Policy
FVCIs - Foreign Venture Capital Investors
FWG - Framework Working Group
FX - Foreign Exchange
GBP - Great British Pound
GCC - General Credit Card
GDP - Gross Domestic Product
GDR - Global Depository Receipts

LIST OF ABBREVIATIONS

GFCE - Gross Final Consumption Expenditure
GFCF - Gross Fixed Capital Formation
GFD - Gross Fiscal Deficit
GIFT - Gujarat International Finance Tech-City
GJRHRS - Golden Jubilee Rural Housing Refinance Scheme
GMM - Generalised Method of Moments
GNDI - Gross National Disposable Income
GoI - Government of India
GRA - Gold Revaluation Account
GRF - Guarantee Redemption Fund
GRQ - General Review of Quotas
GSDP - Gross State Domestic Product
G-Secs - Government Securities
G-SIBs - Global Systemically Important Banks
G-SII - Global Systemically Important Insurer
GST - Goods and Services Tax
GVA - Gross Value Added
GVC - Global Value Chains
HFA - Housing for All
HFCs - Housing Finance Companies
HPI - House Price Index
HQLAs - High Quality Liquid Assets
HRMD - Human Resource Management Department
HTM - Held to Maturity
HUF - Hindu Undivided Family
IADI - International Association of Deposit Insurers
IAERM - Internal Audit and Enterprise Risk Management
IBA - Indian Banks' Association
IBL - Inter-Bank Liabilities
IBS - International Banking Statistics
IBU - IFSC Banking Unit
ICBA - Inter-Central Bank Agreement
ICDR - Issue of Capital and Disclosure Requirements
ICSD - International Central Security Depositories
ICT - Information and Communication Technology
IDFC - Infrastructure Development Finance Company
IDMD - Internal Debt Management Department
IDPMS - Import Data Processing and Monitoring System
IESH - Inflation Expectation Survey of Households
IFC - Indian Financial Code
IFCs - Infrastructure Finance Companies
IFRS - International Financial Reporting Standards
IFSC - International Financial Services Centre
IGIDR - Indira Gandhi Institute of Development Research
IIBM - Indian Institute of Bank Management
IIFC - India Infrastructure Finance Company
IIP - Index of Industrial Production
IIWG - Investment and Infrastructure Working Group
ILO - International Labour Organisation
IMD - India Meteorological Department
IMF - International Monetary Fund
IMPS - Immediate Payment Service

LIST OF ABBREVIATIONS

INR - Indian Rupee
InvITs - Infrastructure Investment Trusts
IOD - Indian Ocean Dipole
IORWG - International Operational Risk Working Group
IOS - Industrial Outlook Survey
IOSCO - International Organisation of Securities Commission
IP - Internet Protocol
IPOs - Initial Public Offerings
IPv6 - Internet Protocol Version 6
IRA - Investment Revaluation Account
IRDA - Insurance Regulatory and Development Authority
IRF - Inter-Regulatory Forum
IRFs - Interest Rate Futures
IRS - Interest Rate Swap
IRS - Incident Reporting System
IRTG - Inter-Regulatory Technical Group
IS - Information System
ISHUP - Interest Subsidy Scheme for Housing the Urban Poor
ISOC - Information Security Operations Centre
ISS - Integrated Security System
IT - Inflation Targeting
IT - Information Technology
IT-BPO - Information Technology-Business Process Outsourcing
ITBs - Intermediate Treasury Bills
ITF - Implementation Task Force
IT-PAN - Income Tax-Permanent Account Number
ITSC - Information Technology Sub Committee
JLF - Joint Lenders Forum
JLGs - Joint Liability Groups
JV - Joint Venture
KCC - Kisan Credit Card
KRA - Key Result Area
KYC - Know Your Customer
LABs - Local Area Banks
LAF - Liquidity Adjustment Facility
LBMA - London Bullion Market Association
LCR - Liquidity Coverage Ratio
LE - Large Exposure
LEI - Legal Entity Identifier
LLPs - Liability Partnership Companies
LOBOM - Lower of Book or Market Value
LOLR - Lender of Last Resort
LOU - Local Operating Unit
LPA - Long Period Average
LPG - Liquefied Petroleum Gas
LR - Leverage Ratio
LRS - Liberalised Remittance Scheme
LSE - London School of Economics
LTV - Loan to Value Ratio
M3 - Money Supply
MAT - Minimum Alternate Tax
MCA - Ministry of Corporate Affairs
MD - Managing Director
MDR - Merchant Discount Rate
MEIS - Merchandise Exports from India Scheme
MEP - Minimum Export Price
MFI - Micro Finance Institution

LIST OF ABBREVIATIONS

MGNREGA - Mahatma Gandhi National Rural Employment Guarantee Act

MI - Market Intelligence

MIBOR - Mumbai Interbank Offer Rate

MICR - Magnetic Ink Character Recognition

MIS - Management Information System

MMLR - Market Maker of Last Resort

MMRP - Modified Mixed Reference Period

MMS - Mail Messaging System

MNOs - Mobile Network Operators

MoSPI - Ministry of Statistics and Programme Implementation

MoU - Memorandum of Understanding

MPC - Monetary Policy Committee

MPD - Monetary Policy Department

MPR - Monetary Policy Report

MSEs - Micro and Small Enterprises

MSF - Marginal Standing Facility

MSMEs - Micro, Small and Medium Enterprises

MSPs - Minimum Support Prices

MT - Million Tonnes

MT - Metric Tonne

MTM - Mark to Market

MTSS - Money Transfer Service Scheme

MUDRA - Micro Units Development Refinance Agency

MW - Mega Watt

NAB - New Arrangements to Borrow

NABARD - National Bank for Agriculture and Rural Development

NACH - National Automated Clearing House

NAV - Net Asset Value

NBFC - Non-Banking Financial Company

NBFC-MFI - NBFC-Micro Finance Institution

NBFCs-D - Deposit-taking NBFCs

NBFCs-ND - Non-Deposit taking NBFCs

NBFCs-ND-SI- Systemically Important NBFCs-ND

NBV - Net Book Value

NCBs - Non-Cooperative Borrowers

NCDs - Non-Convertible Debentures

NCERT - National Council of Education Research and Training

NCLT - National Company Law Tribunal

NCM - National Commission for Minorities

NDA - Net Domestic Assets

NDS-OM - Negotiated Dealing System-Order Matching

NDTL - Net Demand and Time Liabilities

NECS - National Electronic Clearing Service

NEFT - National Electronic Funds Transfer

NEM - Northeast Monsoon

NFA - Net Foreign Assets

NFS - National Financial Switch

NHAI - National Highways Authority of India

NHB - National Housing Bank

NIBM - National Institute of Bank Management

NIC - Notes in Circulation

NIIF - National Investment and Infrastructure Fund

NIIP - Net International Investment Position

NIMs - Net Interest Margins

NM3 - New Monetary Aggregate

NOF - Net Owned Fund

NONG - Non-Oil Non-Gold

NPA - Non-Performing Asset

LIST OF ABBREVIATIONS

NPCI	-	National Payments Corporation of India
NPISH	-	Non-Profit Institutions Serving Households
NRIs	-	Non-Resident Indians
NRLM	-	National Rural Livelihoods Mission
NSDL	-	National Securities Depository Limited
NSDP	-	Net State Domestic Product
NSFR	-	Net Stable Funding Ratio
NSSO	-	National Sample Survey Organisation
NULM	-	National Urban Livelihoods Mission
NUUP	-	National Unified USSD Platform
OBCs	-	Other Backward Classes
OBS	-	Off-Balance Sheet
OD	-	Overdraft
ODI	-	Overseas Direct Investment
OECD	-	Organisation for Economic Co-operation and Development
OIS	-	Overnight Index Swap
OMO	-	Open Market Operations
OPEC	-	Organisation of Petroleum Exporting Countries
ORM	-	Operational Risk Management
OSMOS	-	Off-Site Monitoring and Surveillance System
OSS	-	Off-Site Surveillance
OTC	-	Over-The-Counter
OVD	-	Officially Valid Document
PA	-	Provisional Accounts
PAN	-	Permanent Account Number
PCA	-	Prompt Corrective Action
PDMA	-	Public Debt Management Agency
PDs	-	Primary Dealers
PDS	-	Public Distribution System
PFCE	-	Private Final Consumption Expenditure
PFCVA	-	Provision for Forward Contracts Valuation Account
PFMIs	-	Principles for Financial Market Infrastructures
PFMS	-	Public Finance Management System
PID	-	Protection of Interests of Depositors'
PLF	-	Plant Load Factor
PMG	-	Project Monitoring Group
PMI	-	Purchasing Managers Index
PMJDY	-	Pradhan Mantri Jan DhanYojana
PMS	-	Performance Management System
POL	-	Petroleum, Oil and Lubricants
PoS	-	Point of Sale
PPI	-	Pre-Paid Payment Instrument
PPP	-	Public-Private Partnership
PSBs	-	Public Sector Banks
PSL	-	Priority Sector Lending
PSLCs	-	Priority Sector Lending Certificates
PSS Act	-	Payment and Settlement Systems Act
PSUs	-	Public Sector Undertakings
PvP	-	Payment Versus Payment
QE	-	Quantitative Easing
QFI	-	Qualified Foreign Investor
QIB	-	Qualified Institutional Buyer
QIP	-	Qualified Institutional Placement
R&D	-	Research and Development
RAF	-	Risk Appetite Framework
RBI	-	Reserve Bank of India
RBIA	-	Risk Based Internal Audit

LIST OF ABBREVIATIONS

RBIQ	-	Reserve Bank of India Quiz
RBIWPS	-	Reserve Bank Working Paper Series
RBS	-	Risk Based Supervision
RBSC	-	Reserve Bank Staff College
RCG	-	Regional Consultative Group for Asia
RCs	-	Reconstruction Companies
RD	-	Revenue Deficit
RDA	-	Rupee Drawing Arrangement
RECS	-	Regional Electronic Clearing Service
REITs	-	Real Estate Investment Trusts
RFCA	-	Revaluation of Forward Contracts Account
RFPI	-	Registered Foreign Portfolio Investor
RGS	-	Risk Governance Structure
RHF	-	Rural Housing Fund
RIDF	-	Rural Infrastructure Development Fund
RMD	-	Risk Monitoring Department
RoA	-	Return on Assets
ROC	-	Regulatory Oversight Committee
RoE	-	Return on Equity
ROs	-	Regional Offices
RRBs	-	Regional Rural Banks
RTGS	-	Real Time Gross Settlement System
RTI Act	-	Right to Information Act
RWA	-	Risk Weighted Assets
SAA	-	Swap Amortisation Account
SAARC	-	South Asian Association for Regional Cooperation
SARFAESI	-	Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest
SBIG	-	Shadow Banking Implementation Group
SBP	-	State Bank of Pakistan
SC	-	Securitisation Company
SCAV	-	Standing Committee on Assessment of Vulnerabilities
SCBs	-	Scheduled Commercial Banks
SCs	-	Scheduled Castes
SDF	-	Special Drawing Facility
SDLs	-	State Development Loans
SDR	-	Special Drawing Rights
SDR	-	Strategic Debt Restructuring
SDS	-	Step Down Subsidiary
SEBI	-	Securities and Exchange Board of India
SEIS	-	Services Exports from India Scheme
SEP	-	Self-Employment Programme
SEZs	-	Special Economic Zones
SF	-	SAARCFINANCE
SFT	-	Securities Financing Transaction
SGL	-	Subsidiary General Ledger
SHGs	-	Self Help Groups
SIA	-	Secretariat Industrial Assistance
SIBs	-	Systemically Important Banks
SICA	-	Sick Industrial Companies (Special Provisions) Act
SIDBI	-	Small Industries Development Bank of India
SIOS	-	Services and Infrastructure Outlook Survey
SJSRY	-	Swarna Jayanti Shahari Rozgaar Yojana
SLBCs	-	State Level Bankers' Committees
SLCCs	-	State Level Coordination Committees
SLR	-	Statutory Liquidity Ratio

LIST OF ABBREVIATIONS

SMA	- Special Mention Accounts
SMC	- Senior Management Committee
SMS	- Short Message Service
SNB	- Swiss National Bank
SPMCIL	- Security Printing and Minting Corporation of India Limited
SRC	- Standing Committee on Supervisory & Regulatory Co-operation
SRs	- Security Receipts
StCBs	- State Co-Operative Banks
STOs	- State Treasury Offices
STP	- Straight-Through-Processing
STs	- Scheduled Tribes
SWM	- Southwest Monsoon
SWMA	- Special Ways and Means Advances
TAC	- Technical Advisory Committee
TACS	- Technical Advisory Committee on Surveys
TAG	- Technical Advisory Group
TC	- Technical Committee
TLAC	- Total Loss-Absorbing Capacity
TOLIC	- Town Official Language Implementation Committee
TR	- Trade Repositories
TReDS	- Trade Receivables Discounting System
UBD	- Urban Banks Department
UCBs	- Urban Co-Operative Banks
UK	- United Kingdom
UMP	- Unconventional Monetary Policy
US	- United States
USD	- US Dollar
USSD	- Unstructured Supplementary Service Data
UT	- Union Territory
VAPT	- Vulnerability Assessment and Penetration Testing
VARs	- Vector Auto-Regressions
VC	- Video Conferencing
VEC	- Vector Error Correction
VIF	- Variance Inflation Factor
WACR	- Weighted Average Call Money Rate
WADR	- Weighted Average Discount Rate
WADTDR	- Weighted Average Domestic Term Deposit Rate
WAEIR	- Weighted Average Effective Interest Rate
WALR	- Weighted Average Lending Rates
WAR	- Weighted Average Rate
WLAs	- White Label ATMs
WMA	- Ways and Means Advances
WOS	- Wholly Owned Subsidiary
WPI	- Wholesale Price Index
WSS	- Weekly Statistical Supplement
XBRL	- eXtensible Business Reporting Language
ZTC	- Zonal Training Centre

This Report can also be accessed on Internet
URL : www.rbi.org.in

GOVERNOR'S OVERVIEW: ANNUAL REPORT, 2014-15

1. The Reserve Bank's Annual Report informs the people of India on what RBI intended to accomplish during the past year and what was actually done. In it, RBI also lays out proposals for the coming year. Our actions are influenced both by the current macroeconomic environment as well as our broad medium-term framework for the development of the financial sector.

Challenges in the Current Macroeconomic Environment

2. Despite the immense efforts in recent years of both the Government and RBI to restore macroeconomic stability to the economy, three areas are still "work in progress" from RBI's perspective. First, economic growth is still below levels that the country is capable of. Second, inflation projections for January 2016 (as of early August 2015) are still at the upper limits of RBI's inflation objective. Third, the willingness of banks to cut base rates – whereby they forego income on existing borrowers in order to attract more new business -is muted; not only does weak corporate investment reduce the volume of new profitable loans, some bank capital positions, weakened by NPAs, may prevent them from lending freely.

3. The short term macroeconomic priorities of the Reserve Bank are therefore clear: focus on bringing down inflation in line with the proposed glide path; work with the Government and banks on speeding up the resolution of distressed projects and cleaning up bank balance sheets; ensure banks have the capital to make provisions, support new lending, and thus pass on future possible rate cuts.

Inflation Objective

4. RBI signed a historic agreement with the Government, wherein RBI's mandate is clearly spelled out in terms of a flexible inflation objective over the medium term. This year, the Finance Minister proposes to lay out, after consultation with RBI, the structure of a monetary policy committee that can be formally and legally entrusted with policy decisions. This is a welcome step forward in building the institutions we need for transparent and independent monetary policy.

5. Turning to liquidity management, RBI has largely moved from windows where banks can get liquidity at fixed prices to auctioning liquidity in the market. The intent is to undertake sufficient operations to keep the weighted average call money rate (purged of off-market transactions effected by co-operative banks) close to the policy rate. In choosing between auctioning short term instruments (such as overnight repos and reverse repos) and long term instruments [such as Open Market Operations (OMOs)] to manage liquidity, the Bank estimates the pace at which it wants to grow its "permanent" assets, consisting of the sum of foreign exchange reserves and government bonds, and decides accordingly.

Stressed Assets and Speedy Resolution

6. In dealing with stressed bank assets, RBI has been focused on getting the underlying real projects back on track. There are a number of impediments here. First, the stigma as well as the provisioning (and the associated fall in profitability) attached to a loan being labelled "non-performing" makes banks eager to avoid the label. In some cases, they ignore the reality that existing loans will have to be written down because of the changed situation since they were sanctioned (which includes extensive delays, cost overruns, and overoptimistic demand projections). Regulatory forbearance, where RBI makes it easy for banks

to “extend and pretend” is not a solution. Since no other stake-holder – such as the promoter, tariff authorities and tax authorities - contributes to resolution, the real project limps along becoming increasingly unviable. Meanwhile, analysts grow increasingly suspicious of bank balance sheets and the growing volume of “restructured” assets. Second, some large promoters take advantage of banker fears about assets turning non-performing to extract unwarranted concessions, without any sacrifice in the value of their stake. The judicial process, despite a variety of creditor-friendly bills like the SARFAESI Act, further tends to hamper the ability of creditors to collect their just dues from influential promoters.

7. To remedy both the paralysis as well as the unfair distribution of losses, RBI has taken a number of actions. First, it has created a database of loans over ₹50 million (the CRILC database), and has advised banks and NBFCs to report regularly on the status of the loans. Early identification of distressed projects offers the best opportunity to put them back on track. So if a loan is identified as more than 60 days overdue, all lenders to the borrower have to come together in a Joint Lending Forum (JLF) to see how the underlying problems can be fixed. The JLF has to follow strict timelines, failing which the project loans’ classification has to be downgraded. On the other hand, if the timelines are met, the deterioration in loan classification is halted. Furthermore, by bringing the creditors into one forum, RBI has made it easier for the promoter and the creditors to reach a consensus on actions, even while making it harder for the promoter to play one creditor off against another.

8. Some other regulatory actions are worth noting. RBI ended the forbearance accorded to restructured loans. Henceforth, restructured loans will be classified as non-performing loans. To deal with genuine problems of poor structuring, however, it has allowed bankers to stretch repayment profiles for performing loans to infrastructure and the core sector (the so-called “5/25” rule), provided the project has reached commercial take-off, has a genuinely long commercial life, and the net present value of loans is maintained. RBI is undertaking periodic examination of randomly selected “5/25” deals to ensure they are facilitating genuine adjustment rather than becoming a back-door means of postponing principal payments indefinitely. Also, in cases of restructuring, RBI and SEBI have together allowed banks to write in clauses that allow banks to convert loans to equity in case the project gets stressed again. Not only will such Strategic Debt Restructuring give creditors some upside, in return for reducing the project’s debt, it can also give them the control needed to redeploy the asset (say with a more effective promoter).

9. Going forward, RBI has to monitor the efficacy of the various measures put in place to speed up resolution, and take remedial action where necessary. The move by the Government to add to the recapitalisation fund for banks is also welcome, as is the proposal to allocate it taking into account the progress in cleaning up balance sheets and generating healthy growth. RBI will welcome progress in the coming year on the creation of the institutions necessary for resolution such as the new Bankruptcy Code and the Company Law Tribunals that will administer it and the Financial Resolution Authority (for resolving financial institution distress).

Medium Term Challenges

10. A regulatory view, fashionable in the past, was that the pace of regulatory reforms had to be limited by the capacity of our banks, especially our public sector banks (PSBs). The current stress in the banking system suggests that the real economy will not wait for the banking system, and a slow

pace of reform could lead to greater, rather than lower risk residing in the banking system. Financial sector reforms need to move on many fronts.

11. For a country as big and populous as India, reforms cannot be shots in the dark, subjecting the economy to great uncertainty and risk. Wherever possible, we have to move steadily but firmly, ever expanding the scope of reforms while always limiting the uncertainty they create. The Chinese term this 'Crossing the river by feeling the stones'. It is an appropriate metaphor to guide our own reforms.

12. In the financial sector, we need to increase efficiency through greater entry and competition. The most appropriate institutions will prevail when the competitive arena is level, so we have to remove regulatory privileges as well as impediments wherever possible, especially those that are biased towards some form of ownership or some particular institutional form. We need more participation in our financial markets to increase their size, depth, and liquidity. Participation is best enhanced not through subventions and subsidies but by creating supporting frameworks that improve transparency, contract enforcement, and protections for market participants against abusive practices. Technology can be very helpful in reducing the costs of supportive frameworks, and can bring hitherto excluded populations into the financial fold. It is these ideas that guide our medium-term reform strategy. Let me be more specific.

Banking and Other Financial Institutions

13. The banking system is dominated by PSBs. While a number of extraordinary officers have led PSBs over time, recent bank underperformance suggests room for improvement. Following the Nayak Committee Report, the Government has decided to separate the posts of Chairman and Managing Director of these banks, follow a more open search by considering private sector candidates also for a number of these posts, and professionalise the Boards of these banks by inducting professional Board members with the relevant experience. Going forward, the Government intends to set up a Bank Board Bureau (BBB), composed of eminent personalities with integrity and domain experience, to take over the appointments process.

14. RBI has also stepped away from micromanaging the functioning of the PSB Boards through regulations, allowing Boards to determine how they will carry out their responsibilities for strategic planning, risk management, accounting, *etc.* RBI has also liberalised the compensation of private bank Board members, while maintaining some checks, to ensure Board members are properly incentivised.

15. Because PSBs compete in the same market place for talent as do private sector banks and foreign banks, and because skill gaps are increasing at middle management levels because of past hiring freezes, they will be unnecessarily hampered if they are unable to pay appropriate compensation to middle and senior managers, as well as Board members. Of course, higher pay should come with better accountability for performance. Given that many PSBs have higher overall costs than private sector banks performing similar activities, there is some scope for cost rationalisation even while improving the pattern of compensation. At the same time, we should recognise that PSBs undertake public interest activities (like the rollout of accounts under the *Pradhan Mantri Jan Dhan Yojana*) that are not always fully compensated. Government should endeavour to keep the competitive playing field level by fully compensating banks for activities it wants undertaken in the public interest.

16. A committee under RBI Deputy Governor Shri Gandhi has detailed the ways governance in urban co-operative banks (UCBs) can be improved, including through implementation of the Malegam Committee report. Licensing of new UCBs will follow after the committee's recommendations are evaluated and implemented. The committee has also proposed modalities by which well-functioning co-operatives, including multi-state co-operatives, can convert to joint stock companies.

17. The banking sector will experience a substantial change in the nature of competition as two new universal banks start operations, and a number of payment banks and small finance banks are approved this year for license. Payment banks are expected to offer bank accounts in every corner of the country, facilitating payments and cash transfers through new technologies and physical access points. Small finance banks are expected to channel loans and financial services to small players. The MUDRA Limited will also help in such efforts through refinancing and securitisation services to unincorporated lenders. After reviewing the experience with this first round of licenses, RBI intends to put the licensing process "on tap", with applications being considered as and when they come in.

18. Non-Banking Financial Companies (NBFCs) are an integral and important part of our financial landscape. RBI has endeavoured to streamline regulations across NBFCs, reducing the regulatory burden in case an NBFC is not systemic, does not face retail customers, or does not raise money from the public. It has also harmonised regulations such as NPA norms, capital requirements, provisioning requirements across different types of NBFCs as also between NBFCs and other financial institutions.

Other Regulatory Changes

19. New Basel norms on regulation will require implementation. The Reserve Bank has put out frameworks on the Leverage Ratio, Countercyclical Capital Buffer, Capital for Domestic Systemically Important Banks, the desirable extent of large exposures, and various liquidity ratios. While tailoring the international accords to domestic conditions, the Reserve Bank intends to meet international commitments on schedule.

20. With rapid changes in regulations, we need to go back periodically and revise the entire regulatory handbook. With this in mind, the Reserve Bank plans to come out by January 1, 2016 with thoroughly revised master documents covering different regulatory issues. Each of these master documents is intended to become a complete user-friendly compendium of applicable regulations on a subject. Each will be updated in real time, and will attempt to streamline and simplify regulations where possible.

Supervisory Changes

21. Even as our regulations change, supervision has to keep pace. We are working on improving our collection and dissemination of information, on refining our methods of inspection and analysis, and on enhancing the capabilities of our staff. We will continuously rationalise regulations but will come down hard on non-compliance when detected.

22. More information is being collected and disseminated through the CRILC database of large loans, through a new fraud registry which is being supported with a detailed framework on detecting and dealing with banking frauds, and through a new Early Warning System to track bank stress. Going forward, we plan to integrate all our supervisory data into a seamless database.

23. RBI moved to risk-based supervision of some of our larger banks in 2013. We have

been evaluating our experience and refining our methods, including validating them with the assistance of multilateral agencies. We are also working on systemic risk assessments through our Financial Stability Unit.

24. With changes in technology, cyber security, both at the bank level and at the system level, has become very important. RBI is working on upgrading the capabilities of its inspectors to undertake bank system audit as well as to detect vulnerabilities in them. RBI is also in the process of setting up an IT subsidiary, which will be able to recruit directly from industry, and will give the Reserve Bank better ability to manage and supervise technology.

25. Finally, RBI will help State Level Coordination Committees (SLCCs) become more effective so that they can ferret out unauthorised financial operators before they can misuse public trust. SLCC sub-committees will keep regulators and law-enforcement authorities in constant contact. RBI will help SLCCs develop websites, where the public can get, and give, information about the legitimacy of financial schemes offered by non-bank operators.

Debt Management and Markets

26. RBI has been managing central government and state government debt issuance with a view to reducing risks even while minimising transactions- and financing costs. This means, among other things, articulating a clear medium term debt strategy, spreading issues over different maturities so that there is no bunching of securities, and switching or buying back certain maturing issues. It also means improving liquidity, resilience and depth in the market for government securities by expanding the role of long term players like pension funds and insurance companies, creating more, and predictable, room for Foreign Portfolio Investors, and making it easier for domestic retail investors to participate through their "demat" accounts.

27. In addition to issuing debt on the government's behalf, RBI works closely with the central government and state governments to facilitate the government's electronic payments and receipts, as well as its accounting. Increasingly, through its e-Kuber platform, RBI has been undertaking some functions itself to reduce costs.

28. The Government has announced its intent to move debt management to a separate agency, the PDMA. While the public discourse has sometimes suggested large reductions in government bond yields from setting up an independent PDMA with no conflicts of interest, these stem primarily from such an agency being unable to sell debt to captive government-owned or regulated institutions, thus forcing the government to reduce fiscal deficits. Given the Government has embarked on a fiscal consolidation path, the benefit from such discipline may be small. At any rate, RBI is working closely with the Government in setting up the PDMA.

29. RBI recognises the role of a vibrant financial market in complementing and competing with the banking system in allocating and absorbing risks. Our focus is on improving the variety of products and participants, as well as on reducing the costs of transaction, all the while keeping financial stability in mind.

30. To improve activity in the corporate debt market, RBI has allowed banks to issue long term bonds that will be free of regulatory pre-emptions. It has encouraged the emergence of an international rupee market by allowing multilateral institutions to issue rupee bonds abroad, and will permit Indian corporates to also do so. It is also exploring ways by which banks can enhance corporate bond credit ratings through credit

facilities. Ultimately, though, a robust bankruptcy system is needed for the corporate bond market to really take off. The Government has indicated it will move quickly to put this in place.

31. RBI has encouraged the development of new instruments such as exchange traded interest rate futures. It plans to open the way to interest rate options, a variety of swaps (including a swap execution facility), as well as cross-currency futures and options. Where possible, RBI will be more liberal in allowing a variety of instrument designs and participation when an instrument is initiated, putting greater focus on stability issues once trading picks up.

Currency and Payments

32. Our country still depends on physical currency in many transactions. RBI is constantly seeking to improve the quality of bank notes it issues, even while making sure that notes are available wherever needed. A new series of bank notes are being issued, and we also intend to start a pilot project with plastic/polymer bank notes. We have also examined the logistics of currency distribution and we intend to make significant changes in our current model, with a greater focus on incentivising banks to take over storage and distribution of currency. Moreover, we will emphasise the decentralised return of coins (into coin machines and through coin collection programs) and notes (through ATMs that accept cash and re-circulate it).

33. It is a reality that cash use will fall off over time, lowering transactions costs and reducing the role of black money. RBI is working with the Government to incentivise electronic payments. New institutions, such as the Bharat Bill Payment System, and new technologies, especially through mobile phones, will emerge that will facilitate such payments. While RBI recognises the need for regulatory adaptation, and will work with stakeholders to achieve that, it will not brook the violation of existing regulations simply because a user thinks they are outdated. For instance, after asking an operator to cease violating rules on small value payments, RBI has permitted issuers to dispense with two factor authentication for small value payments, provided some safeguards are in place. Over time, RBI believes mobile- and Internet-based payments will explode, and is working with the financial sector to facilitate them.

Financial Inclusion

34. The *Pradhan Mantri Jan Dhan Yojana* has created a base of accounts for much of the population. Government has taken the next step of attaching a variety of financial services such as accident and life insurance to these accounts, and sending Direct Benefits such as scholarships, pensions, and subsidies to these accounts. We also have to ease access to bank accounts through Business Correspondents, payment banks, and point-of-sales machines so that they are used frequently. Easy payments, access to cash-in and cash-out facilities, and widespread availability of safe savings instruments have to be our next objectives in financial inclusion of households.

35. We also need to ease lending to small producers, whether they are farmers, Self Help Groups, or businesses. For this, we need to improve the structure and working of credit information bureaus, collateral registries, and debt recovery tribunals – ironically, credit flows easily only when the lender is persuaded that he will get his money back, so easier access to credit necessitates closer attention to default prevention mechanism. Perhaps the most important source of collateral value is land. We need better digital mapping and clean records of land ownership across the country so that it can be used more effectively as collateral.

36. New institutions like the Trade Receivables Discounting System (where small firms can post their receivables from large firms for sale) and Small Finance Banks are being set up to facilitate credit flow to small firms. The MUDRA Limited is also likely to propose innovative new ways of channelling flows to small producers.

37. Priority sector in India pertains to those sectors of the economy which, though viable and creditworthy, may not get timely and adequate credit in the absence of any special dispensation. Typically, these are small value loans to farmers for agriculture and allied activities, micro and small enterprises, poor people for housing, students for education and other low income groups and weaker sections. In the context of India, such sectors are spread across the length and breadth of the country and especially prevalent in the hilly and coastal regions.

38. Priority sector activities have to be carried out by banks as part of their normal business operations and, therefore, banks are expected not to view this as a Corporate Social Responsibility. On the part of the Reserve Bank, one important facilitation in this regard has been that pricing of all credit has been made free, though with the expectation that pricing should not be exploitative. Priority sector efforts will not be successful unless market players are willing to take risks by innovating structures, products and processes.

39. RBI revamped priority sector guidelines so as to reemphasise lending to excluded or nationally important sectors in a changing economy. In particular, it set new targets of 8 per cent of Adjusted Net Bank Credit to small and marginal farmers and 7.5 per cent for micro enterprises, while allowing medium-sized firms, social infrastructure such as toilets, and renewable energy investments to qualify for priority sector credit.

40. Financial inclusion also means greater consumer protection for the newly included and typically unsophisticated customers, an easily-accessed and speedy grievance redressal process, and expanded efforts on financial literacy. Following public consultation, RBI has developed a Charter of Consumer Rights. Bank boards have been asked to put in place frameworks that ensure those rights are protected. After those frameworks have been in operation for some time, RBI will take a view on best practices, and needed regulation, if any. In the meantime, field visits by RBI, to check mis-selling as well as proper functioning of bank infrastructure such as branches and ATMs, will be expanded.

41. RBI is reviewing its Banking Ombudsman system to see how it can be extended to non-banks and how it can be more effective in rural areas. Each bank has also been asked to set up an internal Ombudsman system, which will examine the bank's grievance cases to see if resolution is possible before it is escalated to RBI's ombudsman system.

42. Financial literacy, whether through courses in schools, through literacy camps organised by banks and RBI, or through newspaper or social media campaigns, is extremely important. All too often, unscrupulous operators have discovered that greed trumps education – even the sophisticated fail to apply the maxim that if it is too good to be true, it probably is… Nevertheless, it is our duty to try and educate our public and we have to be better than the unscrupulous at exploiting new technologies, including mass and social media, to reach them. RBI intends to increase its focus on such campaigns significantly.

RBI's Organisational Changes and Human Resources Development

43. To respond to its changing responsibilities, especially the need for more specialisation, the

Reserve Bank created some new departments, merged others, and reorganised all into 5 clusters: 1) Monetary Policy and Research; 2) Regulation and Risk Management; 3) Supervision and Inclusion; 4) Financial Markets and Infrastructure; and 5) Human Resources and Operations. The restructuring was carried out this year.

44. Henceforth, most officers will be recruited through a revamped common entrance exam (starting 2015), given an overall view of the Bank during initial training, and then encouraged to specialise in a couple of clusters in their early years. To encourage specialisation, the Bank will also consider promoting some particularly capable employees in situ. For most employees, however, as they become more senior, skill building will shift from acquiring technical skills to acquiring managerial skills. At very senior levels, these officers will again be posted freely between clusters.

45. The Bank intends to make more postings based on the Bank's needs and the staff member's specialisation interests. This also means that we have to help staff assess their own aptitude through an Assessment Centre and help them identify their strengths and weaknesses through a more discriminating Performance Evaluation System. We also must identify the needs of various jobs through careful job profiling. Staff members have to be given the training support, including through scholarships, to build necessary skills as well as to remedy identified gaps. We plan to set up an RBI Academy to offer higher-order skills to RBI staff and bank officials. And staff members who consistently perform well should also be rewarded with more challenging assignments. All this will require substantial effort in the area of Human Resource Development, but is absolutely necessary.

Conclusion

46. RBI is an efficient organisation, which has steadily reduced its employee count from 35,500 in 1981 to 16,700 today, even while performing ever increasing quantities of work. The surplus it generated from its activities this year is ₹659 billion, which has been paid out entirely to the Government. There is, of course, always scope for improvement. For example, to ensure that we meet our commitment to the public, we have put out on our website timelines within which the public can expect responses to applications made to RBI. We will monitor those timelines to ensure our staff delivers as promised.

47. A key factor in RBI's success has been a satisfied staff. In the past, RBI used to have no problem attracting junior officers, losing only an occasional officer who was successful in the IAS exam. Today, we lose more than we should be comfortable with. This is why a revamp of the professional challenges we offer our staff is very much needed, and we hope the changes outlined earlier will help us become a more attractive employer. In this regard, our review of compensation, as well as the long-pending improvement in pensions for our retirees also assume importance.

48. Let me end by thanking all my 16,700 colleagues for their work in the past year and challenging them, in the 81st year of this great institution, to do even better so that the Reserve Bank of India continues to help the nation secure prosperity and economic opportunity for all for many years to come.

*For the Year July 1, 2014 to June 30, 2015**

PART ONE: THE ECONOMY - REVIEW AND PROSPECTS

I ASSESSMENT AND PROSPECTS

I.1 Over the year gone by, the Indian economy remained resilient in a global environment characterised by falling macroeconomic risks but rising financial stability risks. While a modest recovery is tentatively gaining foothold in advanced economies, activity slowed across a broad swathe of emerging economies as commodity prices fell, financing conditions tightened and structural constraints started building. India is a notable exception. Globally, financial risks increased as investors reached for yields, expecting US monetary policy to normalise more slowly. Incipient threats to financial stability were also evident in rising corporate indebtedness in both advanced and emerging economies, stretched asset valuations in some sectors, marked increase in exchange rate volatility and the debt crisis in Greece in the closing months of 2014-15. Spillovers from these external shocks impacted various segments of the financial markets in India, asset prices and capital flows, although the latter remained by and large buoyant.

I.2 Even as banking sector risks remained elevated domestically, the macroeconomic fundamentals of the Indian economy improved gradually over the year, anchored by some easing of inflation and continuing fiscal consolidation. Notwithstanding deterioration in export performance brought on, *inter alia*, by weak external market conditions, the current account deficit narrowed in 2014-15 from its level a year ago on terms of trade gains and weak import demand. With fiscal consolidation firmly underway and with buoyant business optimism, the stage is now set for unshackling stalled investments and for boosting new capital spending in order to accelerate the pace of growth. Drawing on the experience of 2014-15, it is now time to implement an agenda to take the economy to higher growth in 2015-16 and over the medium-term. Concomitantly, recent gains in reducing inflation pressures need to be built upon so that disinflation continues along with higher growth. Importantly, resolute actions are needed to ease stress in financial assets, mitigate/resolve debt burdens so that stranded assets are put back to work quickly wherever feasible and capital buffers are built to enable financial intermediaries to provide adequate flow of credit to productive sectors.

ASSESSMENT: 2014-15

I.3 While the pick-up in the growth of GDP at market prices in 2014-15 was largely sustained by private consumption, the decline in the

* While the Reserve Bank of India's accounting year is July-June, data on a number of variables are available on a financial year basis, *i.e.*, April-March, and hence, the data are analysed on the basis of the financial year. Where available, the data have been updated beyond March 2015. For the purpose of analysis and for providing proper perspective on policies, reference to past years as also prospective periods, wherever necessary, has been made in this Report.

rates of saving and investment for the second consecutive year to 2013-14 emerged as a matter of concern. The improvement in the financial saving of households and the expected decline in government dissaving in 2014-15 should work towards releasing the financing constraints on investment, especially when seen in conjunction with the step-up in capital goods production in the latter half of 2014-15.

I.4 On the production side, the weather-induced slowdown in agriculture impacted rural demand and also necessitated policy interventions to manage food price pressures. In the industrial sector, a turnaround in manufacturing in the latter half of the year was essentially driven by upbeat business sentiment, some unclogging of stalled projects and a robust improvement in electricity generation and coal production in the closing months. A durable upturn in new capex, capacity utilisation and new orders – both domestic and foreign – holds the key to a sustained revival of industrial activity. In the services sector, only a few sub-sectors, such as finance, real estate and construction, grew at a higher pace.

I.5 From June 2014, inflation declined faster than initially anticipated. A combination of favourable factors such as the collapse of international commodity prices, particularly of crude, and loss of pricing power among corporates due to weakening demand as well as pro-active supply management and deregulation of key fuel prices worked in alignment with a disinflationary monetary policy stance that was set from September 2013. Accordingly, inflation expectations eased to single digit for the first time since September 2009 and wage pressures moderated.

I.6 A significant factor influencing the evolution of monetary conditions during 2014-15 was the large surge in capital inflows, which necessitated active and nimble liquidity management operations to sterilise flows in accord with the stance of monetary policy. Still sluggish demand, receding inflation and risk aversion stemming from stress in financial assets restrained bank credit growth and also incentivised substitution of bank lending to take advantage of competitive pricing conditions.

I.7 The revised liquidity management framework introduced in September 2014, and in particular intra-day fine-tuning operations, improved, over time, the alignment of money market rates with the policy repo rate. Notably, large spikes in rates hitherto associated with advance tax payments and balance sheet closure were muted. Gilt yields declined, reflecting the improvement in macro-fundamentals. In the foreign exchange market, two-way movements were associated with lower volatility. Stock markets rallied strongly throughout the year on buoyant investor optimism, both foreign and domestic, stretching valuations before some correction in the closing months of the year.

I.8 While the committed path of fiscal consolidation was adhered to by the central government for the third year in succession, slack revenue mobilisation – particularly through disinvestment – necessitated cutbacks in productive capital expenditure towards the end of the year. This highlights the need for more realistic assessment of revenue targets and expenditure allocations. Furthermore, states need to remain committed to fiscal consolidation.

I.9 The contraction in merchandise exports since December 2014 emerged as an area of concern, sapping aggregate demand and increasing external vulnerability, notwithstanding terms of trade gains and a large saving on POL imports helped contain the current account deficit. Buoyant capital inflows in excess of the external financing requirement raised international reserves to an all-time high by the end of the year.

PROSPECTS: 2015-16

I.10 Turning to 2015-16, the outlook for the global economy has been adversely impacted by the contraction in output in North America in the first quarter of 2015. In the second and third quarters, there are indications of demand picking up in advanced economies; however, the continuing slowdown in emerging economies holds back a fuller global recovery. At the same time, with hardening bond yields and risk premia, emerging economies are contending with volatile currency movements and capital flows. Going forward, these factors could pose risks to the global recovery. Accordingly, the IMF has pared its forecast for global growth in 2015 to 3.3 per cent in its July update, marginally lower than in 2014.

I.11 For the Indian economy, the outlook for growth is improving gradually. Business confidence remains robust, and as the initiatives announced in the Union Budget to boost investment in infrastructure roll out, they should crowd in private investment and revive consumer sentiment, especially as inflation ebbs. While the progress of the monsoon has allayed initial fears of moisture shortfall, uncertainty surrounding the progress and distribution of the monsoon remains a risk to the outlook for both growth and inflation. Comprehensive and pre-emptive food management strategies need to be put in place to contain these spillovers. In the first four months of 2015-16, indicators of real activity have broadly tracked the Reserve Bank's baseline projection of output growth (at basic prices) at 7.6 per cent for the year as a whole, up from 7.2 per cent in 2014-15.

I.12 Taking into account initial conditions, including the prospects for the monsoon and for international crude prices, the Reserve Bank projected in April 2015 a baseline path for inflation in 2015-16 in which it would be pulled down from current levels by base effects till August but is expected to start rising thereafter to below 6.0 per cent by January 2016. So far, inflation outcomes have closely tracked these projections. The risks to this trajectory are balanced as the weather-related uncertainties are offset by falling crude prices. Inflation developments will warrant close and continuous monitoring as part of the overall disinflation strategy that requires inflation to be brought down to 5 per cent by January 2017.

I.13 As regards fiscal policy, the Government's resolve on fiscal consolidation should propel efforts to reach the target for the gross fiscal deficit for 2015-16 at 3.9 per cent of GDP. In the early months of the year, indirect tax collections have been robust and set to achieve budget estimates, though contingent upon a recovery in manufacturing and services. Furthermore, plans for disinvestment need to be front-loaded to take advantage of supportive market conditions, and also to forestall cutbacks in capital expenditure to meet deficit targets. Such cut backs compromise the quality of fiscal consolidation. States need to take advantage of the greater fiscal autonomy stemming from higher devolutions and prioritise capital and developmental expenditure so that the quality of sub-national fiscal correction is maintained.

I.14 In the external sector, merchandise exports have contracted through the first four months of 2015-16, rendering the economy vulnerable to external shocks. Imports have remained subdued, primarily reflecting softening of crude and gold prices. Non-oil non-gold imports have also moderated due to muted domestic activity. Over the rest of the year, some savings may accrue on account of POL and bullion imports; on the other hand, the gradual pick-up in activity anticipated over the rest of the year may revive non-oil non-gold import demand. Remittances from Indians working abroad have weathered the slowdown in global growth and should continue to lend support to the balance of payments. Along with a surplus expected on trade in services as in the past, from software exports and travel earnings, the current account deficit for the year as a whole should be contained below 1.5 per cent of GDP. The outlook for capital flows is highly uncertain, with the widely anticipated normalisation of US monetary policy later in 2015 expected to generate capital outflows from emerging markets and also to harden financing conditions as bond yields rise. In this context, the level of reserves at over US$ 350 billion and equivalent of about nine months of imports should provide a buffer and smooth out normal import and debt servicing requirements over the year.

I.15 Key to the realisation of these expectations is a durable pick up in investment, supported by sustained efforts to alleviate supply constraints. The proposal to introduce a Comprehensive Bankruptcy Code of global standards by 2015-16 and replacement of the existing multiple prior permission procedure for investments by a pre-existing regulatory mechanism is expected to improve the business environment in India. Easing the doing of business has now become a widely cited constraint on the revitalisation of manufacturing. Areas that require significant changes include legal and regulatory environment, labour market reforms, tax regime and administrative environment.

I.16 Gaps in distribution networks and deteriorating financials of power discoms need to be addressed expeditiously for demand to keep pace with the ongoing easing of supply constraints. Focusing on renewable and clean sources of energy should be accompanied by conservation of energy as a medium-term strategy.

I.17 Expansion of the avenues for gainful employment opportunities is vital for efforts to harness the demographic dividend. This calls for careful identification of skill gaps, providing vocational and technical training, and building of new skills. The National Mission for Skill Development which aims at consolidating skill building initiatives spread across several ministries, is relevant in this context. As self-employment holds out greater employment opportunities, the SETU (Self Employment and Talent Utilisation) initiative for supporting all aspects of start-up business and other self-employment activities is crucial. Other initiatives like Digital India and Make in India will also help to enhance the employment potential.

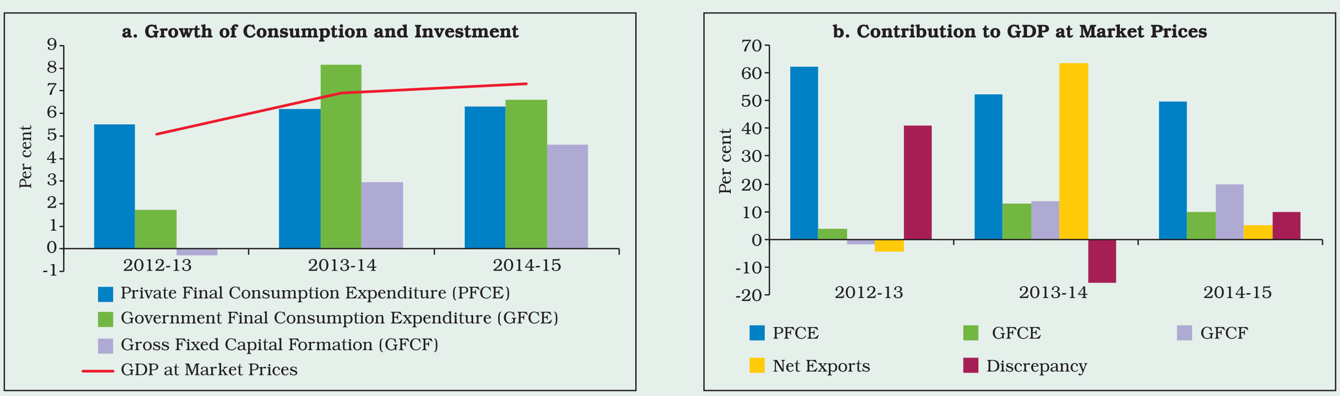
II ECONOMIC REVIEW

The macroeconomic environment in 2014-15 was marked by a modest pick-up in activity amidst building internal and external stability, against the backdrop of a tepid and multi-speed global recovery across regions. Going forward, the economy needs to grapple with significant challenges in the path towards realising its potential and sustaining the growth process. Importantly, structural constraints to growth and asset quality concerns need to be addressed sooner than later.

II.1 THE REAL ECONOMY

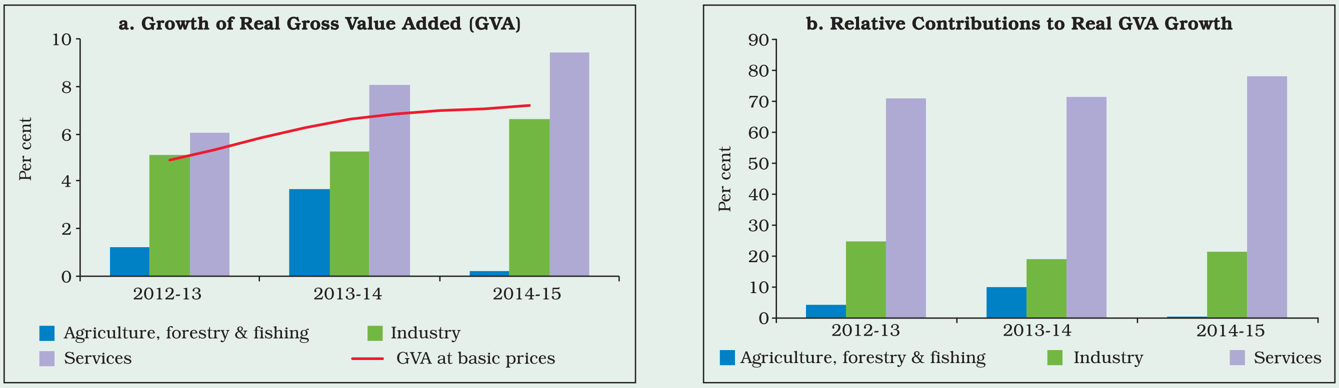
II.1.1 In January 2015, the Central Statistics Office (CSO) released a new series on India's national accounts. The distinguishing features of the new series are: (i) updating the base year from 2004-05 to 2011-12; (ii) improved coverage of corporate activity by (a) using the MCA 21 database[1] of the Ministry of Corporate Affairs, (b) employing value-based indicators such as sales tax collections in conjunction with volume-based indicators such as industrial production, and (c) use of results from the latest surveys, including on activity in the unorganised sector; and (iii) methodological changes such as shifting from the 'establishment' to the 'enterprise' approach for estimating value added in mining and manufacturing. In line with international practices, GDP at market prices will henceforth be the headline measure for output. Gross value added (GVA) at basic prices will measure activity from the supply side instead of GDP at factor cost. In terms of the new series, real activity (at market prices) picked up in 2014-15, rising by 7.3 per cent on top of a growth of 6.9 per cent in 2013-14 (Chart II.1). The firming up of growth during 2014-15 was driven mainly by private consumption and supported by fixed investment, even as government consumption and net exports slackened considerably.

Chart II.1: Growth of Real GDP at Market Prices



[1] The MCA 21 database is an e-governance initiative by the Ministry of Corporate Affairs (MCA) for companies registered under the Companies Act to file their annual accounts electronically under two web platforms: (i) Form 23 AC/ACA and (ii) Extensible Business Reporting Language (XBRL). Currently, banking companies, power companies, non-banking financial companies and insurance companies are exempted from compulsory XBRL filing. For the new series (base: 2011-12), the CSO has incorporated the accounts of about 5 lakh companies for 2011-12 and 2012-13, and around 3 lakh common companies for 2013-14. The database also covers limited liability partnership companies (LLPs) registered with MCA under the LLP Act, 2008.

Chart II.2: Growth in Real GVA at Basic Prices



II.1.2 From the supply side, the quickening of activity in 2014-15 was largely led by industry and services (Chart II.2). Within industry, higher growth was observed in manufacturing and electricity generation. The share of manufacturing was augmented by trading activity of constituent entities which formed part of services in the old series. In the services sector, 'financial, real estate, and professional services' as well as construction were the primary drivers. On the other hand, the agriculture sector lost momentum, adversely impacted by the deficient southwest monsoon (SWM) which affected *kharif* sowing and by unseasonal rains and hailstorms at the time of *rabi* harvesting.

II.1.3 Thus, in terms of the new series, India emerged among the fastest growing economies in the world, notwithstanding the still sluggish global economy which dragged down the contribution of net exports to growth in 2014-15.

Saving and Investment

II.1.4 In 2013-14, the gross domestic saving rate declined for the second consecutive year to 30 per cent of gross national disposable income (GNDI) (Table II.1) This largely reflected the reduction in the saving rate of households on account of a decline in physical assets as well as in valuables. On the other hand, household financial saving gained from returns turning attractive with the

Table II.1: Gross Saving (As a ratio of GNDI)

(Per cent)

Item		2011-12	2012-13	2013-14
1		2	3	4
1	**Gross Savings**	**33.0**	**31.1**	**30.0**
	1.1 Non-financial Corporations	**9.7**	**9.6**	**10.3**
	1.1.1 Public non-financial corporations	1.4	1.2	1.0
	1.1.2 Private non-financial corporations	8.3	8.4	9.3
	1.2 Financial Corporations	**2.9**	**3.1**	**2.8**
	1.2.1 Public financial corporations	1.8	1.7	1.5
	1.2.2 Private financial corporations	1.1	1.4	1.3
	1.3 General Government	**-1.8**	**-1.3**	**-1.0**
	1.4 Household sector	**22.2**	**19.7**	**17.8**
	1.4.1 Net financial saving	7.1	6.8*	7.1*
	1.4.2 Saving in physical assets	14.8	12.6	10.4
	1.4.3 Saving in the form of valuables	0.4	0.4	0.3

Note: Net financial saving of the household sector is obtained as the difference between change in financial assets and change in financial liabilities.
Source: Central Statistics Office.
*: As per Reserve Bank's latest estimates, household financial saving for 2012-13 and 2013-14 are 7.0 per cent and 7.3 per cent, respectively, of GNDI.

moderation in inflation as well as the pick-up in economic activity. For 2014-15, CSO has not yet released its estimates of gross saving. However, in terms of the Reserve Bank's preliminary estimates, household financial saving is placed at 7.5 per cent of GNDI in 2014-15, up from 7.3 per cent in 2013-14.

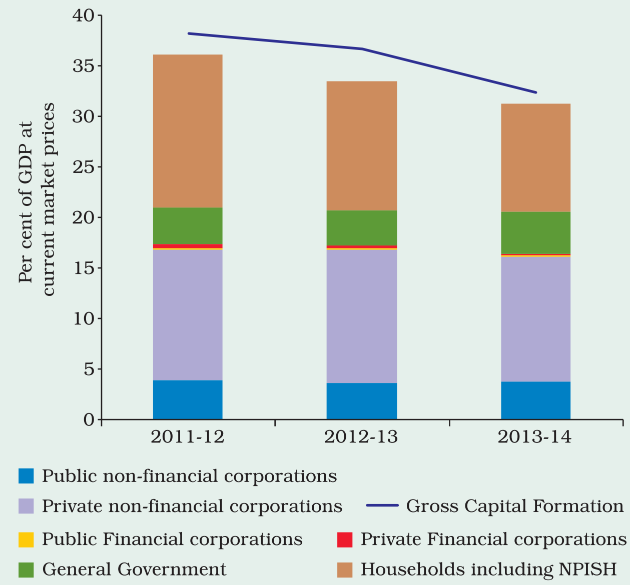
II.1.5 As regards the saving rate of the private corporate sector, non-financial corporations posted a near-steady improvement since 2011-12, *i.e.*, since the new series is available, but it appears that this increase may not have sustained in 2014-15. Private financial corporations, on the other hand, underwent some erosion in saving rates in 2013-14, partly reflecting the slowdown in the growth of operating profits of private sector banks. Available indicators suggest that this has been recouped in 2014-15.

II.1.6 The ongoing reduction in 'dissaving' of the general government boosted the gross national saving rate in 2013-14. With the perseverance of fiscal consolidation, especially by the centre, the decline in the dissaving of the government sector has likely continued into 2014-15. There was, however, a decline in the saving rate of the public financial (including public sector banks) and non-financial corporations in 2013-14. In case of public sector banks, there was a decline in profit after tax during 2014-15.

II.1.7 The investment rate (gross capital formation as a proportion to GDP at current market prices) declined in 2012-13 and 2013-14, largely reflecting the slackening in the non-financial corporations' investment rate on account of weak domestic and external demand and other structural factors such as delay in land acquisition and environment clearances, weak business confidence and policy uncertainties. The household sector's investment rate also declined in 2012-13 and 2013-14. The improvement in general government investment in 2013-14 did, however, provide some offset (Chart II.3).

II.1.8 Viewed in conjunction with other indicators of investment activity such as stalled projects,

Chart II.3: Gross Capital Formation Rate



capital goods imports/production and capex spending, the decline in the private investment intention appears to have become more pronounced in 2014-15 relative to the preceding year. As per the Reserve Bank's data on new projects which were sanctioned financial assistance by banks/ financial institutions (FIs) or funded through external commercial borrowings (ECBs)/foreign currency convertible bonds (FCCBs)/domestic capital market issuance, investment intentions for such projects aggregated to ₹1,459 billion during 2014-15 as against ₹2,081 billion in the previous year. A turnaround in the investment demand cycle, therefore, assumes critical importance to steer the economy on to a sustainable high growth trajectory. The recent experience suggests that a strong step-up in public investment may be required to dispel the inertia constraining private investment and to crowd it in, given the robust business sentiment. Key to this effort will be putting stranded investments in stalled projects back to work while ensuring the availability of key inputs such as power, land (especially for roads) and skilled labour. Steadfast implementation of structural reforms like the goods and services tax (GST) is also required to reinvigorate productivity and competitiveness.

Agriculture

II.1.9 The vagaries of the monsoon were in full play during 2014-15. The likelihood of *El Nino* emerging, was initially placed high, but it eventually did not materialise. Nevertheless, delay, deficiency, and unevenness in rainfall during the SWM season led to a decline in the production of most *kharif* crops. The deficient SWM did not replenish soil moisture adequately and, in addition, the northeast monsoon (NEM) also turned deficient. With the production of most *rabi* crops estimated lower, the initial hope that a good *rabi* harvest could make up for the *kharif* losses was belied. At the end of the seasons, the SWM turned 12 per cent below the long period average (LPA) and the NEM 33 per cent below the LPA. In addition to under-replenishment of reservoirs and intermittent dry halts, a bigger blow to *rabi* crops, mainly to wheat, came in the form of unseasonal rainfall and hailstorms during late February and early March 2015. As per the fourth advance estimates of the Ministry of Agriculture released on August 17, 2015, the total foodgrains production declined by 4.6 per cent. Similarly, the production of oilseeds and cotton declined by 18.5 per cent and 1.2 per cent respectively, though that of sugarcane increased by 2.0 per cent. The impact of a decline in the volume of foodgrains production to 252.7 million tonnes from 265.0 million tonnes a year ago may, however, be mitigated by the availability of food stock buffers of 55.6 million tonnes (end-July 2015), which is much higher than the buffer norm which varies between 21.0-41.1 million tonnes.

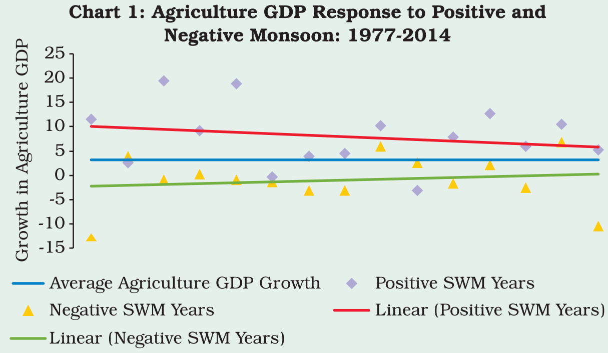
II.1.10 For the 2015 SWM season, the India Meteorological Department (IMD) has forecast precipitation at 88 per cent of the LPA in June 2015, and retained the same forecast in August 2015 with a higher likelihood of *El Nino* effect intensifying during the season[2]. Though delayed in arrival, the rainfall was in excess in June barring the last week when a dry spell set in and continued till mid-July, limiting the season's precipitation to 9 per cent below LPA so far (August 19, 2015). Better rainfall in June augmented sowing under most *kharif* crops *vis-à-vis* last year. In view of these developments, the prospects of *kharif* harvest 2015 could be expected better notwithstanding the persisting risks to supply shortfalls and likely inflation pressures given the unpredictability of SWM during the remaining part of the season, alongside the need for reappraisal of the degree of weather proofing of Indian agriculture in the context of monsoon vagaries (Box II.1).

Box II.1
How Monsoon Proof is Indian Agriculture?

Historically, agricultural failures in India have often been associated with deficient south west monsoons (SWM). The SWM which constitutes 75-80 per cent of total rainfall received in India, coincides with *kharif* sowing and is vital for replenishment of ground water, soil moisture and reservoirs and thus crucial for a good *rabi* harvest as well. Visual observation of trend growth rates of agriculture seems to suggest resilience at least in some bad monsoon years (Chart 1).

Empirical analysis of positive and negative SWM shocks suggests that during 1988-2012, the impact of variations in SWM is statistically significant for agricultural output, but it is

Chart 1: Agriculture GDP Response to Positive and Negative Monsoon: 1977-2014

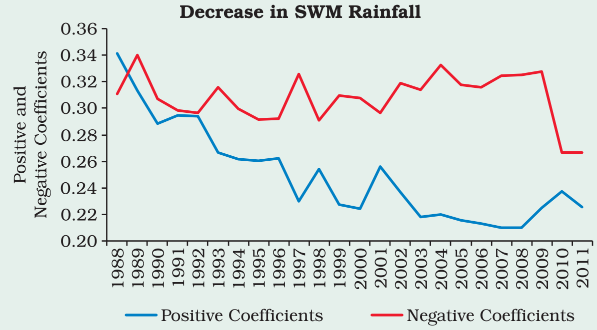


contd.

[2] In July 2015, Skymet, a weather monitoring and agri-risk solutions company revised its forecast of the SWM rainfall to 98 per cent of LPA (error margin of +/-4%) from 102 per cent of LPA (error margin of +/-4%), forecast in March 2015.

much less than that of variations in net sown area (Chart 2). The absence of multicollinearity between rainfall and sown area is validated by variance inflation factor (VIF).

Chart 2: Sensitivity Coefficients for Increase/ Decrease in SWM Rainfall



Clearly, Indian agriculture is yet to become fully weather proof and public policy interventions to insulate crop production from monsoon shocks is an imperative. Saturation of land use and exhaustion of economies of scale can be halted by multi-pronged strategies covering, *inter alia*, credit, capital and machinery, technology, research and development, use of improved and hybrid seeds, irrigation and water management, and land reclamation including in arid and semi-arid areas while more vigorously pursuing the scheme of extending the green revolution in the east. A diversified approach to agricultural development with emphasis on livestock, fishery, forestry and logging will also buffer agricultural output from SWM variations, provided it is pursued in the overall context of food and nutritional security.

Contingency plans put in place during 2009-10 in the face of a 22 per cent shortfall in SWM warrant careful consideration for replication. The provision of quality and short duration seeds, agricultural inputs, an active *rabi* campaign and an action plan for the next cropping season, media telecasting and awareness campaigns, enhanced availability of funds under centrally sponsored programmes, and additional diesel subsidy for irrigation served well, bringing home the point that the impact of adverse monsoon shocks can be ameliorated by pro-active policy measures.

References:

Aggarwal P.K. *et al*. (2009), 'Vulnerability of Indian Agriculture to Climate Change: Current State of Knowledge' available at http://www.moef.nic.in

RBI Bulletin (2015), 'Monsoon and Indian Agriculture – Conjoined or Decoupled?', May.

Industry

II.1.11 Industrial production turned around from the contraction recorded in 2013-14 and posted a growth of 2.8 per cent during 2014-15. The production of consumer durables continued to shrink as in the previous year, especially telephone instruments, including mobile phones which was due to the one-off closure of Nokia's manufacturing unit in Chennai in November 2014. Excluding this category, industrial production would have risen by 5.3 per cent during 2014-15 (Chart II.4).

II.1.12 Higher production of basic metals, electricity and capital goods drove up the index of industrial production (IIP) growth during 2014-15. In terms of the use-based classification, the production of basic and capital goods accelerated, while that of intermediate goods decelerated and the output of consumer goods contracted (Table II.2).

II.1.13 Mining activity recovered during 2014-15 from a three-year slump, buoyed by a sharp increase

Chart II.4: Growth of IIP

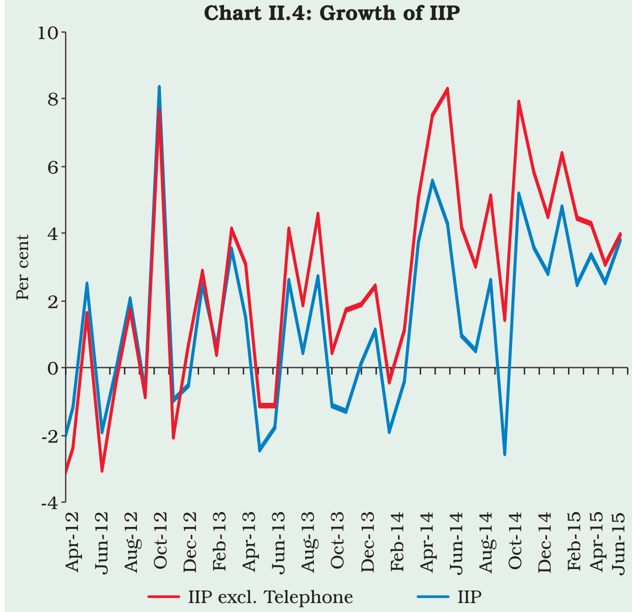


Table II.2: Index of Industrial Production

(Per cent)

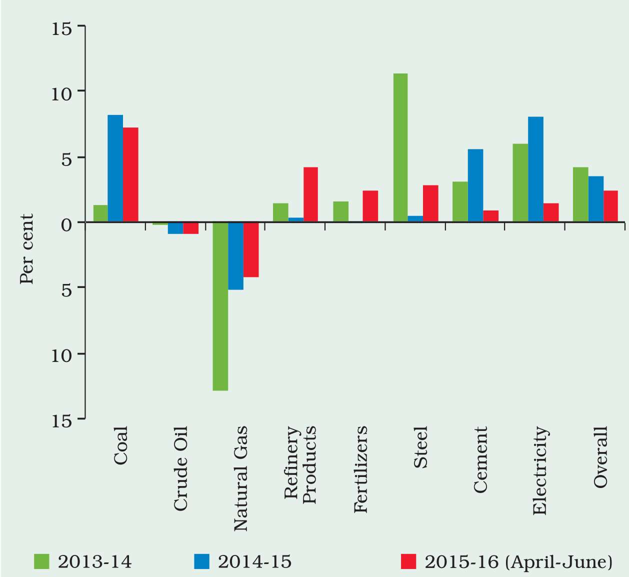
Industry Group	Weight in IIP	Growth Rate				
		2011-12	2012-13	2013-14	2014-15	April-June 2015-16P
1	2	3	4	5	6	7
Overall IIP	**100.0**	**2.9**	**1.1**	**-0.1**	**2.8**	**3.2**
Mining	14.2	-2.0	-2.3	-0.6	1.5	0.7
Manufacturing	75.5	3.0	1.3	-0.8	2.3	3.6
Electricity	10.3	8.2	4.0	6.1	8.4	2.3
Use-Based						
Basic Goods	45.7	5.5	2.5	2.1	7.0	4.7
Capital Goods	8.8	-4.0	-6.0	-3.6	6.4	1.5
Intermediate Goods	15.7	-0.6	1.6	3.1	1.7	1.6
Consumer Goods	29.8	4.4	2.4	-2.8	-3.4	2.4
Consumer Durables	8.5	2.6	2.0	-12.2	-12.6	3.7
Consumer Non-durables	21.3	5.9	2.8	4.8	2.8	1.6

Source: Central Statistics Office. P: Provisional

in the production of coal (Chart II.5). Among other items within the mining sector, the production of crude oil declined on account of ageing oil fields and delay in the execution of new oil field projects. Also, contraction in the production of natural gas from the KG-D6 block affected natural gas production during 2014-15 as in the previous three years. Electricity generation registered its highest growth in the last two decades during 2014-15, facilitated by improved coal supply and higher capacity addition of 22,566 MW (as against a target of 17,830 MW), which is the highest ever achieved in a single year. Capacity addition, coupled with higher generation and improved transmission capacity resulted in a considerable reduction in power shortage from a level of 7 to 11 per cent during the last two decades to a record low of only 3.6 per cent during 2014-15. The plant load factor (PLF) in the thermal power sector was largely sustained in 2014-15. However, there has been some slippage in the PLF in the first quarter of 2015-16.

II.1.14 Weakness in consumer spending, sluggish investment activity and poor external demand operated as drags on manufacturing activity during 2014-15. Within the manufacturing sector, export-oriented industries like textiles, wearing apparels and refined petroleum products decelerated. On the other hand, capital goods industries like machinery and equipment and electrical machinery

Chart II.5: Growth in the Index of Eight Core Industries



registered improved growth. Revival in the production of capital goods after three years of contraction signals improved prospects for investment demand going forward. During April-June 2015, however, the growth in IIP decelerated mainly on account of a sluggish performance in capital goods, electricity and food products.

Services

II.1.15 The services sector is estimated to have grown by 9.4 per cent during 2014-15 mainly driven by 'financial, real estate and professional services' and construction sector. As for 2015-16, available data on lead indicators of services sector including commercial/passenger vehicles sales, air passenger traffic, port and international air cargo, show an improvement over the corresponding period last year. However, railway freight traffic, domestic air cargo, tourist arrivals, cement production and steel consumption - which provide lead indications of construction activity- show moderation. During 2014-15, purchasing managers index (PMI) for services remained in an expansionary mode since May 2014, though the rate of expansion was at a slower pace in ensuing months. However, PMI services contracted in May-June 2015 on account of a decline in both output and new orders though it expanded marginally in July 2015. Also, given the drag emanating from fiscal consolidation by central and state governments on total spending, 'public administration, defence and other services' may not serve as a durable growth driver, going forward.

Employment Generation

II.1.16 Quarterly employment surveys conducted by the Labour Bureau for select export-oriented sectors reveal that the rate of employment generation in these sectors picked up in 2013 and 2014, after a significant decline in 2012. However, the pace of employment generation is yet to recover to its pre-2010 level. Information technology-business process outsourcing (IT-BPO) and textiles continue to be the key export oriented sectors generating large employment from 2009 to 2014.

Infrastructure

II.1.17 The growth of production in core industries (coal, crude oil, natural gas, refinery products, fertilisers, steel, cement and electricity) moderated during 2014-15 (Chart II.5) and remained sluggish during April-June 2015. Structural constraints have resulted in a persistent decline in the production of natural gas, crude oil and fertilisers. The growth of the steel industry was affected by the fall in global prices of steel and the resultant increase in steel imports. On the other hand, the coal sector's impressive growth performance during 2014-15 benefitted from several efficiency enhancing measures taken by the government for Coal India Limited (CIL), like use of mass production technologies, rationalisation of linkages from coal sources to end-users, coordinated efforts with railways for speedy evacuation of coal and shifting to underground mines.

II.1.18 As on mid-August 2015, the government's Project Monitoring Group (PMG) has received proposals for 675 projects (₹10 billion and above or any other critical projects in sectors such as infrastructure, manufacturing and power) with an estimated project cost of ₹28.8 trillion for its consideration. Out of these, 291 projects worth ₹9.9 trillion were cleared by the PMG with the majority of projects pertaining to the power sector, followed by coal, road and petroleum sectors. However, the impact of government initiatives is yet to be felt in terms of the revival of central sector infrastructure projects (₹1.5 billion and above) monitored by the

Table II.3: Status of Projects

Central Sector Infrastructure Projects					
Period	Total No. of Projects	No. of Delayed Projects	Value of Delayed Projects (₹ billion)	No. of projects without DOC	Value of projects without DOC (₹ billion)
1	2	3	4	5	6
May-15	766	237	4,826	371	2,470
Mar-15	751	328	5,752	264	1,531
Dec-14	738	315	4,961	266	1,475
Sep-14	750	312	5,504	302	1,730
Jun-14	729	290	4,975	300	1,805

Source: Infrastructure and Project Monitoring Division, MoSPI, Government of India (GoI).
DOC: Date of Commissioning.

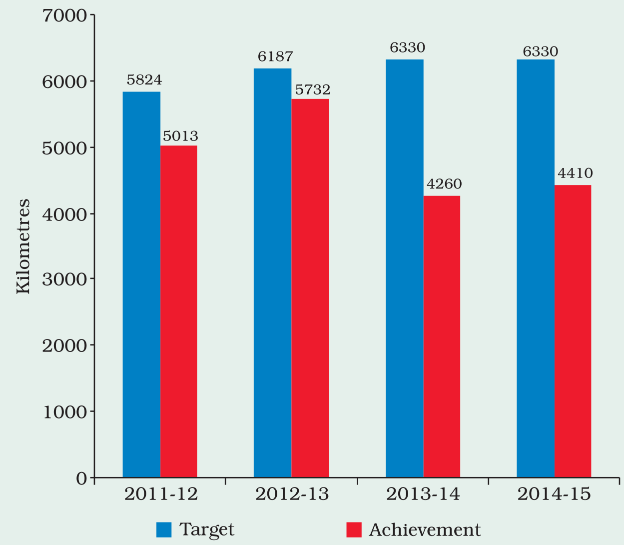
Ministry of Statistics and Programme Implementation (MoSPI) (Table II.3).

II.1.19 While investment through the public-private partnership (PPP) mode was the highest in India during 2008 to 2012 as per the World Bank's database[3], thereafter the private participation in prime infrastructure projects in roads and ports decreased sharply. The focus of the government on construction of highways through the publicly funded engineering, procurement and construction (EPC) mode is reflected in a marginal improvement in road construction activity in 2014-15 *vis-à-vis* 2013-14 (Chart II.6).

II.1.20 Spectrum auctions in March 2015 elicited vibrant bidding for all the four bands (1800 MHz, 900 MHz, 2100 MHz, and 800 MHz). This is the first time that spectrum has been offered simultaneously in all the four bands (Table II.4).

II.1.21 The government initiated a number of structural reforms in the recent period to boost the infrastructure sector: the passing of the Coal Mines (Special Provisions) Act, 2015; auctioning of coal mines; hike in tariffs on iron and steel; adoption of the plug-and-play mode of project execution for mega power projects; allowing foreign direct investment up to 100 per cent in railway infrastructure; the proposed National Investment and Infrastructure Fund; tax free infrastructure bonds for projects in the rail, road and irrigation sectors and increased plan outlays for roads and railways.

Chart II.6: Implementation of Road Projects by NHAI



Source: National Highways Authority of India (NHAI), Government of India.

II.1.22 In order to give a direct thrust to infrastructure investment, the government has stepped in to boost public spending in infrastructure by ₹700 billion in 2015-16. These efforts are also expected to crowd in private participation. Going forward, the government's decision to award new projects only after obtaining the requisite clearances and linkages could catalyse the pace of infrastructure project completion.

Table II.4: Spectrum Auction

Year	Revenue Realisation (₹ billion)
1	2
2010	1062.62
2012	94.07
2013	36.39
2014	611.61
2015	1098.75

Source: Ministry of Information & Communication Technology, GoI.

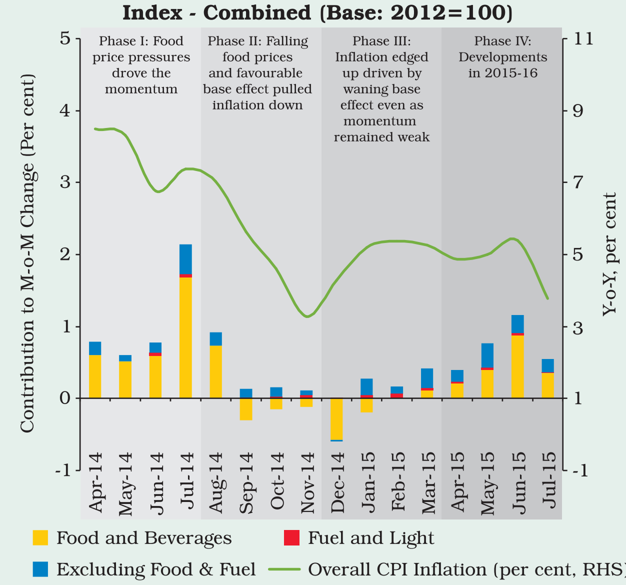
[3] Compendium of *'PPP projects in infrastructure',* Planning Commission, Government of India, March 2014.

II.2 PRICE SITUATION

II.2.1 The year 2014-15 marked a turning point in the evolution of price-cost dynamics in India. In January 2014, the stance of monetary policy was anchored to a path of disinflation that would take inflation (measured in terms of y-o-y changes in the all India consumer price index (combined) or CPI-C, base 2010 =100) down from 8.6 per cent to below 8 per cent by January 2015 and to below 6 per cent by January 2016. This stance was backed by policy rate increases of 25 basis points each in September 2013, October 2013 and January 2014. Although unseasonal food price spikes owing to weather-related transportation disruptions in north India kept inflation stubbornly high till July 2014, steadfast perseverance with the anti-inflationary monetary policy allowed rate increases in the second half of 2013-14 to feed through into the economy. Aided by a range of supply management strategies and a dramatic plunge in international commodity prices[1] by 28 per cent between September 2014 and February 2015, inflation persistence (near double digit CPI inflation for six consecutive years) was finally broken and headline inflation started easing from August 2014. The abatement in food price pressures contributed 76 per cent to the decline in inflation between July and November 2014. By April 2015, it had declined to 4.9 per cent measured by the new CPI series (base 2012=100), thus confirming that disinflation was getting entrenched. Notwithstanding an uptick in June 2015 to 5.4 per cent, largely reflecting fuel price adjustments and short-term food price pressures, inflation moderated significantly to 3.8 per cent in July 2015. Importantly, inflation excluding food and fuel almost halved from 8.3 per cent in May 2014 to 4.2 per cent in March 2015, providing abiding momentum to the disinflation process. However, this moved significantly up to 5.0 per cent in June 2015 before falling to 4.5 per cent in July 2015. By December 2014, households' inflation expectations (both three months ahead and one-year ahead), which had been ruling in double digits persistently since September 2009, eased to single digit.

II.2.2 Average inflation at 5.9 per cent during 2014-15 turned out to be significantly lower than 9.5 per cent a year ago (Chart II.7). Intra-year movements in inflation during 2014-15, however, exhibited three distinct phases – first, weather-related vegetable price pressures till August; second, the subsequent fall in food prices and pass-through of declining global commodity prices into food, fuel and services prices, resulting in a major shift in the inflation trajectory that took inflation down to an intra-year low of 3.3 per cent in November 2014; and finally the reversal of favourable base effect, which pushed inflation up

Chart II.7: Trends in Inflation: Consumer Price Index - Combined (Base: 2012=100)



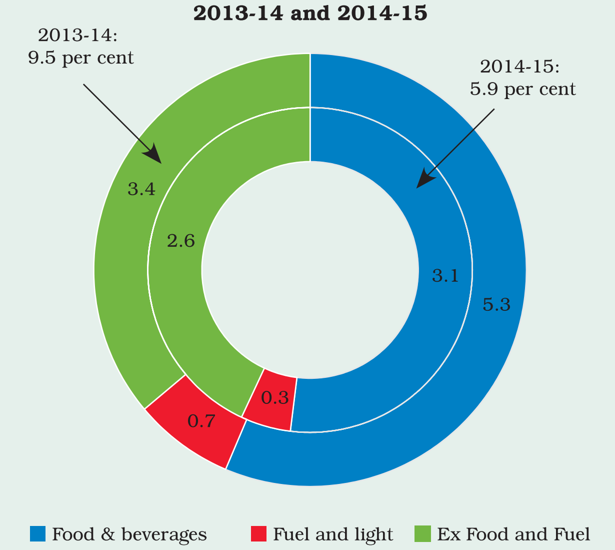
[1] As measured by IMF's primary commodity price index.

to 5.3 per cent in March 2015. Significantly, even as inflation moved up during December 2014 - February 2015, the month-on-month increase in prices remained moderate or negative, attesting to the sustained abatement of inflation risks.

Drivers of CPI Inflation

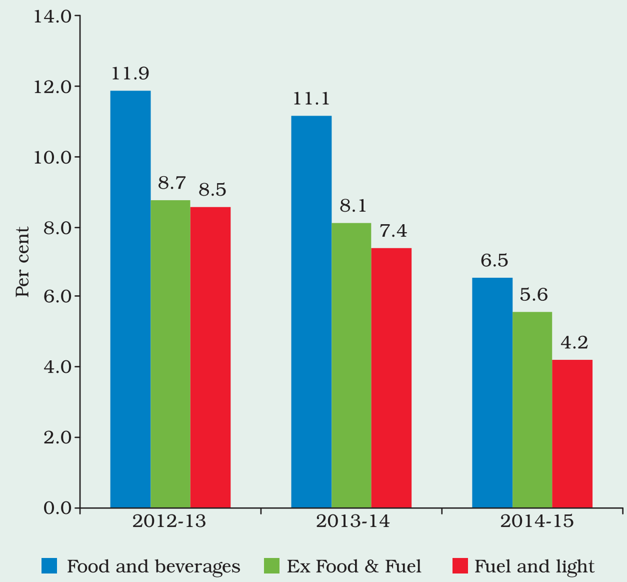
II.2.3 All the three major constituent groups of CPI - food, fuel and categories excluding food and fuel - contributed to a decline in headline inflation, reflecting improvement in supply conditions and the ebbing of inflation momentum (Chart II.8), with the largest impact emanating from the food component. Fuel group's contribution to inflation remained marginal, reflective of its relatively lower weight and declining frequency of changes in administered prices of non-transport fuel items. The fall in inflation, excluding food and fuel, was facilitated by the anti-inflationary monetary policy stance as inflation in most of its sub-components edged down.

Chart II.8: Contributors to CPI Inflation: 2013-14 and 2014-15



Note: Figures within the chart indicate contribution in percentage points.

Chart II.9: CPI Inflation in Major Groups



Food Inflation

II.2.4 The wedge between inflation in food and non-food groups narrowed considerably during 2014-15 (Chart II.9). Two major groups - cereals and vegetables - together accounted for almost 80 per cent of the decline in average food price inflation during the year. Cereals' inflation declined partly on account of the lower order of revision in minimum support prices (MSPs) in 2014-15 (Table II.5) and active supply management under the

Table II.5: Minimum Support Prices of Food Grains (₹ per quintal)

Commodity	2012-13	2013-14	2014-15	2015-16
1	2	3	4	5
Paddy (Common)	1,250	1,310	1,360	1,410
Wheat	1,350	1,400	1,450	-
Gram	3,000	3,100	3,175	-
Arhar (Tur)	3,850	4,300	4,350	4,425
Moong	4,400	4,500	4,600	4,650
Urad	4,300	4,300	4,350	4,425

Source: DAC, Ministry of Agriculture & Farmers Welfare.

public distribution system (PDS), including the open market sale of wheat. Vegetable prices shrugged off bouts of weather-related volatility in H1 of 2014-15 and declined relatively faster in H2 of 2014-15 with policy actions taken to discourage stockpiling, and bringing vegetables under the Essential Commodities Act (ECA). Sugar prices moderated in tandem with global prices, but protein-rich items (eggs, fish, meat, milk and pulses) exhibited downward rigidity in inflation, reflecting structural mismatches between demand and supply.

II.2.5 A number of policy initiatives were taken to improve both supply chain and post-harvest crop management. These included issuing advisories to states to enable free movement of fruits and vegetables by delisting them from the Agricultural Produce Marketing Committee (APMC) Act; bringing onions and potatoes under the purview of ECA, thereby allowing state governments to impose stock limits so as to deal with cartelisation and hoarding and making violation of stock limits a non-bailable offence. Imposing a minimum export price (MEP) of US$ 450 per metric tonne (MT) for potatoes with effect from June 26, 2014 and US$ 300 per MT for onions with effect from August 21, 2014 also helped in maintaining domestic supplies of these perishable items.

Fuel Group Inflation

II.2.6 From August 2014, crude oil prices fell but the full pass-through of this decline was impeded by lingering under-recoveries of the oil marketing companies (OMCs) (Table II.6). Further, the government increased the excise duty on petrol and diesel cumulatively by ₹7.75 per litre for petrol

Table II.6: Under-recoveries of Oil Marketing Companies

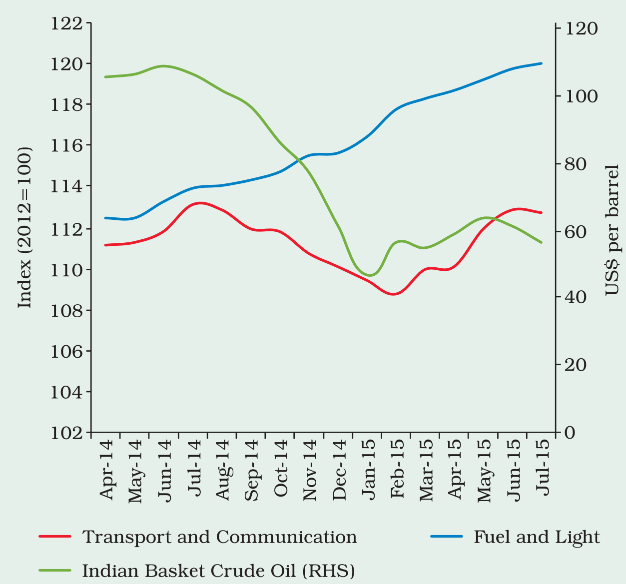
(₹ billion)

Product	2013-14	2014-15
1	2	3
Diesel	628	109
PDS Kerosene	306	248
Domestic LPG	465	366
Total	**1,399**	**723**

Source: PPAC, Ministry of Petroleum & Natural Gas.

and ₹6.50 per litre for diesel during November 2014 - January 2015, which partially offset the overall fall in prices. In case of coal, Indian prices have historically remained substantially lower than the global prices. Therefore, the decline in global coal prices during 2014-15 resulted in bridging the gap between global and domestic prices rather than a fall in domestic prices. Since the CPI fuel group includes a number of items, such as electricity and kerosene whose prices are administered, prices in this category remained sticky (Chart II.10).

Chart II.10: Global and Domestic Fuel Price Movements



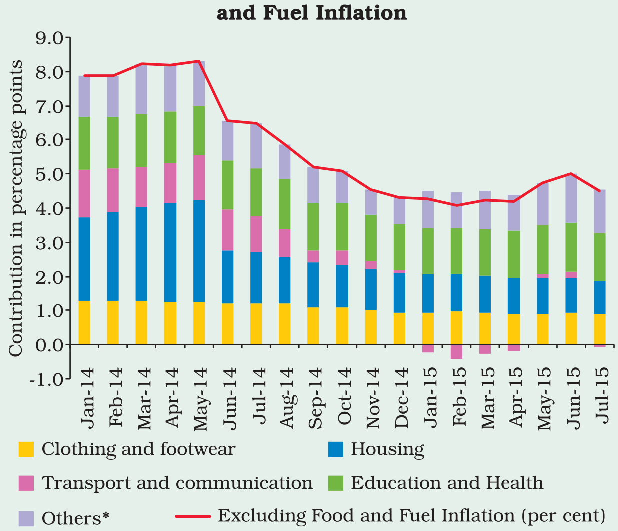
Inflation Excluding Food and Fuel

II.2.7 Prices in respect of the transport and communication sub-group declined in tandem with softening of global crude oil prices. By the end of the year, the transport and communication category contributed negatively to inflation (Chart II.11). Also, housing inflation showed a much more significant moderation under the new series (base 2012=100) partly on account of methodological improvements, which included doubling the sample size for collection of rentals data from 6,684 rented dwellings in the old series to 13,368 in the revised series. Inflation in services components, such as health, education and household requisites declined, reflecting a slowdown in wage growth.

Rural Wage Growth Moderated

II.2.8 Input cost pressures from fuel, farm inputs and rural wages ebbed significantly during 2014-15. After the high and unprecedented rise in rural wages during 2007-08 to 2012-13, the recent slowdown in wage growth has evoked academic and policy interest. Average wage growth, as per the new wage series, for November 2014 to May 2015, remained at 3.9 per cent for agricultural and 5.7 per cent for non-agricultural occupations, respectively. This was substantially lower than the annual average rate of 16 per cent for agricultural occupations and 14 per cent for non-agricultural occupations during the six-year period from 2007 to 2013. However, the role of productivity will have to be examined carefully while assessing the durability of the impact of the changes in wage growth on inflation (Box II.2).

Chart II.11: Drivers of CPI Excluding Food and Fuel Inflation



*: Includes household goods and services, personal care and effects, recreation and amusement.

Wholesale Price Inflation

II.2.9 Inflation measured by the wholesale price index (WPI) declined significantly during 2014-15. Since November 2014, wholesale prices have moved into contraction [(-) 4.1 per cent in July 2015, y-o-y] (Chart II.12). Prices of non-food manufactured products also contracted in July 2015 [(-) 1.4 per cent, y-o-y], indicating the extent of slack in the economy as well as falling cost pressures.

Global Commodity Prices and Supply Conditions

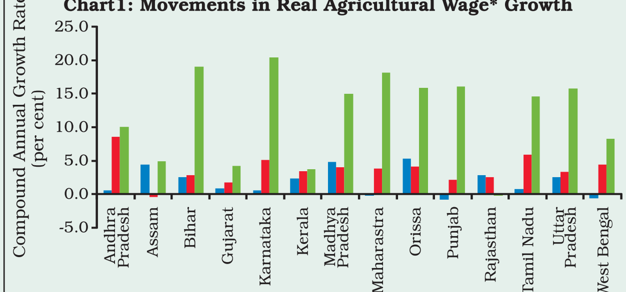
II.2.10 Global commodity prices declined sharply amidst improved supply, large spare capacity and weak demand conditions in 2014-15 (Chart II.13). During the initial part of the year, crude oil prices hardened on account of supply outages in Libya, Nigeria and Syria. From August 2014, global crude oil prices fell substantially, driven by abundant supplies of North American shale oil and the Organisation of Petroleum Exporting Countries' (OPEC) decision not to cut production at its November 2014 meeting. Global crude oil prices reached a trough of US$ 47 per barrel

Box II.2
Wage Growth and Rural Inflation – Are They Related?

An increase in rural wages can influence prices, both by increasing demand and pushing up the cost of production. On the other hand, wage growth in itself could respond to high price increases, particularly food price increases. The wage-inflation nexus also works through productivity - as labour productivity increases, wages rise. An increase in labour productivity will reduce unit labour cost, which is the average cost of labour per unit of output (usually calculated as the ratio of total labour costs to real output) and therefore, it will be possible to pay a higher wage without an increase in final output price. On the other hand, if wage increases are unaccompanied by productivity increases, rise in unit labour costs will lead to further increase in output prices and hence inflation. This dynamics is more complex in a regional perspective, where there is large heterogeneity in product and labour markets.

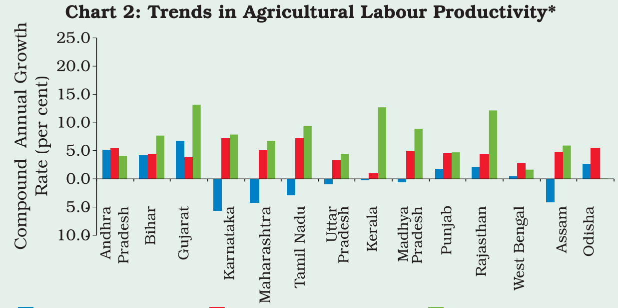
A comparison between agricultural labour productivity and agricultural wages at the all-India level as well as for major states is insightful. Real wage growth, *i.e.*, growth in agricultural wages adjusted for CPI - agricultural labourers (AL) inflation, remained moderate during 1999-00 to 2009-10. Subsequently, it went up sharply during 2009-10 to 2011-12 (Chart 1). This trend was broad-based and observed in major agricultural states like Bihar, Maharashtra, Madhya Pradesh, Tamil Nadu and Uttar Pradesh.

Chart1: Movements in Real Agricultural Wage* Growth



*: Estimated using NSSO data for casual labourers in agriculture, deflated by CPI-AL.

Chart 2: Trends in Agricultural Labour Productivity*



*: NSDP per worker in Agriculture and allied activities at constant prices.

Agricultural labour productivity declined in some states over the period from 1999-2000 to 2004-05, but went up subsequently during the period 2009-10 to 2011-12 at the all-India level as well as for major states (Chart 2). The productivity improvement was partly contributed by a shift in labour force from agricultural to non-agricultural occupations, which led to a decline in the total number of persons engaged in agriculture in 2011-12 *vis-à-vis* 2004-05. Thus, the sharp increase in real wages in recent years was partly offset by a rise in productivity. The impact of rural wage increases on rural food prices was not as large due to commensurate rise in productivity (Goyal and Baikar 2014). Post-2013, real wage growth declined in India barring a few states like Madhya Pradesh, Uttar Pradesh, Gujarat and Tamil Nadu. The fall in real wage growth is mainly contributed by a fall in nominal wage growth.

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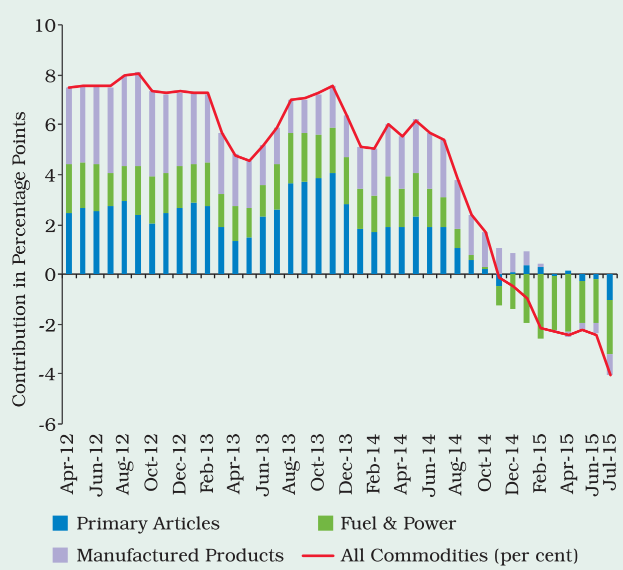
Goyal, A. and A.K. Baikar (2014), 'Psychology, Cyclicality or Social Programs: Rural Wage and Inflation Dynamics in India', WP, IGIDR, Mumbai.

(Indian basket), marking a decline of 57 per cent during June 2014 to January 2015. Though the slow pace of global economic recovery has kept demand prospects weak, the International Monetary Fund (IMF) estimated that lower demand could account for only 20 to 35 per cent

Chart II.12: Group-wise Contribution to WPI Inflation



of the price decline between June and December 2014.

II.2.11 Since January 2015, several factors, such as falling oil rigs in the US, decline in stockpiles and elevated geo-political tensions in the Middle East rekindled upside risks to oil prices. Indian basket prices firmed up to US$ 63.8 per barrel in May 2015 but declined subsequently to US$ 49 per barrel by mid-August 2015 as supply prospects improved with the clinching of the nuclear deal by Iran with the major world powers. Metal prices edged down in 2014 aided by surplus supplies and slowing demand conditions in emerging economies, particularly in China.

II.2.12 Global food prices declined by 3.8 per cent in 2014 as large accumulated stocks continued to pull down international prices of commodities, such as cereals, oils and sugar. The Food and Agriculture Organisation (FAO), in its update of July 2015, forecast that the world cereals production might decline by 1.1 per cent in 2015 while exceptionally high stocks were likely to compensate for the production shortfall. During 2015 so far, prices have continued to move downwards for almost all food items, with large supplies and slow trading activity as buyers are expecting a further fall in prices in the coming months.

Revision in the CPI Base Year

II.2.13 In order to capture shifting consumption pattern of households, the Central Statistics Office (CSO) revised the base year of CPI to 2012 from its earlier base of 2010, using the weighting pattern from the latest consumer expenditure survey (CES), 2011-12 of the National Sample Survey Office

Chart II.13: Trends in Global Commodity Prices

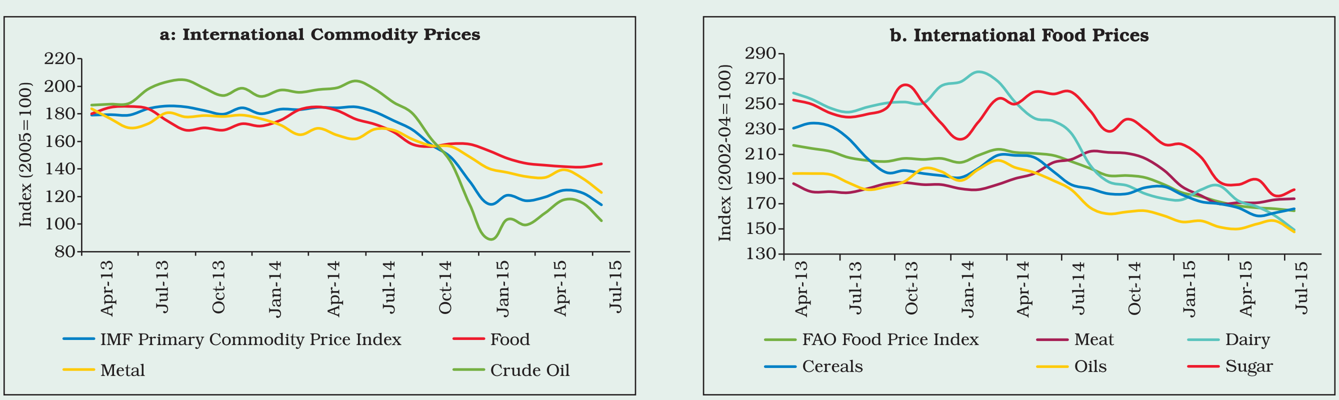


Table II.7: Comparison of Weighting Diagrams–Previous and Revised CPI Series

(Per cent)

Sub-Categories	Base Year: 2010			Base Year: 2012		
	Rural	Urban	Combined	Rural	Urban	Combined
1	2	3	4	5	6	7
Food and Beverages	56.59	35.81	47.58	54.18	36.29	45.86
Pan, Tobacco and Intoxicants	2.72	1.34	2.13	3.26	1.36	2.38
Clothing and Footwear	5.36	3.91	4.73	7.36	5.57	6.53
Housing	--	22.54	9.77	--	21.67	10.07
Fuel and Light	10.42	8.40	9.49	7.94	5.58	6.84
Miscellaneous	24.91	28.00	26.31	27.26	29.53	28.32
Total	**100**	**100**	**100**	**100**	**100**	**100**

'--' : CPI (Rural) for housing is not compiled.

Source: Press Release on CPI base year revision, MOSPI, GoI.

(NSSO). Changing patterns of consumer expenditure over the years are reflected in sub-category-wise weights computed for the new CPI series (Table II.7).

II.2.14 Methodologically, the new series has incorporated certain improvements: a weighting pattern based on the modified mixed reference period (MMRP); internationally accepted 'classification of individual consumption according to purpose' with suitable deviations; and the use of a geometric mean to compute indices at the elementary/item level. Along with the prices of items under the above poverty line (APL) and below poverty line (BPL) categories, prices of items under the *Antyodaya Anna Yojana* (AAY) are also incorporated in the new series. The revision has a number of policy implications: lower sensitivity of the overall index to food price shocks and idiosyncratic price movements and incisiveness in identifying sources of inflation at the item level.

Developments in Inflation: 2015-16 so far

II.2.15 After dipping below 5 per cent in April 2015, CPI inflation edged up to 5.4 per cent in June driven by the food group owing to a fall in pulses production during 2014-15 and short-term pressures in vegetables prices. In July, however, inflation declined significantly to 3.8 per cent aided by favourable base effect and ebbing food price pressures. Excluding food and fuel, inflation moved up substantially to 5.0 per cent in June 2015 from 4.2 per cent in March 2015 on account of a broad-based rise in inflation in services segment, such as health and education as well as retail fuel price increases captured by the transport and communication sub-group. It, however, moderated to 4.5 per cent in July 2015 tracking lower transport costs with recent fall in fuel prices. Importantly, household inflation expectations returned to double digits in June 2015 quarter.

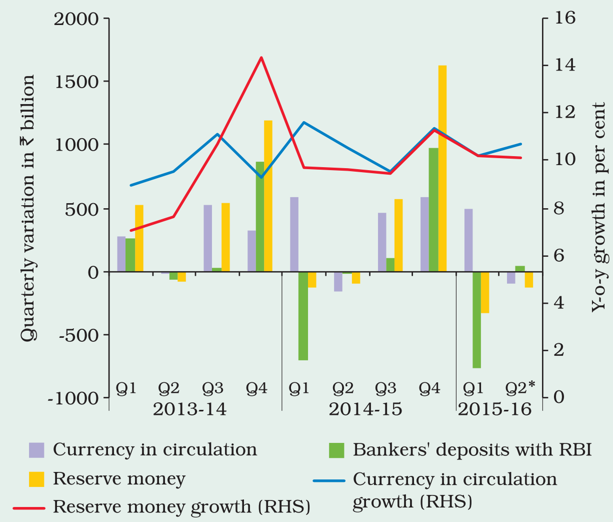
II.3 MONEY AND CREDIT

II.3.1 Monetary and credit conditions remained sluggish through 2014-15 as reflected in the subdued growth in key monetary and banking aggregates. The sizeable expansion in Reserve Bank's net foreign exchange assets driven by surges in capital inflows was largely sterilised by active liquidity management operations. Consequently, reserve money grew at a subdued pace, reflecting the slow pace of economic activity as well as the anti-inflationary monetary policy stance of the Reserve Bank. Growth of money supply (M_3) also slowed in relation to the preceding year reflecting the interaction of a number of factors. First, credit demand was muted reflecting the slack in the economy. Second, increasing levels of non-performing assets (including restructured assets) imparted an element of risk aversion across the banking sector. This inhibited credit supply, especially to stressed sectors such as infrastructure, with substitution at the margin in loan portfolios in favour of personal loans and retail lending where the incidence of non-performing assets (NPAs) was markedly less. Accordingly, banks tended to moderate their access to deposits which were also impacted by inadequate real returns relative to competing financial assets of households and corporate entities.

Reserve Money

II.3.2 During 2014-15, reserve money expanded by 11.3 per cent, down from 14.4 per cent a year ago. On the components side, currency in circulation, constituting around 75 per cent of reserve money, increased by 11.3 per cent. The pick-up in currency demand from 9.2 per cent a year ago reflected the interaction of several factors -election-induced demand for currency and increased food subsidy (Chart II.14). On the other hand, growth of bankers' deposits with the Reserve Bank slowed to 8.3 per cent, mainly reflecting the

Chart II.14: Variation in reserve money and its components



* : Data up to August 7, 2015.

deceleration in deposit growth. The maintenance of reserves evened out across 2014-15 following the introduction of minimum daily CRR balances of 95 per cent since September 2013. Average daily excess reserve holdings by the banking sector declined from around 3 per cent in 2013-14 to 2 per cent in 2014-15, which indicated some efficiency gains under the new liquidity management framework introduced in September 2014. Variable rate auctions have induced some discipline in the banking system in planning liquidity. A system level liquidity flux appears to have eased with assurance on availability of liquidity as needed.

II.3.3 On the sources side, there was a change in the composition of reserve money in 2014-15 in terms of net domestic assets (NDA) and net foreign assets (NFA). With the emergence of India as a preferred destination for foreign capital, the Reserve Bank's foreign exchange operations to mitigate undue volatility in the foreign exchange market resulted in a large increase in NFA, injecting around ₹3.2 trillion primary liquidity (reserve money) into the financial system. Concomitantly, NDA (adjusted for net non-monetary liabilities) declined by around ₹1.9 trillion to partially sterilise the impact of the

Reserve Bank's forex market operations on reserve money expansion.

II.3.4 Global financial markets have been roiled by turbulence associated with divergence in monetary policy stances in the G3 economies. During 2014-15, significant shifts in monetary policy settings were also observed among emerging economies to manage the effects of G3 monetary policies on their financial systems transmitted through capital flows and asset prices as also to deal with domestic fragilities which restrained growth and made them vulnerable to financial shocks. Cross-border externalities associated with the conduct of unconventional monetary policies in advanced and emerging economies alike occupied centre-stage in 2014-15 (Box II.3).

II.3.5 In response to these global factors affecting domestic liquidity conditions, the Reserve Bank endeavoured to contain the expansionary effects in keeping with its commitment to the glide path of disinflation. The Reserve Bank, therefore, appropriately calibrated repo auctions and open

Box II.3
Spillovers and Spillbacks

'Spillovers' have come to be commonly employed in the post-unconventional monetary policy (UMP) literature to refer to the beneficial or damaging effects that a country's economic policies can have on other nations. In the more recent period, the focus has largely been on negative externalities associated with the Fed's quantitative easing (QE) and its widely anticipated normalisation, especially as the Fed's forward guidance on it has been data-dependent and consequently, every incoming data has triggered intense market reactions on its possible timing. In the event, UMPs have generated large capital flows to emerging market economies (EMEs) in an indiscriminate search for yields, while exit from them has increased the risks of substantial capital outflows of which the taper tantrum of the summer of 2013 provided a sinister preview. Empirical evidence suggests that UMPs have amplified the pro-cyclicality of capital flows and leverage in EMEs by strengthening the incentives to engage in maturity transformations, leading to misalignment with fundamentals with adverse implications for macroeconomic and financial stability (Fratzscher *et al.* 2013; Moore et al. 2013). Quite naturally, spillovers from UMPs have been the subject of acrimonious disharmony (Taylor 2013). Given the heterogeneity in the structural characteristics of EMEs, it is important to nuance these findings and qualify them with country-specific experiences.

For India, an analysis of the impact of spillovers from the Fed's QEs using a combination of methodologies, such as the event study framework, generalised method of moments (GMM) and vector auto-regressions (VARs) shows that the largest favourable impact came from QE1 that pushed capital flows into India, helping finance a widening current account deficit. QE2, unlike QE1, was associated with capital outflows from India. These spillovers were transmitted mainly through the portfolio rebalancing channel, followed by the liquidity channel (Patra *et al.* 2014).

'Spillbacks' are a new entrant in this proliferating body of work, essentially the boomerang effects from recipient countries in a vicious loop that in a globally inter-dependent world adversely affect the source country that caused the spillovers in the first place. The larger global role played by EMEs implies that spillbacks from fluctuations in their growth as a result of shocks in advanced economies can be non-trivial. VAR specifications suggest that about 50 per cent of the fluctuations in outputs in advanced economies spill over onto EMEs of which one-third spill back to advanced economies (IMF 2014) (Table 1).

Spillback effects are more pronounced for Japan and the euro area, and less for the United States and the United Kingdom due to stronger trade linkages (Trade openness for the US and the UK is relatively far less).

Overall, spillback effects appear to be modest but could be larger in periods of stress, which in turn might have an

Table 1: Estimated spillovers and spillbacks (per cent)

	US	Euro Area	Japan	UK	Average
1	2	3	4	5	6
EM Spillover	58.3*	59.2*	25.4*	56.3*	52.8
EM Spillback	12.4	29.8*	12.7*	7.2	17.4
EM Spillback/ EM Spillover	21.3	50.4	51.1	12.8	34.4

Source: IMF staff calculations.
*: Significant at the 10 per cent level. Estimates of spillovers and spillbacks from a 1 percentage point increase in growth in advanced economies (eight quarters after impact).

(Contd...)

adverse impact on the setting of monetary policy. Careful calibration and clear communication, with cooperation among policymakers could help in managing spillbacks and spillovers.

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Moore J., S. Nam, M. Suh and A. Tepper (2013),'Estimating the Impacts of US LSAP's on Emerging Market Economies' Local Currency Bond Markets', Staff Report No. 595, Federal Reserve Bank of New York.

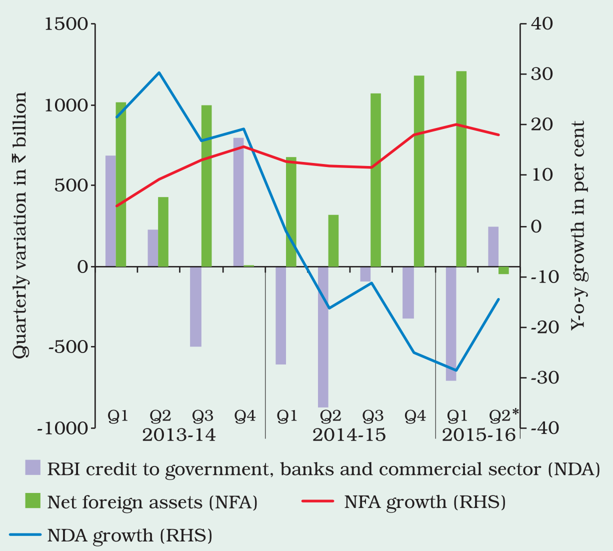
Patra, M.D., J.K. Khundrakpam, S. Gangadaran, Rajesh Kavediya and Jessica Anthony (2014), 'Responding to QE Taper from the Receiving End', mimeo, RBI.

Taylor John B. (2013),'International Monetary Policy Coordination: Past, Present and Future', Paper prepared for presentation at the 12th BIS Annual Conference on 'Navigating the Great Recession: What Role for Monetary Policy', Lucerne, Switzerland, June 21.

market operation (OMO) sales, both outright and on the Negotiated Dealing System-Order Matching (NDS-OM) platform to contract NDA and offset the large increase in NFA (Chart II.15).

II.3.6 Quarterly movements in reserve money in 2014-15 evolved in line with changing drivers of liquidity and resulting composition shifts in the Reserve Bank's balance sheet. On the components side, except for the seasonal decline in Q2, currency in circulation increased throughout the year. On the sources side, the increase in NFA was largely offset by a decline in NDA in the H1 of 2014-15. In Q4, however, end year balance sheet adjustments and

Chart II.15: Variation in sources of reserve money



* : Data up to August 7, 2015.

advance tax payments tightened liquidity conditions, warranting injection of primary liquidity that remained largely unsterilised. Consequently, reserve money growth increased in the last quarter of 2014-15.

II.3.7 There was also a change in the composition of NDA during 2014-15 which was in accordance with modifications in the Reserve Bank's accounting policies as recommended by the Technical Committee formed to review the format of the balance sheet and the profit and loss account of the Reserve Bank (Chairman: Shri Y.H. Malegam). Specifically, net repo operations are now being recorded under the Reserve Bank's credit to banks and commercial sector rather than in its credit to general government as was done earlier. These accounting changes are reflected in a decline in the Reserve Bank's net credit to the government and the commensurate increase in its net claim on banks in 2014-15, though the absolute size of NDA remains unaffected.

II.3.8 Movements in reserve money influence the broader measures of money supply through the money multiplier. In terms of magnitude, the money multiplier stood at 5.5 in March 2015, unchanged from its level a year ago. Both the cash deposit ratio and the cash reserve ratio remained unchanged over the year, imparting stability to the money multiplier.

Money Supply

II.3.9 The money supply growth slowed down in 2014-15 (Table II.8), mainly reflecting easing inflation which lowered the demand for money. The slowdown in money supply in general, and in aggregate deposits in particular, *vis-à-vis* 2013-14 has to be seen in the context of the base effect caused by the swap facility for FCNR(B) deposits operated by the Reserve Bank during September-November 2013 which led to high mobilisation of these deposits in 2013-14. Money supply net of FCNR(B) deposits was marginally lower in 2014-15 than in the preceding year. However, money supply improved in the second half of the year (March 2015 over September 2014) in line with the growth in credit. In tandem, the year-on-year growth in the liquidity aggregate L1 [sum of the new monetary aggregate (NM_3) and postal deposits] remained marginally lower than a year ago.

II.3.10 Growth in aggregate deposits, which forms a major component of money supply, has generally been declining over the years in line with a decrease in the saving rate of the economy. In addition, slowdown in credit growth led to lower deposit mobilisation by banks. The growth in aggregate deposits decelerated to 10.6 per cent in 2014-15 from 14.1 per cent a year ago. On the sources side, a decline in banks' credit growth to the commercial sector was one of the key drivers. Another major constituent from the sources side, that is, net bank credit to the government declined during the year mainly due to reduction in the Reserve Bank's holding of government securities (G-secs). Commercial banks, on the other hand, stepped up their investment in G-secs in view of credit deceleration during the year.

II.3.11 The velocity of money (Chart II.16), which declined over the past six decades hovered around

Table II.8: Monetary Aggregates

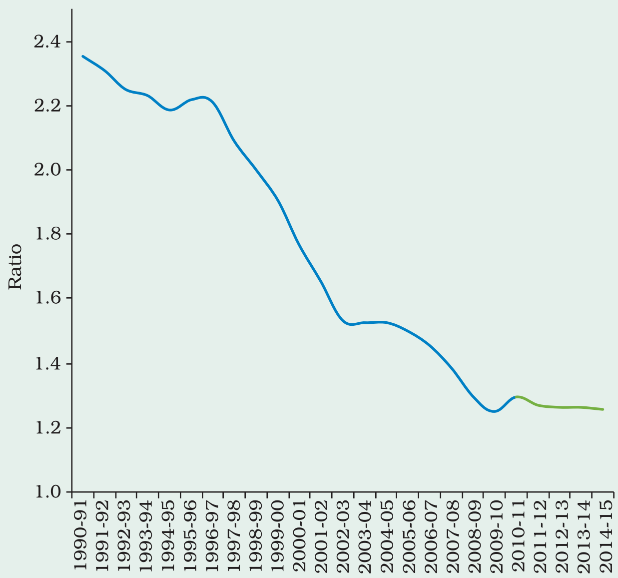
Item	Outstanding as on (₹ billion)		Year-on-year growth rate (in per cent)			Growth rate (in per cent)		
	March 31, 2015	August 7, 2015	2013-14	2014-15	2015-16 (as on August 7)	FY 15: H1	FY 15: H2	FY16: H1
1	2	3	4	5	6	7	8	9
I. Reserve Money	19,285	18,815	14.4	11.3	10.1	-1.4	12.9	-2.4
II. Broad Money (M_3)	105,455	109,830	13.4	10.8	10.9	4.4	6.2	4.1
III. Liquidity Aggregate (L1)	106,759	110,722#	11.2	10.7	11.6#	4.0	6.5	3.7#
IV. Major Components of M_3								
IV.1. Currency with the Public	13,863	14,251	9.2	11.3	9.5	3.4	7.6	2.8
IV.2. Aggregate Deposits	91,446	95,567	14.1	10.6	11.2	4.4	5.9	4.5
V. Major Sources of Money Stock (M_3)								
V.1. Net Bank Credit to Government	30,062	33,781	12.4	-1.3	10.6	-0.5	-0.8	12.4
V.2. Bank Credit to Commercial Sector	70,396	71,627	13.7	9.2	9.0	2.3	6.8	1.7
V.3. Net Foreign Exchange Assets of the Banking Sector	22,506	23,664	17.6	17.0	16.0	3.9	12.6	5.1
M_3 Net of FCNR(B)	102,782	107,009	11.5	11.0	11.1	4.4	6.3	4.1
M_3 Multiplier	5.5	5.8						
M_3 Velocity	1.25	-						

-: Not available; #: Data pertain to July 2015.

Note: 1. Data are provisional.

2. FY 15: H1: Growth rate of September 2014 over March 2014, FY 15: H2: Growth rate of March 2015 over September 2014, and FY 16: H1: Growth rate of August 7, 2015 over March 31, 2015.

Chart II.16: Velocity of money



1.25, indicating stability of the financial system in the post-crisis years. Another commonly referred indicator of financial deepening - M_3 to GDP ratio - which is a reciprocal of velocity, stood at around 80.

CREDIT

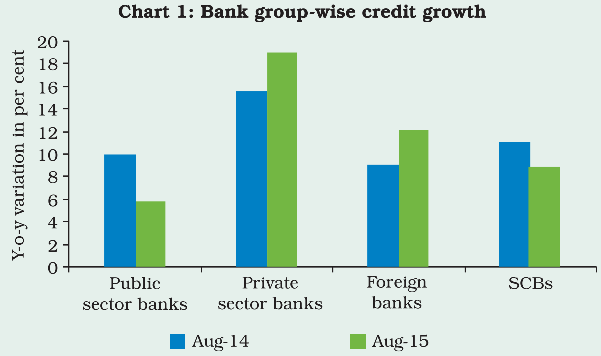
II.3.12 Non-food credit growth decelerated sharply in 2014-15 to 9.3 per cent (y-o-y), with incremental non-food credit declining to ₹5.5 trillion from ₹7.3 trillion in the previous year. A host of factors weighed down on credit off-take, including lower corporate sales, softening of inflation rate, risk aversion by banks due to rise in non-performing loans, and procedural delays in debt recovery (Box II.4). Further, with the availability of alternative sources, both domestic

Box II.4
Factors Underlying Recent Credit Slowdown: An Empirical Exploration

Credit plays an important role in economic development, particularly in a bank-based financial system. Countries which experienced high growth since 2000 also witnessed a surge in private credit (Claessens *et al.* 2011). An empirical analysis also suggests that credit growth is positively influenced by deposit growth, GDP growth, easy global liquidity conditions and exchange rate depreciation, whereas inflation dampens real credit growth (Guo and Stepanyan 2011). In India's bank-based financial system, credit plays an important role in the overall growth dynamics.

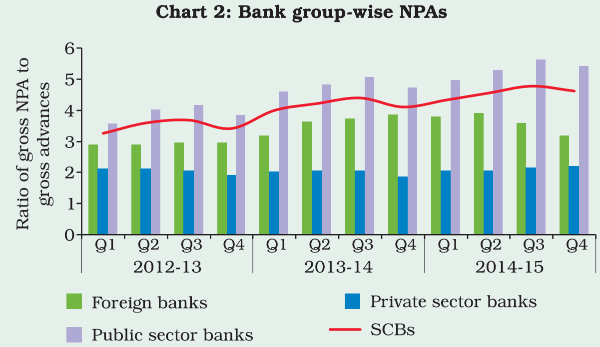
Asset quality concerns resulting in risk aversion are considered to be one of the major factors underlying the current slowdown in credit. Public sector banks, which recorded higher NPA ratios, experienced a sharp decline in credit growth. On the other hand, private sector banks with lower NPA ratios, posted higher credit growth (Chart 1 and 2). At the aggregate level, the NPA ratio and credit growth exhibited a statistically significant negative correlation of 0.8, based on quarterly data since 2010-11.

Chart 1: Bank group-wise credit growth



Note: SCBs exclude RRBs.

Chart 2: Bank group-wise NPAs



Source: Off-site returns as reported by banks, domestic operations.

(Contd....)

Applying the methodology of Guo and Stepanyan (2011) to Indian quarterly data from June 1997 to September 2014, non-food credit was found to be influenced by lagged real GDP growth in a positive and statistically significant manner. The cost of credit proxied by the overnight call rate, as expected, had a negative impact on credit growth. The impact of the interest rate was found to be strong up to two lags, reflecting transmission lags. In line with the theory, the coefficient of gross fiscal deficit (GFD) of the Centre had a negative sign, indicating crowding out effects of fiscal deficit in market for bank credit. Finally, the change in outstanding commercial papers (CPs), a proxy for an alternative source of funds, had a negative and significant coefficient.

$$BC = 7.2 + \underset{(2.4)^*}{0.6\ GDP(-2)} - \underset{(-2.3)^*}{0.3\ WCMR(-2)} - \underset{(-2.4)^*}{0.2\ GFD} - \underset{(-2.3)^*}{0.04\ CP\_Out} + \varepsilon$$

Adjusted R^2=0.30; *: Significant at 5 per cent;

NPAs were not included in the regression as the series had multiple structural breaks.

Note: 1. BC=q-o-q seasonally adjusted growth in bank credit; WCMR=quarterly weighted average call rate; GDP= q-o-q seasonally adjusted growth in GDP (base: 2004-05); GFD: quarterly GFD (Centre) as per cent of GDP at current market price; CP_out: q-o-q seasonally adjusted growth in CP outstanding.

2. The results were subjected to standard robustness checks.

Thus economic activity, cost of credit, the fiscal position and competitive alternative funding sources turned out to be major factors affecting credit behaviour in India.

References:

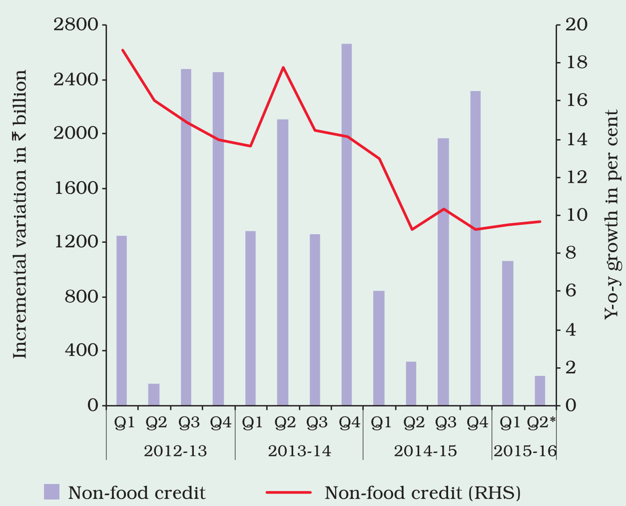
Claessens, S., M. A. Koseand M.E. Terrones (2011), 'How Do Business and Financial Cycles Interact?', IMF Working Paper, No. WP/11/88.

Guo K. and V. Stepanyan (2011), 'Determinants of Bank Credit in Emerging Market Economies', IMF Working Paper WP/11/51.

and foreign, corporates switched some of the demand for financing to non-bank sources. Sale of significantly larger amount of non-performing loans (₹317 billion) by banks to asset reconstruction companies (ARCs) during 2014-15 also contributed to a deceleration in bank credit. Food credit also registered a decline of 4.1 per cent during the year, despite some pick-up in procurement, as a result of enhanced food subsidies which increased by 28.1 per cent in 2014-15.

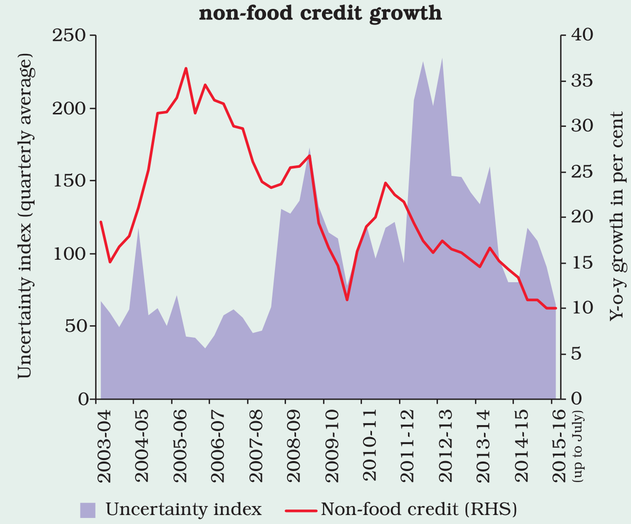
II.3.13 With the deceleration in non-food credit growth on a year-on-year basis, nearly 80 per cent of the incremental credit off-take during 2014-15 took place in the second half of the year, reflecting the improving economic environment (Charts II.17 and II.18). Non-food credit growth increased to 7.1

Chart II.17: Credit off-take skewed towards H2 of 2014-15



*: Data upto August 7, 2015.

Chart II.18: Uncertainty index and non-food credit growth



Source: Economic Policy Uncertainty (http://www.policyuncertainty.com/india_monthly.html).

per cent in H2 of 2014-15 from 2.0 per cent in H1, representing an improvement of 5 percentage points in H2 compared with 0.6 percentage point increase a year ago.

II.3.14 In order to create more space for banks to expand credit to the productive sectors of the economy, the statutory liquidity ratio (SLR) was reduced in three stages from 23 per cent to 21.5 per cent of net demand and time liabilities (NDTL) during 2014-15. However, banks continued to maintain SLR investments around 28 per cent of NDTL, the buffer providing access to collateralised borrowings from the wholesale funding market and the Reserve Bank. Maintaining excess SLR securities also helped banks to weather the impact of the current slow phase of the economic cycle on their balance sheets and earnings.

II.3.15 Data on sectoral deployment of credit, which constitutes about 95 per cent of total bank credit by SCBs, indicate that deceleration in credit off-take in 2014-15 was more pronounced with respect to the industry and services sectors, which together constituted about 68 per cent of total non-food credit. Credit growth in the services sector was weighed down by its major components: trade and non-banking financial companies (NBFCs) that accounted for nearly 48 per cent of the total credit to the services sector. In the industrial sector, growth slowed down across sectors, particularly for infrastructure, basic metals and food processing. The sectors which witnessed lower incidence of NPAs such as personal loans saw higher growth during the year.

II.3.16 Infrastructure accounts for nearly one-third of the credit to the industrial sector. Its main components are power and roads, constituting 60 and 18 per cent of the total infrastructure credit respectively. While deceleration in credit to the power sector was modest, the slowdown was sharp with respect to roads in 2014-15 (Table II.9).

Table II.9: Trends in Credit Deployment to Select Sectors

(Variation in per cent)

	Outstanding at 20-Mar-2015 (₹ billion)	2013-14			2014-15			2015-16
		H1	H2	Year	H1	H2	Year	H1
1	2	3	4	5	6	7	8	9
Non-food Credit (1 to 4)	**60,030**	**6.8**	**6.3**	**13.6**	**2.2**	**6.2**	**8.6**	**1.1**
1. Agriculture & Allied Activities	**7,659**	**3.4**	**9.2**	**12.9**	**8.8**	**5.7**	**15.0**	**3.8**
2. Industry	**26,576**	**6.3**	**6.1**	**12.8**	**-0.1**	**5.7**	**5.6**	**-1.0**
Of which: (i) Infrastructure	9,245	8.8	5.3	14.6	4.3	6.0	10.5	1.0
Of which: (a) Power	5,576	10.7	5.8	17.1	6.6	7.5	14.5	2.8
(b) Telecommunications	919	-0.6	1.1	0.5	-3.6	8.0	4.2	-2.9
(c) Roads	1,687	9.2	10.1	20.2	3.5	3.3	6.9	-0.7
(ii) Basic Metal & Metal Product	3,854	7.2	7.1	14.9	-0.4	7.2	6.8	-0.6
(iii) Food Processing	1,715	3.5	20.4	24.6	-2.6	20.4	17.3	-6.2
3. Services	**14,131**	**9.0**	**6.5**	**16.1**	**-1.2**	**6.9**	**5.7**	**1.4**
4. Personal Loans	**11,663**	**7.5**	**4.6**	**12.5**	**8.0**	**6.9**	**15.5**	**4.0**

Note: Latest available data for H1 of 2015-16 are up to June 2015.

Chart II.19: Trends in credit off-take to major industries

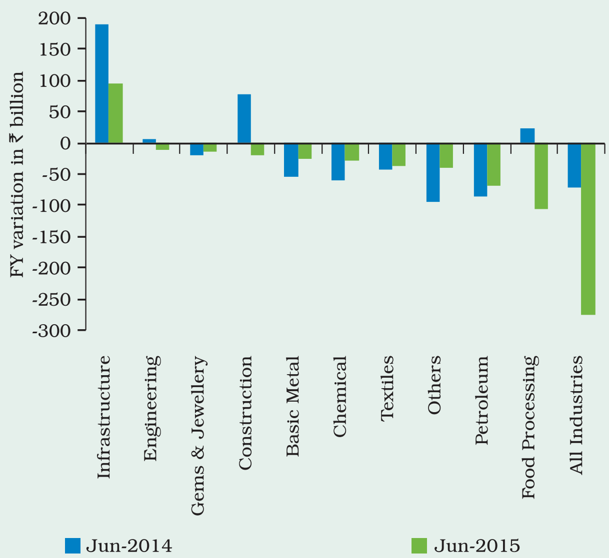
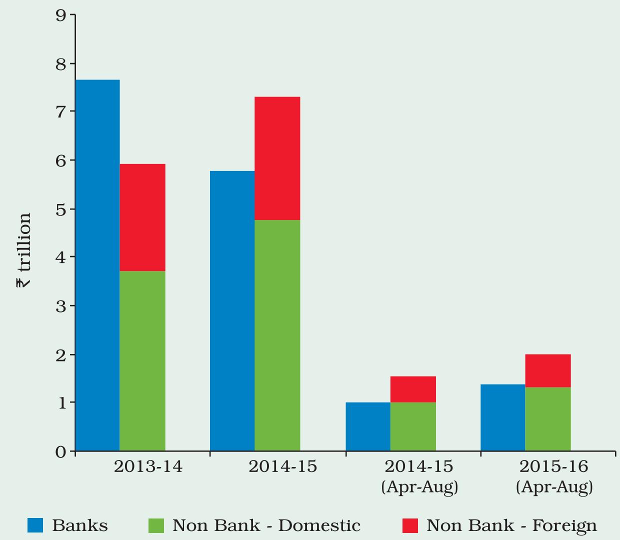


Chart II.20: Flow of resources to the commercial sector



Note: Data up to August 7, 2015.

II.3.17 During 2015-16 so far (up to August 7), credit off-take seems to be picking up reflecting an improving economic and policy environment, though it is too early for a conclusive evidence. Incremental non-food credit stood around ₹1,282 billion as against ₹963 billion during the corresponding period last year. Data on sectoral deployment (up to June 2015) reveal a significant pick-up in services mainly supported by trade and professional services, while industry registered a decline. Within industry, although credit to infrastructure shows signs of pick-up, that to roads continues to be weak (Chart II.19).

Non-bank funding

II.3.18 Slowdown in credit growth dragged down the overall flow of financial resources to the commercial sector in 2014-15, despite higher recourse to non-bank sources of funds (Chart II.20). Amongst the non-bank domestic sources, net issuance of CPs witnessed a four-fold increase during the year, mainly attributable to competitive pricing *vis-á-vis* banks' lending rates. Further, FDI inflows remained strong and accounted for a major chunk of the non-bank foreign resources to the commercial sector. Reliance on non-bank sources continues during 2015-16 so far (up to August 7) amidst comfortable liquidity conditions and competitive rates.

II.3.19 Regime shifts in the conduct of monetary policy shaped monetary and credit conditions in 2014-15. Money supply and other key monetary aggregates decelerated in line with underlying macroeconomic activity. Overall, credit growth was subdued during 2014-15 owing to various factors, such as risk aversion by banks due to rising NPAs and alternative and cheaper sources of non-bank funding, though there was some evidence that a turnaround in the second half of the year might have set in.

II.4 FINANCIAL MARKETS

Global Financial Markets

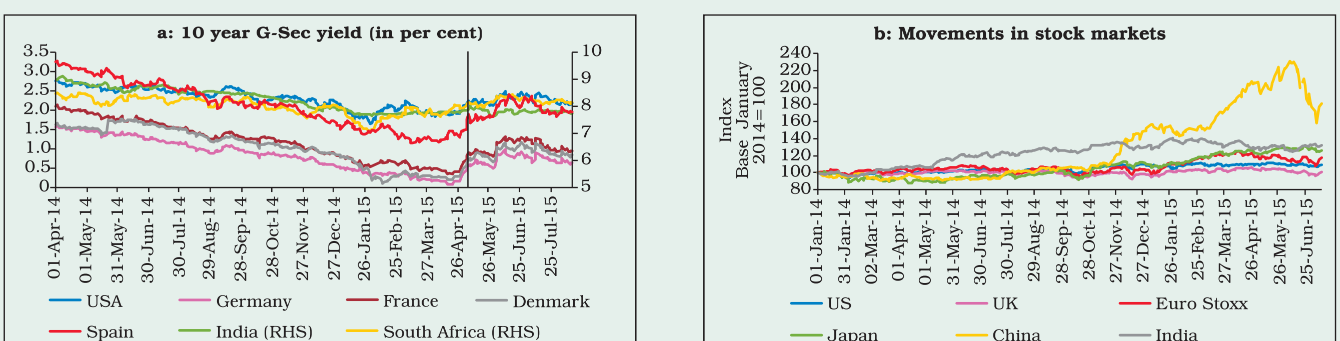
II.4.1 International financial markets remained generally upbeat during 2014-15, lifted by expectations of a relaxed approach of the US Federal Reserve to monetary policy normalisation, quantitative easing by the European Central Bank (ECB) and the Bank of Japan (BoJ) and decline in crude oil prices. Government bond yields for most of the countries were historically low with some European countries even experiencing negative yields (Chart II.21a). A number of stock markets also reached historical highs during 2014-15 as fears about US monetary policy rates lifting off receded and the ECB and the BoJ enhanced their asset purchase programmes. However, markets experienced some volatility in mid-October 2014 on account of uncertainty on the global recovery, a slew of weak data from the US and the euro area and continuing geo-political tensions in the Middle East. Again in the second half of December 2014, markets were affected by the Ukrainian crisis followed by the Russian currency crisis and large exchange rate depreciation in Venezuela and Argentina (Chart II.21b).

II.4.2 The US dollar index, which measures the dollar's movement against other major currencies, strengthened by 23 per cent from 80.1 at end-March 2014 to 98.4 at end-March 2015. While it strengthened primarily on account of a robust US economic recovery, weak economic recovery in the euro zone and Japan during the year resulted in the euro and the Japanese yen depreciating against the US dollar. In January 2015, as ECB prepared to announce quantitative easing, the Swiss National Bank (SNB) abandoned its cap on the Swiss franc/ euro exchange rate which led to heightened exchange rate volatility. During Q4 of 2014-15, a number of emerging markets and developing economies (EMDEs) reduced their policy rates to support economic growth. Interventions in foreign exchange markets to address depreciating pressures also increased.

II.4.3 In May 2015, markets were surprised by the global bond sell-off that started in Germany as the 10-year German Bund yield increased to intra-day high of 0.77 per cent on May 7 from 0.05 per cent on April 17, 2015. Concerns over Greek debt, sustained increase in crude oil prices and profit booking quickly transmitted to US treasury bills as well as emerging market economies.

II.4.4 During June 2015, movements in international financial markets were abuzz with uncertainty relating to the outcome of Greek debt negotiations and meltdown in the Chinese stock market. However, in July financial markets received

Chart II.21: International Financial Markets



Source: Bloomberg.

Source: Bloomberg.

support from the announcement of the bailout deal between Greece and the euro zone members and signing of the nuclear deal between Iran and major world powers. In August, the global financial markets were shaken by China's decision to devalue its currency by around 2 per cent.

Indian Financial Markets

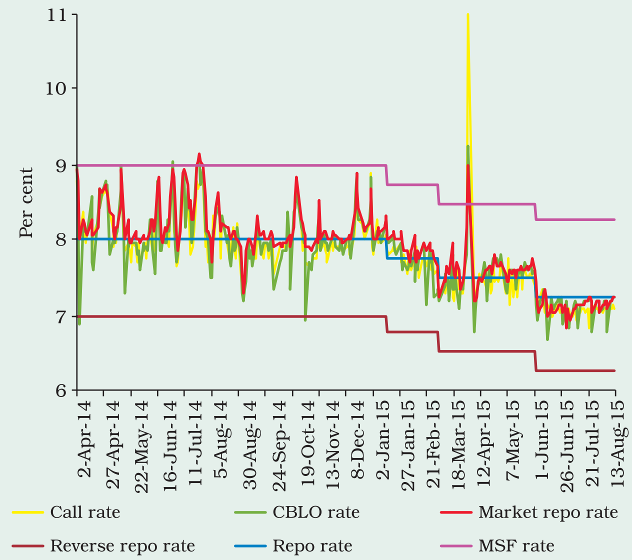
II.4.5 Both domestic and global cues were at play in buoying Indian financial markets during 2014-15. Equity markets reached all-time highs during the year. Money markets were stable and liquid with call money rate evolving tightly around the policy repo rate. Yields on government securities (G-secs) declined gradually and activity in the corporate bond market registered an increase mainly due to primary issuances.

Money Market

II.4.6 Overnight call money rates remained closely aligned to the policy repo rate, with active liquidity management operations under the revised liquidity management framework, except adjustment for the year-end window dressing. Money market rates declined in Q4 in sync with cuts in the policy rate (Chart II.22). With deposit growth generally remaining above credit growth during the year, structural liquidity conditions remained comfortable. During 2015-16 so far, call money rates have remained aligned to the policy repo rate with money market rates declining after the cut in policy rate on June 2, 2015.

II.4.7 The spread of the daily weighted average call rate (excluding Saturdays) over the policy rate narrowed down significantly during 2014-15 from 30 basis points (bps) to 18 bps after the adoption of the revised liquidity management framework in September 2014. The spread further narrowed down to 16 bps during 2015-16 (upto August 14). The spread of collateralised rates (CBLO and market repo) also narrowed down during this period,

Chart II.22: Money Market Rates



Source: The Reserve Bank and CCIL.

indicating synchronised movement among overnight money market rates. The collateralised segment continued to attract a major portion of the turnover in the overnight market, with the uncollateralised (call money) segment registering relatively thin volumes, rendering it susceptible to bouts of volatility. A large part of the assured liquidity support under the Reserve Bank's liquidity adjustment facility (LAF) is being offered through variable rate term repos with one of its main objectives being development of the term money market. Notwithstanding these initiatives, the turnover in the term money market has remained muted.

Issuance of CDs and CPs

II.4.8 The average fortnightly issuance of certificates of deposits (CDs) decreased to ₹297 billion during 2014-15 from ₹306 billion during the previous year (Chart II.23). The easing of liquidity conditions, coupled with a reduction in the policy rate and relatively lower issuances of CDs by banks on the back of subdued credit off-take, led to a decrease in the weighted average effective interest rate (WAEIR) on CDs from 9.74 per cent at end-March 2014 to 8.58 per cent at end-March 2015.

Chart II.23: CD Issuance and WAEIR

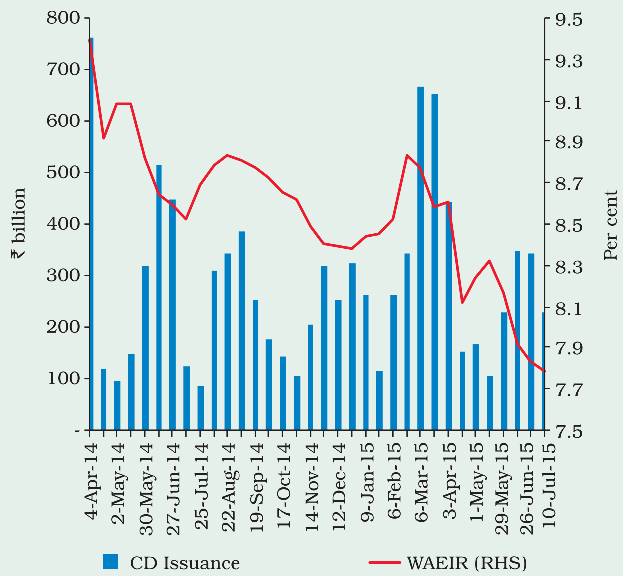
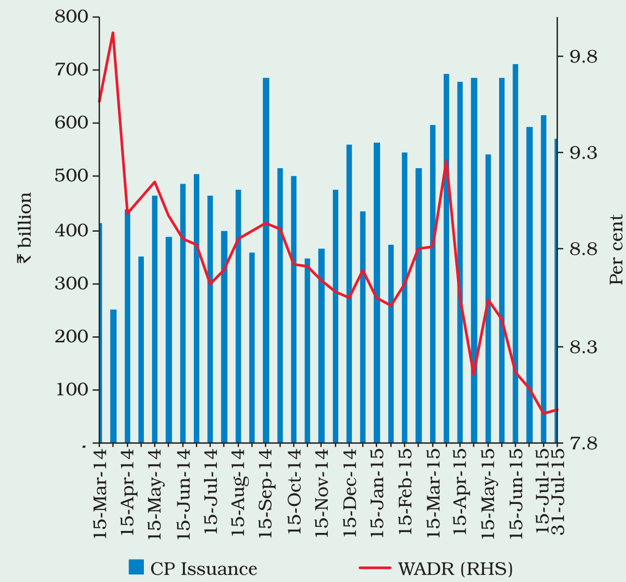


Chart II.24: CP Issuance and WADR



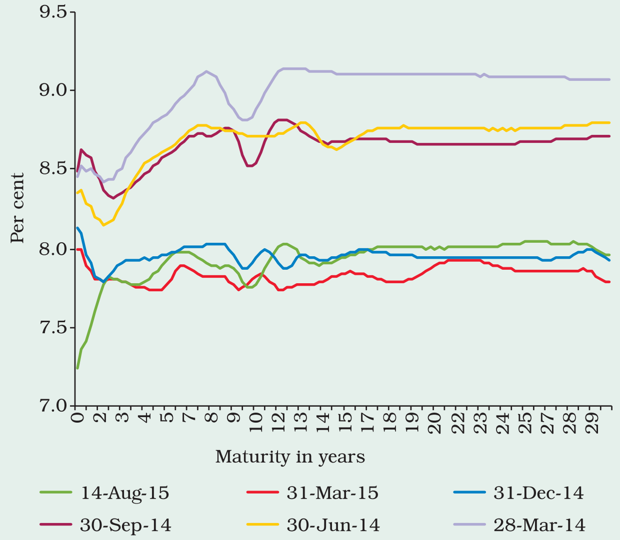
The easing trend has continued during 2015-16 so far with WAEIR declining further to 7.79 per cent by July 10, 2015.

II.4.9 The average fortnightly issuance of commercial papers (CPs) increased by 58 per cent to ₹479 billion during 2014-15, reflecting substitution of short-term bank credit by market based funding on account of the cost effectiveness of CPs for raising funds on the back of significant easing of yields on corporate bonds (Chart II.24). Consequently, the outstanding amount of CPs stood higher at ₹1,933 billion at end-March 2015 as compared to ₹1,066 billion at end-March 2014. The weighted average discount rate (WADR) for CPs decreased to 9.26 per cent at end-March 2015 from 9.92 per cent at end-March 2014, reflecting easing of liquidity conditions during the year and overall downward movement in the interest rate cycle. The declining trend has continued during 2015-16 so far with WADR standing at 7.97 per cent at end-July 2015.

Yields in the G-Secs Market

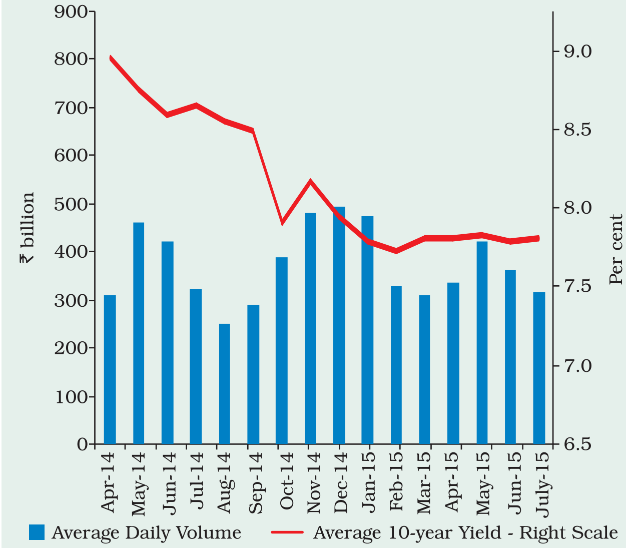
II.4.10 G-secs yields generally softened through 2014-15, reflecting easing of US treasury yields, active buying interest by foreign portfolio investors (FPIs), sharp decline in inflation, improvement in the fiscal situation, positive sentiment after the general elections, steep decline in international oil prices and cuts in policy rate by the Reserve Bank. Some uptick in yields occurred in June and July 2014 due to geo-political tensions in the Middle East as also the announcement of higher net market borrowing in the Union Budget for 2014-15. Yields spiked again in the second half of December 2014 on account of geo-political tensions and the Russian currency crisis. However, the yields softened in Q4 following increased buying by FPIs. Sustained buying interest in government debt by FPIs was discernible as their limit remained almost fully utilised, notwithstanding certain conditions such as debarring FPIs from investing in treasury bills and permitting incremental investment only in G-secs with minimum residual maturity of three years. Notably, the G-secs market weathered the impact of a complete exit from the assets purchase programme by the Federal Reserve in October 2014 with the yields continuing to exhibit a softening bias on the back of buoyant investor sentiment (Chart II.25).

Chart II.25: G-Secs Yield Curve



Source: FIMMDA.

Chart II.26: Average Daily Volume and 10-Year G-Sec Generic Yield



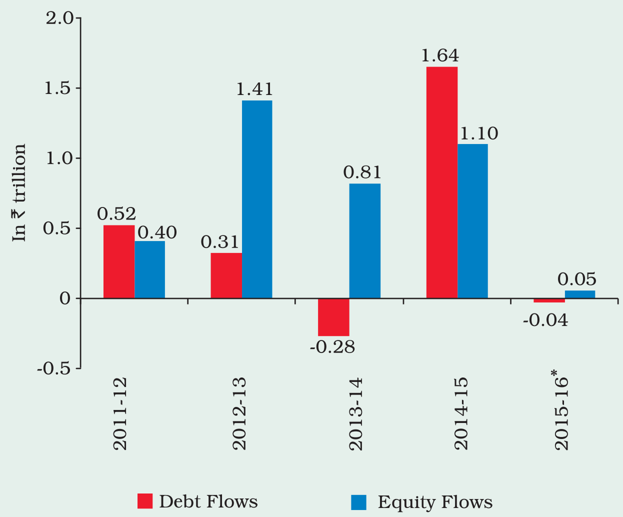
Source: FIMMDA and CCIL.

II.4.11 Bearish sentiment took hold in the G-secs market in February 2015 for a variety of reasons, including, but not limited to, a broadly unchanged size of the government market borrowing programme for 2015-16 and rescheduling of the fiscal consolidation plan by a year as announced in the Union Budget for 2015-16. However, the follow-up policy rate cut of 25 bps each on January 15, 2015 and March 4, 2015, coupled with a sharp fall in US treasury yields, buoyed the market sentiment and led to softening of the 10-year G-Sec yield. The improvement in sentiment was short-lived after a status quo on the policy rate was announced in the bi-monthly monetary policy on April 7, 2015. More pertinently, taking cues from hardening of long-term bond yields in most of the advanced economies on the back of improved growth and inflation outlook, and hardening oil prices, the 10-year yield on Indian G-secs rose during the first half of May 2015, touching a high of 8.09 per cent on May 11, 2015. The yield has, however, softened thereafter with the introduction of a new 10-year benchmark security, cut in policy rate and significant decline in inflation. The 10-year yield stood at 7.75 per cent on August 14, 2015. The average volume generally varied inversely with the movement in 10-year G-sec yield barring the period from October to November 2014 (Chart II.26). The G-secs turnover ratio moved up to 1.95 per cent in 2014-15 from 1.87 per cent in the previous year.

FPI Flows into India

II.4.12 FPIs in the equity and debt markets in India revived during 2014-15. While FPI inflows to the debt market turned positive at ₹1.6 trillion facilitated by an increase in the FPI sub-limit by US$ 5 billion within the overall limit of US$ 30 billion, FPI investments in equity markets were also higher than they were in 2013-14 (Chart II.27). Currently, FPI investors are permitted to invest only in bonds with the minimum residual maturity of three years so as to encourage investments in long term securities and to contain interest rate volatility at the shorter end. The effective FPI limit was increased by allowing FPIs to invest coupons from G-secs, outside the overall limit, with effect from February 5, 2015. During 2015-16 so far (up to August 13, 2015), FPI flows in the debt and equity markets have been subdued at ₹(-)43.2 billion and ₹47.4 billion, respectively, following the global bond sell-

Chart II.27: FPI Flows to Debt and Equity Markets



*: Data upto August 13, 2015.
Source: National Securities Depository Limited (NSDL).

off triggered in the European bond markets on May 7, 2015, concerns over weak quarterly earnings reported for Q4, as also over the minimum alternate tax (MAT) and increased uncertainty in the global financial markets.

Corporate Bond Market

II.4.13 During 2014-15, turnover in the corporate bond market increased by 12 per cent to ₹10,913 billion (Chart II.28a). On the other hand, the yield spread of 5-year AAA rated corporate bonds over G-secs of corresponding maturity declined until mid-November 2014 following the crash in global crude oil prices, stability in the exchange market and Moody's outlook upgrade. Subsequently, however, frictional liquidity pressure on account of advance tax payments and concerns over the rise in the current account deficit for Q2 of 2014 led to a widening of the spreads until mid-January 2015. Following the cuts in the policy repo rate and improved liquidity conditions, yield spreads declined in Q4 of 2014-15 (Chart II.28b). During 2015-16 so far, the yield spread remained range bound, indicating easy liquidity conditions.

Secondary Equity Market

II.4.14 The equity market witnessed heightened activity in 2014-15, scaling new highs on January 29, 2015 (Chart II.29a). During the year, the BSE Sensex rose by 25 per cent on top of the uptick of 19 per cent in 2013-14. Equity market sentiment was supported by political stability, sustained FPI flows, lower international crude oil prices and softening of the policy rate.

II.4.15 The equity market was also supported by global liquidity conditions and the search for yield aided by the US Federal Reserve's commitment to low interest rates, ultra-accommodative monetary policies pursued by the ECB, the BoJ and the People's Bank of China. In US dollar terms, the Sensex rose by 20 per cent, turning out to be one of the best performing markets in the world (Chart II.29b). The domestic equity market also witnessed lower volatility in 2014-15 as compared to equity markets abroad.

Chart II.28: Corporate Bond Market

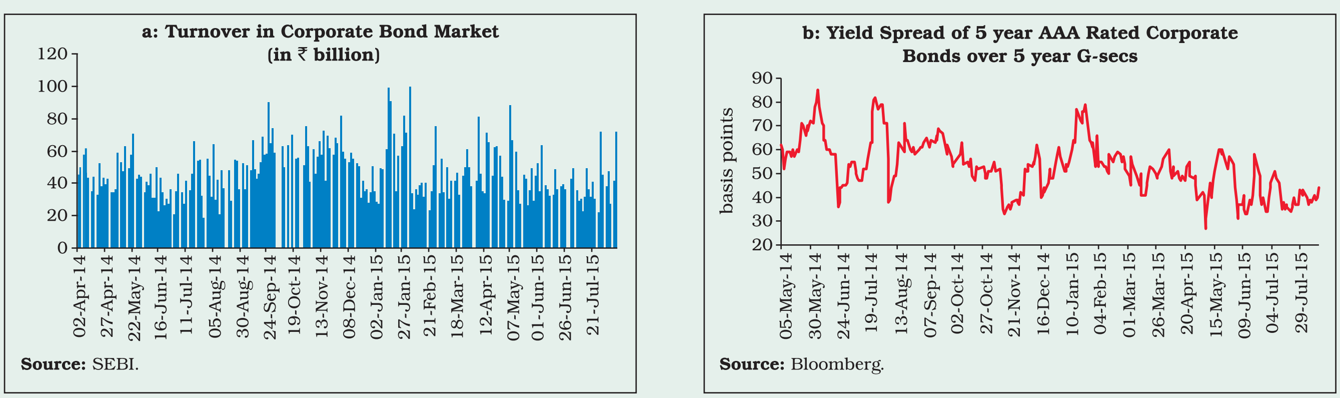
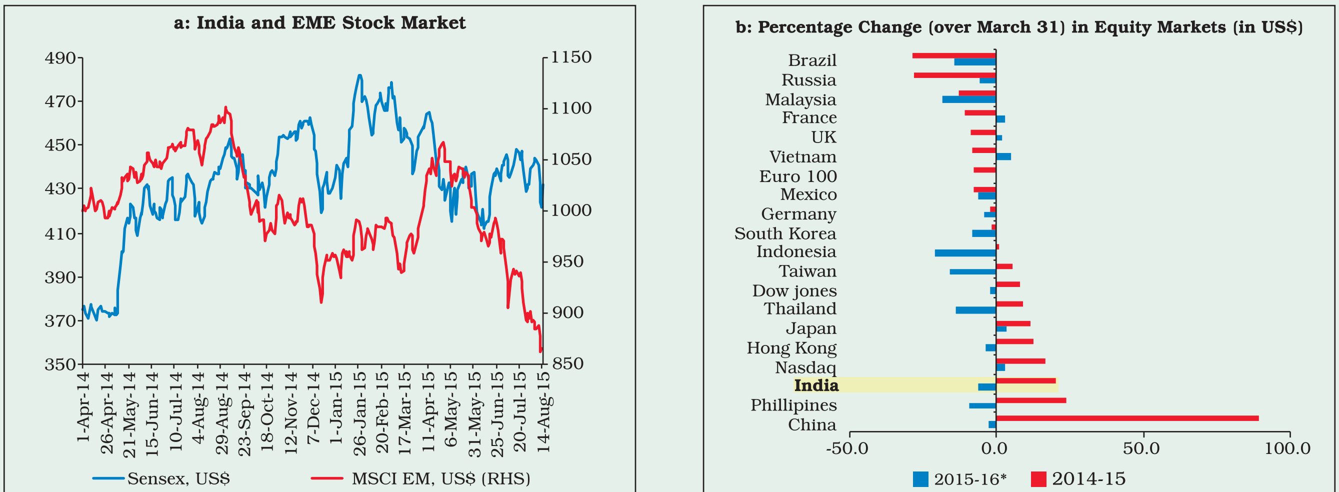


Chart II.29: Performance of Indian Equities *vis-a-vis* other Major Markets



Source: Bloomberg. **Source:** Bloomberg. *: Upto August 13, 2015.

II.4.16 During 2015-16, equity markets had a subdued start on account of FPIs' concern over MAT, weak Q4 corporate earnings and forecast of a below normal monsoon. However, benchmark indices recovered after realisation of above normal rainfall in June. Domestic markets also received support from positive developments relating to Greece and the Iran nuclear deal. In August 2015, the stock markets remained range bound guided, among others, by mixed earnings for Q1 of 2015-16 and global developments such as China's currency devaluation.

Primary Equity Market

II.4.17 During 2014-15, resource mobilisation through equity issues, including qualified institutional placement (QIP) rose significantly by 44 per cent (Table II.10). There were signs of renewed interest in initial public offerings (IPOs) with an increase in the number of companies filing draft red herring prospectuses (DRHPs) with the Securities and Exchange Board of India (SEBI) to raise resources in 2015-16. Going forward, positive sentiment in the secondary market, if sustained, will help raise larger resources through the primary market.

Private Placement of Corporate Bonds

II.4.18 Mobilisation through private placement of corporate bonds at ₹4,041 billion was significantly higher by 46 per cent during 2014-15, while public issues of non-convertible debentures at ₹97 billion were much lower. Mobilisation through public issues of bonds is set to witness a revival in 2015-16 with the Union Budget 2015-16 proposing to raise resources through tax-free bonds for funding infrastructure.

II.4.19 The Central Government has budgeted a receipt of ₹695 billion through disinvestment in 2015-16, of which ₹285 billion is expected to be mobilised through strategic disinvestments. Measures, such as the introduction of e-IPO norms and allowing firms to launch real estate investment trusts (REITs) and infrastructure investment trusts (InvITs) as also the government's disinvestment measures are expected to provide an impetus to the capital markets going forward.

House Price Index (HPI)

II.4.20 Quarterly growth (y-o-y) in HPI went below 16 per cent in Q1 of 2013-14 and further down in

Table II.10: Primary Capital Market Mobilisation

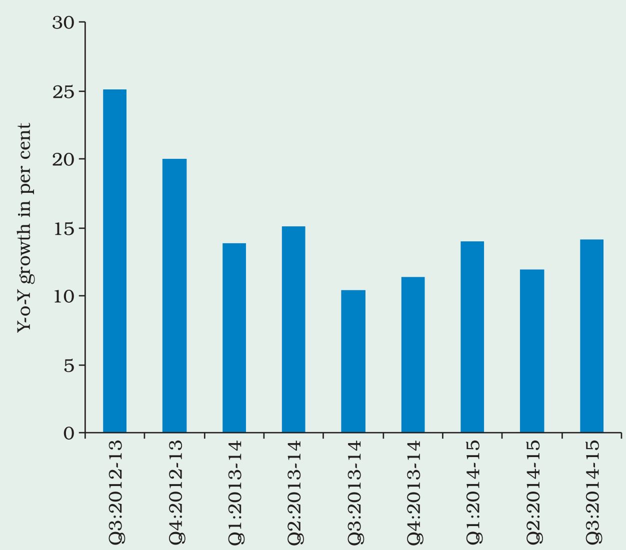
(₹ billion)

Category	2011-12	2012-13	2013-14	2014-15 (P)
1	2	3	4	5
a. Public Issues (i)+(ii)	**460.9**	**219.2**	**510.8**	**127.5**
(i) Public Issues (Equity) *Of which*	104.8	49.4	87.0	30.4
IPOs	59.0	49.4	12.4	30.4
FPOs	45.8	0.0	74.6	0.0
(ii) Public Issues (Debt)	356.1	169.8	423.8	97.1
b. Rights Issues	23.7	89.4	45.8	67.5
Total Equity Issues (i+b)	**128.6**	**138.8**	**132.7**	**97.9**
c. Euro Issues (ADR/GDR)	27.1	10.4	1.2	95.9
d. Mutual Fund Mobilisation (net)	-220.2	765.4	537.8	1032.9
1. Private Sector	-154.5	637.9	488.4	1037.0
2. Public Sector	-65.8	127.5	49.4	-4.1
e. Private placements in the corporate debt market	2612.8	3614.6	2760.5	4041.4
f. QIP	21.6	160.0	136.6	291.0

P: Provisional; IPOs: Initial public offerings; FPOs: Follow on public offers; ADR: American depository receipts; GDR: Global depository receipts; QIP: Qualified institutional placement.
Source: SEBI and Prime database.

Q3 mainly due to subdued demand. However, it moved up in the first three quarters of 2014-15, suggesting a moderate pick up in house price growth, particularly in cities like Delhi and Kolkata (Chart II.30). The demand for residential properties has slowed down in recent times and unsold stock of residential homes has increased considerably at the same time. Genuine home buyers moved away from the housing market due to higher prices and investors stayed away due to the weakening state of the economy. As the economic growth has started to take-off, the overall buyer sentiment is expected to rise. Presumably, developers are counting on this to happen and hence holding the price.

Chart II.30: Movement in the House Price Index



Source: The Reserve Bank.

II.4.21 Financial markets in India performed well during 2014-15. Money market rates closely followed the policy repo rate; and in the backdrop of sluggish credit growth and relatively comfortable structural liquidity, coupled with policy rate easing by the Reserve Bank, the rates on CPs and CDs declined during the year. G-secs yields generally softened in 2014-15 in line with a decline in inflation and continued buying interests by FPIs. Equity markets, primary as well as secondary, fared better than in the previous year.

II.5 GOVERNMENT FINANCES

II.5.1 Public finances have been gradually improving at the level of both the Centre and the states. The impetus for rectitude has mainly emanated from a re-commitment to calibrated paths of fiscal consolidation in the post-global crisis period. Initially quantity-driven, these efforts have been guided by the imperative to stabilise fiscal consolidation on the chosen trajectories and then to re-order expenditure priorities from subsidies to investment, to raise tax buoyancy, to rationalise non-developmental spending and leakages and to contain public debt at sustainable levels for all layers of the government. With annual budgetary targets for the gross fiscal deficit (GFD) met since 2012-13, attention has increasingly turned to the quality of fiscal consolidation. Key deficit indicators of the Central Government were lower in 2014-15, as per the provisional accounts (PA), than a year ago. GFD was lower than the budgetary target, both in absolute terms and as percentage of GDP.

Centre: Receipts and Expenditure

II.5.2 In 2014-15 (provisional accounts), non-debt receipts were sluggish reflecting tepid domestic activity. While gross tax collection suffered a shortfall of 8.8 per cent from the budget estimates (BE), net tax inflows turned out to be 7.7 per cent lower than BE, mainly on account of subdued indirect tax receipts. Non-tax revenue was also lower than BE due to lower collections from general, economic, fiscal and social services. Non-debt capital receipts were significantly lower than the budgetary target, reflecting a large shortfall in disinvestment proceeds.

II.5.3 The shortfall in non-debt receipts warranted a sharp cutback in plan expenditure by more than 20 per cent, both on the revenue and capital accounts, in order to meet deficit targets. A marginal reduction in non-plan expenditure over BE was also effected through reduction in capital expenditure and interest payments.

II.5.4 Both overall capital expenditure and capital outlay were lower than budgeted levels and also lower than last year's levels. This has potentially adverse implications for growth in the medium term.

Recalibration of the Fiscal Consolidation Path in 2015-16

II.5.5 Union Budget 2015-16 has carried forward the process of fiscal consolidation, with all the key deficit indicators projected to decline (Table II.11). The targeted reduction in GFD is proposed to be

Table II.11: Fiscal Performance of the Central Government

(Per cent of GDP)

Variables	2004-08 (Avg)	2008-10 (Avg)	2010-14 (Avg)	2013-14	2014-15(RE)	2014-15 (PA)	2015-16 (BE)
1	2	3	4	5	6	7	8
Non Debt Receipts	**10.4**	**9.5**	**9.5**	**9.3**	**9.3**	**9.1**	**8.7**
Tax revenue	7.8	7.5	7.3	7.2	7.2	7.2	6.5
Non-tax revenue	2.1	1.8	1.8	1.8	1.7	1.6	1.6
Non debt capital receipts	0.4	0.3	0.4	0.4	0.3	0.3	0.6
Total Expenditure	**14.2**	**15.8**	**14.5**	**13.7**	**13.4**	**13.1**	**12.6**
Revenue expenditure	11.9	14.1	12.7	12.1	11.9	11.6	10.9
Capital expenditure	2.3	1.7	1.8	1.7	1.5	1.5	1.7
Plan expenditure	4.0	4.8	4.4	4.0	3.7	3.6	3.3
Non-plan expenditure	10.2	11.0	10.1	9.7	9.7	9.5	9.3
Revenue Deficit	**2.0**	**4.9**	**3.6**	**3.1**	**2.9**	**2.9**	**2.8**
Gross Fiscal Deficit	**3.4**	**6.2**	**5.0**	**4.4**	**4.1**	**4.0**	**3.9**

Note: 1. Avg: Average; RE: Revised Estimates; PA: Provisional Accounts; BE: Budget Estimates.
2. GDP 2014-15 is as per Provisional Estimates of CSO.

attained by a compression in revenue expenditure combined with an increase in non-debt capital receipts. The goalpost for achieving the GFD-GDP target of 3.0 per cent under the FRBM Act/Rules has been shifted by a year to 2017-18 mainly to accommodate higher public investment to support growth, and higher devolution to the states following the recommendations of 14th Finance Commission as also accounting for uncertainties associated with the implementation of the Goods and Services Tax (GST) and the likely burden of the 7th Pay Commission award.

Targets for Indirect Taxes and Disinvestment Proceeds

II.5.6 With an expected growth of 16.4 per cent in gross tax revenue, the ratio of gross tax revenue to GDP is estimated to improve by 0.4 percentage points to 10.3 per cent in 2015-16. The net tax revenue accruing to the Centre is, however, budgeted significantly lower at 6.5 per cent of GDP – down from 7.2 per cent in 2014-15 (PA) due to higher devolution to the states following the 14th Finance Commission award. The implied tax buoyancy for gross tax revenue is significantly higher than the realised buoyancy of less than 1 in the previous two years (Table II.12). Further, the projected increase of 18.9 per cent in indirect taxes as against 9.8 per cent realised in 2014-15 (PA) assumes a buoyancy of about 2 for service tax on the back of a hike in the service tax rate (inclusive of education cess) by 1.64 per cent, pruning of the Negative List under service tax and withdrawal of certain other exemptions to widen the tax base. The projected buoyancy of 1.73 in the case of excise duty collections is mainly supported by *ad hoc* hikes in excise duty on petrol and diesel in 2014-15, increase in excise duty on select products, such as mobile handsets and cigarettes, imposition of excise duty on hitherto untaxed items like condensed milk and peanut butter, and a general increase in excise duty to 12.5 per cent from the prevailing 12.36 per cent. While these measures will facilitate meeting budgeted targets for indirect tax collections in 2015-16, it is crucial to adhere to the timeline for the rollout of GST for a sustainable increase in tax revenues in the medium term.

II.5.7 Non-tax revenue, which includes dividends from public sector undertakings (PSUs), the Reserve Bank, PSU banks and spectrum charges, is budgeted to grow at 12.6 per cent in 2015-16. Disinvestment proceeds are budgeted higher at ₹410 billion, with an additional inflow of ₹285 billion estimated out of strategic disinvestments. The projected increase of about 179 per cent in disinvestment receipts, despite a track record to the contrary in terms of actual realisation, poses possible risks to overall budgetary targets for 2015-16.

Table II.12: Tax Buoyancy and Growth Rates in Tax Collections*

Tax Categories	Tax Buoyancy			Growth Rates (Per cent)		
	2013-14	2014-15(PA)	2015-16 (BE)	2013-14	2014-15(PA)	2015-16 (BE)
1	2	3	4	5	6	7
Gross Tax Revenue	0.73	0.89	1.31	9.9	9.3	16.4
Corporation Tax	0.79	0.82	0.78	10.8	8.7	9.7
Income Tax	1.55	0.82	1.93	21.0	8.6	24.2
Customs Duty	0.30	0.88	0.86	4.1	9.3	10.8
Union Excise Duty	-0.24	1.05	1.73	-3.2	11.1	21.6
Service Tax	1.23	0.81	1.99	16.7	8.5	24.9

*: Buoyancies are worked out with respect to overall GDP growth rate.

Expenditure Pattern

II.5.8 The Centre's total expenditure is budgeted to increase by 8.1 per cent in 2015-16 (BE) with revenue expenditure declining as a proportion to GDP. Capital expenditure is budgeted to increase sharply, reflecting the projected high growth in non-defence capital outlay.

II.5.9 Plan expenditure is expected to increase marginally in 2015-16 reflecting higher capital expenditure. In the non-plan expenditure, subsidies are budgeted to decline on account of around 48 per cent cut in petroleum subsidy following a sharp fall in international crude prices and the deregulation of the retail sale of diesel that was undertaken in 2014. Food subsidies are budgeted to increase at a modest pace, while fertiliser subsidies are expected to decline.

Quality of Fiscal Adjustment in 2015-16

II.5.10 Overall, the Government's plan for fiscal consolidation in 2015-16 through re-orientation of public expenditure in favour of investment rather than subsidies is a welcome move towards improving the quality of fiscal adjustment (Box II.5). Towards achieving this, it will be important to

Box II.5
Quality of Fiscal Adjustment

In the aftermath of the global financial crisis, government finances deteriorated significantly across the world as fiscal stimulus measures were introduced to reinvigorate the growth process and kick-start national economies worldwide. Both advanced and emerging market economies have embarked on fiscal consolidation since 2010, although the speed and extent of consolidation has been country-specific. In India, fiscal consolidation resumed from the second half of 2012-13, bringing about a steady decline in the centre's gross fiscal deficit (GFD) from 5.8 per cent of GDP in 2011-12 to 4.0 per cent in 2014-15 (PA). Notwithstanding such improvement, the quality of fiscal adjustment has remained a cause for concern.

Ideally, a fiscal consolidation strategy should be a mix of rationalisation of expenditure and revenue augmentation so that the welfare burden of consolidation is fairly distributed across society. Apart from obvious steps like reducing government consumption and unproductive expenditure, such as subsidies, a consolidation process must deploy freed-up resources in higher public investment and/or more social spending *via* transfers to the poor. This will induce medium term growth that can compensate the near-term decline in output. Adjustments must necessarily be accompanied by structural reforms to enhance productivity and a credible fiscal consolidation roadmap that will anchor market expectations (Tapsoba 2013).

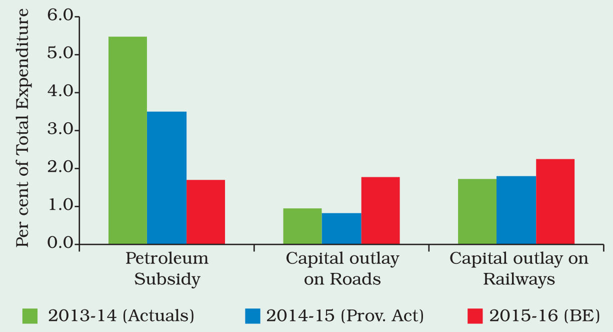
Fiscal consolidation in India has primarily been effected through aggressive cut-backs in expenditure, both on the revenue and capital accounts due to non-realisation of budgeted non-debt receipts. As a result, the onus of fiscal consolidation has disproportionately fallen on expenditure compression. In the process, certain productive expenditures under the central plan suffered cuts in excess of 20 per cent over budget estimates during 2012-13 to 2014-15 (RE). These include irrigation and flood control, communications, rural development and education. Plan capital expenditure suffered a shortfall of 14.4 per cent, on an average, during this period. Fiscal rectitude based on cutbacks in capital expenditure has adverse effects on sustainable growth since the multiplier effects of capital expenditure are found to be larger and more prolonged than those of revenue expenditure (Jain and Kumar 2013).[1]

Union Budget 2015-16 has envisaged a reorientation of government expenditure with capital expenditure budgeted to grow at 29.1 per cent, while expenditure on subsidies is projected to undergo a decline (Chart 1). This re-prioritisation of government expenditure along with the other initiatives discussed in Section II.1 of this Chapter is expected to facilitate pick up in investment in the economy. While this is indicative of an improvement in the quality of expenditure, it is imperative that budgeted targets are converted into actual realisation. In the past three years, the government has been

(Contd....)

[1] As per Jain and Kumar's (2013) estimates, the impact multipliers of non-defence capital outlay, revenue expenditure and aggregate expenditure for the Central Government are 2.09, 0.19 and 0.40, respectively.

Chart 1: Expenditure Re-orientation of the Centre



effecting a cut of about 19 per cent in the actual capital outlay over budgeted levels in view of revenue shortfalls. A comprehensive fiscal consolidation strategy will also need sustainable improvement in government revenue.

References:

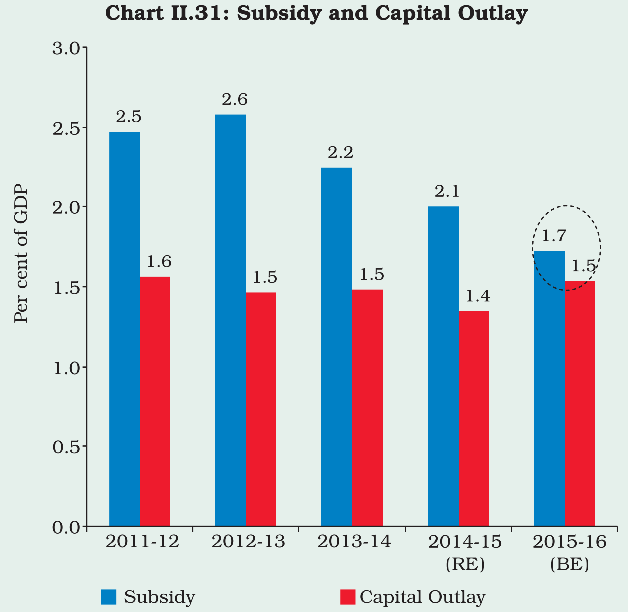
Jain, R., and P. Kumar (2013), 'Size of Government Expenditure Multipliers in India: A Structural VAR Analysis', RBI Working Paper No. 07.

Tapsoba, S. J. (2013), 'Options and strategies for fiscal consolidation in India', IMF Working Paper No.127.

realise the budgeted revenue on the one hand, and adhere to the budgeted expenditure on subsidies on the other (Chart II.31).

II.5.11 Food subsidy is budgeted to increase modestly in 2015-16, despite the proposed expansion in coverage under the National Food Security Act. Capping the food subsidy within the budgeted level will involve a multi-pronged strategy: end-to-end computerisation of the public distribution system, decentralisation of procurement and distribution of food grains and improving the operational efficiency of the Food Corporation of India (FCI). Through direct benefit transfers (DBTs), the government may economise on food subsidy expenditure by eliminating costs associated with procuring, distributing and storing foodgrains. The recently announced Urea Policy of the government, which aims at maximising indigenous production and promoting energy efficiency in urea production units, so as to reduce import dependency and hydrocarbon inputs respectively, is expected to result in direct savings in the fertiliser subsidy of around ₹26.2 billion and indirect savings of around ₹22.1 billion, respectively, over the next four years on account of reduced energy consumption and import substitution.

Chart II.31: Subsidy and Capital Outlay



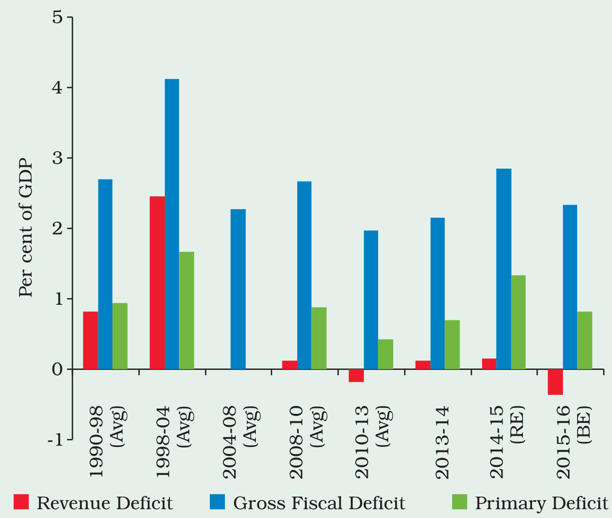
II.5.12 As per the latest available information, the key deficit indicators of the Central Government, *viz*., GFD and RD, as percentages to their budget estimates (BE), were lower during April-June 2015 than in the corresponding period of the previous year. Despite higher total expenditure, robust non-debt receipts resulted in lower GFD during this period. Higher collections under all categories of indirect taxes and higher non-tax revenue provided a boost to the Central Government's receipts. While outgo on major subsidies was lower, capital expenditure was higher on account of higher growth in plan capital expenditure. On July 31, 2015, the Government has approved additional provision of ₹255 billion sought through the first batch of Supplementary Demand for Grants for 2015-16 to

meet priorities like capitalisation of public sector banks, support for social sector and rural development, additional support for metro rail projects, energy sector, food sector, civil aviation, culture and tourism and home affairs.

States' Fiscal Position in 2015-16[2]

II.5.13 The consolidated position of state finances[3] indicates an increase in the GFD-GDP ratio to 2.9 per cent in 2014-15 (RE) from 2.2 per cent in 2013-14, mainly due to an increase in aggregate expenditure which offset the increase in revenue receipts. The capital outlay ratio increased by 0.7 percentage points of GDP in 2014-15 over the previous year's level. The revenue balance continued to be in deficit at 0.1 per cent of GDP.

Chart II.32: Key Deficit Indicators of the State Governments



Note: Figure for 2013-14 to 2015-16 correspond to 25 states.

II.5.14 The BE for 2015-16 projects a decline in the GFD-GDP ratio to 2.3 per cent and turnaround in revenue account from a deficit to a surplus mode, indicating the states' intention to intensify the process of fiscal consolidation (Chart II.32). Improvement in the fiscal position is budgeted through buoyancy in tax revenues and containment of expenditure. Expenditure patterns of the states indicate stagnancy in committed and non-development expenditure and a decline in development expenditure.

Combined Fiscal Outcome in 2014-15

II.5.15 The fiscal position of the general government deteriorated in 2014-15 (RE). The combined fiscal deficit stood at 6.9 per cent of GDP as against 6.6 per cent in 2013-14. The decline in the Central Government's GFD by 0.3 percentage points was more than offset by a 0.7 percentage points increase in the GFD of state governments. The fiscal deficit of the general government, however, is budgeted to improve to 6.3 per cent in 2015-16 (BE), mainly through a lower growth in expenditure *vis-à-vis* non-debt receipts.

II.5.16 Union Budget 2015-16 was formulated with the two-fold objective of promoting growth through stepping up investment and strengthening the federal structure. Accordingly, the fiscal strategy during 2015-16 is focused on creating space for infrastructure spending through a mix of own resources as well as a sharp increase in investments by central public sector enterprises and a substantial increase in resource transfer to the states. While the increased devolution to the states will constrain the Central Government's finances, it will help the states design, implement and finance programmes according to their specific needs. However, with an increase in the fiscal autonomy of the states, it will be crucial for them to effectively invest their resources.

[2] Data pertain to 25 states.

[3] An aggregative analysis tends to disguise significant differences across states in terms of fiscal position and policies. In this regard, the Reserve Bank's annual publication titled 'State Finances: A Study of Budgets of 2014-15' provides an in-depth analysis of state finances at a disaggregated level.

II.6 THE EXTERNAL SECTOR

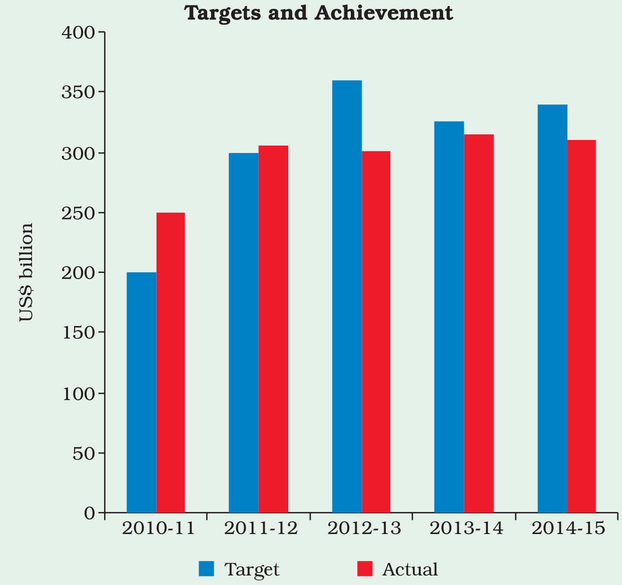
II.6.1 Global developments impacted India's external sector significantly in 2014-15. The collapse in international commodity prices, particularly of crude, delivered a positive shock, yielding a large measure of savings in imports. Export performance remained resilient to the commodity price plunge and large movements in G3 exchange rates for the greater part of the year. However, the conjunction of weak global demand, decline in crude prices affecting exports of petroleum products (POL) and persisting real appreciation of rupee, eventually took its toll, resulting in export contraction in the last four months of the year. With import prices falling faster than export prices, however, unexpected terms of trade gains accrued. Imports of gold remained subdued until the liberalisation of restrictions prompted a surge in volumes in the later part of the year. The combination of these factors restrained the current account deficit within sustainable limits.

II.6.2 In response to large macroeconomic adjustments undertaken since the summer of 2013 and also buoyed by ebullient optimism surrounding political change and expectations of structural reforms, foreign investments - both direct and portfolio - recorded substantial inflows. Consequently, the external financing requirement was comfortably met and there was large accretion to the reserves. Indicators of external sustainability, which improved from their levels a year ago, will buffer the Indian economy in light of an increase in policy rates by the US Fed later in the year or in 2016.

Merchandise Export Performance

II.6.3 India's merchandise exports fell below the target set by the government for the third successive year (Chart II.33); the modest rise in volumes was eroded by a decline in unit value realisations.

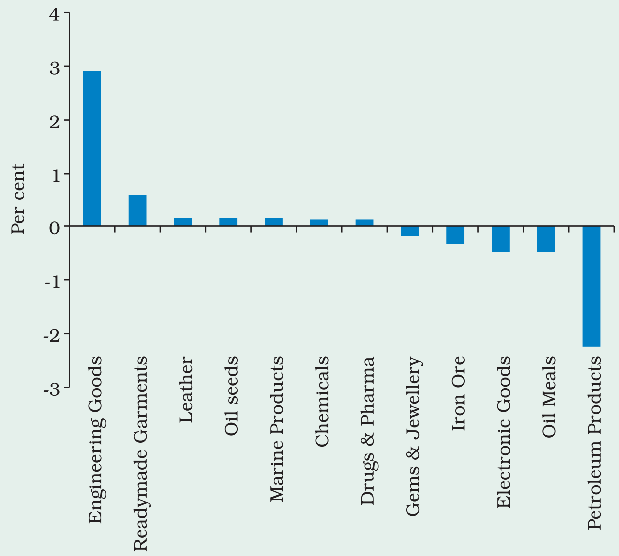
Chart II.33: Merchandise Exports - Targets and Achievement



Weighed down by a sharp fall in Q4, the volume of both POL and non-POL exports grew only modestly in 2014-15. Merchandise export growth in US dollar terms held up well in Q1 of 2014-15, but gradually lost momentum in Q2 and Q3, followed by a decline of about 16 per cent in Q4 - the sharpest contraction since Q2 of 2009-10 at the height of the global financial crisis. Export contraction was steeper in Q1 of 2015-16, though the downward drift was slower in July 2015.

II.6.4 Amongst the major sectors, petroleum products, oil meals, electronic goods, iron ore and gems & jewellery dragged down the overall export performance in 2014-15 (Chart II.34). While the fall in exports of petroleum products reflected the softening of international crude oil prices in the last three quarters of 2014-15, weakness in demand for other commodity classes interacted with domestic supply constraints related to infrastructure and other inputs to hit non-oil exports. Destination-wise, exports to China, the EU, Singapore, Japan and Saudi Arabia suffered a larger setback in 2014-15. Given greater trade integration, India's trade

Chart II.34: Relative Contribution to Export Growth in 2014-15



seems to have become increasingly responsive to global economic and financial conditions (Box II.6).

Merchandise Imports

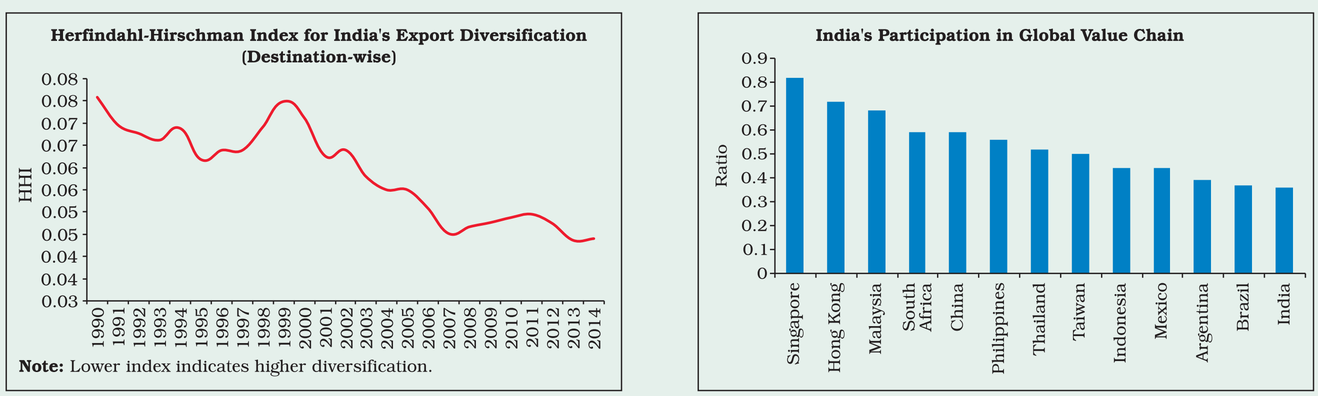
II.6.5 The plunge in global prices of crude oil by nearly 50 per cent between June 2014 and March 2015 compressed India's POL import bill by 16 per cent yielding a saving of US$ 26.5 billion in relation to the outgo on this account a year ago. Global crude oil prices stayed modest in Q1 of 2015-16 (Chart II.35). Gold imports, however, recorded an increase in terms of both value (20 per cent) and volume (38 per cent) in response to a surge in demand in H2 of 2014-15. The uptick in gold imports in the later part of 2014-15 could largely be attributed to festival demand, permission to trading

Box II.6
Trade Linkages and Elasticities

India's cross-border trade linkages have strengthened over time. Not only has India diversified its exports in terms of destinations, but its participation in global value chains (GVCs) has also increased over the years, *albeit* at a lower level than other peer economies (Chart 1), particularly in chemicals and electrical equipment (OECD 2014). Participation in GVC allows domestic firms to enter markets by specialising in niche intermediate activities within a chain and enables suppliers to upgrade production into higher-value segments of their industries. This enhances comparative advantages, productivity growth and development levels in economies.

Greater cross-border linkages through GVCs also tend to increase the sensitivity of trade to external business cycle shocks (Gangnes *et al.* 2014). Since the world is gradually transitioning to a stage in which GVC trade is assuming more importance than it did before, there appears to have been a long-run increase in the elasticity of global trade with respect to world economic activity (Escaith *et al.* 2010). In this context, estimation of country-specific trade elasticities assumes importance, especially in an international environment in which competitive monetary policy stances and exchange rate effects have implications for export competitiveness.

Chart 1: India's Cross-border Trade Linkages



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For India, the size of real exchange rate elasticity of real non-oil exports is estimated to be in the range of 0.7 to 0.9 with a lag of less than one year, while the income elasticity of real non-oil exports is 2.1 to 2.7 (Jain and Tewari. *2014*). Similarly, the volume of imports is found to be predominantly responsive to domestic demand while its elasticity with respect to the real exchange rate is broadly in the range of 0.3 to 0.5. The estimates of income and exchange rate elasticities are broadly in line with other studies undertaken for India (Table 1). Overall, there appears to be support for the Marshall-Lerner condition implying the efficacy of exchange rate changes in moving the trade balance to the desired level.

In order to improve trade linkages with the rest of the world, India's participation in GVC must improve. Policy focus should be concentrated on cluster development in particular sectors with large presence of MSMEs so that they can integrate effectively in the global production network. Another way for domestic firms to integrate into GVC is through a joint venture or strategic partnership to achieve synergy gains. Cross-border foreign investments should be encouraged. While inward FDI benefits domestic firms in terms of capital, technology transfer and research and development (R&D) capabilities, outward FDI increases their productivity by providing access to scarce raw materials, a skilled labour force and expanding production networks. Firms also need to specialise in logistics, design, assembly and R&D. Thus, further policy attention is warranted to support in-house R&D so as to enable domestic firms to achieve quality standards and specialise in high value added activities. There is ample scope for improvement in the quality and efficiency of services (for example, basic infrastructure and air transport) which will help India raise its share in GVC.

Table 1: Major studies undertaken for India

Author (s)	Findings
Hsing (2010)	Marshall-Lerner condition holds
Aziz and Chinoy (2012)	IE (4.0) and ERE (0.6)for exports
UNCTAD (2013)	IE (1.9) and ERE (0.54) for exports
Pandey (2013)	Marshall-Lerner condition holds
Mohan and Kapur (2014)	ERE (0.21 to 0.65) for X and (0.19 to 0.42) for M
Raissi and Tulin (2015)	IE (>1.5)

Note: X: Exports; M: Imports; ERE: Exchange rate elasticity; IE: Income elasticity.

Greater participation in GVC also makes a country's trade more susceptible to global economic and financial conditions (that is, demand/supply conditions and exchange rate changes). Given the sensitivity of India's trade to income conditions and exchange rate changes, policymakers need to be cognizant of external shocks especially through capital flows and domestic inflation and productivity levels as they may have significant implications for real effective exchange rate movements which eventually impact India's trade balance.

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Aziz, Jahangir and Sajjid Chinoy (2012), 'India: More Open Than You Think', Economic Research, J.P.Morgan.

Escaith, Hubert, Nannette Lindenberg, and Sébastien Miroudot (2010), 'International Supply Chains and Trade Elasticity in Times of Global Crisis', Economic Research and Statistics Division Staff Working Paper 2010-08, World Trade Organisation, Geneva.

Gangnes, Byron S., Alyson C. Ma and Ari Van Assche (2014), 'Global Value Chains and Trade Elasticities', UHERO Working Paper No. 2.

Hsing, Y. (2010), 'Test of the Marshall-Lerner Condition for Eight Selected Asian Countries and Policy Implications', *Global Economic Review*, 39 (1): 91-99.

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Kapur, Muneesh and Rakesh Mohan (2014), 'India's Recent Macroeconomic Performance: An Assessment and Way Forward', IMF Working Paper No.14/68.

Pandey, Ritesh (2013), 'Trade Elasticities and the Marshal Lerner Condition for India', *Global Journal of Management and Business Studies*, 3 (4): 423-28.

Raissi, Mehdi and Volodymyr Tulin (2015), 'Price and Income Elasticity of Indian Exports - The Role of Supply-Side Bottlenecks', IMF Working Paper No. 15/161.

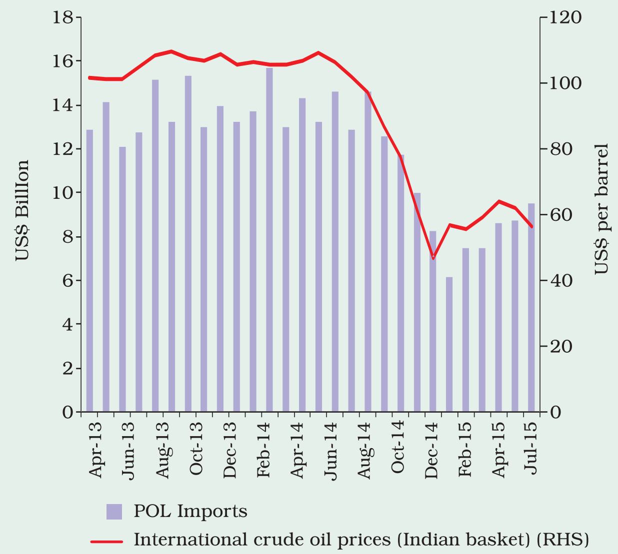
OECD (2014), *India Policy Brief*, November.

UNCTAD (2013), *Impact of the Global Slowdown on India's Exports and Employment.* New York and Geneva: United Nations.

houses to import gold for domestic consumption as well as the withdrawal of the 20:80 scheme and other restrictions for gold imports.[1] Further, sharp increase in gold imports in March and April 2015

[1] On May 13, 2013, the Reserve Bank restricted the import of gold by banks on a consignment basis to meet the genuine needs of exporters of gold jewellery, followed by the 20:80 scheme on July 22, 2013 under which all nominated banks/agencies were to ensure that at least one-fifth of every lot of import of gold was exclusively made available for the purpose of exports. Effective May 21, 2014, nominated banks/agencies/ premier or star trading houses/special economic zone units/export-oriented units were permitted gold imports under the 20:80 scheme. While the gold metal loan scheme was also restored in May 2014, the 20:80 scheme was withdrawn in November 2014. Further, imports on a consignment basis were also restored.

Chart II.35: International Crude Oil Prices and POL Imports



also reflected suppressed demand in preceding months in anticipation of a cut in customs duty in Union Budget 2015-16 and demand surge on account of *Akshaya Trithiya.* After being subdued, gold imports again spiked in the month of July 2015, as gold prices dipped to the lowest level in last four years, stimulating domestic consumption demand (Chart II.36).

II.6.6 Non-oil non-gold imports picked up modestly in 2014-15 largely in response to domestic requirements of industry (Chart II.37). Higher imports of iron and steel, iron ore, coal, non-ferrous metals, chemicals and machinery also resulted from shortfalls in domestic production in certain sectors. In particular, the rise in coal imports reflected higher requirements of power companies which have added capacity to meet growing domestic demand for power. Import of vegetable oils was also driven by shortages in domestic production. Non-oil non-gold imports increased in the current financial year up to July 2015, though at a modest pace.

II.6.7 With the decline in exports exceeding the fall in imports, the merchandise trade deficit widened marginally in 2014-15 from its level in 2013-14. While softening of oil prices compressed India's POL trade deficit, the non-POL trade deficit widened from US$ 34.2 billion in 2013-14 to US$ 55.7 billion in 2014-15 (Table II.13). However, the trade deficit at US$ 45.0 billion during first four months (April-July) of 2015-16 was lower than that in the same period of 2014-15.

Chart II.36: Gold Imports

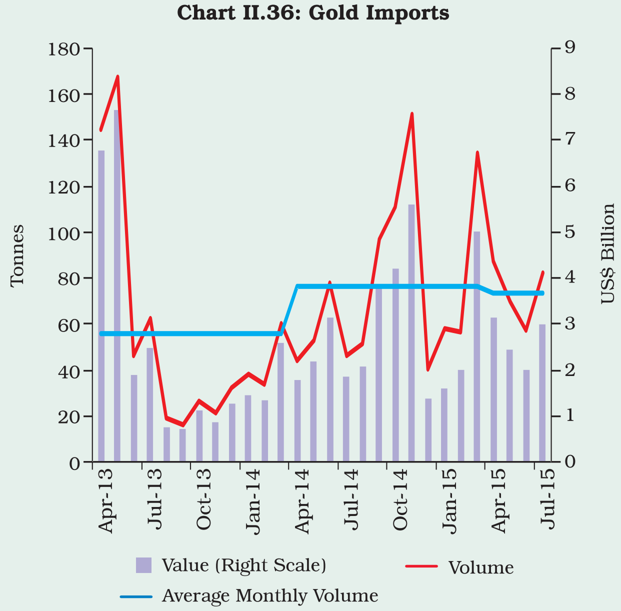


Chart II.37: Non-Oil Non-Gold Imports

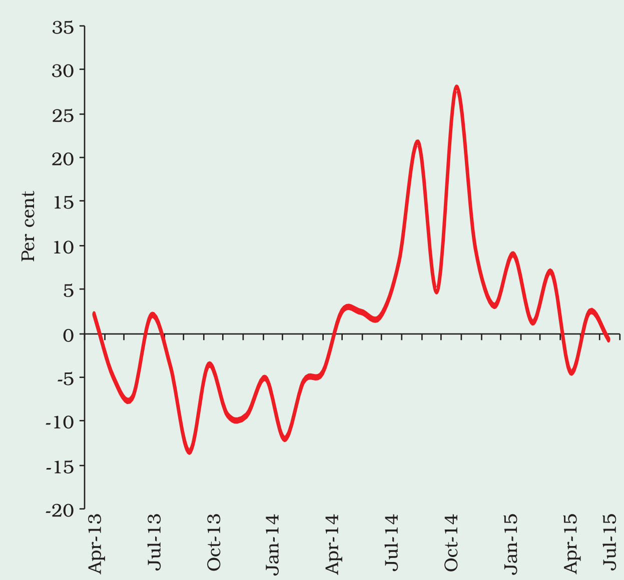


Table II.13: Merchandise Trade Deficit

(US$ billion)

Item	2014-15 (P)		2013-14 (R)	
	Value	% Growth	Value	% Growth
1	2	3	4	5
Export	**310.5**	**-1.2**	**314.4**	**4.7**
Of which:				
POL	57.0	-9.7	63.2	3.8
Non-oil	253.5	0.9	251.2	4.9
Imports	**447.5**	**-0.6**	**450.2**	**-8.3**
Of which:				
POL	138.3	-16.1	164.8	0.4
Gold	34.4	19.9	28.7	-46.7
NONG	274.8	7.0	256.7	-5.9
Trade Deficit	**-137.0**		**-135.8**	
Of which:				
POL	-81.3		-101.6	
Non-POL	-55.7		-34.2	
Memo Item:				
Trade Deficit as % of GDP	-6.7		-7.2	

Source: DGCI&S.
Note: P: Provisional, R: Revised, POL: Petroleum, Oil, Lubricants. NONG: Non-oil non-gold

Current Account Deficit

II.6.8 The merchandise trade deficit (BoP basis) was partly offset by a rise in net exports of services. Aided by better growth in the US, higher technology adoption and the strength of the US dollar against the rupee, India's software exports seemed to have benefitted, though appreciation of the rupee against the euro and sluggish demand might have dampened software exports to the euro area. Net exports of travel services recorded a decline largely due to higher payments on account of personal services availed for education, medical reasons and holidays. Notwithstanding the fall in international oil prices, the flow of remittances remained stable.

II.6.9 India's current account deficit (CAD) shrank to1.3 per cent of GDP in 2014-15 from 1.7 per cent a year ago. Holding the CAD at a sustainable level going forward will hinge on a turnaround in merchandise exports. This will also involve assigning priority to unlocking domestic supply-side bottlenecks in terms of infrastructure and other key inputs, including through active policy interventions to restore productivity and competitiveness across a broad spectrum of leading sectors (Box II.7).

Financing of CAD

II.6.10 During 2014-15, India became a preferred destination for private capital flows, which responded

Box II.7
India's New Foreign Trade Policy 2015-20

On April 1, 2015, the Ministry of Commerce and Industry announced the Foreign Trade Policy 2015-20 (FTP) with a vision to making India a significant participant in world trade by 2020 and to enable the country to assume a leadership position in the international trade discourse. FTP links rules, procedures and incentives for exports and imports with other initiatives (for example, Make in India, Digital India and Skill India) with a view to improving 'ease of doing business' in India. The salient features of FTP are:

- To increase India's exports of merchandise and services from US$ 465.9 billion in 2013-14 to US$ 900 billion by 2019-20 and to raise India's share in world exports from 2 per cent to 3.5 per cent during this period.
- A new scheme, the Merchandise Exports from India Scheme (MEIS) aimed at the simplification of the incentive structure, replacing multiple schemes is in place.
- A new scheme, the Services Exports from India Scheme (SEIS) with expanded scope is in place, which will benefit all 'service providers located in India' instead of only 'Indian service providers'.
- Allowing transferability and greater flexibility in using 'duty credit scrips' which exporters will get under MEIS and SEIS.
- Prioritisation of sectors which have domestic manufacturing capabilities and potential demand (for

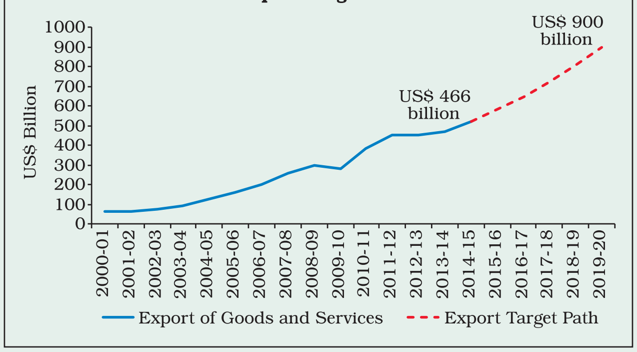
(Contd....)

example, drugs and pharmaceuticals, chemicals and electronics) where exports need to grow significantly to achieve overall growth targets.

- Other sectors identified with great export potential include engineering, leather, textiles, medical devices, natural resource based items, gems and jewellery, agri products and defence equipment.
- Emphasis on the need to increase India's participation in global supply chains. Adoption of the 'whole-of-government' approach as a significant step towards better coordination with state governments/other departments.
- Indication of the revival of the interest subvention scheme for exports from identified sectors for a period of three years, though sectoral coverage and rate of interest subvention are not indicated.
- Envisages a move towards paperless working in a 24x7 environment to facilitate the ease of doing business in India.

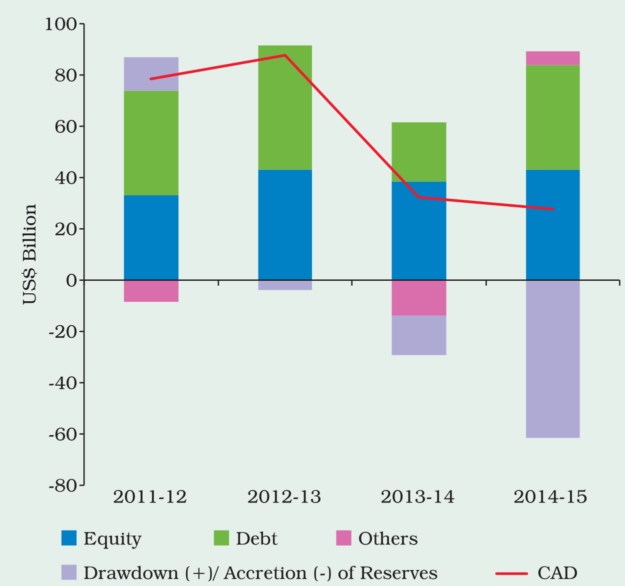
Under the new FTP, the government has expanded the scope of the new schemes to special economic zones (SEZs). Even though the target set for 2019-20 for exports of goods and services appears achievable, demand conditions in major trade partner economies will have to be supportive and domestic bottlenecks (both in terms of infrastructure and policy) need to be eased significantly. If the world economy grows faster during 2015-19 than in the 2009-14 period as projected by the IMF (2015), India's exports may fare better than in previous years. Nonetheless, taking exports to the level of US$ 900 billion by 2019-20 will need a higher compound annual rate of growth (CARG) of about 14 per cent during the FTP period (2015-16 to 2019-20) which could be a challenge (Chart 1).

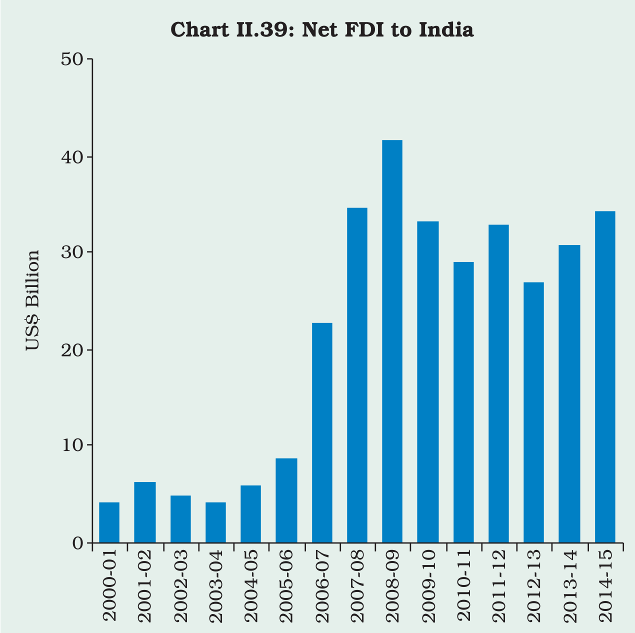
Chart 1: Export Target for 2019-20



to improved perceptions of fundamentals, optimism engendered by a stable government at the centre and expectations surrounding resurgence of business sentiment in an improved climate for investors, both foreign and domestic. The abundance of global liquidity in view of unconventional monetary policies in advanced economies also emerged as a push factor driving a relentless search for returns. Non-debt creating capital inflows alone far exceeded the financing requirement (Chart II.38). Foreign portfolio investors brought in about US$ 41 billion to Indian equity and debt markets, making India the most attractive destination among emerging markets. Further, net foreign direct investment (FDI) inflows picked up strongly in response to initiatives that are geared towards a better business environment with policy certainty. In particular, policy measures have been undertaken with regard to easing of norms for FDI in certain sectors, allocation of natural resources, the subsidy regime, financial inclusion, employment and job creation for the youth and an improved and non-adversarial tax administration. FDI inflows to India, excluding disinvestments, were the highest after

Chart II.38: Financing Pattern of Current Account Deficit





2008-09 (Chart II.39). FDI mainly flowed into the manufacturing sector responding to the government's 'Make in India' initiative, followed by financial services, retail and wholesale trade. Within the manufacturing sector, transport equipment and chemical sectors were the major recipients and accounted for about 50 per cent of the total FDI in 2014-15. Inflows to NRI deposits and in the form of external commercial borrowings were moderate during 2014-15 relative to the preceding year, signifying policy induced inflows in the past. With net capital inflows exceeding CAD sizeably, there was net accretion to reserves to the tune of US$ 61.4 billion on a BoP basis (that is, excluding valuation effects).

External Sustainability

II.6.11 External vulnerability indicators improved significantly in 2014-15 on account of both a lower accretion to the external debt stock and the build-up of foreign exchange reserves. Key debt and reserve-related indicators of external vulnerabilities reflected an improved ability to discharge external obligations. While the import cover ratio rose to 8.9 months as at end-March 2015, the ratio of short-term debt (by original as well as residual maturity) to reserves and the ratio of total external debt to reserves declined over the same period (Table II.14).

Table II.14: India's External Sector Vulnerability Indicators

(Per cent unless indicated otherwise)

Indicator/Ratios	End-Mar 2011	End-Mar 2012	End-Mar 2013	End-Mar 2014	End-Mar 2015
1	2	3	4	5	6
1. External Debt to GDP ratio	18.2	20.9	22.3	23.6	23.8
2. Short-term to Total Debt (Original Maturity)	20.4	21.7	23.6	20.5	17.8
3. Short-term to Total Debt (residual maturity) #	40.6	40.9	42.1	39.6	38.9
4. Concessional Debt to Total Debt	14.9	13.3	11.1	10.4	8.8
5. Reserves to Total Debt	95.9	81.6	71.3	68.2	71.8
6. Short-term Debt to Reserves	21.3	26.6	33.1	30.1	24.8
7. Short-term Debt (residual maturity) to Reserves #	42.3	50.1	59.0	57.4	54.2
8. Reserves Cover of Imports (in months)	9.5	7.1	7.0	7.8	8.9
9. Debt-Service Ratio	4.4	6.0	5.9	5.9	7.5
10. External Debt (US$ billions)	317.9	360.8	409.4	446.3	475.8
11. Net International Investment Position (NIIP) (US$ billion)	-207.0	-264.7	-326.7	-336.8	-363.0
12. NIIP/GDP ratio*	-12.1	-14.4	-17.8	-17.8	-18.1
13. CAD/GDP ratio	2.8	4.2	4.8	1.7	1.3

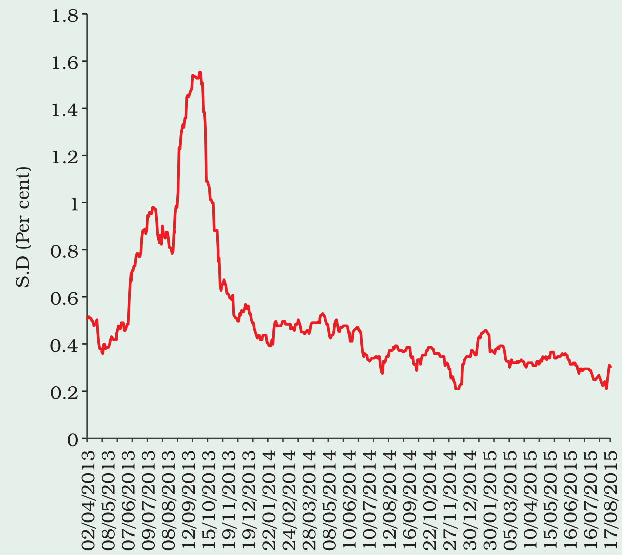
Note: #: RBI estimate; *: Based on US$ terms.

Exchange Rate Movements

II.6.12 The US dollar gained significantly against most international currencies during the year. The Indian rupee, however, depreciated only marginally against the US dollar; therefore, by the same token, it gained strongly against other major currencies, *viz*., euro, GBP and Japanese yen, reflecting the weak economic outlook for these economies and their ultra-accommodative monetary policies. Reflecting persisting inflation differentials and appreciation of the rupee in nominal terms *vis-à-vis* India's major trade partners, the real effective exchange rate of the rupee during 2014-15, on average, appreciated by 6.1 per cent and by 5.5 per cent (y-o-y) for the basket of 6 and 36 currencies respectively. The rupee exchange rate also witnessed lower volatility in 2014-15 and 2015-16 so far than in the earlier period (Chart II.40).

II.6.13 Going forward, external sector sustainability will need close monitoring, especially in a global environment characterised by high volatility in financial markets, asynchronicity in monetary policies of major advanced economies and in particular, the widely expected lift-off of US interest rates, and still high geo-political risks. Although international crude oil prices stayed at modest levels in Q1 of 2015-16 and dropped sharply in August 2015 due to excess supply and subdued demand, continuation of benign conditions for the remaining part of the year still remains uncertain.

Chart II.40: Volatility in Daily Movements in Indian Rupee (30 days-moving window)



II.6.14 For India, every US$ 1 increase in international crude prices broadly translates into an increase in the net POL import bill by US$ 1 billion. Second, following the withdrawal of gold import related measures, the import demand for gold seems to be bouncing back as evident from a growth (volume terms) of 38.5 per cent in 2014-15 and 34.3 per cent in April-July 2015. Third, key to ensuring the viability of the external sector in this backdrop is a renewed thrust on exports in terms of both products and markets. Export diversification has provided a means of insulation in the face of sluggish global economic conditions and this should be vigorously pursued to strengthen resilience and to minimise the spillovers of external shocks.

PART TWO: THE WORKING AND OPERATIONS OF THE RESERVE BANK OF INDIA

III MONETARY POLICY OPERATIONS

The conduct of monetary policy in India is undergoing a transformation, transiting to a flexible inflation targeting (FIT) framework. During 2014-15, a formal architecture for FIT based on an agreement between the Reserve Bank and the Government of India pertaining to the monetary policy framework was put in place. The liquidity management framework was revised to bring in proactive liquidity operations based on variable rate term repo/ reverse repo auctions to align the weighted average call rate, that is, the operating target around the policy rate. With ebbing inflationary pressures, receding risks to the inflation outlook and commitments to fiscal prudence, the Reserve Bank eased its monetary policy stance with a cumulative 75 bps cut in the policy repo rate during January-August 2015.

III.1 Sustaining the disinflation path set in motion in 2013-14 and instituting a robust and transparent institutional framework assigning primacy to price stability constituted the over-riding goals that the Reserve Bank had set for itself in formulating and conducting monetary policy in 2014-15. These are the first building blocks of its medium-term vision of ensuring price stability on a durable basis as a necessary pre-condition for fostering higher economic growth.

The Changing Institutional Edifice of Monetary Policy

III.2 There was a fundamental change in the conduct of monetary policy in 2014-15. Several institutional and operational innovations were put in place in the preceding year to enable this regime shift based on the recommendations of the Expert Committee to Revise and Strengthen the Monetary Policy Framework. These included improved communication by means of bi-monthly policy reviews; introduction of term repos to offset the reduction in access to liquidity through overnight fixed rate repo under the liquidity adjustment facility (LAF); and the adoption of headline consumer price index (CPI) inflation as the nominal anchor for the conduct of monetary policy. Set against this backdrop, managing the transition to a flexible inflation targeting (FIT) framework in a non-disruptive manner in 2014-15 became a key challenge. Ensuring disinflation consistent with the glide path announced in January 2014 required maintaining an anti-inflationary monetary policy stance till upside risks to the inflation outlook had been contained. Greater transparency on monetary policy necessitated release of Monetary Policy Reports (MPRs). Sector specific refinance facilities were phased out to create conditions for more effective transmission of monetary policy. A new liquidity management framework had to be put in place to ensure market-based liquidity operations through auctions, while striving to ensure consistency of liquidity conditions with the stance of monetary policy. Besides forward looking surveys, the need to strengthen technical research through forecasting and policy analysis models in order to facilitate decision making under uncertainty also assumed significance.

Agenda 2014-15: Implementation Status

Disinflation Consistent with the Glide Path

III.3 The Reserve Bank had set out a formal framework to guide monetary policy operations in 2014-15. First, in January 2014, it announced a disinflationary glide path for bringing down CPI inflation to below 8 per cent by January 2015 and to below 6 per cent by January 2016. Second, in September 2014, the Reserve Bank introduced a revised liquidity management framework that brought flexibility and transparency to liquidity management operations, while aiming at strengthening transmission in the money market by anchoring the weighted average call rate (WACR) at or closely aligned to the repo rate. Third, a landmark agreement was signed between the Government of India and the Reserve Bank in February 2015 that provided the formal architecture for conducting monetary policy operations consistent with FIT and related institutional and accountability processes.

III.4 In response to the upside risks to inflation stemming from the impact of a sub-normal monsoon on food prices and still elevated international crude oil prices, the policy rate was kept unchanged in Q1 of 2014-15. The disinflationary effects of rate increases undertaken during September 2013-January 2014 were transmitted through the economy, tempering inflationary pressures. Concerns about tepid economic activity nevertheless required the commencement of a process of gradual reduction in the statutory liquidity ratio (SLR) to give banks more freedom to expand credit to productive sectors.

III.5 By Q2, perseverance with the anti-inflationary policy stance had yielded a softening bias to inflation outcomes and was supported by a host of other factors that created room for a softer stance for monetary policy. Besides temporary base effects pulling down headline inflation, international commodity prices, particularly of crude oil (Indian basket), declined sharply by about 57 per cent between June 2014 and January 2015, aiding the disinflationary momentum. Furthermore, there were indications of a more durable downward movement in headline inflation driven by transport and communication and household requisites, suggesting that prices of non-tradables were responding to policy impulses. Awaiting a clearer assessment of the balance of risks and the durability of disinflation, the policy rate was kept unchanged during Q2 and Q3.

III.6 Inflation for January 2015 turned out to be nearly 300 basis points (bps) below the target of 8 per cent. Moreover, by January 2015, there was increasing evidence of a robust disinflationary process having taken hold. For instance, household inflation expectations three months ahead as well as one year ahead eased to a single digit for the first time since September 2009. On January 15, 2015, the policy repo rate was reduced by 25 bps to 7.75 per cent. Further, monetary policy actions were made contingent on on-going evidence about continuing disinflationary momentum and sustenance of high quality fiscal consolidation.

III.7 The new CPI re-based to 2012, which was released on February 12, 2015, confirmed that strong disinflationary impulses were underway in the economy. The pre-conditions for effecting a change in the monetary policy stance materialised in quick succession with inflation ebbing and the Union Budget for 2015-16 suggesting a tangible progress on fiscal consolidation for 2014-15 alongside a renewed medium-term commitment about fiscal rectitude. Consistent with the forward guidance, the Reserve Bank announced a cut in the repo rate outside the normal policy review cycles to 7.50 per cent in March 2015. This pre-emptive policy action was intended to utilise available space for monetary accommodation, given low capacity utilisation and continuing weakness in production and credit off-take.

III.8 The first bi-monthly policy statement for 2015-16 announced on April 7, 2015 noted that the stance of monetary policy going forward would centre around a gradual and durable disinflation, taking headline CPI inflation to 6 per cent by January 2016 and to 4 per cent by the end of 2017-18. The identified upside risks included the possibility of a sub-normal monsoon, large deviations from their seasonal patterns in vegetable and fruit prices, larger than anticipated administered price revisions, faster closing of the output gap, geo-political risks causing hardening of global commodity prices and external spillovers through the exchange rate and asset price channels. Downsides originating from global deflationary/disinflationary tendencies, the benign outlook on global commodity prices and slack in the domestic economy appeared to ameliorate upside risks. Accordingly, key policy rates were kept unchanged, pending expected transmission of past policy rate reductions to lending rates by banks.

III.9 The second bi-monthly policy statement of June 2, 2015, recognised that the headline inflation trajectory had evolved according to the projected path while the economic activity continued to be fragile. Therefore, while awaiting further data for greater clarity on the risks in meeting the medium term disinflation targets, a cut in the policy repo rate by 25 bps was front-loaded, taking it to 7.25 per cent.

III.10 Taking into account the developments in 2015-16 thus far and the balance of risks as also the front-loaded policy action of June, the third bi-monthly policy on August 4, 2015 kept the policy rate unchanged, while maintaining the accommodative stance of monetary policy. The statement noted that the short-term real risk free rates were supportive of borrowing by interest rate sensitive consumer segments such as housing and automobiles and as greater transmission of front-loaded past actions was awaited, developments would be monitored for emerging room for more accommodation.

Improved Transmission in the Money Market

III.11 The operating framework of monetary policy provides clarity on how the objectives of monetary policy respond to changes in policy rate - the repo rate. The link from the policy rate to inflation target requires a systematic and stable transmission path linking the policy rate, the operating target, an intermediate target and a transparent set of rules guiding liquidity and monetary operations on a day-to-day basis (see Box IV.I in MPR of April 2015). Liquidity management is key to aligning the operating target of monetary policy to the policy rate and is thus critical for the first leg of monetary transmission.

III.12 In India, currently the WACR is the operating target of monetary policy. Recognising the long and variable lags in transmission of monetary policy, inflation forecasts - or the projected baseline inflation path - are used as the intermediate target. This makes monetary policy proactive and forward looking.

III.13 In line with the recommendations of the Expert Committee, Q3 of 2014-15 saw the implementation of a revised liquidity management framework aimed at making liquidity management operations flexible, transparent and predictable. The revised liquidity management framework has the following features: (i) subject to availability of excess SLR securities, assured access to central bank liquidity of 1 per cent of banks' net demand and time liabilities (NDTL) comprising 0.25 per cent provided through overnight fixed rate repo auctions conducted daily, and 0.75 per cent provided through 14-day variable rate term repo auctions conducted on every Tuesday and Friday; (ii) fine-tuning operations through variable rate repo/reverse repo auctions of maturities ranging from overnight to 28 days; (iii) outright open market operations to manage enduring liquidity mismatches; and (iv) overnight marginal standing facility (MSF) up to excess SLR plus 2 per cent below SLR of individual banks.

III.14 The revised framework has necessitated a more proactive approach to liquidity management by the Reserve Bank, that is, assessing the system level expected liquidity mismatch on a daily/intra-day basis, providing more information to the market to enable precision in liquidity planning and proactive assuaging of frictional and structural liquidity mismatches.

III.15 Since introduction of the revised framework, WACR has moved close to the repo rate, indicative of growing precision in monetary policy operations. Even quarter-end spikes in WACR reflecting advance tax payments and window dressing by banks have become relatively muted, a drastic change from the past experience of large spikes around these events (Chart III.1).

III.16 The Expert Committee had recognised that in India developing market-based benchmarks could enable pricing of deposits and loans to be sensitive to changes in the policy repo rate, thereby facilitating monetary transmission. Regular auctions of 14-day term repos (twice a week) allow market participants to use the primary liquidity for longer durations. This flexibility is intended to facilitate the emergence of a market-based term money benchmark.

III.17 The spread between 14-day term repo rate and the overnight fixed repo rate has narrowed significantly after the introduction of the revised liquidity management framework, barring the year-end spikes (Chart III.2). This process is intended to be taken forward by the establishment of transparent external benchmarks, based on the marginal cost pricing principle (see para III.31).

Chart III.1: Liquidity Conditions

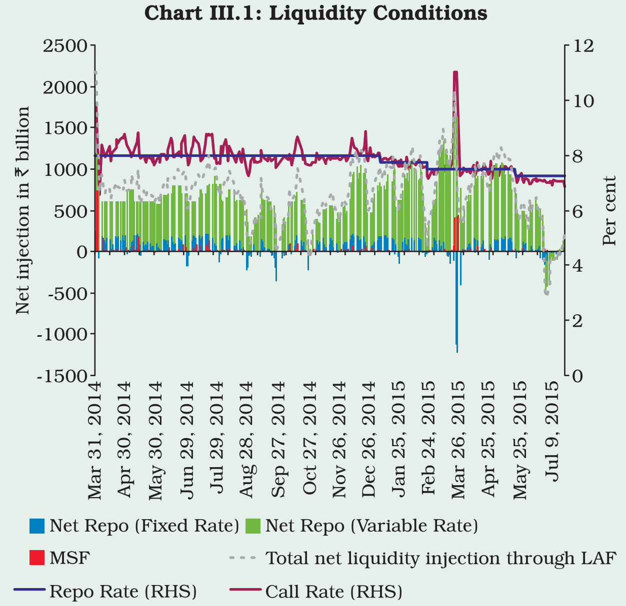
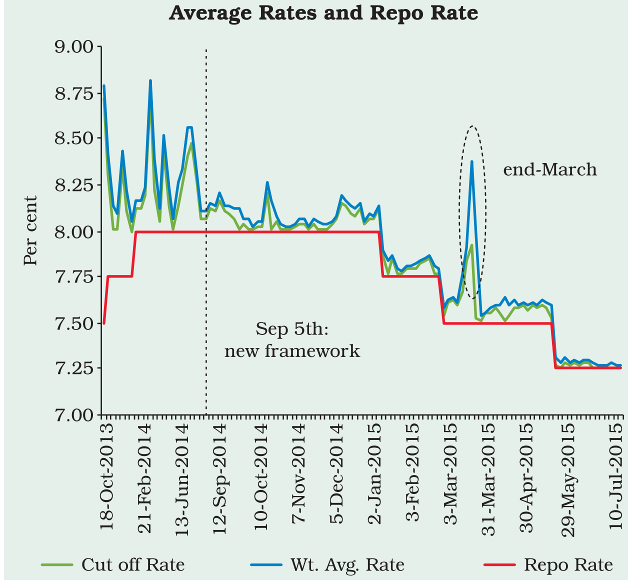


Chart III.2: 14-day Term Repo Cut off, Weighted Average Rates and Repo Rate



III.18 For smooth conduct of banking operations, the Reserve Bank has allowed access to the MSF and reverse repo windows on Saturdays with effect from February 21, 2015. Recognising that sector-specific refinance facilities at the fixed repo rate could interfere with the transmission process, the export credit refinance (ECR) facility was phased out gradually during the year and replaced with the provision of system-level liquidity with effect from February 7, 2015.

III.19 The liquidity framework was tested in March 2015 as liquidity tightened due to accumulation of cash balances of the government and banks with the Reserve Bank peaking at the end of the financial year on balance sheet and year-end considerations. In April 2015, these balances reversed, declining significantly and creating surplus liquidity conditions in the inter-bank market. The Reserve Bank managed these alternating but large movements in liquidity through 7-day, 2/3-day and overnight reverse repo auctions to fine-tune liquidity. Since mid-April, the liquidity requirement of the system has moved in a narrower range of around 1 per cent of NDTL, which has been managed through additional variable rate overnight and term repos/ reverse repos. With the increase in spending by the government, liquidity conditions improved significantly in June and July. The Reserve Bank absorbed the excess liquidity through the variable rate reverse repo auctions of varying terms. Besides, the Reserve Bank also absorbed the excess liquidity to the tune of ₹82.7 billion through OMO sales conducted on July 14, 2015.

Agreement on the Monetary Policy Framework

III.20 On February 20, 2015, the Government of India and the Reserve Bank signed an agreement on the Monetary Policy Framework. The agreement makes price stability the primary objective of monetary policy; defines price stability numerically - below 6 per cent CPI inflation for 2015-16 (to be achieved by January 2016) and 4 +/- 2 per cent for all subsequent years; sets out what will constitute a failure in achieving the target; and specifies that the Reserve Bank in the event of failure will report to the government on: (a) reasons for deviation of inflation from the target over three consecutive quarters, (b) remedial measures, and (c) an estimated time frame over which inflation will be brought back to the target.

III.21 The agreement represents a fundamental institutional reform in India as it mandates the Reserve Bank to pursue FIT with transparency, predictability and accountability. The government's commitment to the agreement also enhances the credibility of the framework, bringing confidence about the process of fiscal consolidation and supply management, both of which are highly relevant for maintaining price stability.

Monetary Policy Reports and Transparency

III.22 In pursuance of the recommendations of the Expert Committee, the first issue of the MPR was released along with the fourth bi-monthly monetary policy statement in September 2014, providing a medium-term outlook and the balance of risks around a variety of potential shocks. With the publication of MPR, India joins a select band of countries that lay emphasis on transparency and forward looking communication to ensure public understanding and accountability of monetary policy formulation and operations (Box III.1).

III.23 Forward guidance provided in the fifth bi-monthly policy statement in December 2014 indicated the possible commencement of an easing cycle by early 2015 if the disinflationary process moved along the expected trajectory, coupled with evidence of softening inflationary expectations, quality and quantity of fiscal consolidation, steps to augment supply of key inputs and unlocking of stalled investments so as to revive the economy

Box: III.1
Monetary Policy Report – A Communication Tool under Inflation Targeting

The inflation targeting (IT) framework is based on the premise that an explicit and clearly communicated numerical target level of inflation over a specified period will help anchor long-run inflation expectations. Achieving credibility by way of anchoring inflation expectations to the target is crucial for the framework to be successful. This requires an effective communication strategy between the central bank and the public. A core element of this communication strategy is that of providing forecasts of inflation, an analysis underpinning these forecasts and the rationale embedded in the policy decisions taken by the central bank. Thus, a high degree of transparency embodied in high quality reports is often considered essential for establishing and maintaining the credibility of the framework (Svensson 2002). Consequently, inflation targeting central banks typically publish a regular Inflation or Monetary Policy Report (MPR) with the aim of making monetary policy transparent, comprehensible and predictable, and hence, credible as far as possible (Table 1).

In fact, transparency and communication has become a *sine qua non* for effective and successful conduct of monetary policy in recent years; even non-IT central banks such as the Federal Reserve now communicate through an MPR.

In India, based on the recommendations of the Expert Committee, the monetary policy framework began a phased transition to a flexible inflation targeting (FIT) framework from the first bi-monthly monetary policy statement in April 2014. Along with this transition, a half-yearly MPR has been introduced since September 2014. Consequent to the agreement signed between the Government of India and the Reserve Bank in February 2015 to formally adopt a FIT framework, it has become mandatory for the Reserve Bank to publish a six-monthly report explaining the sources of inflation and forecasts of inflation for six to 18 months ahead. The first report after the agreement was published as the second MPR in April 2015. As with other IT countries, the endeavour is to make MPR a prominent communication tool to bring about transparency and credibility in the conduct of monetary policy in India. The MPR brings out the assessment of the Reserve Bank's staff on the macroeconomic outlook based on a forward looking assessment and on model-based forecasts along with baseline assumptions and balance of risks, which form the basis for its monetary policy stance. The report also carries a detailed assessment of economic and financial conditions which inform the overall macroeconomic outlook.

References:

Svensson, L.E.O. (2002), 'Monetary Policy and Real Stabilization', in 'Rethinking Stabilisation Policy: A Symposium by the Federal Reserve Bank of Kansas City,' MO: Federal Reserve Bank for Kansas City

Reserve Bank of India (2014), *Report of the Expert Committee to Revise and Strengthen the Monetary Policy Framework*, January.

Table1: Inflation targeting countries and objectives of the Monetary Policy Report

Countries	*Report*	*Main Objective*	*Countries*	*Report*	*Main Objective*
1	2	3	4	5	6
Armenia	IR	Transparency	**New Zealand**	MPS	Communication
Australia	SMP	Transparency	**Norway**	MPR	Communication
Brazil	IR	Transparency	**Peru**	IR	Communication
Canada	MPR	Transparent communication	**Philippines**	IR	Transparency
Chile	MPR	Transparent communication	**Poland**	IR	Communication
Colombia	IR	Transparency	**Romania**	IR	Transparency
Czech Republic	IR	Transparent communication	**Russia**	MPR	Transparency
Ghana	MPR	Transparency	**Serbia**	IR	Communication
Guatemala	MPR	Transparency	**South Africa**	MPR	Transparency
Hungary	IR	Transparency	**South Korea**	MPR	Communication
Iceland	Monetary Bulletin	Accountability	**Sweden**	MPR	Communication
Indonesia	MPR	Transparency and accountability	**Thailand**	MPR	Communication
Israel	MPR	Transparency	**Turkey**	IR	Communication
Mexico	Quarterly Report	Transparency	**Uganda**	MPR	Communication
Moldova	IR	Transparency	**UK**	IR	Communication

Source: Central banks' websites and IMF.
Note: SMP: Statement on monetary policy; MPS: Monetary policy statement, IR: Inflation report; MPR-Monetary Policy Report/ Review

more generally. Policy rate reductions, in January, March and June 2015 were consistent with this guidance.

Monetary Policy Transmission to Lending and Deposit Rates

III.24 The transmission of monetary policy is typically characterised by long, variable and uncertain time lags with asymmetric market responses to policy impulses in terms of magnitude and/or direction across segments in different phases of liquidity conditions. Furthermore, the transmission of policy rate changes to deposit and lending rates of banks is lagged and less complete relative to money market rates, reflecting the presence of structural rigidities in the credit market (Table III.1). Therefore, improving the efficacy of monetary policy impulses to their fullest effect remains incomplete even as some degree of pass through of rate reductions in the recent period has been translated into lending rates. The Reserve Bank announced a number of initiatives and measures during the year to incentivise banks to improve transmission at their end. Progress in this direction is expected to be seen going forward.

III.25 The improvement in liquidity conditions following the implementation of the revised liquidity

Table III.1: Asymmetry in Transmission Across Financial Markets in Different Phases of Monetary Policy Cycles

Items	Variation (Percentage Points)			
	Tightening Phase (March 19, 2010 to April 16, 2012)	Easing Phase (April 17, 2012 to July 15, 2013)	Tightening Phase (July 16, 2013 to Jan 14, 2015)	Easing Phase** (Since Jan 15, 2015)
1	2	3	4	5
Policy Rate (Repo Rate)	3.75	-1.25	0.75	-0.75
CRR	-1.00@	-0.75	0.00	0.00
Call Rate	4.98	-1.51	0.36	-0.21$
CBLO Rate	5.43	-2.34	2.14	-0.96
Market Repo Rate	6.12	-1.49	0.61	-0.37
91-Days Treasury Bill	4.53	-1.29	0.83	-0.90
3-Month CP Rate	4.24	-2.17	0.43	-0.96
3-Month CD Rate	4.36	-2.08	0.50	-0.98
5-Year Corporate Debt Yield	0.93	-0.71	-0.21	-0.16
10-Year Corporate Debt Yield	3.13	-1.02	-0.09	-0.43
2-Year G-Sec Yield	1.87	-0.35	0.26	-0.13
3-Year G-Sec Yield	1.34	-0.57	0.32	-0.10
5-Year G-Sec Yield	1.05	-0.84	0.20	-0.04
10- Year G-Sec Yield	0.64	-1.10	0.34	-0.05
Median Term Deposit Rate	**2.31**	**0.00**	**0.07**	**-0.39**
Median Base Rate*	**2.75**	**-0.35**	**0.25**	**-0.30**
WALR (Outstanding Loans)	**2.13**	**-0.44**	**-0.10**	**-0.17#**
WALR (Fresh Rupee Loans)	**-**	**-**	**0.13**	**-0.51#**

Source: Bloomberg and the Reserve Bank of India.
*: Base rate system was introduced from July 1, 2010. **: Data are till Aug 14, 2015.
@: CRR was cut to create the desirable liquidity conditions ahead of the repo rate cuts in the next easing phase.
- : Not Available. #: End-point relates to June 2015. WALR: Weighted average lending rate.
$: Including off-market deals effected by co-operative banks.
Note : (i) Policy rate, deposit and base rates are at end-month while money and bond market rates are the monthly average.
(ii) Data on WALR are provisional.

Table III.2: Deposit and Lending Rates of SCBs (Excluding RRBs)

(Per cent)

Month-end	Repo Rate	Term Deposit Rates		WALR	
		Median	WADTDR	Outstanding Rupee Loans	Fresh Rupee Loans
1	2	3	4	5	6
Mar-14	8.00	7.74	8.79	12.21	11.64
Jun-14	8.00	7.74	8.73	12.21	11.68
Sep-14	8.00	7.72	8.70	12.12	11.59
Dec-14	8.00	7.55	8.64	12.11	11.59
Mar-15	7.50	7.50	8.57	12.06	11.25
June-15	7.25	7.22	8.43	11.94	11.08
Aug 14,15	7.25	7.14	-	-	-
Variation (Percentage Points) (since Jan 15, 2015)	**-0.75**	**-0.39**	**-0.21**	**-0.17**	**-0.51**

-: Not available.
WADTDR: Weighted average domestic term deposit rate.
Note: Data on WADTDR and WALR are provisional.

management framework in September 2014 was reflected in a decline in deposit and lending rates of banks. The decline in deposit rates was, however, not fully reflected in the weighted average lending rates (WALR) of banks, indicating their efforts to maintain net interest margins (NIMs) in an environment characterised by weak credit demand and risk aversion amidst rising non-performing loans (NPAs). The WALR on fresh rupee loans sanctioned by banks declined by 51 bps to 11.08 per cent since the first round of reduction in the repo rate (Table III.2). WALR on outstanding rupee loans, however, declined by only 17 bps during the same period as the interest rates on loans disbursed earlier are reset with a time lag.

III.26 While the response of commercial banks to a reduction in the policy rate by 75 bps is still unfolding, the movement of lending rates across various sectors is uneven, presumably reflecting the differential risk assessment of banks (Table III.3).

III.27 The base rate system introduced in 2010 has been an improvement over the benchmark prime lending rate (BPLR) system, disallowing sanctioning of a large proportion of the loans at sub-prime rates. Banks are free to determine their lending rates based on cost of funds or any other relevant market based benchmark. Base rates have converged to a narrow range of 9.70-10.15 per cent for public sector banks (PSBs). However, the base rates are found to be sticky and impeding transmission of monetary policy.

Table III.3: Weighted Average Lending Rates of SCBs (Excluding RRBs)* - Select Sectors
(at which 60 per cent or more business is contracted)

(Per cent)

End-Month	Agriculture	Industry (Large)	MSME	Infrastructure	Personal Loans			
					Housing	Vehicle	Education	Credit Card
1	2	3	4	5	6	7	8	9
Mar-14	10.70	13.06	13.10	13.09	10.85	12.38	12.96	35.46
Jun-14	10.79	13.05	13.04	13.05	10.61	12.09	12.91	36.70
Sep-14	10.79	13.01	13.09	13.02	10.52	11.97	12.90	38.23
Dec-14	10.93	12.95	13.05	13.05	10.76	11.83	12.90	37.86
Mar-15	10.96	12.80	12.91	12.89	10.99	11.62	12.87	37.88
June-15	10.76	12.62	12.36	12.24	10.81	11.39	12.58	37.87
Variation (Percentage Points) (Jun15-15 over Jan-15)	**-0.17**	**-0.33**	**-0.69**	**-0.81**	**0.05**	**-0.44**	**-0.32**	**0.01**

*: Based on outstanding rupee loans.
MSME: Micro, Small, and Medium Enterprises

III.28 As highlighted in the Report of the Expert Committee, the sluggish transmission to credit markets reflects the interaction of several factors. The major factors impeding transmission include rigidities in re-pricing for fixed deposits, high volume of government borrowing, practice of yearly resetting of administered interest rates on small savings (including public provident fund) linked to G-sec yields, interest rate subventions, high level of NPAs and a significant presence of informal finance. There could also be risks emanating from a possible migration of deposits to alternative financial assets, as well as physical savings yielding higher expected real rates of return. Further, in the calculation of the base rate, the repo rate does not enter directly, operating only through the costs of wholesale funding which are sensitive to changes in the repo rate.

III.29 In an easing phase, banks tweak the spread over the base rate while pricing loans instead of changing the base rate itself. This is an opaque practice that leads to discrimination among new and old borrowers. The issue was highlighted by the Working Group on Pricing of Credit and accordingly in January 2015, banks were allowed greater operational flexibility to price credit with the freedom to revise the methodology every three years instead of every five years as was done earlier.

III.30 Moreover, to address the issue of arbitrary charging of spread, banks were advised: (a) to have a board-approved policy, delineating the components of spread charged to a customer; and (b) to ensure that the spread charged to an existing borrower (other than a consortium and multiple banking arrangements) does not increase, except on account of deterioration in the credit risk profile of the customer or change in the tenor premium. Going forward, these measures are expected to improve transparency and fairness in the credit pricing framework in India.

III.31 In its first bi-monthly monetary policy statement for 2015-16 announced on April 7, 2015, the Reserve Bank stated that the base rate calculated on the basis of a marginal cost of funds should be more sensitive to changes in policy rate. In order to improve the efficiency of monetary policy transmission, the Reserve Bank will encourage banks to move to a marginal cost-of-funds-based determination of their base rates. Once the Financial Benchmark India Pvt. Ltd., an independent benchmark administrator, starts publishing various indices of market interest rates, the Reserve Bank will encourage banks to use the indices as an external benchmark for pricing bank products.

Projected and Actual Trajectories of Growth and Inflation

III.32 The Reserve Bank’s growth and inflation projections are prepared under considerable uncertainty and shifting balance of risks. While common assumptions (covering some of the key determinants of inflation and growth) are used to generate the baseline projected paths, upside/ downside risks and the resultant likely deviations of the inflation and growth paths from the baseline are presented as part of the assessment of balance of risks in the MPRs.

III.33 The actual inflation path during Q4 of 2014-15 turned out to be significantly below what was indicated in the September 2014 MPR in view of the large changes in underlying conditions which were widely unanticipated. Two major factors, *inter alia*, necessitated this revision. First, in February 2015, the CSO updated the all India CPI-Combined series base from 2010=100 to 2012=100. As per CSO, inflation on an average in 2014 in the new series was 50 bps lower than what was recorded in the old series. The divergence varied from (+) 0.04 to (-) 1.11 percentage points in different months. Second, crude prices registered a sharp fall between September 2014 and January 2015 and, on an average, crude oil prices were 36 per cent lower than what was considered as part of the baseline assumptions in the MPR of September 2014. The release of the new series on national accounts by the CSO in January 2015 was another major exogenous shock to the Reserve Bank's projections. Growth projection for 2014-15 was retained unchanged at 5.5 per cent since January 2014 till the revised national accounts numbers were released by the CSO in January/February 2015. The stronger than anticipated growth momentum in the CSO data (new base) relative to the data as per the old base was the key factor behind the deviation of the Reserve Bank's projected output growth for 2014-15 from CSO's estimates. The Reserve Bank is continuously engaged in refining and modernising its analysis and forecasting capacities so as to improve precision and stability. These efforts notwithstanding, improving projection performance in the face of major data revisions and large magnitudes of supply/external shocks will remain a key challenge for forward looking conduct of monetary policy.

Anchoring Inflation Expectations

III.34 The monetary policy framework of the Reserve Bank aims at anchoring inflation expectations as close as possible to the target. During 2014-15, anchoring expectations, especially breaking the rigidities that had set in from the experience of 2009-13 turned out to be a major challenge.

III.35 Large divergence between the wholesale price index (WPI) and CPI inflation in the first half of 2015 also posed a major challenge for monetary policy communication, given the formal adoption of CPI-C inflation jointly by the government and the Reserve Bank to set the inflation target against the backdrop of growing expectations of a highly accommodative monetary policy stance based on deflationary WPI. The Expert Committee had examined all the policy relevant issues involving WPI and CPI, and also reviewed the choice of a relevant measure of inflation in other advanced and emerging economies for the conduct of monetary policy. The coverage of items in the two price indices – CPI-C and WPI - is different. The weight of food in the CPI-C basket is higher at about 46 per cent, as against about 24 per cent in WPI. Nearly a quarter of CPI-C is composed of services whereas this component is not covered in WPI. CPI-C, therefore, is the most representative of available measures of price indices in India. The decline in WPI in the last 9 months has been driven by the sharp fall in global commodity prices, including crude petroleum and industrial raw materials, such as metals and chemicals. Generally, divergent inflation trends as per different price indices do not persist for long. Even if such divergences persist, anchoring the expectations of all agents in the economy as per the CPI-C inflation target will be important, even though divergent trends may entail differential welfare effects on different sections of the population depending on their own consumption baskets and range of inputs used in the production processes.

Uncertain and Time Varying Macro-dynamics

III.36 Modern day monetary policy operating frameworks focus on price stability under dynamic liquidity and financial conditions. Macro-financial linkages can, however, change significantly, and the conduct of monetary policy should recognise this and respond in a timely manner. An assessment of the natural real rate of interest assumes critical importance in this context under the explicit recognition that it is not static and may vary over time. Model-based estimates of natural real interest rate for India in Q4 of 2014-15 suggest a range of 0.6 per cent to 3.1 per cent, with +/- one standard error of about 50 bps (Box III.2).

III.37 There were, however, some challenges that were not fully addressed during 2014-15. First,

Box III.2
Time-varying Natural Interest Rate in India

The natural rate of interest propounded by Wicksell (1898) has become a standard reference point in assessing the monetary policy stance of central banks since the 1990s, particularly after the growing popularity of flexible inflation targeting (FIT) and the use of Taylor type interest rate rules. While it was originally conceptualised as an equilibrium real rate at which desired saving equals desired investment, in its modern day formulation it is equated with the real rate of interest that is consistent with a zero output gap and inflation stable around its target over the business cycle. In any Taylor rule type assessment of a monetary policy stance, the natural real interest rate is often assumed as constant, even though in reality it may vary over time in response to supply and demand side shocks, which could be large and persistent.

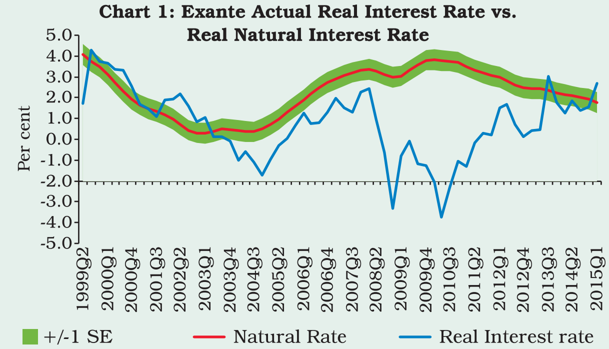
Trend changes in productivity, population growth and households' time preference in terms of consumption and saving decisions over their life cycle have been the conventional determinants of the natural real interest rate. The global saving glut that preceded the global financial crisis had already imparted a significant downward pressure to global natural real interest rates. After the global crisis, the collapse of investment demand and subsequent deleveraging by corporations and households seem to have amplified the downward pressure on natural real interest rates in advanced economies (AEs).

Estimates for the US economy suggest that the natural real interest rate which declined from about 3.5 per cent in 1990 to about 2 per cent in 2007, fell sharply to zero over the recession years of 2008 and 2009, and since then remained near zero for five years up to 2014 (Williams 2015). Secular stagnation is widely believed to keep the natural real interest rate near zero in the medium-run.

In India there has been a significant fall in total factor productivity after the global crisis which is a major structural factor pushing down the natural real interest rate. The sharp deceleration in the annual rate of increase in gross fixed capital formation over the six-year period 2009-10 to 2014-15 relative to the pre-crisis phase of high growth reflects the change in time preference of entrepreneurs, that is, to wait and delay new investment projects in the midst of elevated uncertainty. Households, in turn, had to face persistently high inflation in the midst of a weakening outlook for employment and income growth, and their preference for inflation hedges in the form of gold and real estate led to a decline in financial savings. Favourable demography and the associated shift in the pattern of demand for credit and saving behaviour over life-time to smooth consumption could also alter the natural rate.

When so many factors potentially alter the natural rate, the time varying natural rate for India, estimated using the Kalman filter (Laubach and Williams 2003), has moved in the range of 0.5 per cent to 4 per cent over time, and seems to have declined since 2010 gradually to about 2 per cent now (Chart 1). The estimation of the natural rate of interest is highly sensitive to the underlying model, choice of variables, assumptions used for approximating potential output, the representative measure of inflation expectations and even the inflation target (that is, 6 per cent *vis-à-vis* 4 per cent). Alternative estimates of the risk free natural real interest rate accordingly suggest a range of 0.6 per cent to 3.1 per cent for Q4 of 2014-15. Uncertainty about the true value of the natural rate is a challenge for the conduct of monetary policy.

Chart 1: Exante Actual Real Interest Rate vs. Real Natural Interest Rate



References:

Williams, John C. (2015), 'The Decline in the Natural Rate of Interest', Federal Reserve Bank of San Francisco, March 2.

Laubach, Thomas and John C. Williams (2003), 'Measuring the Natural rate of Interest', *Review of Economics and Statistics*, 85(4), November.

efforts for a better assessment of intra-day liquidity conditions to support more effective fine-tuning of liquidity operations were handicapped by the uncertainties involved in predicting government cash balances. Second, the capacity to assess the impact of external spillovers on the domestic economy was also limited owing to the suddenness characterising various international developments, particularly, blurred assessments worldwide on the magnitude and timing of these events. Third, the transmission of repo rate cut to deposit and lending rates remained incomplete, and credit growth continued to be sluggish in an easing cycle of monetary policy. Besides the several factors mentioned earlier and the various steps taken by the Reserve Bank, the lower share of wholesale funding of banks in India has also partly hampered effective transmission of the policy rate to deposit and lending rates. Bank funding in India has a preponderance of retail deposits/savings that inhibits a seamless moderation in the cost of funds in response to reductions in the policy rate.

Agenda for 2015-16

III.38 In the context of the agenda set for 2014-15, the stance of monetary policy on the back of conducive supply management and the government's fiscal measures aided by favourable commodity prices helped in achieving sustained and significant disinflation to levels well below the set trajectory. The new liquidity management framework contributed to lower volatility in money market rates while allowing these rates to be determined through market forces in response to policy repo rate signals and day-to-day normal and fine-tuning liquidity operations. Two macro models were institutionalised for generating forecasts and scenario analyses, and the publication of two bi-annual MPRs contributed to strengthening communication with enhanced transparency on key aspects of the forward looking new monetary policy framework.

III.39 Going forward, the focus of the Reserve Bank's monetary policy stance during 2015-16 will be on fostering a gradual and durable disinflationary process towards the target of below 6 per cent by January 2016 in order to achieve the centrally projected rate of 4 per cent by the end of 2017-18. At the same time, the efficacy of the monetary policy transmission mechanism needs to improve since the pass-through of recent cuts in policy rate to the bank lending rate has been partial, reflecting constraints in transmission under the existing base rate system. Identifying the impediments in pass-through and implementing an alternative method, such as marginal cost based credit pricing or identifying an appropriate benchmark for the bank lending rate will be a priority for the Reserve Bank. In this regard, it is imperative to develop market based benchmarks by developing the term segment of the money market. Thus, liquidity support may have to be progressively provided through regular auctions of longer term repos with reduced dependence on overnight fixed-rate liquidity support. While doing so, it will also be important to dampen deviations of WACR and other money market rates such as CBLO rates from the repo rate in a narrow range. The Reserve Bank will continue to explore and augment its instruments of liquidity management, including standing deposit facility for absorption of surplus liquidity, as recommended by the Expert Committee.

IV CREDIT DELIVERY AND FINANCIAL INCLUSION

The Reserve Bank kept up its efforts to ensure universal access to banking services throughout the country and improving credit delivery during the year. Apart from continued emphasis on enhancement of credit to agriculture, the major thrust during the year was on improving availability of credit to the micro, small and medium enterprises to help the sector realise its full potential. The launch of the Pradhan Mantri Jan Dhan Yojana (PMJDY) provided an added impetus to the various initiatives undertaken by the Reserve Bank towards furthering financial inclusion and financial literacy.

IV.1 Within the developmental and regulatory role of the Reserve Bank as a full service central bank, efficient and comprehensive credit delivery through panoply of channels/institutions for provision of financial products has always been accorded priority with a view to ensuring adequate financing for the productive sectors of the Indian economy. Over the years, the credit delivery system has been scaled up and expanded with innovations that reach out to the diverse financing needs of society. More recently, the effort has been to spread the economies of scale and scope and experience gained in urban and semi-urban areas to geographical regions and sections of society that asymmetric credit markets tend to exclude in view of their lack of pricing power. In 2014-15, the focus was on improving the availability of credit to micro, small and medium enterprises (MSMEs), revising priority sector guidelines to foster greater inclusiveness and enhancing the flow of credit to agriculture.

IV.2 In line with this, the Financial Inclusion and Development Department (FIDD) being the nodal department for financial inclusion focused on creating an enabling environment for providing universal access to banking services throughout the country and ensuring timely and smooth flow of credit to the priority sectors of the economy with a view to developing an efficient and inclusive financial system.

Agenda 2014-15: Implementation Status

IV.3 Guided by its core objective of fostering greater inclusiveness, the Reserve Bank's endeavour during the year was to continue its efforts to ensure extension of banking facilities to all unbanked villages and make financial inclusion a viable proposition for banks to improve credit delivery. Under the on-going Phase-II of the roadmap for financial inclusion, which envisages opening of banking outlets in all unbanked villages with population less than 2,000, the strategy included identifying unbanked villages and allotting such villages to banks for coverage. To address the need for aligning priority sector lending guidelines with national priorities, the Reserve Bank constituted an Internal Working Group to revisit the guidelines.

IV.4 In pursuance of its developmental role, the Reserve Bank accords priority to efficient and comprehensive credit delivery, particularly to priority sectors comprising primarily of the agricultural and MSME sectors, and the weaker sections of society. The guidelines on priority sector lending were revised during the year with a view to widening the scope of the sector and improving the flow of credit. Financial inclusion efforts received a big fillip with the launch of the *Pradhan Mantri Jan Dhan Yojana (PMJDY)* coupled with synchronised efforts by the Reserve Bank. To simplify credit dispensation, the need to submit 'no due certificates' to scheduled commercial banks by individual borrowers, including self help groups (SHGs) and joint liability groups (JLGs) for all types of loans, irrespective of the amount involved, was discontinued. Innovative steps to provide support to MSMEs like guidelines for introduction of a mechanism to address the issue of delayed payment in the form of a technology enabled Trade Receivables Discounting System (TReDS), conducting research on matters relating to MSMEs, design and conduct of training programmes for the MSME division-in-charges and trainers in commercial banks were initiated during the year. Additionally, MSME divisions were opened by regional offices of the Reserve Bank to focus on issues concerning lending to the sector in their respective jurisdictions.

CREDIT DELIVERY

Priority Sector Lending

IV.5 Priority sector refers to those sectors of the economy which, though viable and creditworthy, may not get timely and adequate credit in the absence of a special dispensation. Typically, priority sector loans are small value loans to farmers for agriculture and allied activities, micro and small enterprises, poor people for housing, students for education, other low income groups and weaker sections. Such sectors are spread across the length and breadth of the country and especially prevalent in the hilly and coastal regions. Priority sector lending needs to be extended by banks as part of their normal business operations and should not be viewed as a corporate social responsibility. Towards this end, pricing of all credit has been made free, though with the expectation that pricing should not be exploitative (Table IV.1).

Table IV.1: Performance in Achievement of Priority Sector Lending Targets

(Amount in ₹ billion)

Outstanding as on March 31	Public Sector Banks	Private Sector Banks	Foreign Banks
1	2	3	4
2014	16,190 (39.4)	4,645 (43.9)	907 (35.8)
2015	17,512 (37.3)	5,303 (42.8)	970 (35.9)

Notes: 1. Figures in parenthesis are percentages to ANBC or CEOBE, whichever is higher in the respective groups.
2. The data for 2015 are provisional.

IV.6 Drawing upon the recommendations of an Internal Working Group, revised guidelines on priority sector lending were issued in April 2015. With the intention of giving a thrust to the MSME sector, medium enterprises were brought in the ambit of the priority sector. Additionally, a specific target was introduced for lending to micro enterprises. In addition to medium enterprises, two new categories, *viz.,* social infrastructure and renewable energy were included under the priority sector (Box IV.1).

Box IV.1
Priority Sector Lending – A Fresh Look

The salient features of the revised priority sector lending guidelines are:

- Separate targets of 8 per cent for small and marginal farmers (within the agriculture target of 18 per cent) and 7.5 per cent for micro industries have been prescribed to be achieved in a phased manner by 2017. These targets will be made applicable to foreign banks with 20 branches and above post 2018 after a review in 2017.
- Priority sector widened to include medium enterprises, social infrastructure and renewable energy.
- Monitoring of priority sector lending compliance on a 'quarterly' average basis at the end of the respective year from 2016-17.
- Priority Sector Lending Certificates (PSLCs) will be an eligible tradable instrument for achieving priority sector targets. The buyer (a deficient bank) will pay a 'price/

(Contd...)

fee' to the seller bank (a bank which has over achieved its PSL requirements) for purchasing a specified amount of PSL obligation applicable for a particular date.

- Educational loans (including loans for vocational courses) up to ₹1 million irrespective of the sanctioned amount to be considered as eligible for the priority sector.
- Export credit up to 32 per cent of adjusted net bank credit (ANBC) or credit equivalent amount of off-balance sheet exposure (CEOBE), whichever is higher, to be eligible as part of the priority sector for foreign banks with less than 20 branches. For domestic and foreign banks with 20 branches and above, the incremental export credit over the corresponding date of the preceding year will be reckoned up to 2 per cent of ANBC or CEOBE (whichever is higher), as part of the priority sector.
- Foreign banks with less than 20 branches are required to achieve the total priority sector target of 40 per cent of ANBC or CEOBE, whichever is higher, in a phased manner by 2020.

Flow of Credit to Agriculture

IV.7 The target for agricultural credit is fixed by the Government every year. Led by the performance of scheduled commercial banks (SCBs), the actual flow of credit to the agriculture sector has been consistently higher than the target in recent years. Co-operative banks and regional rural banks (RRBs), however, could not achieve their targets for 2013-14 and 2014-15 (Table IV.2).

Stressed Assets in Agriculture

IV.8 SCBs' non-performing assets (NPAs) in the agriculture sector have been rising steadily since 2010, reflecting, *inter alia,* a decline in the recovery of agriculture advances (Tables IV.3 and IV.4).

IV.9 Although the Government has been incentivising repayment of agricultural loans through the interest subvention scheme, this has not helped in improving the asset quality. The Government has been examining various measures to improve the efficacy of the scheme. The scheme has been extended for 2015-16.

Credit Flow to Micro and Small Enterprises (MSEs)

IV.10 Reflecting the focus of the Government and the Reserve Bank on enhancing credit flow to the MSE sector, credit to the sector showed a growth of 13.6 per cent as compared to the overall bank credit growth of 9.0 per cent during 2014-15 (Table IV.5).

Initiatives for the MSME Sector

IV.11 Continuing its efforts of promoting financial inclusion in the MSME sector, the Reserve Bank launched several initiatives during the year to address impediments in the credit flow to the sector. To address the issue of delayed payments to the MSME sector, TReDS has been conceptualised as an authorised electronic platform to facilitate discounting of invoices/bills of exchange of MSMEs (see Chapter IX for details). TReDS is expected to speed up the

Table IV.2: Targets and Achievements for Agricultural Credit

(₹ billion)

End March	Scheduled Commercial Banks		Cooperative Banks		RRBs		Total	
	Target	Achievement	Target	Achievement	Target	Achievement	Target	Achievement
1	2	3	4	5	6	7	8	9
2013-14	4,750	5,090	1,250	1,199	1,000	827	7,000	7,116
2014-15*	5,400	5,997	1,400	1,384	1,200	1,025	8,000	8,406

*: Provisional.

Table IV.3 : NPAs in the Agriculture Sector

End-March	Agriculture Loans Outstanding (₹ billion)	Gross NPAs in Agriculture* (₹ billion)	Ratio of Gross NPAs (Agriculture) to Agriculture Loans Outstanding (per cent)
1	2	3	4
2010	4,636	104	2.2
2011	5,072	167	3.3
2012	5,802	248	4.3
2013	6,428	302	4.7
2014	7,698	340	4.4
2015	8,295	391	4.7

*Only SCBs.

realisation of receivables and reduce the incidence of sickness in this sector.

IV.12 Regional offices of the Reserve Bank have set up MSME specific divisions to: (i) collate and analyse data on credit flow and sickness from the region; (ii) monitor banks' efforts towards nursing and rehabilitation of MSME units in the region; (iii) monitor the level of banking activity in identified and unidentified clusters and initiate steps to enhance banking activity, wherever required; (iv) organise capacity building activities for bank functionaries involved in lending to the MSME sector; and (v) conduct research on matters relating to MSMEs, such as credit issues, availability of banking services in clusters, sickness and capacity building.

IV.13 As part of capacity building of MSME divisions in banks and to develop entrepreneurial sensitivity, the Reserve Bank's College of Agricultural Banking (CAB), Pune has designed training programmes for the MSME division-in-charges and trainers in commercial banks. CAB, Pune has also developed a syllabus for the regional offices of the Reserve Bank, which, in turn, will conduct workshops for capacity building for branch managers of specialised MSME branches in their jurisdictions.

Table IV.4: Recovery of Direct Agriculture Advances

Year	Total Demand (₹ billion)	Total Recovery (₹ billion)	Per cent of Recovery to Demand
1	2	3	4
2012	1,917.7	1,428.9	74.5
2013	2,596.2	1,975.7	76.1
2014	2,814.9	2,066.0	73.4

Table IV.5: Credit Flow to MSEs

Year	Number of Accounts (million)	Amount Outstanding (₹ billion)	MSE credit as per cent of ANBC
1	2	3	4
2014	12.6 (12.3)	8,510.9 (23.9)	15.7
2015	13.8 (10.1)	9,664.8 (13.6)	17.8

Note: 1. Data for 2015 are provisional.
2. Figures in parentheses indicate y-o-y change in per cent.
Source: Scheduled commercial banks.

FINANCIAL INCLUSION

Roadmap for Provision of Banking Facilities in Unbanked Villages with Population less than 2,000

IV.14 The Reserve Bank continued with its efforts to ensure extension of banking facilities to all unbanked villages. For this, about 490,000 unbanked villages with population less than 2,000 were identified and allotted to banks for coverage under the ongoing Phase-II of the roadmap. At end-March 2015, as reported by State Level Bankers Committees (SLBCs), 390,387 villages were covered by 14,207 branches, 357,856 business correspondents (BCs) and 18,324 other modes, such as automated teller machines (ATMs) and mobile vans. In view of the ongoing implementation of PMJDY, banks were advised to complete Phase-II coverage by August 14, 2015 instead of March 31, 2016 as prescribed earlier.

Pradhan Mantri Jan Dhan Yojana (PMJDY)

IV.15 The Government of India launched PMJDY on August 28, 2014, for extending formal financial services to the excluded population. The major features of the scheme include: (i) the facility to open a basic saving bank deposit (BSBD) account in any bank branch or BC outlet; (ii) accidental insurance cover (₹ 0.1 million) and life insurance cover (₹ 30,000); and (iii) an overdraft (OD) facility after satisfactory operation of the account for six months. Since the inception of the scheme, 165.7 million accounts had been opened by June 30, 2015. The Government of India has initiated routing of subsidy payments and also introduced insurance and pension products for BSBD account holders including for those accounts opened under PMJDY. To ensure increased activity in these accounts, the efforts that needed to be taken include: (i) rolling out direct benefit transfer (DBT) for all Central and State Government payments; (ii) offering appropriate credit products (farm and non-farm sector) after due diligence; (iii) strengthening the BC network; and (iv) increasing awareness through financial literacy initiatives.

IV.16 Reflecting the focus of the Reserve Bank on financial inclusion, the 80th anniversary celebrations of the Reserve Bank were held in Mumbai on April 2, 2015, with financial inclusion as the central theme (Box IV.2).

Financial Inclusion Plan (FIP)

IV.17 The Reserve Bank has been encouraging banks to adopt a structured and planned approach to financial inclusion with commitment at the highest levels by preparing board-approved FIPs. Out of 3,445 rural bank branches opened during 2014-15, 2,230 branches were opened in unbanked rural centres. Around 155 million basic savings bank deposit accounts (BSBDAs) were added taking the total BSBDAs to 398 million. This includes 147 million accounts opened under PMJDY. With the addition of 2.6 million small farm sector credits (kisan credit cards-KCCs) and 1.8 million small non-farms sector credits (general credit cards-GCCs), the total number of such accounts went up to nearly 42.5 million and 9.2 million respectively (Table IV.6).

Constraints in Financial Inclusion

IV.18 Though the initiative under financial inclusion has led to opening of large number of basic bank accounts of people from the excluded segment, the effort for ensuring that these accounts remain operational has to continue. This is possible

Box IV.2
RBI@80: Conference on Financial Inclusion

A financial inclusion conference was organised by the Reserve Bank in Mumbai on April 2, 2015. The Prime Minister of India was the chief guest on the occasion. Other dignitaries who attended the conference included the Governor of Maharashtra, the Finance Minister of India and the Chief Minister of Maharashtra, apart from experts from the banking and finance fraternity. The Prime Minister released the *Concise History of Reserve Bank of India: 1935-1981* at the function.

The Prime Minister encouraged the Reserve Bank to prepare a roadmap for achieving financial inclusion objectives by setting targets in a phased manner till the centenary year of the establishment of the Reserve Bank.

Panel discussions were held on the following topics as part of the conference: (i) 'Financial Inclusion - Let All Efforts Bloom'; (ii) 'Building the Business Case for Financial Inclusion - Whether BC Model is the Way to Go?'(iii) 'Financial Inclusion - the Way Forward'; and (iv) 'The linkage between Financial Inclusion, Financial Literacy and Consumer Protection'. Some of the key points which emerged from the discussions are:

- Concerted efforts of the Government of India, the Reserve Bank and banks are necessary to further the financial inclusion agenda. The strategy to realise this goal will comprise of a mix of conducive policy environment, use of innovative channels/technology and optimal utilisation of the BC model.
- The risks associated with the BC model can be mitigated by putting in place a secure system, use of appropriate technology, effective supervision, efficient cash management services and capacity building.
- Raising the level of acceptance of technology by customers will require sustained financial literacy initiatives on the part of bankers.
- Customers' awareness about their rights and duties is integral to developing a conducive consumer protection environment. This will also necessitate banks to develop strong internal grievance redressal mechanisms.

Table IV.6: Financial Inclusion Plan-Summary Progress of All Banks Including RRBs

Particulars	Year ended March 2010	Year ended March 2014	Year ended Mar 2015	Progress April 2014 - Mar 2015
1	2	3	4	5
Banking Outlets in Villages - Branches	33,378	46,126	49,571	3,445
Banking Outlets in Villages – Branchless mode	34,316	337,678	504,142	166,464
Banking Outlets in Villages -Total	67,694	383,804	553,713	169,909
Urban Locations covered through BCs	447	60,730	96,847	36,117
Basic Savings Bank Deposit A/c through branches (No. in million)	60.2	126.0	210.3	84.3
Basic Savings Bank Deposit A/c through branches (Amt. in ₹ billion)	44.3	273.3	365.0	91.7
Basic Savings Bank Deposit A/c through BCs (No. in million)	13.3	116.9	187.8	70.9
Basic Savings Bank Deposit A/c through BCs (Amt. in ₹ billion)	10.7	39.0	74.6	35.6
BSBDAs Total(No. in million)	73.5	243.0	398.1	155.1
BSBDAs Total (Amt. in ₹ billion)	55	312.3	439.5	127.3
OD facility availed in BSBDAs (No. in million)	0.2	5.9	7.6	1.7
OD facility availed in BSBDAs (Amt. in ₹ billion)	0.1	16.0	19.9	3.9
KCCs (No. in million)	24.3	39.9	42.5	2.6
KCCs (Amt. in ₹ billion)	1,240.1	3,684.5	4,382.3	697.8
GCC (No. in million)	1.4	7.4	9.2	1.8
GCC (Amt. in ₹ billion)	35.1	1,096.9	1,301.6	204.7
ICT A/Cs BC Transaction (No. in million)*	26.5	328.6	477.0	477.0
ICT A/Cs BC Transactions (Amt. in ₹ billion)*	6.9	524.4	859.8	859.8

*: During the financial year.

if all government payments are routed through the banking channel. A step ahead will be to remunerate banks appropriately for routing these transactions through the banking channel. In addition, since the last mile delivery of all banking services is expected to be done mostly through the large BC network created across the country, it is necessary to ensure that appropriate control system for oversight over BC operations is provided by banks. The success of the Information and Communication Technology based BC model critically depends upon the availability of proper network connectivity across the country.

Simplifying Credit Dispensation

IV.19 SCBs have been advised to dispense with no due certificate from individual borrowers (including SHGs and JLGs) for all types of loans, irrespective of the amount involved. Banks have been encouraged to use an alternative framework of due diligence for credit appraisal, which could consist of one or more of the following : (i) credit history check through credit information companies; (ii) self-declaration or an affidavit from the borrower; (iii) central registry of securitisation asset reconstruction and security interest (CERSAI) registration; (iv) peer monitoring; (v) information sharing among lenders; and (vi) information search (writing to other lenders with an auto deadline).

FINANCIAL LITERACY

Financial Literacy Camps

IV.20 Apart from direct initiatives, the Reserve Bank's efforts to expand financial literacy are channelled through banks. In terms of current instructions, financial literacy centres (FLCs) and rural branches of banks are required to conduct financial literacy camps at least once a month with focus on financially excluded people. Additionally,

Table IV.7: Activities Undertaken by Financial Literacy Centres

Particulars	2013-14 (April-March)	2014-15# (April-March)
1	2	3
No. of operational FLCs	942	1,181
No. of activities conducted*	56,985	84,089
Total no. of participants*	3,826,068	5,238,358
No. of participants opened accounts after attending the camps	NA	1,442,546
No. of participants already having accounts while attending camps	NA	2,890,204

*: Includes both outdoor and indoor activities. However, indoor activities have been discontinued w.e.f. April 2014.
NA: Not available. #: Provisional.

Table IV.8 : Activities Undertaken by Rural Branches

Particulars	2014-15*
1	2
No. of Rural branches	52,934
No. of Rural branches conducted camps	32,509
No. of camps conducted	306,188
Total no. of participants	14,826,647
No. of participants opened accounts after attending the camp	5,657,092
No. of participants already having accounts while attending camps	6,686,518

*: Provisional.

banks are encouraged to conduct such camps in unbanked locations. As at end March 2015, 1,181 FLCs were operational in the country, up from 942 as at end March 2014. During the period April 2014 to March 2015, financial literacy camps were conducted by 32,509 rural branches of banks and 1.4 million and 5.7 million participants opened accounts in the camps organised by the FLCs and rural branches of banks, respectively (Table IV.7 and IV.8).

Agenda for 2015-16

IV.21 Going forward, the mechanism for issue of priority sector lending certificates (PSLCs) will be made operational. This will provide banks with an instrument to aid them in priority sector target achievement and allow leveraging of their comparative advantage in lending to the priority sector. To work out a medium-term (five year) measureable action plan for financial inclusion, the Reserve Bank has constituted a Committee on Medium-term Path on Financial Inclusion (Chairman: Shri Deepak Mohanty). Studies will be conducted to assess the efficacy of existing schemes on lead bank, credit guarantee trust for micro and small enterprises (CGTMSE), KCC, SHG - bank linkage and the BC model.

IV.22 Operationalisation of TReDS, which has been conceptualised as an authorised electronic platform to facilitate discounting of invoices/bills of exchange of MSMEs, will be taken up during the course of the year. In pursuance of the objective of fostering a conducive policy environment for the MSME sector, there will be continuous monitoring of banks' efforts towards nursing and rehabilitation of MSME units, collation and analysis of data on credit flow and sickness in such units. With a view to developing 'entrepreneurial sensitivity' and improving the skills of dealing functionaries of banks, the Reserve Bank proposes to roll out a national capacity building programme. This is expected to help the functionaries understand the genuine credit needs of MSME entrepreneurs and provide timely response.

V REGULATION OF FINANCIAL MARKETS AND FOREIGN EXCHANGE MANAGEMENT

During 2014-15, the Reserve Bank undertook several measures to improve the financial markets. The efforts were targeted at increasing participation, simplifying procedures and making the markets deeper, efficient, accessible and stable. Developing the money market with appropriate instruments and adequate participation assumed central importance. Further, refining and rationalising foreign exchange regulations should contribute to the widening and deepening of the foreign exchange market. In the derivatives markets, the measures taken during 2014-15 were aimed at simplifying the documentation requirements and increasing participation in both over-the-counter and exchange traded currency derivatives.

V.1 Broadening and deepening financial markets and putting in place an appropriate architecture for regulating them have been an on-going engagement of the Reserve Bank. During 2014-15, guided by the five-pillar approach set out in the Second Quarter Review of Monetary Policy of 2013-14 to drive its developmental and regulatory policies, the Reserve Bank undertook several measures to improve liquidity, activity and resilience of various segments of the financial market spectrum, especially in the context of a volatile and uncertain international environment, so that these markets perform efficiently their intermediation role in financing India's growth. The efforts were targeted at increasing participation, simplifying procedures and making the markets deeper, efficient, accessible and stable.

V.2 In the money market, the endeavour was to further develop term/repo markets. In the government securities (G-secs) market, the objective, as in the past, was to promote liquidity and broad based participation, including by foreign investors and resident individuals. In the foreign exchange market, emphasis was placed on the liberalisation of transactions, both current and capital and inward and outward. In the derivatives segment, the objective was to develop participation through simplification of procedures. Three departments of the Reserve Bank are primarily entrusted with the roles of developing and regulating of financial markets, financial market operations and foreign exchange management.

FINANCIAL MARKETS REGULATION DEPARTMENT (FMRD)

V.3 FMRD was set up on November 3, 2014 with a mandate to regulate, develop and oversee financial markets in an integrated manner. The primary activities of the department include regulation and development of the money, G-secs, foreign exchange and related derivatives markets. The department is also responsible for the implementation of the recommendations of the Committee on Financial Benchmarks (Chairman: Shri P. Vijaya Bhaskar), strengthening of the financial market infrastructure and market surveillance. A Market Intelligence Cell is proposed to be set up as part of FMRD. Going forward, the department will focus on (i) making market access norms easier for all participants; (ii) expanding the menu of products and participants across all segments; (iii) strengthening market infrastructure in line with global standards; and (iv) leveraging the market analytics and surveillance mechanism for policy inputs.

Agenda 2014-15: Implementation Status

V.4 During 2014-15, FMRD undertook measures targeted at increasing participation, simplifying procedures and making the markets more efficient. The Technical Advisory Committee (TAC) on Money, Forex and G-secs Markets (Chairman: Harun R. Khan) was reconstituted in April 2015 with representation from various stakeholders to advise the Reserve Bank in this endeavour.

V.5 With the objective of implementing the recommendations of Committee on Financial Benchmarks, a new company, Financial Benchmarks India Pvt Ltd (FBIL), jointly promoted by the Fixed Income Money Market and Derivatives Association of India (FIMMDA), the Foreign Exchange Dealers' Association of India (FEDAI) and the Indian Banks' Association (IBA), has commenced operations in February 2015. As a first step, FBIL overnight Mumbai interbank offer rate (FBIL-Overnight MIBOR) was launched on July 22, 2015.

V.6 An appropriate public dissemination system was to be instituted at the Clearing Corporation of India Ltd. (CCIL) for disclosing the price and volume information on major interbank over-the-counter (OTC) foreign exchange derivatives. CCIL has, accordingly, started disseminating data on USD-INR forwards and USD-INR currency options with effect from April 13, 2015. The data disseminated are on an aggregated basis and contain tenor-wise traded rate/implied volatility in terms of open, high, low, last, weighted average rate (WAR), volumes and number of trades (Box V.1).

V.7 As planned, limits for short sale have been increased and undertaking short sales in the OTC market has been permitted. Re-repo of G-secs

Box V.1

G20 Commitments and Reforms in the OTC Derivatives Market in India

In response to the global financial crisis of 2007, the G20 initiated reforms to strengthen the regulation and oversight of the financial system, and tasked the Financial Stability Board (FSB) with coordination of the reforms. The reforms include improving transparency and enhancing the resilience of OTC derivatives markets. An implementation group for OTC derivatives (Chairman: Shri R. Gandhi), constituted on the direction of the sub-committee of the Financial Stability and Development Council (FSDC) has set out a roadmap for reforms.

Standardisation

- Following the standardisation of inter-bank trades in credit default swaps (CDS) and the rupee overnight index swap (OIS) based on overnight MIBOR, interest rate swaps (IRS) referenced to other benchmarks will be standardised in phases.
- Standardisation of foreign exchange derivatives will be addressed at the end of 2015 since they are generally 'plain vanilla' and market liquidity is low in currency swaps, IRS in foreign currency (FCY) and interest rate options.

Exchange or electronic platform trading

- As the market develops for forex options, currency swaps (CS), FCY-IRS and interest rate options in FCY and CDS, the possibility of introducing a trading platform will be examined.

Reporting to trade repositories (TRs)

- As in the case of all OTC forex and interest rate derivatives, client transactions in rupee IRS/ forward rate agreement (FRA) and CDS, FCY interest rate options will be brought under the reporting framework but as and when its liquidity picks up.
- Thus, India has become fully compliant with the G20 commitment on reporting of OTC derivatives transactions to TRs.

Central clearing

- More than 80 per cent of IRS trades are being centrally cleared on a non-guaranteed basis without a regulatory mandate. In principle approval has been given to CCIL to provide central counterparty (CCP) based clearing for IRS trades which will be made operational shortly.
- In the case of forex derivatives, CCP's clearing of forex forwards has been mandated. CCP clearing for forex options, CS, IRS and interest rate options in FCY and CDS in which liquidity remains low will be reviewed by end-2015.

Margin requirements

- Detailed modalities for OTC derivatives, including CDS will be prescribed taking into account the recommendation of the Basel Working Group on margin requirements and other international developments.

Capital requirements for non-centrally cleared OTC derivatives

- Rules on capital requirements for banks' exposures to CCPs have been made effective from January 1, 2014, reducing the capital requirements for centrally cleared products. In addition, credit valuation adjustment (CVA) capital charge for non-centrally cleared derivatives has also been made effective.

acquired under reverse repo has also been permitted. Facilitating participation of foreign portfolio investors (FPIs) in G-secs was one of the key mandates for the year. In this direction, FPIs were permitted to acquire G-secs directly from any counterparty in the secondary market, obviating the requirement of a broker. Settlement of all FPI transactions in G-secs has been permitted on T+2 basis. FPIs were allowed to reinvest coupons, received on their investments in G-secs, outside the existing limit and also permitted to hedge the currency risk of the coupon receipts on debt securities falling due during the following 12 months.

V.8 With the objective of introducing new products and expanding markets, 6-year and 13-year cash settled interest rate futures (IRFs) on Government of India (GoI) securities with residual maturity of 4-8 years and 11-15 years, respectively, were permitted on exchanges. A Working Group (Chairman: Prof. P.G. Apte) has been constituted for introduction of interest rate options.

V.9 To make documentation in forex markets less onerous, the certification required from the hedging entity's statutory auditors has been replaced with an undertaking from the designated officials of the entity, both in the OTC and the exchange traded currency derivatives (ETCD) markets. The eligibility limits for hedging for importers, based on past performance, have been brought at par with exporters, both in the OTC and ETCD markets. The permissible position limits on the exchanges, without the requirement of establishing underlying exposure, have been enhanced to US$ 15 million for USD-INR and US$ 5 million for all other permitted currency pairs put together.

V.10 Towards achieving the objective of providing overseas entities greater access to onshore hedging markets, external commercial borrowings (ECBs) lenders in rupees have been permitted to enter into swap transactions with their overseas bank which shall, in turn, enter into a back-to-back swap transaction with any authorised dealers (AD) category-I bank in India. In order to improve transparency and broad base participation in interest rate swaps (IRS), an anonymous electronic trading platform for IRS contracts referenced to overnight MIBOR benchmark was launched on August 3, 2015 with the CCIL's guaranteed settlement.

V.11 In respect of a few areas identified for implementation, while action has been initiated, full implementation is yet to be achieved. With regard to upgradation of the negotiated dealing system order-matching (NDS-OM) platform, necessary approvals were given to CCIL. While the architecture, messaging structure and technology infrastructure have been finalised for the purpose, software development is at an advanced stage.

V.12 Examining the feasibility of international settlements for Indian sovereign debt securities was another planned activity. There has been continuous engagement with the GoI and the major international central security depositories (ICSD), Euroclear and Clearstream, in this regard. A feasible mechanism addressing all concerns is likely to become operational during 2015-16.

Agenda for 2015-16

V.13 The regime for fixing limits for FPI investment in debt securities has undergone changes over the years. The Reserve Bank, in consultation with the GoI, intends to put in place a structured process for fixing these limits along with a framework for periodic reviews. Encouraging retail participation in G-secs continues to engage the Reserve Bank's attention. To enable seamless movement of securities from the subsidiary general ledger (SGL) form to the demat form and *vice versa,* it was announced to provide demat account holders a functionality to put through trades on NDS-OM. An implementation group with representatives from all stakeholders has been set up to roll out the measures by December 2015.

V.14 A deep and liquid corporate bond market has been a shared policy goal of the GoI and financial regulators. Introduction of an electronic platform for facilitating repo in corporate bonds will be considered for implementation. In order to impart liquidity to the options segment in the OTC forex market and attract greater all-round participation, final guidelines allowing exporters and importers to write covered options against their contracted exposures are expected to be issued shortly. Based on the recommendations of the Working Group on interest rate options, the final guidelines will be issued. A framework for assessment of benchmark submission practices by market participants will also be put in place in 2015-16.

FINANCIAL MARKETS OPERATIONS DEPARTMENT (FMOD)

V.15 As part of organisational restructuring, FMOD was created from the erstwhile Financial Markets Department (FMD) on November 3, 2014 by hiving off the surveillance function. With this, FMOD has primarily become an operational department responsible for conducting financial market operations efficiently. The role of FMOD is to facilitate vibrant, efficient and stable financial markets to support a rapidly growing real economy.

Agenda 2014-15: Implementation Status

V.16 FMOD is primarily entrusted with the task of conducting market operations in consonance with the policies of the Reserve Bank. Thus, as in the previous years, maintaining orderly conditions in the forex market through its operations in both spot and forward segments was high on the agenda for 2014-15. Efforts were also directed at maintaining appropriate levels of liquidity in the financial system through liquidity management operations, which include the liquidity adjustment facility (LAF) (fixed/ variable rate repo/reverse repo of various tenors) and overnight marginal standing facility (MSF), other standing facilities and open market operations (OMOs) with a view to ensuring better alignment between money market rates and the policy rate for more efficient transmission of monetary policy signals. Regular analyses and research on developments in financial markets and market operations were also carried out.

V.17 During 2014-15, exchange rate of the rupee exhibited stability, unlike in the previous year when it witnessed intense volatility during July-August 2013 on account of taper tantrums. For better liquidity management, the LAF was revised in September 2014 which entailed more frequent 14-day term repo auctions besides use of variable rate repo/reverse repo auctions of various tenors for fine tuning. These steps helped in reducing volatility in the money market and ensuring closer alignment of the money market rates with the policy rate.

Agenda for 2015-16

V.18 The department aims to continue with its endeavour to carry out liquidity management operations effectively, conduct foreign exchange operations, including interventions, in an effective manner and carry out policy oriented research on financial markets. The department also intends to undertake technological up-gradation to facilitate smoother and more flexible liquidity management operations.

FOREIGN EXCHANGE DEPARTMENT (FED)

V.19 With increasing globalisation, and evolving business practices and models, effective integration of the needs of both residents and non-residents is necessary while meeting the basic objectives of the Foreign Exchange Management Act (FEMA), 1999. Since India is likely to remain a capital deficit country in the near to medium term, the regulatory regime needs to provide a framework which is simple, comprehensive and principle based so as to reduce the regulatory cost and improve the ease of doing business. This has to be implemented within the overarching principle of calibrated progress towards capital account liberalisation within the constraints imposed by macro-prudential stability. Within the Reserve Bank, FED acts as the nodal department for this purpose.

Agenda 2014-15: Implementation Status

V.20 With normalcy returning to the external sector, the Reserve Bank rolled back many of the emergency steps taken in 2013-14 and focussed on ensuring robust and stable capital flows to finance the current account deficit and supplement savings in financing the investment needs of the economy. In 2014-15, efforts were directed at further simplifying the foreign investment regime and making it more user-friendly both for domestic firms and foreign investors. A review of the existing framework of the ECBs was also envisaged.

Easing of FDI and FPI Regimes

V.21 On a review of the policy on eligible instruments for foreign direct investment (FDI) and FPI, partly paid equity shares and warrants issued by an Indian company were allowed to be considered as eligible instruments for the purpose of FDI and FPI schemes. To provide greater freedom and flexibility in the FDI framework, the issue and transfer of shares, including compulsorily convertible preference shares/debentures, with or without optionality clauses (without any assured return), was allowed to be carried out at a price worked out as per the guidelines issued by the Securities and Exchange Board of India (SEBI) in case of listed companies and any internationally accepted pricing methodology in case of unlisted companies on an arm's length basis. Further, Indian companies were permitted to issue equity shares against any funds payable by them, remittances of which did not require prior permission of the government or the Reserve Bank under FEMA, 1999 or any rules/regulations framed or directions issued thereunder.

V.22 AD category-I banks were permitted to allow pledge of equity shares of an Indian company held by non-resident investor/s in accordance with the FDI policy in favour of non-banking financial companies (NBFCs) to secure credit facilities extended to the resident investee company. Following the changes announced by the Government in the FDI policy, regulations were amended to enable foreign investments: (a) up to 49 per cent in the defence sector under the government approval route; and (b) up to 100 per cent in railway infrastructure and manufacturing of medical devices under the automatic route. In addition, FDI in the insurance sector was increased to 49 per cent from the earlier level of 26 per cent.

V.23 A new depository receipts scheme, 2014 was notified by the Reserve Bank on January 22, 2015, under which a person is eligible to issue or transfer eligible securities to a foreign depository for the purpose of converting the securities into depository receipts.

Review of Framework for ECBs

V.24 The scope of ECB was expanded and recognised non-resident lenders were allowed to extend loans in Indian rupees to eligible resident borrowers. The facility, besides providing greater flexibility for structuring of ECB arrangements, shifts the currency risk from borrowers to lenders. For better structuring of the draw-down of ECB proceeds and their subsequent utilisation for permitted end uses, eligible ECB borrowers were allowed to park ECB proceeds in term deposits with AD Category-I banks in India for a maximum period of six months, pending utilisation. The set of eligible securities for raising ECBs was made more broad-based to include movable assets and financial securities in addition to immovable assets.

Simplification of Non-trade Outward Remittances and Travel-related Transactions

V.25 Policies relating to overseas direct investment (ODI) were liberalised with a view to providing flexibility to residents for availing fund based or non-fund based facilities for overseas joint ventures (JVs), wholly owned subsidiaries (WOS) and step down subsidiaries (SDS). This, *inter alia*, included permitting pledging of shares of its overseas SDS and creating a charge on domestic/ foreign assets.

V.26 In view of the resumption of buoyant capital inflows in the recent period and as part of macro-prudential management, the limit under the liberalised remittance scheme (LRS) was enhanced to US$ 2,50,000 per individual per financial year from the existing limit of US$ 1,25,000. Further, to ensure ease of transactions, all the facilities for release of exchange/ remittances for current account transactions available to resident individuals under Schedule III of the Foreign Exchange Management (Current Account Transactions) Rules, 2000, as amended from time to time, were subsumed under this limit.

V.27 To mitigate the hardships faced by people travelling to Nepal and Bhutan, individuals were permitted to carry higher value denomination notes up to a value of ₹25,000. Earlier, individuals travelling to these two countries were allowed to carry Indian currency without any limit in denominations of only up to ₹100.

Export Data Processing and Monitoring System (EDMPS)

V.28 An EDPMS was put in place in March 2014 to bring about efficiency and ease in data reporting as also enabling more effective monitoring of export transactions. EDPMS has a single master database for all export transactions and is shared by all the stake-holders involved (Reserve Bank of India, customs and banks). EDPMS effectively addressed the long standing issue of unmatched export transactions reported by customs but not detected in the banking channel.

International Financial Services Centre (IFSC)

V.29 Regulations were framed in March 2015 to enable functioning of IFSCs under which a financial institution or a branch of a financial institution will be treated as a person resident outside India and its transactions with a person resident in India will be treated as those between a non-resident and a resident and subject to the provisions of FEMA, 1999.

Rupee Denominated Overseas Bonds

V.30 A few international institutions were permitted since 2013 to issue rupee bonds in overseas markets, which elicited a positive response. In the monetary policy statement of April 2015, the Reserve Bank, in consultation with the GoI, decided to permit Indian corporates eligible to raise ECBs to issue rupee denominated bonds overseas. The draft framework on overseas issuance of rupee linked bonds by multilateral financial institutions and eligible borrowers was placed in the public domain and the policy in this regard is likely to be finalised soon.

Agenda for 2015-16

V.31 Considering the progress that the country has made in foreign exchange management and to facilitate the ease of doing business, there is a need for aligning the regulations issued under FEMA, 1999 with evolving business models and practices. Accordingly, the Reserve Bank proposes to (i) complete the task of rationalising and simplifying the notifications issued under FEMA, which commenced last year; (ii) issue master regulations covering all instructions on a subject in a more user friendly format; and (iii) rationalise the returns submitted to it in order to reduce the regulatory load on users of foreign exchange. The task of simplifying the ECB guidelines is an ongoing process and the Reserve Bank will also take into account the recommendations of the Committee to Review the Framework of Access to Domestic and Overseas Capital Markets (Phase II, Part II: Foreign Currency Borrowing, Report III; Chairman: Shri M.S. Sahoo). Encouraged by the stabilisation of EDPMS, the Reserve Bank will initiate work on installing an import data processing and monitoring system (IDPMS) in coordination with the government agencies.

VI REGULATION, SUPERVISION AND FINANCIAL STABILITY

Following the economic slowdown and sector-specific factors, the banking sector has been beset with the problem of deteriorating asset quality. In response, the Reserve Bank focused on strengthening the regulatory and supervisory framework to identify stress at the incipient stage and initiate corrective action. Alongside, the Reserve Bank sought to infuse competition in the banking sector by allowing new private sector banks and differentiated banks. Asset reconstruction companies were also encouraged for recovery management. Simultaneously, focus was placed on aligning the regulatory framework for NBFCs and UCBs with the rest of the banking sector. In pursuance of customer protection, the Reserve Bank released the Charter of Customer Rights, enunciating five basic rights for bank customers.

VI.1 The year under review was marked by rising financial stability risks worldwide - uncertainty surrounding the normalisation of monetary policy in the US and market reactions to incoming data that prompted risk-on risk-off switches in sentiment, asset prices and capital flows around its timing; highly accommodative monetary policies in the euro area and Japan with large swings in financial asset prices; and financial rebalancing and managing domestic vulnerabilities in emerging market economies, higher corporate indebtedness and growing exposure to market and liquidity risks. Against this backdrop, safeguarding financial stability through well-designed macro-prudential measures addressing both banking and non-banking constituents of the financial system assumed critical importance.

VI.2 With asset quality and profitability of banks coming under stress due to a combination of global and domestic developments, the Reserve Bank's focus during 2014-15 was on strengthening the regulatory and supervisory frameworks by aligning them with Basel III norms and also with those established by other international standard setting bodies.

VI.3 The regulatory and supervisory regime for non-banking financial companies (NBFCs) and urban cooperative banks (UCBs) was also fortified by aligning it with that of the banking system while promoting technological upgradation and sharing credit histories of borrowers. The banking structure itself was sought to be strengthened by infusion of new entrants, including in niche domains, such as small finance and payments banks and by extending the reach of the payment system infrastructure by bringing into its fold non-bank authorised entities. The Reserve Bank also signed memoranda of understandings (MoUs)/ exchange of letters/ statements of cooperation with a host of supervisors of other countries to promote greater cooperation and sharing of supervisory information relating to Indian banks with overseas operations and foreign banks operating in India.

VI.4 A critical area in the banking space that warranted prioritised attention was the mounting overhang of stressed assets. Besides mechanisms for early corrective actions, a multi-pronged strategy was adopted comprising higher provisioning against restructured assets, recovery management through asset reconstruction companies and strategic debt restructuring.

VI.5 Towards this end, various departments of the Reserve Bank dealing with the regulation and supervision of financial intermediaries as also customer interest set out for themselves an agenda of work plans in 2014-15. The following paragraphs outline the activities undertaken by them, the challenges faced and the way forward for 2015-16.

FINANCIAL STABILITY UNIT (FSU)

VI.6 In the aftermath of the global financial crisis, maintaining financial stability has emerged as a prime responsibility of central banks. FSU of the Reserve Bank was set up in July 2009 to monitor stability related matters with the objective of strengthening the financial system. This is envisaged to be achieved by conducting macro-prudential surveillance on an on-going basis, systemic stress tests and dissemination of the status of financial stability in addition to supporting the institutional mechanism for financial stability in the country, *viz.,* Financial Stability and Development Council (FSDC).

Agenda for 2014-15: Implementation Status

VI.7 As planned for 2014-15, two Financial Stability Reports (FSRs) were published - one in December 2014 and the other in June 2015. It is the endeavour of the Reserve Bank to bring about improvements to its stress testing framework. Accordingly, refinements were made to the macro stress testing methodology with respect to the variables used (*e.g.,* using the consumer price index (CPI) instead of the wholesale price index (WPI), and weighted average lending rate in place of call rate). In addition, FSU collaborated with the International Monetary Fund (IMF) in the areas of modelling risk weighted asset (RWA) dynamics and modelling corporate sector distress and its impact on the banking sector in order to make further refinements in the stress testing framework as also to develop new predictive models. Analyses of power and iron and steel industries, with emphasis on stressed assets were undertaken. Further, their impact on the banking sector was assessed to gauge the resilience of the banking system.

VI.8 As the secretariat to the sub-committee of FSDC, FSU conducted three meetings of the sub-committee during 2014-15. The sub-committee's recommendation for putting in place an enabling framework for creating an 'account aggregation' facility for customers to view all their financial assets through a single window, is being worked out. Based on the discussions in the sub-committee, the Central Registry of Securitisation, Asset Reconstruction and Security Interest of India (CERSAI) will be acting as the central know your customer (KYC) registry to ensure both uniformity in the approach to KYC and its inter-usability across the financial sector.

VI.9 Drawing on the sub-committee's recommendations, various steps have been taken to strengthen State Level Coordination Committees (SLCCs) to make them more effective in the dissemination of market intelligence on unauthorised deposit taking schemes. Enactment of the Protection of Interests of Depositors' (PID) Act has been undertaken across a number of states/ union territories.

VI.10 Based on the sub-committee's direction to capture information on lending by insurance companies to corporates, insurance companies were advised to subscribe to the Central Repository of Information on Large Credits (CRILC), a repository of information on large credits set up by the Reserve Bank.

VI.11 Further, FSU also serves as the secretariat for the inter-regulatory technical group (IRTG), a sub-group of the FSDC sub-committee and in this capacity it conducted four meetings during 2014-15, in which issues such as legal entity identifier (LEI), reporting of lending against shares by NBFCs, account aggregation and common KYC, among others, were discussed. The IRTG has advised all regulators to draw a road map to mandate use of LEI by entities identified in their jurisdiction.

Agenda for 2015-16

VI.12 Going ahead, conducting macro-prudential surveillance and publishing FSR in December 2015 and June 2016 are envisaged along with conducting meetings of the FSDC sub-committee. FSU will continue to undertake analyses of some of the critical industrial sectors. In addition, it is also proposed to collaborate with international agencies/ other central banks to review the tools and techniques used for conducting stress tests.

REGULATION OF FINANCIAL INTERMEDIARIES

Commercial Banks: Department of Banking Regulation (DBR)

VI.13 On the banking regulation front, the Reserve Bank strives to ensure a robust and resilient banking system in line with the best international practices capable of catering to the financial and associated needs of all sections of society efficiently and effectively. Accordingly, the department initiated a number of measures in 2014-15 for strengthening the banking structure.

Agenda for 2014-15: Implementation Status

Basel III Liquidity Standards

VI.14 During 2014-15, significant progress was made towards implementation of the two Basel III Liquidity Ratios - liquidity coverage ratio (LCR) which is set to impart resilience in the short term liquidity risk profile of banks, and the net stable funding ratio (NSFR) that seeks to limit over-reliance on short-term wholesale funding. While LCR was phased in for Indian banks with a minimum requirement of 60 per cent from January 1, 2015, NSFR is set to be implemented at the minimum requirement of 100 per cent from January 1, 2018.

Basel III Leverage Ratio (LR)

VI.15 In line with the Basel Committee on Banking Supervision (BCBS), the Reserve Bank issued a revised framework for LR in January 2015 as a credible supplement to risk-based capital requirements. While the final minimum LR for Indian banks will be stipulated in line with the final rules to be prescribed by BCBS by end-2017, the Reserve Bank will meanwhile monitor individual banks against an indicative LR of 4.5 per cent as part of a parallel run and also for the purpose of public disclosure of Tier 1 LR by banks.

Countercyclical Capital Buffer (CCCB) Framework

VI.16 Guidelines on implementation of CCCB in India have been issued covering aspects, such as constituents of CCCB, main and supplementary indicators to decide CCCB activation and calibration of CCCB based on indicators. Implementation of this buffer requirement will be pre-announced with a lead time of four quarters so as to provide sufficient time to meet CCCB requirements.

Framework for Dealing with Domestic Systemically Important Banks (D-SIBs)

VI.17 In line with the global practice of identifying global systemically important banks (G-SIBs), the Reserve Bank has released the framework for dealing with D-SIBs, which discusses the methodology for identifying D-SIBs and additional regulatory/ supervisory policies for them. The names of banks classified as D-SIBs will be disclosed in August every year starting from 2015.

Large Exposures Framework

VI.18 The danger of concentration of a bank's assets with a single counterparty or a group of connected counterparties poses a systemic risk. Accordingly, the Reserve Bank has proposed a regulatory framework in line with international best practices to address the concerns arising from large exposures of banks and to prevent building up of concentrated exposures (Box VI.1).

Partial Credit Enhancement on Corporate Bonds

VI.19 During 2014-15, ways to incentivise corporates to reduce dependence on bank finance for their long-term resource requirements were explored. Pursuant to this, draft guidelines were issued to banks to provide partial credit enhancement to corporate bonds. The final guidelines in this regard are underway.

Revitalising Stressed Assets

VI.20 Towards greater alignment of prudential norms on project finance with international best practices, banks were allowed to extend structured

Box VI.1
Discussion Paper on Large Exposures (LE) Framework and Enhancing Credit Supply through the Market Mechanism

Internationally, concentration risk has been addressed by prescribing regulatory and statutory limits on exposures towards counterparties and various sectors of the economy. Since 1989, the Reserve Bank has been prescribing regulatory limits on a bank's exposures to its single and group borrowers. At present, the exposure limits stand at 15 per cent and 40 per cent of capital funds (CFs), respectively. On account of exposures towards infrastructure sector and further on the special discretion of the board of a bank, these exposure limits can be taken up to 25 per cent and 55 per cent of its CFs, respectively. Besides, there are certain other specific counterparty, sectoral and activity-based exposure limits (Table 1).

In order to ensure regulatory convergence in the area of large exposures internationally, the Basel Committee on Banking Supervision (BCBS) issued the 'Supervisory Framework for Measuring and Controlling Large Exposures' in April 2014 that will be fully applicable from January 1, 2019. Accordingly, the sum of all the exposure values of a bank to a single counterparty or to a group of connected counterparties must, at all times, not be higher than 25 per cent of the bank's available eligible capital base, *i.e*, the effective amount of Tier 1 capital fulfilling the criteria defined in the Basel III capital framework.

The Reserve Bank has sought to align exposure limits (both single and group) in India with the BCBS LE framework. In this context, a discussion paper on the proposed LE framework was issued on March 27, 2015. The discussion paper also contained proposals on enhancing credit supply to large corporates through the market mechanism (corporate bonds, commercial papers and other instruments).

Table 1: Major Exposure Limits

Specific Counterparty/ Sector/ Activity	Regulatory Exposure Limits
NBFCs predominantly engaged in loan against gold jewellery	7.5 per cent of CFs; can exceed by 5 per cent of CF for infrastructure
Other NBFCs (excluding AFCs/ IFCs)	10 per cent of CFs; can exceed by 5 per cent of CF for infrastructure
Direct Capital Market Exposures	20 per cent of net worth
Total Capital Market Exposures	40 per cent of net worth
Borrowing from the Call Money Market	100 per cent of CFs on a fortnightly average basis; can increase up to 125 per cent of CF on any day
Lending to the Call Money Market	25 per cent of CFs on a fortnightly average basis; can increase up to 50 per cent of CF on any day
Inter-Bank Liabilities	200 per cent of net worth as on 31 March of the previous year; can increase up to 300 per cent of the net worth for banks having minimum CRAR of 11.25 per cent
Investment in instruments issued by other banks/ FIs and eligible for capital status for the issuing bank/ FI	10 per cent of CF*
Investments in equity shares of other banks	5 per cent of the investee bank's equity capital*
Leasing, Hire Purchase and Factoring Services	10 per cent of total advances of a bank for each of such activities

*: A bank/ FI's equity holdings in another bank held under provisions of a statute will be outside the purview of the ceiling prescribed.
AFCs: Asset Finance Companies; IFCs: Infrastructure Finance Companies; CRAR: Capital to Risk-Weighted Assets Ratio; FIs: Financial Institutions.

(Contd....)

Under the proposed LE framework, a large exposure is one where the sum of all exposure values of a bank to a counterparty or a group of connected counterparties, is equal to or above 10 per cent of the bank's eligible capital base. Further, exposures to the central government, the Reserve Bank, intra-day inter-bank exposures, intra-group exposures and clearing exposures of qualified central counterparties are exempt from the LE limit. The LE Framework also prescribes differential exposure limits for certain counterparties, such as non-banking financial companies (NBFCs) and systemically important banks (SIBs), both global and domestic (G-SIBs and D-SIBs). Connected counterparties are proposed to be identified on the basis of 'control' as well as 'economic interdependence' criteria as against only the 'control' criteria under the extant exposure norms.

Computation of exposures under the LE framework will be permitted after taking into account credit risk mitigation adjustment based on risk-based capital framework techniques. Under the framework, banks may also be required to use 'look through approach' for assigning exposures to the underlying counterparties in structured products.

An internal study of the 20 largest group borrower exposures of the 10 largest banks has revealed that average exposure to groups of connected counterparties is 10.6 per cent of their CF as against the current permissible limit of 40 per cent of CF. In terms of Tier 1 capital, the present average exposure is 14.75 per cent as against the proposed LE limit of 25 per cent. Therefore, it is assumed that banks will not face any material difficulty with regard to their group exposures while adhering to the proposed LE limit.

long-term project loans with tenors up to 80 per cent of the initial economic life of a project, with a periodic refinancing option to avoid asset liability mismatch, fund cost over-runs up to a limit and extend the date of commencement of commercial operations (DCCO) subsequent to the change in ownership of the borrowing entity. These measures are expected to further strengthen banks' abilities to deal with complexities in project finance.

Strategic Debt Restructuring (SDR)

VI.21 With a view to enhancing banks' capabilities to initiate change in ownership for accounts which fail to achieve the projected viability milestones under a restructuring package, the Reserve Bank introduced a SDR scheme in June 2015. Under SDR, secured creditors of a Joint Lenders' Forum (JLF) can convert their loan dues into equity shares at a 'fair price' as per the pricing formula prescribed by the Reserve Bank, which has been exempted from the SEBI's ICDR (Issue of Capital and Disclosure Requirements) Regulations, 2009 subject to certain conditions. Lenders under JLF should collectively become majority shareholders post conversion. SDR will not be treated as restructuring for the purpose of asset classification and provisioning. JLF can appoint a suitable professional management to run the affairs of the company and should divest its holdings at the earliest. In this regard, the proposal of a comprehensive Bankruptcy Code in the Union Budget, 2015-16 is expected to bring about speed, clarity, predictability and fairness to the restructuring and recovery process (Box VI.2).

Treatment of Wilful Defaulters and Non-Cooperative Borrowers (NCBs)

VI.22 Regulations governing treatment of wilful defaulters and NCBs having aggregate fund-based and non-fund based facilities of ₹50 million from a bank/ financial institution (FI) were strengthened during 2014-15 and banks/ FIs were mandated to put in place transparent mechanisms for identifying NCBs as also for reporting.

Two New Entrants in the Banking Domain

VI.23 In its endeavour to foster healthy competition, the Reserve Bank laid out a framework for licensing new banks in the private sector in February 2013. Accordingly, in-principle approval was granted in April 2014 to IDFC Limited, an NBFC, and Bandhan Financial Services Private Limited, an NBFC-MFI (micro-finance institution) to set up banks. In June-July

Box VI.2
Bankruptcy Procedures in India

Stronger bankruptcy laws enable a sound debtor-creditor relationship by protecting the rights of both debtors and creditors; promoting predictability; clarifying the risks associated with lending; and ensuring efficient collection of debt through bankruptcy proceedings. The Union Budget 2015-16 identified bankruptcy law reforms as a key priority and proposed a comprehensive Bankruptcy Code in line with global standards to provide for necessary judicial capacity. It is envisaged to bring about legal certainty, speed and also improve the ease of doing business.

At present, there is no comprehensive policy/ law on corporate bankruptcy in India. The Sick Industrial Companies (Special Provisions) Act (SICA), 1985 remains to date the most important corporate restructuring law in force for revival and rehabilitation of sick companies, despite its well-recognised drawbacks. Other legislative attempts to overhaul the corporate rescue regime in India have not yet been made operational. For instance, Chapter XIX of the Companies Act, 2013 that provides for a broader, more balanced corporate rescue procedure applicable to all companies has not been notified for commencement. Similarly, Chapter VIA of the Companies Act, 1956, inserted by the Companies (Second Amendment) Act, 2002, which provides for the National Company Law Tribunal (NCLT) to exercise powers in relation to sick industrial companies remains to be notified.

With a view to overcoming the existing inadequacies, the Bankruptcy Law Reform Committee (BLRC) (Chairman: Shri TK Vishwanathan) was established in August 2014 and entrusted with the task of examining the present legal framework for corporate insolvency and suggesting immediate reforms; and developing an 'Insolvency Code' for India covering all aspects of personal and business insolvency. Salient recommendations of the BLRC made in line with international best practices are:

- A secured creditor can initiate rescue proceedings if the debtor company fails to pay a single undisputed debt above a prescribed value within 30 days of a notice of demand; or pre-emptively on the grounds of likelihood of inability to pay debt.
- Unsecured creditors representing 25 per cent of the debt can initiate rescue proceedings against the debtor company.
- Once a company has been declared sick, 75 per cent of the secured creditors in value should be able to appoint a company administrator directly.
- Amendment to the Companies Act, 2013 so that at the time of sanctioning a scheme of revival creditors within the same class are treated equally; and dissenting creditors receive as much as they would in liquidation.
- An administrative mechanism for resolving financial distress of viable MSMEs through 'Committees for Distressed Micro, Small and Medium Enterprises' to be established by banks by amending the Micro, Small and Medium Enterprises Development Act, 2006.
- Bankruptcy codes in the US and the UK provide for an automatic/ interim moratorium on the enforcement of claims upon filing for bankruptcy. However, in view of problems with an automatic moratorium under SICA, it is proposed to retain the present provisions in the Companies Act, 2013, while stipulating clear principles regarding exercise of discretion by NCLT on grant of moratorium or not.

BLRC has provided a comprehensive and improvised framework for strengthening the bankruptcy procedures in India. This will result in considerable improvement in the credit climate in the country.

Reference:

Government of India (2015), 'Interim Report of The Bankruptcy Law Reform Committee', Ministry of Finance.

2015, Bandhan Bank Limited and IDFC Bank Limited were granted license to carry out the banking business in India.

Licensing of Differentiated Banks

VI.24 Guidelines on 'Payments Banks' and 'Small Finance Banks' were issued on November 27, 2014. These banks are 'niche' or 'differentiated' banks with the common objective of furthering financial inclusion. The Reserve Bank received 72 and 41 applications for small finance banks and payments banks respectively; these are under review. So far, 11 applicants have been granted in-principle approval to set up payments banks.

New Banking Structure to Facilitate International Financial Services Centres (IFSCs)

VI.25 Pursuant to the announcement of Government of India on setting up of an IFSC in Gujarat International Finance Tech-City (GIFT), the Reserve Bank has formulated a scheme for setting up of IFSC banking units (IBUs). This scheme will provide the financial services entities in GIFT as well as other future IFSCs with a sound supporting regulatory framework. The IBUs are expected to offer financial services to non-residents as also to residents subject to the provisions of Foreign Exchange Management Act (FEMA), 1999.

Corporate Governance

VI.26 In pursuance of the recommendations of the Committee to Review Governance of Boards of Banks in India (Chairman: Dr P. J. Nayak), set up by the Reserve Bank, guidelines were issued to banks on: fixing of upper age limit for whole time directors of private sector banks; replacing the calendar of reviews with seven key themes; and compensation for non-executive directors of private sector banks. Further, the post of chairman and managing director (CMD) has been split into an executive managing director (MD) and a non-executive chairman. The revamped process for appointment of non-executive chairmen on the boards of public sector banks (PSBs) has been initiated by the government.

KYC Norms Simplified

VI.27 KYC guidelines were revised in April 2014 to ease difficulties in opening and operating bank accounts. Accordingly, the physical presence of a customer categorised as 'low risk' is not mandatory at the time of KYC updation. Fresh proof of identity and address is not required for 'low risk' customers for updation in case of unaltered status. Self-certification of proof is allowed and banks can accept a certified copy by mail/ post; and no fresh documents are required if an existing KYC compliant customer desires to open another account in the same bank. Banks can now rely on third party due diligence at the time of account opening, provided the third party is regulated and supervised and has adequate measures in place for compliance with client due diligence.

Partial Freezing of Accounts in Case of KYC Non-Compliance

VI.28 In case of non-compliance of KYC requirements despite repeated reminders, banks should impose 'partial freezing' of such accounts in a phased manner to mitigate the threat of money laundering and financing of terrorism. If the account is still KYC non-compliant after six months of 'partial freezing', banks may render it inoperative. The account can be revived on submission of KYC documents.

Deposit Callability, Sole Criteria for Differential Rates

VI.29 Effective April 16, 2015, banks are allowed to offer differential rates of interest on term deposits on the basis of tenor and premature-withdrawal facility for deposits of less than ₹10 million and on the basis of quantum, tenor and premature-withdrawal facility for deposits of ₹10 million and above, subject to certain conditions. However, all term deposits of individuals (held singly or jointly) of ₹1.5 million and below should, necessarily have premature withdrawal facility.

Rationalisation of Penal Charges

VI.30 From April 1, 2015, banks are required to notify a customer by SMS/ email/ letter before applying penal charges for non-maintenance of minimum balance in the inoperative savings account. Furthermore, penal charges have to be directly proportional to the extent of shortfall observed and levied after one month from the date of notice to a customer.

Distribution of Insurance Products

VI.31 Detailed customer protection guidelines were issued to banks conducting insurance distribution activities, *e.g.,* ensuring customer suitability while selling an insurance product only when the customer volunteers to purchase it, prohibiting payment of commission/ incentive directly to the staff, transparency in disclosure of brokerage/ fee earned from the insurer, adherence to KYC guidelines and requirement of having a robust grievance redressal mechanism.

Agenda for 2015-16

VI.32 In continuation of the stance that guided regulatory actions in 2014-15, it is proposed to implement the final framework for the LE regime and for NSFR in the ensuing year. Besides, the Reserve Bank will be issuing draft guidelines for consultation on counterparty credit risk exposures, Pillar 3 disclosures and the securitisation framework. These regulations will reflect the revised BCBS norms in the respective areas.

VI.33 The Reserve Bank will also be initiating suitable measures towards convergence of accounting standards with the International Financial Reporting Standards (IFRS). In-principle approvals will be issued to suitable applicants for setting up of Small Finance Banks/ Payments Banks while the regulatory framework for them will be formulated. On the future of local area banks (LABs), a consultation process will be initiated while draft guidelines for on tap licensing of universal banks will be framed.

VI.34 Implementation of certain major recommendations of the Nayak Committee regarding governance reforms in PSBs, including remuneration and professionalisation of the boards will be taken forward. For more effective monetary transmission, banks will be encouraged to move in a time-bound manner to a marginal cost of funds-based determination of their base rates. It is further proposed to examine the current framework on presence of foreign banks in India in line with emerging international developments as well as the experience gained so far. To add additional clarity, frequently asked questions (FAQs) will be issued on various aspects of the wholly owned subsidiary framework issued in November 2013. Guidelines will also be framed on ownership in private sector banks which will include raising the ceiling on voting rights from 10 to 15 per cent.

Cooperative Banks: Department of Cooperative Bank Regulation (DCBR)

VI.35 As UCBs play an important role in the Indian financial system, the Reserve Bank has always endeavoured to strengthen the regulatory and supervisory framework so that they emerge financially strong and have sound governance. DCBR plays the lead role in framing regulations for UCBs apart from State Cooperative Banks (StCBs) and District Central Cooperative Banks (DCCBs).

Agenda for 2014-15: Implementation Status

VI.36 The agenda of DCBR for 2014-15 focused on putting in place a revised supervisory action framework, pursuing legal/ regulatory amendments to facilitate conversion of UCBs into commercial banks and also to facilitate takeover of assets and liabilities of UCBs by commercial banks. Accordingly, a revised supervisory action framework was put in place in 2014-15. As regards legal amendments to facilitate conversion of UCBs into commercial banks, while the Companies Act, 2013 has enabling provisions there is need for corresponding provisions in the Multi State Cooperative Societies Act, which have been taken up with the government. With regard to commercial banks taking over assets and liabilities of UCBs, necessary tweaking of the regulations was accomplished during the year. This enables commercial banks to complete the effort on a fair price basis. The other important achievements during the year were:

Reserve Requirements

VI.37 Cash reserve ratio (CRR) requirements for non-scheduled UCBs and statutory liquidity ratio (SLR) requirements for all UCBs have been aligned with those of commercial banks following the Banking Laws (Amendment) Act, 2012 coming into force. Accordingly, UCBs were required to comply with the stipulated SLR by March 31, 2015. Balances with StCBs/ DCCBs and term deposits with PSBs are not eligible to be reckoned for SLR with effect from April 1, 2015. StCBs and DCCBs were also required to maintain SLR only in the form of approved securities from April 1, 2015. On a review, they have been allowed to shift their SLR term deposits to approved securities in phases by March 31, 2017.

Liquidity Adjustment Facility (LAF) Extended to Scheduled UCBs

VI.38 With a view to providing an additional avenue for liquidity management, LAF has been extended from November 28, 2014 to scheduled UCBs that are core banking solution (CBS)-enabled, have capital to risk-weighted assets ratio (CRAR) of at least 9 per cent and are fully compliant with the eligibility criteria prescribed for LAF.

Technology Adoption

VI.39 In order to integrate with the financial system and to improve regulatory reporting, UCBs were advised to implement CBS by December 31, 2014. At end-June 2015, 1,040 of the 1,577 UCBs had implemented CBS. Implementation of CBS has been prescribed as an additional criterion for being considered as financially sound and well managed (FSWM) bank, a criterion applied for extending various regulatory approvals to UCBs, including opening new branches. In order to bring in transparency and objectivity, 'regulatory comfort', an important aspect considered for classifying a bank as FSWM, has been redefined to include compliance with standard regulatory provisions during the last two financial years.

VI.40 FSWM UCBs are allowed to offer internet banking (view only) facilities to their customers provided they have migrated to the Internet Protocol Version 6 (IPv6). They can also open on-site/ off-site/ mobile automated teller machines (ATMs) without prior approval of the Reserve Bank provided they have a minimum net worth of ₹0.5 billion.

VI.41 Similarly, with a view to providing greater freedom to StCBs to expand their business and to provide technology-enabled services to their customers, StCBs can also open off-site/ mobile ATMs without prior approval of the Reserve Bank subject to certain prescribed criteria. These initiatives are aimed at bringing cooperative banks on par with commercial banks.

Supervisory Action Framework for UCBs

VI.42 As indicated in the last Annual Report, trigger points necessitating supervisory/ regulatory action have been revised for UCBs for early identification of stress and its rectification. UCBs are required to go for corrective action if the gross non-performing assets (NPAs) to advances ratio exceeds 10 per cent or they experience an incremental gross NPA ratio of 3 percentage points each during the last two consecutive years, whichever is earlier. Other triggers for corrective actions include regulatory capital falling below 9 per cent, incurring losses for two consecutive years and the credit deposit ratio exceeding 70 per cent.

VI.43 UCBs have been advised to constitute special committee of the board for monitoring and following up cases of frauds involving amounts of ₹10 million and above exclusively. The Audit Committee of Board (ACB) will continue to monitor all the cases of frauds, in general. UCBs have also been advised to become members of all the four credit information companies (CICs), and furnish historical data to them with a view to enhancing accuracy of the credit information.

Agenda for 2015-16

VI.44 A High Powered Committee for UCBs (Chairman: Shri R Gandhi) constituted, *inter alia,* to examine and recommend an appropriate set of businesses, size, conversion and licensing terms for UCBs has since submitted its report. The recommendations of the committee will be considered for implementation during the year. The Reserve Bank will also initiate measures to improve the quality of statutory audits in UCBs during the year. The process of harmonisation of regulation of UCBs and Rural Cooperative Banks will be continued.

NBFCs: Department of Non-Banking Regulation (DNBR)

VI.45 The regulation of the NBFC sector is guided by the need to foster additional credit delivery channels while preserving financial stability. DNBR which was carved out of the erstwhile Department of Non-Banking Supervision (DNBS) is the nodal department for regulation of NBFCs, including stand-alone primary dealers (PDs). Keeping in view the role of shadow banking activities in intensifying the global financial crisis as also the rising role of NBFCs domestically, the Reserve Bank's focus during 2014-15 was on addressing gaps in regulation of NBFCs and harmonising regulations to enable delivery of innovation and last mile connectivity in credit. Further, in the light of significant progress made by NBFC-MFIs following the crisis in then Andhra Pradesh in 2008-09, a comprehensive review of their regulation was also completed during the year.

Agenda for 2014-15: Implementation Status

Review of the Regulatory Framework for NBFCs

VI.46 The NBFC sector has evolved considerably in terms of its size, operations, technological sophistication and entry into newer areas of financial services and products. Accordingly, the entire regulatory framework for the sector was reviewed with a view to transitioning, over time, to an activity-based regulation of NBFCs while ensuring that NBFCs having lower risk profiles will be lightly regulated (Box VI.3).

Aligning NBFC Regulation

VI.47 Aligning regulation of the non-banking financial sector with that of the banking sector not only fosters competition but also helps lower regulatory arbitrage and contain a possible build-up of systemic risks outside the banking system. Accordingly, a number of regulatory initiatives were undertaken covering lending by NBFCs against shares, restructuring of advances, structuring of long term project loans to infrastructure and core industries, levy of foreclosure charges and private placement of non-convertible debentures.

*Shadow Banking Implementation Group (*SBIG*)*

VI.48 In line with the Financial Stability Board's (FSB) approach to shadow banking activities, a preliminary inter-regulatory study was conducted to identify the nature of non-bank credit intermediation in India. Accordingly, a SBIG has been formed to assess the level of regulatory compliance *vis-a-vis* FSB guidelines and recommend possible approaches for implementation of reforms. SBIG is expected to submit its report shortly.

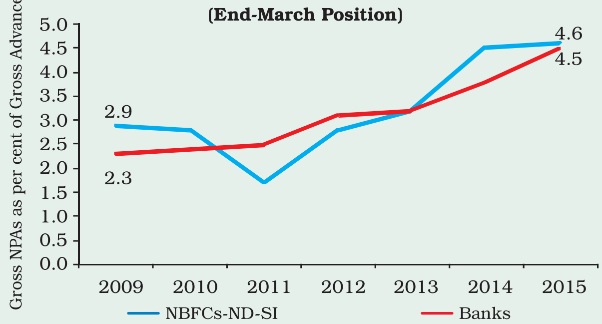
Box VI.3
Asset Quality of NBFCs and Revised Guidelines

In recent years, asset quality of the systemically important non-deposit taking NBFCs (NBFCs-ND-SI) has gone through the vicissitudes of overall deterioration spreading across the financial system as the economy slowed. Their gross NPAs as per cent of credit deployed rose to 4.6 per cent by end-March 2015 (Chart 1).

With a view to strengthening the early warning system for recognising incipient financial stress, NBFCs were directed in March 2014 to create a sub-asset category 'Special Mention Accounts' (SMAs). They were also directed to report relevant credit information to the Central Repository of Information on Large Credits (CRILC).The scheme for encouraging banks to extend long-term loans (known as the 5/ 25 structure) to infrastructure with a flexible structuring/ tenure to absorb potential adverse contingencies has also been extended to NBFCs from January 2015.

The revised regulatory framework for NBFCs issued in November 2014 aligns NPA norms for NBFCs with that of banks in a phased manner. Accordingly, the time limit for classifying a loan account as NPA will be progressively reduced to 90 days by March 2018. Furthermore, to bring parity in the regulation of NBFCs with other financial institutions (FIs) in matters relating to recovery of bad loans, NBFCs registered with the Reserve Bank and having asset size of ₹5 billion and above will be considered for notification as FIs in terms of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act, 2002.

Chart 1:Trend in Gross NPAs (End-March Position)



Source: Report on Trend and Progress of Banking in India, and Financial Stability Report, various issues.

Other key changes to the regulatory framework include:

- All existing NBFCs (those registered prior to April 1999) need to attain net owned funds (NOFs) of minimum ₹20 million in a phased manner by end-March 2017, with failure resulting in cancellation of their Certificates of Registration.
- Only NBFCs with the minimum investment grade credit rating can accept deposits. Existing unrated Asset Finance Companies (AFCs) need to be rated by end-March 2016. Further, the limit for acceptance of deposits has been harmonised to 1.5 times the NOF across all deposit-taking NBFCs (NBFCs-D).
- The threshold for defining systemic significance for non-deposit taking NBFCs (NBFCs-ND-SI) has been revised to ₹5 billion.
- NBFCs-NDs have been exempted from the requirement of CRAR and credit concentration norms.
- Tighter prudential norms have been prescribed for NBFCs-ND-SI and all NBFCs-D in a phased manner - minimum Tier 1 capital requirement to be increased from 7.5 to 10 per cent (by end-March 2017), provision for standard assets to be increased to 0.4 per cent (by end-March 2018) and dispensation of 5 per cent given to AFCs from the prescribed credit concentration norms have been done away with.

Additional corporate governance standards and disclosure norms for NBFCs have been issued to all NBFCs-D and those NBFCs-ND-SI with an asset size over ₹5 billion. Accordingly, these NBFCs need to create various committees for audit, risk management and for nomination of directors based on fit and proper criteria. They also need to frame internal board-approved corporate governance guidelines and make them public on their websites.

References:

Reserve Bank of India (2014), 'Early Recognition of Financial Distress, Prompt Steps for Resolution and Fair Recovery for Lenders: Framework for Revitalising Distressed Assets in the Economy', March.

——— (2014), 'Revised Regulatory Framework for NBFCs', November.

———(2015), 'Flexible Structuring of Long Term Project Loans to Infrastructure and Core Industries', January.

MUDRA Limited

VI.49 In line with the announcement in Union Budget, 2015-16, a Micro Units Development Refinance Agency (MUDRA) Ltd. was established on March 18, 2015 for regulating and refinancing MFIs (Box VI.4).

Box VI.4
Micro Units Development Refinance Agency (MUDRA) Ltd.

Union Budget, 2015-16 announced the establishment of MUDRA Ltd. that will be responsible for both regulating and refinancing all micro-finance institutions (MFIs) which are in the business of lending to micro/ small business entities engaged in manufacturing, trading and service activities and also partner with state level/ regional level coordinators to provide finance to last mile financers of small/ micro business enterprises. The government will allocate a sum of ₹200 billion to MUDRA from the shortfall in priority sector lending for creating a refinance fund to provide refinance to last mile financers. Another ₹300 billion will be provided to MUDRA from the Budget to create a credit guarantee corpus for guaranteeing loans provided to micro-enterprises.

Appropriate legislation is being drafted by the central government for setting up MUDRA. Pending legislative approval, MUDRA Ltd. was incorporated on March 18, 2015, under the Companies Act, 2013, as a wholly owned subsidiary of the Small Industries Development Bank of India (SIDBI) to carry out activities relating to development and financing of small micro-enterprises, and was registered with the Reserve Bank as a non-deposit taking NBFC on April 6, 2015. SIDBI has been exempted for its proposed investment of ₹7.5 billion in MUDRA from the cross-holding of capital among banks/ FIs.

Agenda for 2015-16

VI.50 The process of regulatory convergence between banks and non-banks will be taken forward in 2015-16. Further, activity based regulation is envisaged for the sector, thereby doing away with multiple categories of NBFCs. As a first step, NBFCs are being progressively classified into two broad heads - core investment companies and non - core investment companies. In addition, government owned NBFCs are being brought in within the regulatory ambit of the Reserve Bank.

SUPERVISION OF FINANCIAL INTERMEDIARIES

Commercial Banks: Department of Banking Supervision (DBS)

VI.51 DBS is entrusted with the supervisory responsibility of commercial banks, and aims at designing and implementing policies and strategies for supervision to develop a safe and efficient banking system. In this endeavour, managerial practices in banks and All India Financial Institutions (AIFIs) that strengthen their corporate governance and internal controls are also encouraged. DBS also functions as the secretariat to the Inter Regulatory Forum set up under the aegis of the sub-committee of FSDC for oversight of identified financial conglomerates (FCs) in coordination with other domestic regulators.

Agenda for 2014-15: Implementation Status

Risk Based Supervision (RBS) and Capacity Building

VI.52 The Reserve Bank is moving progressively from a performance based CAMELS (capital adequacy, asset quality, management, earning, liquidity and system and control) framework to a forward looking RBS framework for early detection of risks, timely and appropriate supervisory interventions and more generally for improving the quality of supervisory processes in line with global best practices. Two more banks were brought under RBS in 2014-15, taking the total to 30 major banks. Six more banks have been migrated to RBS framework from 2015-16 assessment cycle. The RBS model was also optimised, fine-tuning data collection from commercial banks. The need for preparedness at the banks' level, including a robust management information system for RBS was highlighted.

Oversight of Financial Conglomerates (FCs)

VI.53 The Reserve Bank, in coordination with other domestic regulators, concluded discussion meetings with two bank-led FCs and participated in a discussion meeting of one insurance company-led FC organised by Insurance Regulatory Development Authority (IRDA), to review group level and inter-regulatory issues in the operations of these FCs.

Early Warning System (EWS) *and Prompt Corrective Action (PCA)*

VI.54 A framework on EWS to track deviation of critical financial indicators triggering granular investigations has since been finalised and its details are being worked out. Alongside, the existing PCA framework for banks, first introduced in 2002 is being revamped. This will subsequently be extended to FCs in coordination with other domestic regulators.

Global Supervisory Cooperation

VI.55 As part of cross-border supervisory cooperation and exchange of information, the Reserve Bank signed MoUs with six overseas banking supervisory authorities in 2014-15 - Hong Kong Monetary Authority; Central Bank of Kenya; Banco Central do Brasil; Bank of Uganda; Central Bank of Seychelles and Maldives Monetary Authority. A statement of cooperation with three US financial regulators, *viz.,* Board of Governors of the Federal Reserve System, Office of the Comptroller of Currency and Federal Deposits Insurance Corporation has also been established. Till date, the Reserve Bank has executed 26 MoUs, one letter for supervisory cooperation and one statement of cooperation with overseas supervisors/ regulators.

VI.56 In line with the BCBS principles on cross-border consolidated supervision, the Reserve Bank is instituting supervisory colleges for Indian banks with considerable overseas presence. Supervisory colleges have been set up for State Bank of India, ICICI Bank Ltd., Bank of Baroda, Bank of India, Punjab National Bank and Axis Bank Ltd.

Agenda for 2015-16

VI.57 Going forward, all small foreign banks operating in India are set to be brought into RBS. While a new format is being devised for inspection of the AIFIs - National Bank for Agriculture and Rural Development (NABARD), SIDBI, Export-Import (EXIM) Bank of India and the National Housing Bank (NHB), the revised format for CRILC reporting, including improved analytics is expected to be rolled out soon. In coordination with the IRDA, it is proposed to collect CRILC data from insurance companies as well.

VI.58 All Off-site Monitoring and Surveillance System (OSMOS) returns are planned to migrate to an eXtensible Business Reporting Language (XBRL)/ data warehouse environment towards developing a single information system for supervisory purposes. A new framework for fraud detection, reporting and monitoring has been rolled out on May 7, 2015. Further, a central fraud registry for use by banks is also under preparation. Though disparate systems used by the regulated entities hinder the process of automated data flow, the Reserve Bank will continue to encourage banks to switch over to entirely automated modes of data submission.

VI.59 Capacity building, with particular focus on RBS processes, system audit and information technology vulnerability/ penetration testing, is planned to be rolled out in 2015-16. The EWS as well as the revamped PCA framework for banks are likely to be finalised in 2015-16. Work relating to developing a PCA framework for FCs is expected to be initiated in coordination with other domestic regulators. The Reserve Bank is also exploring ways, including appropriate penal measures towards improving the compliance culture amongst regulated entities.

Cooperative Banks: Department of Cooperative Bank Supervision (DCBS)

VI.60 DCBS was carved out of the erstwhile Urban Banks Department (UBD) and it is primarily focused on ensuring the financial soundness of individual UCBs as well as the sector as a whole.

Agenda for 2014-15: Implementation Status

VI.61 During the year, 968 UCBs, comprising all scheduled UCBs, C and D rated non-scheduled UCBs, and A and B rated non-scheduled UCBs due for inspection, were subjected to on-site inspections and appropriate supervisory action. While the licences of nine UCBs were cancelled, two UCBs were merged with other UCBs and 'All Inclusive Directions' were imposed on seven UCBs. All the 1,589 UCBs were supervised through off-site surveillance system. Towards developing a single point platform for data collection, processing and dissemination, 13 returns for UCBs have been migrated to the XBRL-based reporting system from the existing off-site surveillance reporting system. Training programmes to improve professionalism and governance in UCBs were also organised by the Reserve Bank.

Agenda for 2015-16

VI.62 While ensuring effective supervision of UCBs, further reduction in the number of UCBs with negative net worth has been envisaged for 2015-16. The migration of all the returns to the XBRL-based reporting platform will be completed in the coming year. The initiatives for capacity building in the UCB sector will be carried forward in the coming year too.

NBFCs: Department of Non-Banking Supervision (DNBS)

VI.63 This department is the supervisory wing of NBFCs and it aims at establishing an enabling environment for a healthy and sound NBFC sector while protecting the interests of depositors, customers and other stakeholders as also safeguarding the country's financial system from contagion risks out of this sector. The department also endeavours to increase public awareness on the legal/ regulatory framework for entities engaged in various types of financial activities.

Agenda for 2014-15: Implementation Status

VI.64 Deposit taking and systemically important' non-deposit taking NBFCs continued to be the focus of on-site inspections. During 2014-15, 72 deposit taking companies and 182 non-deposit taking companies were inspected. To deal with delinquent and unauthorised entities, SLCCs were reconstituted in May 2014 with the Chief Secretary to the State Government as the Chairman and the Reserve Bank as the secretariat to facilitate regular sharing of market intelligence (MI) and taking coordinated timely action. The Reserve Bank also hosted two conferences of Chief Secretaries/ Administrators of the states/ union territories (UTs) during the year to deliberate on issues concerning fund mobilisations by unauthorised entities. MI cells were also created across 16 regional offices of the Reserve Bank.

Securitisation/ Asset Reconstruction

VI.65 Asset Reconstruction Companies (ARCs) have been steadily increasing their presence in the debt recovery process (Table VI.1). At the end of March 2015, there were 15 securitisation companies (SCs)/ reconstruction companies (RCs) registered with the Reserve Bank. At end-March 2015, the book value of assets acquired by the ARCs stood at around ₹508 billion. While the ARCs are already under off-site surveillance, they will be supervised through on-site inspections in the coming year in view of their increasing importance.

Agenda for 2015-16

VI.66 Small NBFCs which have so far been exempted from regulatory returns will be covered

Table VI.1: Key Financial Parameters for the ARC Sector

(₹ billion)

Item	Mar-14	Mar-15
1	2	3
Owned Fund	30.2	34.0
Acquisition cost of the assets acquired by the SC/ RC	205.8	226.6
Total SRs issued	204.1	224.4
SRs held by SC/ RC in its own account	13.8	29.9
SRs held by seller banks/ FIs	187.6	191.6
Amount of SRs issued to other QIBs	2.4	2.9
SRs held by FIIs	0.2	0.0
SRs redeemed (during the year)	11.9	16.5

SR: Security Receipts; QIBs: Qualified Institutional Buyers; FIIs: Foreign Institutional Investors
Source: COSMOS returns (quarterly).

under off-site monitoring in 2015-16. For dissemination of information amongst SLCC members/ general public, a dedicated website will be launched in the coming year. CRILC information on large borrowers from NBFCs will be taken up for analysis once the platform is fully operationalised. The consultative approach followed by the department is proposed to be formalised to having periodical interactions with the industry in 2015-16.

Deposit Insurance and Credit Guarantee Corporation (DICGC)

VI.67 Deposit insurance extended by DICGC, a wholly-owned subsidiary of the Reserve Bank, covers all banks including LABs, regional rural banks (RRBs) and cooperative banks in the country. As per the International Association of Deposit Insurers' (IADI) Core Principles for Effective Deposit Insurance System 2014, deposit insurance coverage should be limited, credible and cover a large majority of depositors but leave a substantial amount of deposits exposed to market discipline. The current limit of deposit insurance is ₹0.1 million per depositor in the same right and same capacity. As on March 31, 2015, 92.3 per cent of the accounts were fully protected. Amount-wise, insured deposits at ₹26.1 trillion constituted nearly 31 per cent of the assessable deposits. An effective deposit insurance design should be capable of managing its risk by seeking compensation for the risks being transferred to it. Hence, risk-based collection of premium could be an important step in this direction (Box VI.5).

VI.68 During 2014-15, aggregate claims for ₹3.2 billion with respect to 30 cooperative banks taken

Box VI.5
Risk-based Premium for Banks

Deposit insurance can create an incentive for banks to choose high leverage and for customers of banks to be lenient on monitoring. In order to deal with this kind of moral hazard, the premium of deposit insurance should properly reflect the effective underlying risk associated with a bank's activities. It could be partially mitigated by introducing risk-adjusted premium for a deposit insurance scheme. Although a flat-rate premium system has the advantage of being relatively easy to understand and administer, it does not take into account the level of risk that a bank poses to the deposit insurance system and can be perceived as unfair in terms of premium rate and risk profile across banks (IADI 2011).

Literature on deposit insurance identifies two different approaches for determining risk-based premium. The expected loss pricing approach is centred on the expected default probability of a bank, which can be estimated using either fundamentals, rating or market analysis. The Merton type approach uses option pricing theory in order to estimate the probability of default by a company.

In practice, risk-based contributions are defined in terms of a contribution base, adjusted for a factor that is proportional to the risk attitude of the members and a factor reflecting the overall conditions in the banking system in the respective country (Walter and Schaller, 2012). The premium assessment can be summarised in a simple risk function:

$$P_{it} = r_{s,t} * r_{it} * D_{it}$$

where, the bank-specific risk-based contribution (P_{it}) consists of size and risk variables and is defined in terms of a contribution base ($D_{i,t}$), usually the total amount of eligible deposits, plus or minus a percentage ($r_{i,t}$) proportional to the risk attitude of a member (specific risk) and a percentage (r_{st}) reflecting the overall conditions in the banking system in the country (systemic risk).

(Contd....)

The practice in the European Union (EU) suggests that key financial ratios currently applied in assessment of a member institution's risk across member states are quite heterogeneous and the variables taken into account to define them are not identical. The 2014 EU Directive on Deposit Insurance Schemes gives only broad guidance for a risk measure but leaves the fine details to the wisdom of member states. In the US, new rules for risk-based assessment were issued in November 2006 and significant refinements were made to risk-related premium pursuant to financial reform legislation enacted in 2010. For small banks, supervisory CAMELS ratings are combined with financial ratios to determine risk-based assessment rates against deposits. For large banks, in 2011, the US Federal Deposit Insurance Corporation (FDIC) adopted a risk differentiation scheme that combines CAMELS rating and forward looking financial measures of risk.

In India, there have been periodic recommendations for the application of risk-based premium for banks. The Narasimham Committee Report on Banking Sector Reforms (1998), while focusing on structural issues recommended introduction of a risk-based premium system in lieu of the flat-rate premium system. This view was echoed by the Reserve Bank's Capoor Committee on Reforms in Deposit Insurance in India (1999). The Committee on Credit Risk Model (2006) constituted by DICGC also recommended the introduction of risk-based premium, to begin with for SCBs and UCBs.

Notwithstanding the recommendations of various committees in the past, the implementation of risk-based premium could not be operationalised, *inter alia*, due to cooperative banks and RRBs (forming over 90 per cent of insured banks) being under restructuring until recently and lack of a robust supervisory rating for all insured banks, especially cooperative banks which serves as an important input for the rating model. However, there has been a persistent demand from stakeholders and public representatives for a hike in the deposit insurance cover from the current level of ₹0.1 million. A hike in cover without calibrating premium rates to the risk profiles of insured banks covered only exacerbates the risks of an inherent moral hazard. Keeping this in view, a Committee on Differential Premium for Banks (Chairman: Shri Jasbir Singh) was constituted in March 2015 to make recommendations for the introduction of risk-based premium in India.

References:

International Association of Deposit Insurers (IADI) (2011), 'General Guidance for Developing Differential Premium Systems'.

Walter and Schaller (2012), 'An Alternative Way of Calculating Risk Based Premium' in New Paradigms in Banking, Financial Markets and Regulation? ed Balling et al., SUERF.

European Commission (2008), 'Risk-based Contributions in EU Deposit Guarantee Schemes: Current Practices', Joint Research Centre.

into liquidation/ reconstruction/ amalgamation were settled as compared to ₹1.0 billion in the previous year. The size of the deposit insurance fund (DIF) stood at ₹504.5 billion as at end-March 2015, yielding a reserve ratio (DIF/ insured deposits) of 1.9 per cent.

National Housing Bank (NHB)

VI.69 NHB, a wholly owned subsidiary of the Reserve Bank, was set up on July 9, 1988, under the National Housing Bank Act, 1987, to operate as a principal agency to promote housing finance institutions both at local and regional levels and to provide financial and other support incidental to such institutions.

VI.70 As the apex institution for housing finance, NHB registers, regulates and supervises housing finance companies (HFCs). As on June 30, 2015, there were 65 HFCs registered with NHB. NHB is focused on promoting innovative market based solutions for affordable housing finance to low income housing segments. NHB extends refinance to HFC, scheduled commercial banks (SCBs) and cooperative sector institutions, against their housing loans. It also provides project lending to a range of borrowers in public and public-private partnerships, MFIs, state level housing boards and area development authorities for large scale integrated housing projects and slum redevelopment projects. The cumulative disbursements in 2014-15 stood around ₹218.5 billion of which 25.4 per cent (₹55.4 billion) was made for rural housing loans under the Rural Housing Fund (RHF) and the Golden Jubilee Rural Housing Refinance Scheme (GJRHRS).

VI.71 The government has identified NHB as one of the central nodal agencies to channelise subsidy to lending institutions and monitoring the progress of the component under the Credit Linked Subsidy Scheme (CLSS). CLSS will be implemented across the country in all 4,041 statutory towns (as per Census 2011) and is part of the Pradhan Mantri Awas Yojana - Housing for All (HFA) mission, which seeks to address the housing requirements of urban poor, including of slum dwellers. NHB has also been a nodal agency for government schemes, such as the Interest Subsidy Scheme for Housing the Urban Poor (ISHUP), 1 per cent Interest Subvention scheme and the Solar Capital Subsidy scheme.

VI.72 NHB also manages the Credit Risk Guarantee Fund Trust for low income housing set up by the Government of India to ensure better flow of institutional credit for housing in urban areas. NHB launched RESIDEX in July 2007 for tracking residential property prices across 26 cities in India on a quarterly basis. The central government enhanced allocations for NHB from ₹40 billion to ₹80 billion in 2014-15 to expand and support rural housing in the country.

CONSUMER EDUCATION AND PROTECTION

Consumer Education and Protection Department (CEPD)

VI.73 CEPD focuses on pursuing public interest, providing a level playing field between suppliers and consumers of financial services by reducing the imbalances emanating from information asymmetries, limited product choices, inadequate disclosures, *etc.* Consumer protection is a key to promoting financial inclusion.

Agenda for 2014-15: Implementation Status

Charter of Customer Rights

VI.74 As a structured measure towards protection of bank customers and setting standards of customer service, a Charter of Customer Rights as broad, over-arching principles for protecting bank customers was formulated by the Reserve Bank in 2014-15 (Box VI.6). The Indian Banks' Association (IBA) and Banking Codes and Standards Board of India (BCSBI) have since jointly formulated a model customer rights policy/

Box VI.6
Charter of Customer Rights

The Charter of Customer Rights released on December 3, 2014, enshrines broad, over-arching principles for protection of bank customers and enunciates five basic rights for bank customers as:

(i) *Right to Fair Treatment:* Both the customer and the financial services provider have a right to be treated with courtesy. The customer should not be unfairly discriminated against on grounds such as gender, age, religion, caste and physical ability when offering and delivering financial products.

(ii) *Right to Transparency, Fair and Honest Dealing:* The financial services provider should make every effort to ensure that the contracts or agreements it frames are transparent, easily understood and well communicated to the common person. The product's price, associated risks, customer's responsibilities and the terms and conditions that govern its use over the product's life-cycle, should be clearly disclosed. The customer should not be subject to unfair business or marketing practices, coercive contractual terms or misleading representations. Over the course of their relationship, the financial services provider cannot threaten the customer with physical harm, exert undue influence or engage in blatant harassment.

(iii) *Right to Suitability:* The products offered should be appropriate to the needs of the customer and based on an assessment of the customer's financial circumstances and understanding.

(iv) *Right to Privacy:* Customers' personal information should be kept confidential unless they have offered specific consent to the financial services provider or such information is required to be provided under the law or it is provided for a mandated business purpose

(Contd....)

(for example, to credit information companies). The customer should be informed upfront about likely mandated business purposes. Customers have the right to protection from all kinds of communications, electronic or otherwise, which infringe upon their privacy.

(v) *Right to Grievance Redress and Compensation:* The customer has a right to hold the financial services provider accountable for the products offered and to have a clear and easy way to have any valid grievances redressed. The provider should also facilitate the redress of grievances stemming from the sale of third party products. The financial services provider must communicate its compensation policy for mistakes, lapses in conduct, as well as non-performance or delays in performance, whether caused by the provider or otherwise. The policy must lay out the rights and duties of the customer when such events occur.

These rights aim to protect the customer against unfair discrimination, unfair business or marketing practices, coercive contractual terms or misleading representations and aim to promote appropriate need warranted financial products with a better understanding of the various risks and charges involved therein.

code based on the Charter of Customer Rights. Banks were advised to formulate board approved customer rights policies by July 31, 2015 incorporating the Charter of Customer Rights, and periodically review its implementation internally.

Internal Ombudsman in Banks

VI.75 For strengthening the grievance redressal mechanism available to bank customers, all PSBs, select private sector and foreign banks were advised to appoint Chief Customer Service Officers as Internal Ombudsman in banks who should examine complaints, which remained unresolved/ partially resolved by the internal grievance redressal mechanism of the bank.

Ascertaining Field Level Feedback and Enhancing Awareness

VI.76 For initiating appropriate corrective action, incognito visits of select bank branches were undertaken to ascertain field level feedback on complaints regarding mis-selling of third party products by banks like insurance and mutual funds. The feedback received was forwarded to all stakeholders. Further, in view of the large number of complaints on fictitious offers of money, public awareness campaigns about such fictitious offers, including the availability of the Banking Ombudsman (BO) scheme were conducted, particularly in rural and semi-urban areas.

Agenda for 2015-16

VI.77 The Reserve Bank will focus on full-fledged operationalisation of the Charter of Customer Rights in banks. The BO scheme is also being taken up for a complete review in 2015-16. Focused field visits/ study on mis-selling by banks in semi-urban areas and non-functioning/ mal-functioning ATMs across various parts of the country have also been planned.

VII PUBLIC DEBT MANAGEMENT

The Reserve Bank successfully completed the borrowing programme of the Government of India and the state governments during 2014-15 despite several challenges, such as scaling up of the size of borrowing and elevated yields in the first half of the year. It continued the strategy of elongating the maturity, consolidating the debt portfolio and imparting more liquidity to the secondary market. In pursuance of the objective of minimising the rollover risk, the maturity profile of the debt portfolio was elongated during the year with a resultant marginal increase in weighted cost. Leveraging on increased appetite for longer maturity debt, the Reserve Bank announced issuance of 40-year security during 2015-16 to extend the yield curve beyond 30 years. A medium term debt management strategy in line with sound international practices, regular quarterly calendar for state borrowings, review of the WMA scheme for the states, an efficient market infrastructure to aid a deeper and wider government debt market and expanding the investors' base, are some of the important agenda items slated for 2015-16.

VII.1 In terms of Sections 20 and 21 of the Reserve Bank of India Act, 1934, the Reserve Bank has the obligation and right to transact Central Government business in India and manage its public debt. Similarly, the Reserve Bank is the debt manager for all the 29 state governments and the union territory of Puducherry as also a banker to them except the Government of Sikkim in terms of their agreement with the Reserve Bank under Section 21A of the RBI Act, 1934. Further, the Reserve Bank makes advances to the Central and state governments to tide over temporary mismatch in the cash flows. Such advances are termed as 'ways and means advances' (WMA), which are repayable in each case not later than three months from the date of making the advances in terms of Section 17 (5) of the RBI Act.

VII.2 The Reserve Bank has set for itself a medium-term agenda of transforming the financial sector into a stronger, deeper, more efficient and inclusive system. Within this broader agenda, the approach for debt management as entrusted to the Internal Debt Management Department (IDMD) encompasses: a comprehensive debt management strategy in alignment with sound international practices, minimising the borrowing cost, extending maturities to cater to the requirements of diverse investors, consolidation of public debt and reduction in the rollover risk through active switch/buyback operations.

Agenda and Implementation Status in 2014-15

VII.3 In 2014-15, the debt management strategy aimed to:

i. conduct debt management operations in an orderly manner and successfully meet the market borrowing programmes in a smooth and non-disruptive manner while minimising the cost of borrowing;

ii. ensure reasonable distribution in issuances over the first half and the second half with issuance of new bonds coupled with bonds of non-standard maturity to avoid concentration of redemptions in the first half of the year;

iii. smoothen the maturity profile of GoI securities to reduce redemption pressures in 2014-15 through buybacks/switches;

iv. ensure quicker and wider dissemination of auction related information to market participants and other stakeholders;

v. promote liquidity in government securities (G-secs) through a scheme for market making by PDs in semi-liquid and illiquid G-secs; and

vi. improve efficiency of cash management and ensure reasonable returns on the CSF/GRF (consolidated sinking fund/guarantee redemption fund) of the states.

DEBT MANAGEMENT OF THE CENTRAL GOVERNMENT

VII.4 The gross market borrowings of ₹5,920 billion (BE ₹6,000 billion) and net market borrowings of ₹4,532 billion, which funded 90.3 per cent of the gross fiscal deficit (GFD), were successfully raised in 2014-15 (Table VII.1). With relatively comfortable liquidity and stable market conditions during 2014-15, there was lower devolvement of ₹53 billion on primary dealers (PDs) on three occasions as compared with 26 instances amounting to ₹175 billion in 2013-14.

VII.5 Debt management operations faced several challenges during 2014-15. First, the combined market borrowings of the Centre and the states increased over the level in the preceding year in both gross and net terms (that is, net of repayments) resulting in a sizeable scaling up of debt issuances in the primary market, particularly for the states. The Reserve Bank held auctions of government securities (including T-bills and SDLs or state development loans) on 118 days, leading to a total of 548 issuances and 41 underwriting auctions. Second, elevated level of yields in the first half of the year when the borrowing programme was front-loaded posed challenges for the cost of borrowing. Under these testing conditions, the efficacy of debt management can be gauged from the modest 12 bps increase in the weighted average yield of dated securities issued by the Centre during the year to 8.51 per cent (Table VII.2) despite a lengthening of maturity. Third, the Reserve Bank continued debt consolidation through reissuances and eased redemption pressures through buybacks/switches during the year and also elongated the maturity profile of government debt, thereby mitigating rollover risks.

VII.6 Although yields on government dated securities gradually declined during the course of the year from relatively higher levels in the early months (Chart VII.1), the weighted average yield of dated securities issued during 2014-15 was somewhat higher than in the previous year. Higher issuances of long dated securities lengthened the average maturity of outstanding debt (Table VII.3).

VII.7 As part of the consolidation of Government debt, 95 per cent of the securities were reissued. Buybacks/switches were conducted to smoothen the maturity profile of GoI securities and reduce redemption pressures. Buyback of short-term securities amounting to ₹188 billion from the market was completed through reverse auctions in

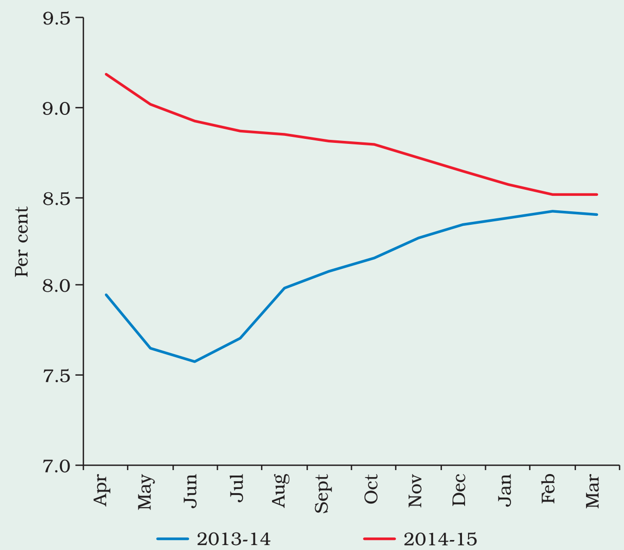
Table VII.1: Gross and Net Market Borrowings of the Central Government#

(₹ billion)

Item	2004-05	2012-13	2013-14	2014-15	2015-16*
1	2	3	4	5	6
Net Borrowings	460	4,674	4,686	4,532	1,757 (4,564)
Gross Borrowings	803	5,580	5,636	5,920	2,670 (6,000)

Note: 1. Figures in brackets are budget estimates. 2. Figures excluding buyback/ switches.
#: Issuance through dated securities; * : upto August 14, 2015.

Chart VII.1: Weighted Average Yield of Primary Issuances of GoI Dated Securities (Cumulative)



September 2014 and switches of ₹88 billion were conducted in February 2015. A conversion operation of securities from the Reserve Bank's portfolio amounting to ₹302 billion was conducted in March 2015. By these measures, the Reserve Bank ensured the elongation of maturity of the outstanding debt while containing the rollover risk for GoI.

VII.8 Commercial banks remained predominant investors in dated government securities, holding around 43 per cent at end-March 2015, followed by insurance companies and provident funds at around 21 and 8 per cent, respectively. The share of the Reserve Bank's holding declined to 14 per cent from a high of 16 per cent in the previous two years. The share of foreign portfolio investors (FPIs), which have emerged as active market players in the recent period, more than doubled to 3.7 per cent from a year ago.

VII.9 Net market borrowings of the Centre through treasury bills and dated securities stood at ₹4,779 billion in 2014-15, 6 per cent lower than those in 2013-14. Yields on treasury bills also softened at the shorter end in 2014-15 reflecting comfortable liquidity conditions. Continuing its pursuit of the market development strategy, the Reserve Bank ensured quicker and wider dissemination of auction related information among market participants and other stakeholders. The system of displaying primary auction results of treasury bills, SDLs and GoI dated securities in e-Kuber and NDS-OM along with publication of the

Table VII.2: Central Government's Market Loans-A Profile#

(yield in per cent / maturity in years)

Year	Range of YTMs at Primary Issues			Issued during the year			Outstanding Stock (As at end-March)	
	under 5 years	5-10 years	Over 10 years	Weighted average yield	Tenor of securities (range)	Weighted average maturity	Weighted average maturity	Weighted average coupon
1	2	3	4	5	6	7	8	9
2008-09	7.71-8.42	7.69-8.77	7.77-8.81	7.69	6-30	13.80	10.45	8.23
2009-10	6.09-7.25	6.07-7.77	6.85-8.43	7.23	5-15	11.16	9.82	7.89
2010-11	5.98-8.67	7.17-8.19	7.64-8.63	7.92	5-30	11.62	9.78	7.81
2011-12	8.21-8.49	7.80-10.01	8.25-9.28	8.52	5-30	12.66	9.60	7.88
2012-13	8.82-8.21	7.86-8.76	7.91-8.06	8.36	5-30	13.50	9.67	7.97
2013-14*	7.22-9.00	7.16-9.40	7.36-9.40	8.39	6-30	14.22	10.00	7.99
2014-15*	-	7.66-9.28	7.65-9.42	8.51	6-30	14.67	10.23	8.08

#: Excludes issuances under market stabilisation scheme; YTM: Yield to maturity; *: Excluding inflation linked bonds and buyback/switch in GoI securities.

Table VII.3: Issuance of the Central Government Dated Securities - Maturity Pattern

(Amount in ₹ billion)

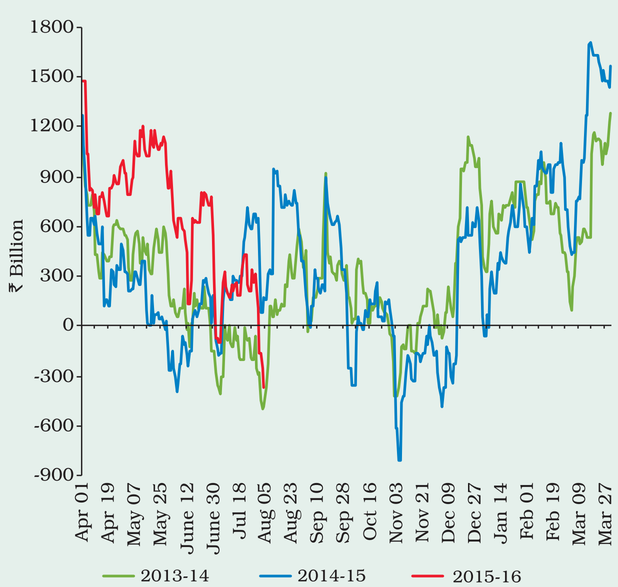
Residual Maturity	2012-13		2013-14		2014-15	
	Amount raised	Percentage to total	Amount raised	Percentage to total	Amount raised	Percentage to total
1	2	3	4	5	6	7
Less than 5 years	470	8.42	110	1.95	-	-
5 -9.99 years	1,910	34.23	2,305	40.91	2,350	39.69
10-14.99 years	1,730	31.00	1,340	23.78	1,510	25.51
15 -19.99 years	270	4.84	930	16.50	960	16.22
20 years & above	1,200	21.51	950	16.86	1,100	18.58
Total	**5,580**	**100.00**	**5,635**	**100.00**	**5,920**	**100.00**

results on the Reserve Bank's website has been implemented.

Cash Management

VII.10 The Government started the fiscal year with a cash build-up of ₹1,284 billion and the cash position remained comfortable until the third week of May 2014 (Chart VII.2). Following spending by the Government, cash balance declined and the Government intermittently availed WMA for 61 days altogether *vis-à-vis* 42 days during the previous year. It also issued cash management bills (CMBs) for ₹100 billion in November 2014.

Chart VII.2: Cash Balance of the Government of India



VII.11 From December 16, 2014 onwards, the Government's cash balance held with the Reserve Bank is being reckoned for auction through variable rate repo as part of the Reserve Bank's revised liquidity management framework. The Government ended the fiscal year with a cash balance of ₹1,573 billion.

VII.12 WMA limits for the first half (April-September) and the second half (October-March) of 2014-15 were fixed at ₹350 billion and ₹200 billion, respectively, for the Central Government. The WMA limit for the first half of 2015-16 was raised to ₹450 billion.

DEBT MANAGEMENT OF STATE GOVERNMENTS

Market Borrowings

VII.13 The Reserve Bank entered into an agreement with the Government of Telangana for carrying out its cash and debt management operations effective June 2, 2014, under Section 21A of the Reserve Bank of India Act, 1934.With this, the Reserve Bank is now the debt manager for all the 29 states and for the union territory (UT) of Puducherry. All of them participated in market borrowing programme in 2014-15, with the net borrowing rising by 26 per cent (Table VII.4).

VII.14 Despite higher market borrowings, the weighted average yeild of state government securities issued during the year stood lower at

8.58 per cent as compared to 9.18 per cent last year. Alongside, the weighted average spread came down significantly to 38 bps over GoI securities of comparable maturities from 75 bps in the previous year (Table VII.4).

Cash Management of State Governments

VII.15 The Reserve Bank has been extending WMA to state governments since 1937 under the provisions of Section 17(5) of the RBI Act with the objective of covering temporary mismatches in their cash flows. There are two types of WMA: (i) normal WMA or clean advances, and (ii) special WMA (SWMA) or secured advances (the nomenclature of SWMA was changed in June 2014 as 'special drawing facility' (SDF) by amending the agreement with state governments). An overdraft (OD) occurs whenever the Reserve Bank's credit to a state government exceeds the SDF and WMA limits.

VII.16 The aggregate WMA limit for the states, including the Government of the Union Territory of Puducherry was raised by 50 per cent to ₹154 billion in November 2013 and the same limit was continued in 2014-15. The monthly average utilisation of WMA and OD by the states was higher in 2014-15 even as the number of states resorting to WMA remained unchanged at 12. Fourteen states resorted to SDF, up from 12 in 2013-14. Ten states availed of OD in 2014-15 as against eight states in 2013-14.

VII.17 The Reserve Bank's recent initiatives in the government banking business are expected to enhance efficiency in the cash management of state governments (Box VII.1).

Investments in the Consolidated Sinking Fund (CSF)/Guarantee Redemption Fund (GRF)

VII.18 As the fund manager of state governments, the Reserve Bank has been managing their consolidated sinking funds (CSF) and guarantee redemption funds (GRF). In addition to dated government securities, the Reserve Bank has started investing in SDLs and other high yielding securities (for example, treasury bills) as per the mandate given by the respective state governments. The outstanding investment in CSF and GRF stood at ₹703 billion at end-March 2015, a rise of 14.8 per cent over the previous year. In its endeavour to create awareness among Finance Department officials of state governments, capacity building programmes were organised by the Reserve Bank in a number of states including Tripura, Mizoram, Jharkhand, Odisha and Uttarakhand.

Table VII.4: States' Market Borrowings

(₹ billion)

Item	2012-13	2013-14	2014-15	2015-16@
1	2	3	4	5
Net Allocation	1,881	2,185	2,365	NA
Gross Allocation	2,187	2,506	2,564	NA
Gross Amount Raised during the Year	1,772	1,967	2,408	824
Net Amount Raised during the Year	1,467	1,646	2,075	720
Weighted Average Yield (%)	8.84	9.18	8.58	8.22
Weighted Average Spread (bps)	71	75	38	34
SDLs outstanding (at the end period)	9,291	10,619	12,755	13,474

@: as on August 12, 2015.

Agenda for 2015-16

VII.19 Union Budget, 2015-16 has projected a marginal increase in the Centre's net market borrowings in 2015-16. With signs of improvement in macroeconomic conditions and moderation in inflationary pressures, the governments' market borrowing programmes are likely to be completed in an orderly manner, while minimising the cost of borrowing.

VII.20 A medium term debt management strategy, in consultation with GoI, in line with best international

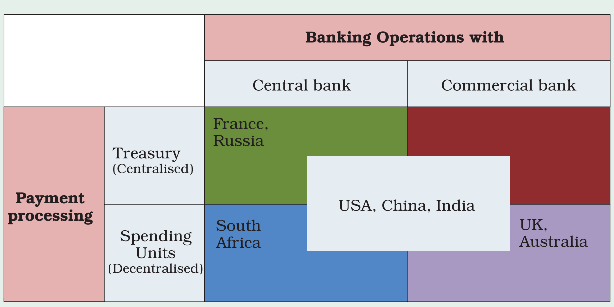
Box VII.1
New Initiatives in Government Banking

Internationally, arrangements for the government banking business vary across countries. For instance, it is performed by the central banks in France and Russia while in the UK and Australia it is performed by commercial banks. The payment processing is centralised in France and Russia but decentralised in South Africa. Larger countries, such as the US, China and India have adopted a mixed approach, depending on the nature and type of transactions (Chart 1).

As part of its initiatives to improve efficiency in government banking services, the Reserve Bank constituted a Working Group to Bring in Uniformity and Standardisation in Procedures/Data Structure of e-Receipt/e-Transactions of State Governments. The group submitted its report in April 2014. Its recommendations focus on migrating to a broadly uniform model for receipts and payments for all the states and integration with e-Kuber, the core banking solution of the Reserve Bank. As discussed in the State Finance Secretaries Conference organised by the Reserve Bank in May 2015, it was decided to implement the recommendations of the report on a pan-India basis. Accordingly, a task force has been constituted for monitoring the implementation process. Till date, 15 states have started this process and are at various stages of implementation. Efforts are on to bring the remaining states on board.

E-receipt and e-payment functions have been developed in e-Kuber to provide enhanced operational efficiency and facilitate better fund management of governments. The e-receipts system envisages revenue collection through agency banks, flow of information to the Reserve Bank and final transfer of funds to the respective state government's accounts. The system is designed for faster processing without giving rise to any reconciliation issues. The agency banks participating in the revenue collection of a state are required to prepare details of daily receipts in a standardised ISO 20022 format file and upload it on the e-Kuber portal which is used by banks for their interface with the Reserve Bank. After processing the files, e-scrolls with all relevant information are transmitted electronically to the state governments in a straight-through-processing (STP) manner. The interface of e-Kuber with the public finance management system (PFMS) of the Central Government has been scaled up to serve all central ministries for effecting inter-government transactions on a STP basis.

Chart 1: International practices in government banking business



Based on Pessoa and Williams (2012).

For e-payments, wherever a state has a centralised treasury system, integration of its IT system with e-Kuber will be done and the details of payments to be effected by the government will be directly received, processed and transmitted to the National Electronic Funds Transfer (NEFT) system for effecting payments, with no manual intervention. Transaction-wise e-scrolls will be sent on the same day, duly indicating status of payments (whether successful, or returned). This will ensure that all payments are processed efficiently and beneficiaries receive the payments without delay.

With a view to maximising benefits from technological developments, a Working Group on Business Process Re-engineering with participation from government agencies, banks and the Reserve Bank has been set up. The group will examine the workflows, systems and processes for handling government business, related institutional infrastructure and reporting structures. The group is expected to submit its report by October 2015. With these initiatives, banking arrangements of the governments including their cash management are set to witness significant efficiencies in the years to come.

References:

Pessoa, M. and M. Williams (2012), 'Government Cash Management: Relationship between the Treasury and the Central Government', International Monetary Fund.

Pattanayak, S. and I. Fainboim (2011), 'Treasury Single Account: An Essential Tool for Government Cash Management', International Monetary Fund.

practices will be placed in the public domain during 2015-16. In order to manage GoI's maturity profile and also to reduce the rollover risk, it is planned that buybacks and switches will be part of the regular calendar of issuance from the second half of 2015-16. To cater to the demand from long term investors like insurance companies and pension funds, a 40-year security is proposed to be issued during 2015-16, taking in view a relatively flat yield curve.

VII.21 Market borrowings of state governments have been budgeted higher for 2015-16 than the previous year. To improve predictability of market borrowings, all the states will be encouraged to move over to a quarterly calendar of issuances with effect from 2015-16 and the first of this calendar has been announced for the second quarter of 2015-16. The states have also been advised to actively engage with investors within their states to diversify the investor base.

VII.22 The report of the Advisory Committee on Ways and Means Advance to State Governments (Chairman: Sumit Bose) is expected to be finalised and will be taken up for implementation.

VII.23 The Reserve Bank will continue with the agenda of enabling easier and increased access to retail investors. As part of this, a web-based solution on the e-Kuber platform for participation of all mid-segment/retail investors having gilt accounts is being implemented. To develop a more liquid government securities market, a scheme of market making in select semi-liquid securities by PDs will be implemented. The non-competitive bidding facility available to retail investors is currently applicable only to auctions of dated securities. It is proposed to allow the non-competitive bidding facility in treasury bills to individuals as well. The Reserve Bank in consultation with all stakeholders will enable seamless movement of securities from the subsidiary general ledger (SGL) form to demat form and *vice versa* to promote trading of G-secs on stock exchanges. The Reserve Bank will work to put in place a more predictable framework on the size and scope of investments in G-secs by foreign portfolio investors taking into account the risks and benefits associated with such flows into the debt market.

VII.24 The Reserve Bank will closely work with the Government of India in the preparatory arrangements for the establishment of the Public Debt Management Agency (PDMA).

VIII CURRENCY MANAGEMENT

Banknotes and coins continued to be in high demand in 2014-15. The Reserve Bank intensified its efforts to strengthen further the security features to improve integrity of banknotes. The Reserve Bank entered into agreements with banks to expand the currency management base. In consultation with the Government of India, the Reserve Bank made efforts towards the indigenisation of banknotes.

VIII.1 In line with the core statutory functions envisaged for it as per the Preamble and Section 22 of the Reserve Bank of India Act, 1934, the approach adopted by the Reserve Bank for currency management operations during 2014-15 focused on ensuring an adequate supply of clean banknotes and coins of various denominations to meet legitimate business requirements of members of the public, and creating, stocking and distributing banknotes and coins and destruction of soiled, mutilated notes and uncurrent coins.

TRENDS IN CURRENCY

VIII.2 Demand for banknotes and coins increased in 2014-15, notwithstanding the use of technology driven non-cash modes of payment.

Banknotes in Circulation

VIII.3 The value of banknotes in circulation increased by 11.4 per cent to ₹14,289 billion as at end-March 2015 over the previous year. Further, the volume of banknotes in circulation increased by 8.1 per cent to 83.6 billion pieces over the same period. Notes of denominations of ₹500 and ₹1,000 together accounted for approximately 85 per cent of the total value of banknotes in circulation at end-March 2015. Notes of ₹10 and ₹100 together accounted for 54 per cent of the volume at end-March 2015 (Table VIII.1).

Table VIII.1: Banknotes in Circulation

Denomination (₹)	Volume (million pieces)			Value (₹ billion)		
	Mar 2013	Mar 2014	Mar 2015	Mar 2013	Mar 2014	Mar 2015
1	2	3	4	5	6	7
2 and 5	11,624	11,698	11,672	46	46	46
	(15.8)	(15.1)	(13.9)	(0.4)	(0.4)	(0.3)
10	25,168	26,648	30,304	252	266	303
	(34.2)	(34.5)	(36.3)	(2.2)	(2.1)	(2.1)
20	3,825	4,285	4,350	77	86	87
	(5.2)	(5.5)	(5.2)	(0.6)	(0.7)	(0.6)
50	3,461	3,448	3,487	173	172	174
	(4.7)	(4.5)	(4.2)	(1.5)	(1.3)	(1.2)
100	14,421	14,765	15,026	1,442	1,476	1,503
	(19.6)	(19.1)	(18.0)	(12.4)	(11.5)	(10.5)
500	10,719	11,405	13,128	5,359	5,702	6,564
	(14.6)	(14.7)	(15.7)	(46.0)	(44.4)	(46.0)
1,000	4,299	5,081	5,612	4,299	5,081	5,612
	(5.9)	(6.6)	(6.7)	(36.9)	(39.6)	(39.3)
Total	**73,517**	**77,330**	**83,579**	**11,648**	**12,829**	**14,289**

Note: Figures in parentheses represent share in total volume/value.

Coins in Circulation

VIII.4 Coins in circulation witnessed sustained increase in demand in 2014-15. While the total value of coins in circulation increased by 12.1 per cent, in volume terms the increase was 8.0 per cent (Table VIII.2).

Increased Demand for Coins and Supply-enhancing Measures

VIII.5 In recent years, demand for coins has increased at a faster pace *vis-à-vis* supply mainly due to several toll plazas operating in the country,

Table VIII.2: Coins in Circulation

Denomination	Volume (million pieces)			Value (₹ billion)		
	Mar 2013	Mar 2014	Mar 2015	Mar 2013	Mar 2014	Mar 2015
1	2	3	4	5	6	7
Small Coin	14,788	14,788	14,788	7	7	7
	(17.4)	(16.1)	(14.9)	(4.6)	(4.1)	(3.6)
₹1	35,884	38,424	41,627	36	38	42
	(42.4)	(41.9)	(42.1)	(23.5)	(21.9)	(21.7)
₹2	22,113	24,823	27,038	44	50	54
	(26.1)	(27.1)	(27.3)	(28.8)	(28.9)	(27.8)
₹5	10,675	11,577	12,761	53	58	64
	(12.6)	(12.7)	(12.9)	(34.6)	(33.5)	(33.0)
₹10	1,267	2,017	2,750	13	20	27
	(1.5)	(2.2)	(2.8)	(8.5)	(11.6)	(13.9)
Total	**84,727**	**91,629**	**98,964**	**153**	**173**	**194**

Note: Figures in parentheses represent the percentage share in total.

structure of bus/auto/train/taxi fares, rising affluence of rural and urban poor, especially in view of Government sponsored schemes like Mahatma Gandhi National Rural Employment Guarantee Scheme and increased use of fast-moving consumer goods (FMCG) in small sachets. Mismatch in indent and supply of coins during the past few years is given in Table VIII.3.

VIII.6 To meet the enhanced demand, the Reserve Bank has increased the indent with the Government of India mints and taken the following additional steps to further streamline distribution:

(i) Shopkeepers and other business establishments, tollgate agencies, *etc.,* have been linked to the nearest currency chest for their requirements of coins;

Table VIII.3: Indent and Supply of coins

(pieces in million)

Year	Indent	Supply
1	2	3
2012-13	9,554	6,878
2013-14	12,033	7,677
2014-15	13,840	7,907

(ii) Banks were advised to organise coin melas for issue of coins directly to members of the public;

(iii) Bulk users of coins, such as large retailers and toll plazas have been advised to increase the usage of point of sale (POS) terminals/cards/ e-tokens in order to reduce their dependence on coins; and

(iv) Banks were being incentivised for establishing coin vending machines (CVMs) and machines which extend cash related services to the public.

VIII.7 The Reserve Bank has suggested to the Central Government to permit import of coins as a short term measure till the production capacity of the mints is augmented; consider allowing minting of coins by private parties as enabled under the Coinage Act, 2011; and increase the present production capacity of mints/ set up new mints as a medium term measure. The Reserve Bank is also working on ways to encourage recirculation of coins by members of the public.

CURRENCY MANAGEMENT INFRASTRUCTURE

VIII.8 Currency management infrastructure consists of a network of 19 issue offices, 4,132 currency chests (including sub-treasury offices and a currency chest of the Reserve Bank at Kochi) and 3,813 small coin depots of commercial, cooperative and regional rural banks spread across the country (Table VIII.4). The procedure for opening currency chests was simplified during the year by introducing a single layer approval system instead of the multiple layers of approvals.

Lead Bank Scheme

VIII.9 The Lead Bank Scheme for currency management was introduced on a pilot basis in 2013 by identifying one district of each state and

Table VIII.4: Currency Chests and Small Coin Depots as at end-March 2015

Category	No. of Currency Chest	No. of Small Coin Depot
1	2	3
State Bank of India	2,033	1,930
SBI Associate Banks	763	733
Nationalised Banks	1,162	987
Private Sector Banks	153	149
Co-operative Banks	4	4
Foreign Banks	4	4
Regional Rural Banks	5	5
State Treasury Offices (STOs)	7	0
RBI	1	1
Total	**4,132**	**3,813**

assigning the same to a lead bank, which, in turn, is responsible for ensuring that genuine needs of members of the public for clean notes and coins are met through coordination with currency chests and small coin depots situated in that area. The lead bank as a nodal bank for currency management (BCM) attends to issues, such as linkage of non-currency chest branches to currency chests, facilitation of supply and issue of banknotes and coins to and from bank branches in the area, prompt routing of diversion requests and redressal of public grievances. The nodal BCM undertakes functions relating to spreading awareness/literacy campaigns on security features of genuine notes and exchange of mutilated notes. After a year of operation, the scheme was reviewed and it was decided to continue it in 2014-15; it is under review for 2015-16.

CLEAN NOTE POLICY

Demand Estimation and Supply of Banknotes and Coins

VIII.10 Demand for currency is estimated using econometric models *inter alia*, factoring in real GDP growth prospects, rate of inflation and disposal rate of soiled notes denomination-wise. Accordingly, the total supply of banknotes was raised to 23.7 billion in 2014-15 from 20.9 billion pieces (an increase of 13.1 per cent) in 2013-14 (Table VIII.5). The supply of coins was also increased by 3.0 per cent in 2014-15 as compared to 11.6 per cent in 2013-14 (Table VIII.6).

Table VIII.5: Indent and Supply of Banknotes by BRBNMPL and SPMCIL to the Reserve Bank

Denomination (₹)	Volume (million pieces)				
	2013-14		2014-15		2015-16
	Indent	Supply	Indent	Supply	Indent
1	2	3	4	5	6
5	0	0	0	0	0
10	12,164	9,467	6,000	9,417	4,000
20	1,203	935	4,000	1,086	5,000
50	994	1,174	2,100	1,615	2,050
100	5,187	5,131	5,200	5,464	5,350
500	4,839	3,393	5,400	5,018	5,600
1,000	975	818	1,500	1,052	1,900
Total	**25,362**	**20,918**	**24,200***	**23,652**	**23,900**

*: The figures published in the Annual Report 2013-14 were subsequently revised.
BRBNMPL: Bharatiya Reserve Bank Note Mudran Private Limited.
SPMCIL: Security Printing and Minting Corporation of India Limited.

Disposal of Soiled Notes

VIII.11 During 2014-15, around 15.1 billion pieces of soiled banknotes were disposed of as against a target of around 17.1 billion pieces and 14.2 billion pieces disposed during 2013-14.

Table VIII.6: Indent and Supply of Coins by SPMCIL to the Reserve Bank

Denomination	Volume (million pieces)				
	2013-14		2014-15		2015-16
	Indent	Supply	Indent	Supply	Indent
1	2	3	4	5	6
50 Paise	50	40	40	20	40
₹1	5,418	3,092	6,000	3,247**	6,100
₹2	3,546	2,424	4,000	2,367	4,000
₹5	1,819	1,393	2,000	1,091	2,100
₹10	1,200	728	1,800	1,187	2,000
Total	**12,033**	**7,677**	**13,840***	**7,912****	**14,240**

*The figures published in the Annual Report 2013-14 were subsequently revised.
**Includes 5 million pieces of ₹1 currency notes.

Table VIII.7: Number of Counterfeit Notes Detected (April to March)

(No. of pieces)

Year	Detection at Reserve Bank	Other Banks	Total
1	2	3	4
2013-14	19,827	468,446	488,273
	(4.1)	(95.9)	(100.0)
2014-15	26,128	568,318	594,446
	(4.4)	(95.6)	(100.0)

Note: 1. Figures in parentheses represent the percentage share in total.
2. Does not include counterfeit notes seized by the police and other enforcement agencies.

COUNTERFEIT NOTES

VIII.12 During 2014-15, 594,446 pieces of counterfeit notes were detected in the banking system, of which 95.6 per cent were detected by commercial banks, while 4.4 per cent were detected at the Reserve Bank offices (Table VIII.7). During 2014-15, the number of counterfeit notes detected increased for all denominations except ₹2 and ₹5 (Table VIII.8).

VIII.13 In accordance with the international practice of not having multiple series of banknotes simultaneously in circulation, the process of withdrawal of pre-2005 series of banknotes, in phases, was initiated in 2014. Though a majority of these pre-2005 notes have been withdrawn from circulation through bank branches, it was decided to extend the date up to December 31, 2015 to ensure withdrawal of the remaining pre-2005 old design banknotes with least inconvenience to members of the public.

EXPENDITURE ON SECURITY PRINTING AND DISTRIBUTION

VIII.14 Towards faster distribution of notes across the country, the Reserve Bank has been implementing a scheme of direct remittance of banknotes from the note printing presses to currency chests, obviating the need for repeated logistical and security arrangements. Total expenditure incurred on security printing stood at ₹37.6 billion during 2014-15 (July–June) as compared to ₹32.1 billion during 2013-14. The increase was mainly on account of increased supply of banknotes by 13.1 per cent over the previous year. During 2014-15, the Reserve Bank, in

Table VIII.8:Denomination-wise Counterfeit Notes Detected in the Banking System as a Proportion of the Notes in Circulation (in pieces) (April to March)

Denomination (₹)	2013-14			2014-15		
	Number of Counterfeit Notes	Notes in Circulation	FICN as a proportion of NIC	Number of Counterfeit Notes	Notes in Circulation	FICN as a proportion of NIC
1	2	3	4	5	6	7
2 and 5	1	11,698,000,000	0.00000000	0	11,672,000,000	0.00000000
10	157	26,648,000,000	0.00000001	268	30,304,000,000	0.00000001
20	87	4,285,000,000	0.00000002	106	4,350,000,000	0.00000002
50	6,851	3,448,000,000	0.00000199	7,160	3,487,000,000	0.00000205
100	118,873	14,765,000,000	0.00000805	181,799	15,026,000,000	0.0000121
500	252,269	11,405,000,000	0.00002212	273,923	13,128,000,000	0.00002087
1000	110,035	5,081,000,000	0.00002166	131,190	5,612,000,000	0.00002338
Total	**488,273**	**77,330,000,000**	**0.00000631**	**594,446**	**83,579,000,000**	**0.00000711**

FICN: Fake Indian Currency Notes. NIC: Notes in Circulation.
Note: Does not include counterfeit notes seized by the police and other enforcement agencies.

Box VIII.1
Efforts for Indigenisation of Currency Printing

India is the largest producer and consumer of currency notes, next only to China. Currency continues to be the dominant means of payment with the banknotes in circulation (in value terms) placed at ₹14.3 trillion as of end March 2015.

Sustained increase in demand for currency notes, exceeded the capacity of government note presses (at Nashik and Dewas) by the late 1980s. The Reserve Bank established two currency presses in 1996 at Mysore and Salboni through a wholly owned subsidiary of the Reserve Bank, the Bharatiya Reserve Bank Note Mudran Pvt. Ltd. (BRBNMPL), making the country self-reliant in currency note printing by 1999. Currently, more than 40 per cent of the currency notes circulated in India are printed by government presses while the remaining 60 per cent emanate from Reserve Bank currency presses. However, the Reserve Bank depends largely on imports for the main ingredients required for printing currency. In case of inks, India produces Offset and Intaglio ink while Optically Variable Ink is imported. Some of the security features, such as security thread and water mark used in the current series of banknotes are also imported. With regard to the paper used for banknotes, India produces only 5 per cent of the paper required annually for currency note printing, necessitating import of the rest. Dependence on imports makes the printing process of currency vulnerable in terms of price, quantity and timeliness.

The Reserve Bank has embarked on a multi-pronged strategy for the indigenisation of currency note printing, keeping in view the associated benefits of backward integration in the form of assured, smooth and timely supply, cost saving (by way of reduction in the import bill), employment generation and effective deterrent to counterfeiting. To enhance the pace of indigenisation, a paper mill is being set up in Mysore, with an annual capacity of 12,000 MT which will substantially meet the paper requirement for currency printing. The Reserve Bank is also making efforts to develop domestic capabilities in the area of security features of banknotes. In order to have a time-bound programme for indigenisation of security features, the Reserve Bank, in consultation with the Government of India has set up a high level steering committee (Chairman: Shri R. Gandhi) which will identify agencies/institutions that could be encouraged to develop indigenous security features over the next few years.

consultation with the Government of India, made concerted efforts towards indigenisation of currency printing (Box VIII.1), elongation of the life of banknotes and resolution of issues associated with the shape and size of coins.

DEPARTMENT OF CURRENCY MANAGEMENT

VIII.15 On issues in currency management, the Department of Currency Management (DCM) plays a pivotal role in ensuring continuous supply and circulation of adequate quantities of clean banknotes and good coins of various denominations across the country. During 2014-15, the goals set for the Reserve Bank included field trial of plastic banknotes, exploring alternatives for extending the life of banknotes, harnessing technological advancements in the area of storage, transport, distribution; setting up a fully automated cash processing centre (CPC) on a pilot basis, introduction of new series of banknotes to leverage the latest innovations of currency note printing technology to stay ahead of counterfeiters, redesigning coins to make them user friendly and long lasting, and improving banknote packaging to facilitate handling and making operational processes more labour friendly.

Agenda for 2014-15: Implementation Status

Field Trial of Plastic Banknotes

VIII.16 The request for proposal for supply of plastic Indian banknotes in the denomination of ₹10 was issued and its technical evaluation undertaken. However, certain technical infirmities emerged and the process could not be taken further.

Exploring Alternatives for Extending the Life of Banknotes

VIII.17 A committee comprising stakeholders and research institutions was constituted to evaluate means to elongate the life of banknotes. A study on the subject has been taken up and is expected to be completed in 2015-16.

Fully Automated Cash Processing Centres

VIII.18 It was felt that a hub and spoke model would lead to greater efficiency. Accordingly, commercial banks were encouraged to set up such processing centres and two banks have commenced establishment of CPCs.

Staying Ahead of Counterfeiters

VIII.19 Banknotes in the denomination of ₹100 with a new numbering pattern were introduced during the year. The new numbering pattern will be introduced in a phased manner in all other denominations. In June 2015, the process of introduction of new security features was taken forward through issuance of a global pre-qualification bid for supply of security features.

Redesigning Coins and Improving Banknote Packaging

VIII.20 The Government of India has decided to constitute a committee to look into the shape and size of coins. The Reserve Bank will be associated with the same. It was decided, in consultation with stakeholders, to introduce corrugated fibre boxes for packing of banknotes in accordance with the International Labour Organisation (ILO) Convention 127 and recommendation 128 (wherein, maximum weight to be carried by an adult workman should not exceed 55 kg). Such boxes will be more environment friendly than wooden boxes which are presently in use. Two of the printing presses have commenced supplies of banknotes in the new corrugated fibre boxes.

Agenda for 2015-16

VIII.21 Taking forward the activities initiated in 2014-15 in the areas of introduction of new series of banknotes, new numbering pattern, braille like signs for the differently abled, and clean note policy, the Reserve Bank plans the following initiatives during 2015-16: towards elongating the life of banknotes, a development tender on plastic banknotes will be considered. Further, the project of exploring other alternatives for increasing the life of banknotes will be taken forward.

Customer Service

VIII.22 The scheme of incentives and penalties for banks for provision of banknotes and coin related services will be rationalised. The distribution network of banknotes and coins will be strengthened by encouraging alternate means, including leveraging technology. Further, note refund rules which were last reviewed in 2009, will be taken up for further refinement. The Reserve Bank will continue with its medium/long term objective of indigenisation of security features for Indian banknotes.

BHARATIYA RESERVE BANK NOTE MUDRAN PRIVATE LIMITED (BRBNMPL)

VIII.23 To augment the production of banknotes and to bridge the gap between their demand and supply in the country, BRBNMPL was established by the Reserve Bank as its wholly owned subsidiary on February 3, 1995. The company manages two presses, one in Mysore in Karnataka and the other in Salboni in West Bengal.

VIII.24 BRBNMPL produces 60 per cent of the annual requirement of banknotes and had supplied 15,515.88 million banknotes to the Reserve Bank as at end-March, 2015. It recorded a net profit after tax of ₹1.38 billion during 2014-15 as against a net profit after tax of ₹1.33 billion in the previous year.

VIII.25 The company has been continually enhancing productivity and operational efficiency through research and development activities and process innovations. It has established testing and research facilities at its laboratories in Mysore and Salboni for ensuring strict quality controls. These laboratories are currently focused on enhancing the life of banknotes, selection and evaluation of substrates for banknotes, comparison of various materials and their properties, and evaluation of security features.

VIII.26 The Bank Note Paper Mill India Private Limited (BNPMIPL) in Mysore, with a capacity of 12,000 tonnes per annum was established in October 2010 as an equal joint venture between the Government of India owned SPMCIL and the Reserve Bank subsidiary BRBNMPL. However, glitches arising out of the processes and modalities of securing statutory approvals from the concerned agencies impeded operationalisation of the facility. It is expected to commence production in 2015-16. This facility is expected to lead to self-sufficiency in manufacturing of paper for banknotes, substantially reducing imports.

IX PAYMENT AND SETTLEMENT SYSTEMS AND INFORMATION TECHNOLOGY

In pursuance of the vision of encouraging electronic payments and achieving a less cash society, the Reserve Bank continued its endeavour to have safe, inclusive and efficient payment systems in the country. Initiatives in this direction included rationalisation of policies relating to ATM transactions, prepaid payment instruments, white label ATMs and relaxation of additional factor of authentication for small value contact-less card present payments. In addition, the Reserve Bank also initiated the process of infrastructure enhancement in bill payments and MSME bill discounting segments by putting in place policy framework for setting up of Bharat Bill Payment System (BBPS) and Trade Receivables Discounting System (TReDS). The Reserve Bank also undertook a slew of in-house IT initiatives to brace up with the emerging challenges.

DEPARTMENT OF PAYMENT AND SETTLEMENT SYSTEMS

IX.1 Efficient and secure payment and settlement systems are essential components of a well-developed financial system. The department being the nodal wing of the Reserve Bank in matters of payment and settlement systems, focused towards migrating to a less cash society and on enhancing the efficiency and security of electronic transactions, while at the same time improving convenience of operations. Another key area of focus was enhancing access to finance through strengthening the inter-operable payment system infrastructure and putting in place a firm legal basis for payment system activities in conformity with international standards. With a view to ensuring seamless financial transactions, the Reserve Bank has been leveraging technology to upgrade the payment and settlement systems on a continuous basis over the years, resulting in a gradual shift from cash and paper based transactions to electronic modes of payments. The Reserve Bank while taking all these steps, recognised developments in technology and provided a facilitating environment for innovations in the payments sphere.

TREND AND PROGRESS IN PAYMENT SYSTEMS

IX.2 The electronic payment systems registered high volumes in 2014-15, following the determined efforts made by the Reserve Bank for migration to electronic payments (Table IX.1). Correspondingly, transactions processed by the paper-based clearing systems have shown a continuous decline both in volume and value terms. Overall, the payment and settlement systems posted a higher growth of 27.1 per cent in volume and a lower growth of 5.4 per cent in value in 2014-15 in relation to the previous year.

Paper clearing

IX.3 The share of paper-based transactions in total transactions continued to show a declining trend over the years. In volume terms, paper-based transactions accounted for 25.4 per cent of the total transactions during 2014-15, down from 33.9 per cent in the previous year. Their share in value terms also declined to 5.4 per cent from 6.2 per cent.

Retail electronic payments

IX.4 The growth in retail electronic payments has been encouraging both in terms of coverage and usage. As on March 31, 2015, the national

Table IX.1: Payment System Indicators - Annual Turnover

Item	Volume (million)			Value (₹ billion)		
	2012-13	2013-14	2014-15	2012-13	2013-14	2014-15
1	2	3	4	5	6	7
Systemically Important Financial Market infrastructures (SIFMIs)						
1. RTGS	68.5	81.1	92.8	676,841.0	734,252.4	754,032.4
Total Financial Markets Clearing (2+3+4)	**2.3**	**2.6**	**3.0**	**501,598.5**	**621,569.6**	**672,455.6**
2. CBLO	0.2	0.2	0.2	120,480.4	175,261.9	167,646.0
3. Government Securities Clearing	0.7	0.9	1.0	119,948.0	161,848.2	179,372.0
4. Forex Clearing	1.4	1.5	1.8	261,170.1	284,459.5	325,437.6
Total SIFMIs (1 to 4)	**70.8**	**83.7**	**95.7**	**1,178,439.5**	**1,355,822.0**	**1,426,488.0**
Retail Payments						
Total Paper Clearing (5+6+7)	**1,313.7**	**1,257.3**	**1,195.8**	**100,181.8**	**93,316.0**	**85,439.3**
5. CTS	275.0	591.4	964.9	21,779.5	44,691.4	66,769.9
6. MICR Clearing	823.3	440.1	22.4	57,504.0	30,942.8	1,850.4
7. Non-MICR Clearing	215.3	225.9	208.5	20,898.3	17,681.8	16,819.0
Total Retail Electronic Clearing (8+9+10+11+12)	**694.1**	**1,108.3**	**1,687.4**	**31,881.1**	**47,856.3**	**65,365.5**
8. ECS DR	176.5	192.9	226.0	1,083.1	1,268.0	1,739.8
9. ECS CR	122.2	152.5	115.3	1,771.3	2,492.2	2,019.1
10. NEFT	394.1	661.0	927.6	29,022.4	43,785.5	59,803.8
11. Immediate Payment Service (IMPS)	1.2	15.4	78.4	4.3	95.8	581.9
12. National Automated Clearing House (NACH)	-	86.5	340.2	-	214.8	1,220.9
Total Card Payments (13+14+15)	**932.6**	**1,261.8**	**1,737.7**	**2,052.1**	**2,575.4**	**3,324.5**
13. Credit Cards	396.6	509.1	615.1	1,229.5	1,539.9	1,899.2
14. Debit Cards	469.1	619.1	808.1	743.4	954.5	1,213.4
15. Prepaid Payment Instruments (PPIs)	66.9	133.6	314.5	79.2	81.0	211.9
Total Retail Payments (5 to 15)	**2,940.3**	**3,627.4**	**4,620.9**	**134,115.0**	**143,747.7**	**154,129.3**
Grand Total (1 to 15)	**3,011.1**	**3,711.1**	**4,716.6**	**1,312,554.5**	**1,499,569.7**	**1,580,617.3**

- : Not applicable

Note: 1. Real Time Gross Settlement (RTGS) system includes customer and inter-bank transactions only.
2. Settlement of Collateralised Borrowing and Lending Obligation (CBLO), government securities clearing and forex transactions is through the Clearing Corporation of India Ltd. (CCIL).
3. Consequent upon migration of total cheque volume to the cheque truncation system (CTS), there is no Magnetic Ink Character Recognition (MICR) Cheque Processing Centre (CPC) location in the country as of now.
4. The figures of cards are for transactions at point of sale (POS) terminals only.
5. The National Automated Clearing House (NACH) system was started by the National Payments Corporation of India (NPCI) (on December 29, 2012), to facilitate inter-bank, high volume, electronic transactions which are repetitive and periodic in nature.
6. Figures in the columns might not add up to the total due to rounding off of numbers.

electronic funds transfer (NEFT) facility was available through 121,845 branches of 161 banks, in addition to the business correspondent (BC) outlets. NEFT handled 928 million transactions valued at around ₹60 trillion in 2014-15 as against 661 million transactions for ₹44 trillion in the previous year. During the month of March 2015, NEFT processed the largest ever monthly volume of 106 million transactions.

IX.5 The increasing trend is also reflected in case of bulk electronic payments systems [total of electronic clearing service (ECS) and National Automated Clearing House (NACH)]. Banks continued to use both NACH operated by National Payments Corporation of India (NPCI) as well as ECS operated by the Reserve Bank.

IX.6 As regards card transactions, during 2014-15, 615 million transactions valued at around ₹1.9

trillion were carried out through credit cards, while 808 million transactions valued at ₹1.2 trillion were carried out through debit cards. Transactions through prepaid payment instruments (PPIs) also grew substantially, recording 314 million transactions valued at ₹212 billion. Mobile banking service, which is a relatively newer entrant among the payment options, has shown encouraging growth and handled 171 million transactions valued at ₹1 trillion during the year.

Agenda for 2014-15: Implementation Status

Mobile banking

IX.7 As part of the agenda for 2014-15, it was planned that efforts would be made to provide a fillip to mobile banking and undertake necessary groundwork to put in place standards for customer on-boarding, security of transactions and redressal of customer grievances, besides engaging with stakeholders to explore the feasibility of having a standardised application for mobile banking across banks. The Reserve Bank issued necessary guidelines to banks in December 2014 to enhance the usage of mobile banking in the country. Banks were advised to provide their customers options for easy registration for mobile banking services, through multiple channels, including ATMs, thereby minimising the need for branch visit to avail such services. NPCI is in the process of facilitating mobile banking registration at ATMs on the National Financial Switch (NFS) network. Similarly, NPCI was advised with regard to setting standards for industry agreements between banks and mobile network operators (MNOs) for handling customer grievances, particularly in the context of the National Unified USSD (Unstructured Supplementary Service Data) Platform (NUUP).

Trade Receivables Discounting System (TReDS)

IX.8 In order to provide quick and efficient financing options for the micro, small and medium enterprises (MSME) segment, it was proposed to set up an electronic TReDS to bring together the MSME, their corporate buyers as well as financiers and reduce the constraints faced by the MSME segment in liquidity management. The participants in the TReDS will be corporate buyers, including government departments and public sector undertakings (PSUs). The system will also facilitate factoring of both receivables as well as payables. Accordingly, policy measures were taken towards setting up of TReDS. Seven applications received to set up TReDS are being scrutinised for consideration of their authorisation during 2015-16 under the Payment and Settlement Systems (PSS) Act, 2007.

Bharat Bill Payment Systems (BBPS)

IX.9 The guidelines for BBPS were issued in November 2014 as per the agenda for 2014-15. BBPS is being set up by NPCI as a pan-India integrated bill payment system under the PSS Act, 2007 offering inter-operable and accessible bill payment services to customers through a network of agents. It is expected to address the problems faced by consumers who are required to use multiple options (as put in place by respective billers) to meet their bills payment requirements. The process of authorisation of NPCI to act as a Bharat Bill Payment Central Unit (BBPCU) and authorisation of Bharat Bill Payment Operating Unit (BBPOU) will be completed during 2015-16.

Consolidation of Payment Systems

IX.10 The ECS suite and NACH provide similar services. As envisaged in the agenda for 2014-15, consolidation of these payment systems has commenced from December 2014 with migration of volume from the ECS suite to NACH and thus, almost all participants are on board in the NACH system.

Other developments during 2014-15

IX.11 In line with the objective of the department to enhance greater acceptance of electronic payments, the following policy changes were introduced during the year.

Expansion of infrastructure / service providers

IX.12 For ensuring availability of additional payment options, authorisation was issued to nine entities, increasing the number of authorised payment system operators to 63 in 2014-15. The number of entities authorised for operating PPIs increased to 34 with five entities authorised during 2014-15. The remaining four entities were authorised for the money transfer service scheme (MTSS) (cross-border inward remittances), white label ATMs (WLAs) and instant money transfer. As on March 31, 2015, there were 7,881 WLAs installed across the country, out of which 4,932 were in Tier III to VI centres.

IX.13 With expanding infrastructure and service providers, it is equally important that they operate as per the norms set out by the Reserve Bank. The Reserve Bank has accordingly devised an assessment template for retail payment systems. Non-bank entities were asked to submit a self-assessment as per the template.

Security and efficiency

IX.14 Security and efficiency of payment system infrastructure being critical in development of payment systems, the NEFT platform was migrated to UNIX platform under the data centre architecture, which not only enhanced the processing capacity but also addressed the concerns of business continuity. Similarly, in case of large value payment systems, activation of hybrid features in the revamped real time gross settlement (RTGS) system has facilitated the settlement of transactions on a gross basis as well as through multilateral off-setting. Further, to enhance the efficiency and customer service aspects, acceptance of future value-dated transactions for settlement (up to three business days) has been activated, and the business hours of RTGS have been extended.

IX.15 With a view to mitigating certain risks in large value payment systems, the Clearing Corporation of India Limited (CCIL) took several initiatives. CCIL migrated its USD-INR settlement of inter-bank forex transactions to a payment *versus* payment (PvP) mode in April 2015 addressing the Herstatt risk[1]. It has carried out the first cycle of portfolio compression in the forex forward segment, achieving a compression of about 62 per cent and thereby, reducing counterparty exposure. CCIL is also carrying out exposure checks in the forex forward rupee derivatives segment on an online basis for interest rate swap (IRS)/forward rate agreement (FRA) trades which facilitate checking the adequacy of margins in advance and thereby, mitigating the risk of rejection of trades by CCIL.

Customer convenience and innovations

IX.16 With the objective of ensuring convenience in the use of the payment system and also to facilitate the migration to electronic payments, the policy guidelines related to PPIs, mobile banking, usage of ATMs and additional factor of authentication (AFA[2]) were amended.

IX.17 The guidelines for issuance of PPIs were rationalised in December 2014 to ensure its

[1] The risk that one party in a foreign exchange trade pays out the currency it sold but does not receive the currency it bought, is called foreign exchange settlement risk or “Herstatt” risk.

[2] AFA is a security process in which the user provides additional means of identification, one of which is typically a physical token, such as a card, and the other of which is typically something memorised, such as a security code.

increased usage. The limit for full-KYC semi-closed PPIs was enhanced from ₹50,000 to ₹100,000; the validity of gift cards was increased from one year to three years; banks were allowed to issue multiple PPIs for dependent family members from full-KYC compliant bank accounts. In order to provide convenience to visiting foreign nationals and NRIs and also to reduce cash transactions emanating from this segment, banks were allowed to issue rupee denominated open system non-reloadable PPIs to visiting foreign nationals and NRIs during their stay in India, with the permissible ceiling on such PPIs being ₹200,000 with cash withdrawal restricted to ₹50,000 per month.

IX.18 The guidelines on WLAs were reviewed to allow for acceptance of international credit/debit/prepaid cards, besides the facility of dynamic currency conversion (DCC). WLA operators are now permitted to tie up with other commercial banks, besides the sponsor bank for supply of cash to the WLAs.

IX.19 Recognising the need for balancing aspects of security and convenience of card transactions, the requirement of AFA, which was earlier introduced for security of operations, was relaxed for small value card present transactions using contact-less EMV (*i.e.,* Europay, Mastercard and Visa) chip cards. Banks have also been advised to put in place suitable velocity checks while at the same time clearly indicate the maximum liability, if any, devolving on the customer.

Moving towards less cash

IX.20 Keeping in view the interoperable ATM infrastructure and the geographical dispersion of ATMs, the number of mandated free transactions at ATMs was rationalised in big cities. The minimum number of free transactions for savings bank account holders at other bank's ATMs was reduced to three per month from five in six metro centres. Further, banks were advised to provide their savings bank account holders with at least five free transactions per month at their own ATMs. Beyond the mandatory free ATM transactions, banks were permitted to charge their customers up to a maximum of ₹20 (plus service tax) per transaction. However, banks can put in place their own policies offering more number of free transactions at ATMs.

Sound legal framework and compliance with international standards

IX.21 A firm legal framework for payment systems is equally critical and hence, in conformity with the international standards, certain amendments to the PSS Act 2007 were introduced during the year.

IX.22 Following the global financial crisis, trade repositories (TR) and legal entity identifier (LEI) system have gained importance for strengthening the over the counter (OTC) derivatives markets. Further, the functioning of a central counter party (CCP) and legal certainty in the event of its insolvency is critical. In order to provide specific legal backing to close out netting in the event a CCP goes insolvent, as also for regulation and supervision of TR and local operating unit (LOU - an entity issuing LEI) by the Reserve Bank, after extensive deliberations by the Select Committee of the Rajya Sabha in which the Reserve Bank participated actively, amendments to the PSS Act, 2007 were carried out. This provides legal backing/clarity to various issues like close-out netting in the event of insolvency of a CCP; regulating and supervising TR; LOU under the LEI system; and protection of customer funds for systems operated by authorised non-bank entities.

IX.23 In terms of focus areas in large value payment systems, efforts were directed at compliance with the Principles for Financial Market Infrastructures (PFMIs) by Financial Market Infrastructures (FMIs). Towards this end, the Committee on Payments and Market Infrastructures-

International Organisation of Securities Commissions (CPMI-IOSCO) which has been carrying out the Level 1 assessment[3] against PFMIs, has rated the Indian jurisdiction as "4"[4], *i.e.,* final implementation measures are fully in force.

Other initiatives

IX.24 The Reserve Bank organised an international seminar in November 2014 at Kovalam, Kerala, with a focus on the evolving role of central banks in retail payments, cash to cashless, role of non-banks in retail payments, innovations in retail payments, government payments and remittances, risk management and security and financial inclusion. A 'Payment Systems Innovations Day' was organised in December 2014 to provide a platform for presenting the various innovations taking place in payment systems. The Reserve Bank hosted the 14th SEACEN Advanced Course on Payment and Settlement Systems for Emerging Economies during May 2015 with a special focus on 'Resilience of Payment Systems to Cyber Crime'.

Agenda for 2015-16

IX.25 The Reserve Bank would continue to encourage innovation in payment systems and play the role of a facilitator keeping the focus on safety and efficiency of payment systems. Given the fast changing payment landscape, the Reserve Bank will prepare a vision document for a 2/3 years horizon. The work with respect to authorisation of entities for operating TReDS and BBPS will be completed in 2015-16.

IX.26 In line with the endeavour to disincentivise cash transactions and incentivise card transactions, measures for enhancing card acceptance infrastructure by acquiring banks will be examined and policy framework on ATMs and cash at POS will be reviewed along with the interchange/ merchant discount rate (MDR) structure in consultation with all the stakeholders.

IX.27 With the growing e-commerce segment in the country, the role of payment aggregators and intermediaries is also increasing significantly. The Reserve Bank will engage with stakeholders to explore the need/feasibility of having a direct/ indirect regulatory framework for these entities. An assessment of RTGS against PFMIs would be undertaken in 2015-16 by the Reserve Bank.

IX.28 CCIL has been identified as LOU for issuing LEI and endorsed as pre-LOU by the Regulatory Oversight Committee (ROC). It has since commenced issuance of LEI in India. A roadmap for use of LEI will be drawn in consultation with the Securities and Exchange Board of India (SEBI).

DEPARTMENT OF INFORMATION TECHNOLOGY

IX.29 The department continued to focus on the Reserve Bank's IT vision of enabling the use of information technology (IT) as a strategic resource for bringing about overall efficiency in the Reserve Bank's operations, improving standards of services being provided to its customers, strengthening governance and facilitating analytical and information based decision making in a safe and secure IT based environment. Information Technology Sub Committee (ITSC) of the Central Board continued to provide guidance in furthering this vision. ITSC met three times during 2014-15

[3] Whether jurisdictions have completed the process of adopting the legislation and other policies implementing the 24 Principles for FMIs and four of the five Responsibilities for authorities within the regulatory framework that applies to FMIs.

[4] Rating Level 1: Draft implementation measures not published; Rating Level 2: Draft implementation measures published; Rating Level 3: Final implementation measures published; Rating Level 4: Final implementation measures fully in force; Rating Level NA: No implementation measures needed (*i.e.*, not applicable).

and discussed major issues relating to IT projects and information security in the Reserve Bank; data warehouse; audits pertaining to information security; operations of the data centres (DCs); efficacy of disaster recovery drills; and working of the office of the chief information security officer (CISO).

Agenda in 2014-15: Implementation Status

Enterprise knowledge portal (EKP)

IX.30 The revamped EKP, launched in November 2013 provides a knowledge sharing platform within the Reserve Bank. During 2014-15, the portal was further enhanced with features like e-learning modules and improved search options. They were well received by users resulting in increased usage of the portal.

Video conferencing (VC) system

IX.31 The VC within the Reserve Bank which was upgraded in 2013-14 witnessed large scale usage; 532 VC sessions involving multiple locations were held during 2014-15, in addition to point-to-point user-based sessions. This has reduced the need for physical meetings.

Mail messaging system (MMS)

IX.32 The Reserve Bank's corporate mail messaging system was reinforced with advanced archival solutions which ushered in ease of usage and enhanced security. The up-gradation work on hardware commenced during the year and after its installation, the migration process to the new system is expected to be completed by the end of September 2015.

Committee on data standardisation

IX.33 A Committee on Data Standardisation (Convener: Shri P. Parthasarathi) which was constituted to bring about synergy and uniformity in the efforts being undertaken in the areas of data reporting and data standardisation, placed its draft report in the public domain for feedback. Based on the inputs received, the committee has finalised its report. Work on implementation of the recommendations has since commenced.

Enhancements in core banking system (CBS) and stabilisation of e-treasury

IX.34 E-Kuber, the CBS of the Reserve Bank was introduced in 2012 for banks to participate in government borrowing programmes, liquidity adjustment operations and current account operations. During 2014-15, changes were made to e-Kuber to provide for the deployment of cash balances of the government (also see chapter VII). The Depositor's Education and Awareness (DEA) Fund scheme was implemented in e-Kuber at the very outset, enabling a flow of around ₹45 billion into the fund within two days. Treasury operations of the Department of External Investments and Operations of the Reserve Bank were successfully migrated from a legacy system to e-Kuber. This implementation, the first of its kind amongst central banks worldwide has brought in operational efficiency and unification of accounting processes.

Agenda for 2015-16

IX.35 The major initiatives planned for 2015-16 are discussed below.

Establishment of an IT subsidiary of the reserve bank

IX.36 Central banking operations have undergone a sea change thanks to the large scale integration of IT processes in banking. To handle the ever increasing complexities in a changing environment and to address cyber security and other related challenges, it is essential that a fully dedicated team of technical experts be continuously associated with this work. To this end, the Central Board of the Reserve Bank has approved the setting up of its IT Subsidiary. This initiative is being taken forward with guidance from experts in the industry.

Implementation of the electronic document management system (EDMS) within the Reserve Bank

IX.37 As a means towards large scale electronification of work processes within the Reserve Bank and to move towards a 'less paper' office environment, initiatives were undertaken to set up an electronic work flow and document management system along with data storage. The EDMS project, which commenced last year, is under progress. Given the enormous potential of the EDMS system on the overall efficiency of the Reserve Bank and its role in empowering its staff with knowledge, a comprehensive business process re-engineering (BPR) is being undertaken apart from evaluating the various software products available in the market. It is expected that a pilot implementation would commence during the first half of 2016.

Revamping of IT Infrastructure at DCs

IX.38 With the increased application systems operating from DCs and higher requirement of electric power, it is essential to improve the existing infrastructure at the DCs. Keeping in view the need to be environment friendly, work on virtualisation of hardware servers has commenced. As a first step, the migration of the RTGS system to a new IBM mainframe system was completed during the year.

Implementation of information security operating centre (ISOC)

IX.39 To handle enterprise wide IT security, ISOC is being set up. The project commenced with the issue of expression of interest (EOI) followed by the shortlisting of potential bidders. The tendering process has commenced and the project is expected to be completed by April 2016.

Extension of e-receipts and e-payments across all States using e-Kuber CBS

IX.40 The standardised e-receipt and e-payment functionalities using e-Kuber was demonstrated to most of the States, as well as in the recently held Conference of the State Finance Secretaries. In sequel, State Governments of West Bengal, Uttarakhand, Tamil Nadu and Kerala started using the system in 2014-15. The other states are at different stages of implementation. Efforts will be focussed on scaling up use of the system across all the major states in 2015-16.

Integrating currency management functions with CBS

IX.41 Accounting of currency movement and reporting is a potential area for integration with e-Kuber. A study of the system requirements, reverse presentation, discussions, design, development, testing and rollout of the modules will be undertaken during 2015-16 to facilitate its integration.

X GOVERNANCE, HUMAN RESOURCES AND ORGANISATIONAL MANAGEMENT

At the onset of its 81st year, the Reserve Bank rearticulated its core purpose, values and vision in 2014-15. The organisational structure was fine-tuned to create synergies and improve the effectiveness of the delivery mechanism. It continued to place focus on upgrading its human resources through training and providing diverse exposures. It also organised conferences, seminars and outreach programmes during the year to disseminate research and promote knowledge sharing. The Reserve Bank adopted an enterprise-wide risk management framework to ensure business continuity and for effectively managing various risks that it faces in its operations and functioning. It also took steps to focus on international financial diplomacy and participation in global regulatory standards.

X.1 This chapter discusses three critical ingredients of the Reserve Bank - governance, human resources and organisational management apart from covering the activities of a number of departments dealing with communication, international relations, banking services to the government and banks, forex reserves management, economic research, statistics, legal matters, corporate strategy and budgeting, corporate support services, Rajbhasha and premises. During 2014-15, the Reserve Bank sought to further improve its governance, management and operational framework through re-articulation of its core purpose, values and vision. The organisational structure was streamlined further to create functional synergies and optimise the delivery of output both in terms of quantity and quality keeping in view the evolving operating environment. Developing human resources through an appropriate incentive structure, including training, exposure and rotation to harness the potential of its staff members for effective delivery was a major area of focus. Through its communication policy, the Reserve Bank sought to reach out to the wider public in pursuance of transparency, knowledge sharing and creating awareness about financial risks faced by the public in day-to-day life. Risk management and audit operations of the Reserve Bank placed a greater focus on a holistic approach to ensure business continuity.

GOVERNANCE STRUCTURE

X.2 The Reserve Bank seeks to uphold the highest standards in corporate governance, independence and quality of decision making while discharging its core functions and staying committed to its values in terms of a corporate code of ethics. The governance structure of the Reserve Bank ensures that its general policy, strategy, administration and business are aligned with its core purpose and that the processes followed are compliant with its shared values. The Secretary's Department which acts as the secretariat to the Central Board provides support services to the top management.

X.3 The Central Board of Directors is the apex body in the governance structure. With the Governor in the chair, it comprises of four Deputy Governors of the Reserve Bank, Government nominees and independent directors, who are eminent achievers in different fields commensurate with the Reserve Bank's objectives. There are four Local Boards for the Northern, Southern, Eastern and Western areas of the country to take care of local interests. The Government of India appoints/nominates directors to the Central Board and members to Local Boards in accordance with the Reserve Bank of India (RBI) Act, 1934. The Central Board is assisted by three committees - Committee of the Central Board

(CCB), Board for Financial Supervision (BFS) and Board for Regulation and Supervision of Payment and Settlement Systems (BPSS). In addition, the Central Board also has four sub-committees – the Audit and Risk Monitoring Sub-Committee, the Human Resource Management Sub-Committee, Building Sub-Committee and Information Technology Sub-Committee.

Meetings of the Central Board and the CCB

X.4 The Central Board held six meetings in 2014-15 in Chennai, New Delhi (two meetings), Kolkata, Hyderabad and Goa. The Hon'ble Finance Minister of India addressed the two post-budget meetings held in New Delhi on August 10, 2014 and March 22, 2015. The Governor interacted with the chief ministers of the concerned state governments and senior officials of commercial banks and financial institutions on the sidelines of some of these meetings.

X.5 The CCB held 46 meetings during the year out of which 22 were held through electronic mode, obviating the need for physical assembly at a common location. The committee attended to the current business of the Reserve Bank, including approval of its Weekly Statement of Affairs pertaining to the Issue and the Banking departments. A Standing Committee of the Central Board held two meetings to discuss region-specific issues and concerns.

Central Board/ Local Boards – Changes

X.6 Shri Rajiv Mehrishi, Finance Secretary, Government of India and Dr. Hasmukh Adhia, Secretary, Department of Financial Services, Ministry of Finance, Government of India were nominated as Directors on the Central Board under Section 8(1)(d) of the RBI Act, 1934 with effect from November 25, 2014 and November 11, 2014 *vice* Dr. Arvind Mayaram and Dr. Gurdial Singh Sandhu, respectively. Shri Ajay Tyagi, Additional Secretary (Investment), Department of Economic Affairs, Ministry of Finance, Government of India was nominated by the Central Government as Director on the Central Board under Section 8(1)(d) of the RBI Act, 1934 in terms of notification dated June 22, 2015 *vice* Shri Rajiv Mehrishi.

X.7 Shri Kamal Kishore Gupta and Shri Mihir Kumar Moitra ceased to be members of the Northern Area Local Board with effect from August 25, 2014 and September 23, 2014, respectively, in terms of the provisions of Section 9(3) of the RBI Act, 1934.

Attendance of Directors

X.8 The details of participation of the directors in the meetings of the Central Board are given in Table X.1.

Table X.1: Attendance of Directors - 2014-15

Name	Appointed/ Nominated under RBI Act, 1934	No. of Meetings held	No. of Meetings Attended
1	2	3	4
Raghuram G. Rajan	8 (1) (a)	6	6
Harun R. Khan	8 (1) (a)	6	6
Urjit R. Patel	8 (1) (a)	6	5
R. Gandhi	8 (1) (a)	6	6
S.S. Mundra	8 (1) (a)	6	5
Anil Kakodkar	8 (1) (b)	6	5
Kiran S. Karnik	8 (1) (b)	6	6
Nachiket Mor	8 (1) (b)	6	6
Y.H. Malegam	8 (1) (c)	6	6
Dipankar Gupta	8 (1) (c)	6	3
G.M. Rao	8 (1) (c)	6	5
Ela Bhatt	8 (1) (c)	6	5
Indira Rajaraman	8 (1) (c)	6	6
Y.C. Deveshwar	8 (1) (c)	6	2
Damodar Acharya	8 (1) (c)	6	6
Arvind Mayaram*	8 (1) (d)	3	1
Gurdial Singh Sandhu**	8 (1) (d)	3	1
Hasmukh Adhia #	8 (1) (d)	3	1
Rajiv Mehrishi ##	8 (1) (d)	3	1

* : Ceased to be director w.e.f. November 25, 2014;
** : Ceased to be director w.e.f. November 11, 2014;
\# : Nominated as director w.e.f. November 11, 2014;
\##: Nominated as director w.e.f. November 25, 2014.

Executive Directors - Changes

X.9 Shri B. Mahapatra and Shri G. Padmanabhan, Executive Directors retired on August 31, 2014 and May 31, 2015, respectively. Dr. Michael D. Patra, Shri K.K. Vohra and Shri G. Mahalingam were promoted as Executive Directors effective October 7, 2014. Smt. Meena Hemachandra was promoted as Executive Director effective June 1, 2015.

Obituary

X.10 Shri Suresh Neotia, Director of the Central Board from June 27, 2006 to September 23, 2011, passed away in Kolkata on May 7, 2015. Dr. A.P.J. Abdul Kalam, Director of the Central Board from November 27, 2000 to June 14, 2002 passed away in Shillong on July 27, 2015.

Visits of Foreign Dignitaries/Delegations

X.11 Twenty delegations from 12 countries visited the Reserve Bank during the year. They interacted with the top management on a wide range of bilateral and global issues and on the Reserve Bank's policy initiatives in different areas of its functioning. Foreign dignitaries who visited the Reserve Bank during 2014-15 included H.M. Queen Maxima of the Netherlands, United Nations' Secretary-General's Special Advocate for Inclusive Finance for Development; Rt. Hon. George Osborne, Chancellor of Exchequer, UK; Ms. Penny Pritzker, US Secretary of Commerce; Mr. Bill Gates and his team; Dr. Valiollah Seif, Governor, Central Bank of Iran; Rt. Hon. Alan Yarrow, Lord Mayor of the City of London; Hon. Andrew Robb, MP, Australian Minister for Trade and Investment; Mr. Jacob J. Lew, US Treasury Secretary; Mr. Stanley Fischer, Vice-Chairman, Central Board of Governors, Federal Reserve System and Ms. Christine Lagarde, Managing Director, IMF.

Measures to Improve Governance

X.12 Measures were taken during the year to enhance the quality of corporate governance while simultaneously reducing its cost. The Reserve Bank, as it entered the 81st year of its establishment, rearticulated, in contemporary terms, its core purpose as given in the preamble to the RBI Act, 1934 (Box X.1).

Box X.1
Reserve Bank of India: Core Purpose, Values and Vision Statement

As the Reserve Bank entered the 80th year of its existence, a need was felt to rearticulate in contemporary terms its core purpose as given in the preamble to the RBI Act, 1934, the founding statute of the Reserve Bank. The purpose was to delineate the Reserve Bank's strategic objectives and provide a framework and backdrop within and against which the Reserve Bank's policies will be formulated and the direction that it will chart. Accordingly, the Reserve Bank issued its 'Core Purpose, Values and Vision' statement in April 2015, which is available at the Bank's website.

Core Purpose

To foster monetary and financial stability conducive to sustainable economic growth and to ensure the development of an efficient and inclusive financial system.

The Core Purpose reflects the Reserve Bank's commitment to the nation:

To foster confidence in the internal and external value of the rupee, and contribute to macro-economic stability;

To regulate markets and institutions under its ambit to ensure financial system stability and consumer protection;

To promote the integrity, efficiency, inclusiveness and competitiveness of the financial and payments system;

To ensure efficient management of currency as well as banking services to the government and banks; and

To support the balanced, equitable and sustainable economic development of the country.

Values

The Reserve Bank of India commits itself to the following shared values that guide organisational decisions and employee actions in pursuit of the Reserve Bank's core purpose:

(Contd....)

Public Interest

The Reserve Bank of India, in its actions and policies, seeks to promote public interest and the common good.

Integrity and Independence of Views

The Reserve Bank of India seeks to maintain the highest standards of integrity and independence of views through openness, trust and accountability.

Responsiveness and Innovation

The Reserve Bank of India seeks to be a dynamic organisation responsive to public needs and encourages innovation and a spirit of enquiry.

Diversity and Inclusiveness

The Reserve Bank of India cherishes and supports diversity and inclusiveness.

Introspection and Pursuit of Excellence

The Reserve Bank of India is committed to self-appraisal, introspection and professional excellence.

Vision

The Reserve Bank of India is committed to pursue public interest and common good as a leading central bank that is recognised for its credible, transparent and proactive policies.

X.13 Important items to be placed before the Board are now brainstormed in an informal pre-Board meeting so as to improve the quality of decision making by the Board. The Reserve Bank of India General Regulations were amended during the year to enable fortnightly meetings of CCBs, if felt necessary in the future, in place of weekly meetings. In the forthcoming year, the Reserve Bank will continue to look for ways to further streamline the decision making process.

COMMUNICATION PROCESSES

X.14 The Reserve Bank has been pursuing a dynamic communication policy enabling swift response to domestic and international developments. The Department of Communication (DoC) as the nodal wing has endeavoured to build and nurture a fruitful partnership between the Reserve Bank and the public through a two-way communication: transparent, timely and credible dissemination and feedback.

Agenda for 2014-15: Implementation Status

Refurbishing the Website

X.15 In April 2015, a refurbished website of the Reserve Bank was launched providing a more user friendly access to function-wise information, search facility and an accessibility toolbar for users with disabilities. The website is now integrated with two social media sites, Twitter and YouTube. Accordingly, the Governor's post monetary policy conferences were disseminated *via* YouTube this year in addition to usual live streaming media.

Awareness Campaigns and Outreach Programmes

X.16 In view of increasing public victimisation to fictitious offers, the Reserve Bank undertook a campaign jointly with the Ministry of Consumer Affairs under its '*Jago Grahak Jago*' initiative to caution the public about the menace of fictitious mails. The public awareness drive was conducted in the print media. Besides, an awareness campaign was also carried out on security features of currency notes.

Workshops for Top Management, Officers and Media

X.17 During the year, two workshops on effective media management, one each for the top executives, and the newly appointed regional directors and chief general managers were conducted. A workshop on writing skills for managers and assistant general managers was also conducted. Besides, several informal briefings/workshops were arranged for the media on the Reserve Bank's reports and releases.

Review of Communication Policy

X.18 With the adoption of flexible inflation targeting, the role of communication has assumed further importance, particularly for anchoring inflation expectations. In this backdrop as also in view of several external and internal developments, the communication policy of the Reserve Bank is currently being reviewed by a Committee (Chairman: Dr. Michael D. Patra) which is expected to submit its report during 2015-16. Towards improving internal communication in the Reserve Bank, two Banking Hall events for Reserve Bank employees were arranged with the Governor, one in Bangalore and the other in Chandigarh in 2015.

Agenda for 2015-16

X.19 During 2015-16, multi-pronged engagement/outreach/campaigns with stakeholders along those held last year will be continued. It is planned to add social media like Facebook and LinkedIn to the Reserve Bank website, making it accessible to youth. A workshop for media in Nepal is scheduled to be conducted during 2015-16. Follow up steps will also be taken in the light of the forthcoming report of the Committee to Review the Communication Policy of the Reserve Bank.

HUMAN RESOURCE INITIATIVES

X.20 The Reserve Bank has a wide canvas of operations, requiring a robust set of internal capabilities to fulfill its mandate. The human resource strategies and initiatives led by the Human Resource Management Department (HRMD) are, therefore, designed and developed as a two-way interface between the environment, the internal capacities, the setting of goals at the corporate level as well as at the department and functional levels.

Agenda for 2014-15: Implementation Status

X.21 In 2014-15, organisational restructuring was carried out by the Reserve Bank following a cluster approach, that is, by clubbing closely related work areas to better serve the evolving financial sector (Box X.2).

Training

X.22 The skill and knowledge development initiatives focused on strengthening technical and

Box X.2
Organisational Restructuring of the Reserve Bank

The Reserve Bank has, in the recent past, been deliberating on a range of strategic considerations for adopting a more flexible and responsive organisational structure for enhanced performance in an increasingly dynamic business environment. As part of this process, a Committee on Organisational Restructuring of the Reserve Bank (Chairman: Shri Deepak Mohanty; Co-Chairman: Shri B. Mahapatra) was set up. Broadly based on the recommendations of the committee and the outcomes of an elaborate internal consultative process, the organisational restructuring of the Reserve Bank was effected from November 3, 2014.

As part of the restructuring exercise, two new departments have been constituted in the Reserve Bank: (i) Department of Corporate Services, and (ii) International Department. Alongside, some of the existing departments have been rechristened and new units set up/being set up within some departments as detailed in Tables 1-3.

Table 1: Renaming of the departments

Old Nomenclature	New nomenclature
Department of Banking Operations and Development (DBOD)	Department of Banking Regulation (DBR)
Rural Planning and Credit Department (RPCD)	Financial Inclusion and Development Department (FIDD)
Customer Services Department (CSD)	Consumer Education and Protection Department (CEPD)
Department of Expenditure and Budgetary Control (DEBC)	Corporate Strategy and Budget Department (CSBD)

(Contd....)

Table 2: Creation/carving out of new departments

Existing department	Name of the new department	Remarks
Urban Banks Department (UBD)	Department of Cooperative Bank Regulation (DCBR) Department of Cooperative Bank Supervision (DCBS)	UBD will cease to exist
Financial Markets Department (FMD)	Financial Markets Regulation Department (FMRD) Financial Markets Operations Department (FMOD)	FMD will cease to exist
Department of Non-Banking Supervision (DNBS)	Department of Non-Banking Regulation (DNBR) Department of Non-Banking Supervision (DNBS)	Regulation hived off from DNBS

Table 3: Creation of new units

Existing department	Name of the new unit
Department of Statistics and Information Management (DSIM)	Data and Information Management Unit (DIMU) within DSIM.
Monetary Policy Department (MPD)	Forecasting and Modelling Unit within MPD.
Human Resource Management Department (HRMD)	HR Operations Unit within HRMD.
Financial Markets Regulation Department (FMRD)	Market Intelligence Unit within FMRD.

Similarly the regional offices (ROs) of the Reserve Bank have been categorised into three tiers. Tier-I or Metro ROs will now comprise of four offices of the Reserve Bank in Mumbai, New Delhi, Kolkata and Chennai. Tier-II or Non-Metro ROs will comprise 14 ROs; (i) Ahmedabad; (ii) Bengaluru; (iii) Bhopal; (iv) Bhubaneswar; (v) Chandigarh; (vi) Guwahati; (vii) Hyderabad; (viii) Jaipur; (ix) Jammu; (x) Kanpur; (xi) Lucknow; (xii) Nagpur; (xiii) Patna; and (xiv) Thiruvananthapuram. Tier-III ROs will comprise of 10 small offices: (i) Agartala; (ii) Belapur; (iii) Dehradun; (iv) Gangtok; (v) Kochi; (vi) Panaji; (vii) Raipur; (viii) Ranchi; (ix) Shillong; and (x) Shimla.

The restructured ROs depending on size and volume of work will have the following clusters:

Tier I and II will have four clusters: (i) Supervision, Market Intelligence and Research; (ii) Currency and Banking Services; (iii) Financial Inclusion and Customer Service; and (iv) Human Resources Management (HRM) and Infrastructure.

Tier III will have three clusters: (i) Supervision and Market Intelligence; (ii) Financial Inclusion/Financial Literacy, Public Awareness, Customer Service, and Research; and (iii) HRM and Infrastructure.

It is expected that this organisational restructuring will bring greater managerial synergies and also allow the Reserve Bank staff members to better develop their expertise in various key work areas.

behavioural skills so as to facilitate personal growth and improve effectiveness at work. Six training establishments of the Reserve Bank catered to its training requirements (Table X.2).

Training at External Institutions

X.23 During 2014-15, a number of officers were deputed to participate in training programmes, seminars and conferences organised by external

Table X.2: Reserve Bank Training Establishments: Number of Programmes Conducted (July-June)

Training Establishment	2012-13		2013-14		2014-15	
	Programmes	Participants	Programmes	Participants	Programmes	Participants
1	2	3	4	5	6	7
RBSC, Chennai	126	2,676	105	2,560	141	2,626*
CAB, Pune	164	5,105	127	3,909	215	7,183@
4 ZTCs (Class I)	116	2,526	99	2,222	104	2,215
4 ZTCs (Class III)	64	1,492	70	1,510	98	2,036
4 ZTCs (Class IV)	58	1,184	37	725	53	1,041

*: Includes 30 foreign participants; @: Includes 63 foreign participants; RBSC: Reserve Bank Staff College, Chennai; ZTC: Zonal Training Centre.

management/banking institutions in India and abroad (Table X.3). Further, a number of Class III and Class IV employees were trained in external institutions in India.

Golden Jubilee Scholarship and Study Leave

X.24 Under the Golden Jubilee Scholarship Scheme, six officers were selected to pursue higher studies in reputed universities abroad. Ten officers availed study leave under different schemes for pursuing higher studies during the year. Further, 599 employees pursued select part-time/distance education courses under the Reserve Bank's incentive scheme.

Grants and Endowments

X.25 Towards promoting research, training and consultancy in the banking and financial sector, the Reserve Bank provided financial support of ₹300 million to the Indira Gandhi Institute of Development Research (IGIDR), Mumbai; ₹140 million to the Centre for Advanced Financial Research and Learning (CAFRAL), Mumbai; ₹18.4 million to the National Institute of Bank Management (NIBM), Pune; ₹6.9 million to the Indian Institute of Bank Management (IIBM), Guwahati; and ₹10 million to the London School of Economics (LSE) India observatory and the IG Patel Chair.

RBIQ

X.26 Almost 5,000 schools and 10,000 students participated in RBIQ 2014, an all-India inter-school quiz launched by the Reserve Bank in 2012. It was held at 62 different locations all over India. The zonal and national finals were conducted in Mumbai and telecast on Doordarshan's National Channel.

Table X.3: Number of Officers Trained in External Training Institutions in India and Abroad

Year	Trained in India	Trained abroad
1	2	3
2012-13	874	510
2013-14	798	530
2014-15	913	562

Industrial Relations

X.27 Industrial relations remained by and large peaceful during 2014-15. Periodic meetings were held with recognised associations of officers and employees/workmen on various issues relating to service conditions and welfare of employees.

Superannuation Benefits

X.28 In 2003, the Reserve Bank, with the approval of the Central Board, had made some improvements in the monthly pension paid to employees who retired prior to November 1, 1997. However, the government had observed that the improvements in the pension scheme could not be effected without suitably amending Regulation 2(2) of the RBI Pension Regulations, 1990 and requested the Reserve Bank for their withdrawal. In October 2008, these improvements in monthly pension were withdrawn by the Central Board. This was, however, challenged in the High Court of Judicature in Bombay, where the Hon'ble High Court set aside the Reserve Bank's circular regarding withdrawal of improvements. Since then, there has been persistent demand from all the pensioners/retirees for improvements in pensions. However, the matter remains unresolved till date, though the Reserve Bank and the Government are fully engaged with the issue.

Recruitment and Staff Strength

X.29 With the recruitment of 784 employees in 2014, the total staff strength as on December 31, 2014, stood at 16,794 as compared with 17,360 a

Table X.4: Recruitment by the Reserve Bank in 2014 (January-December)

Category of recruitment	Category-wise strength				
	Total	*of which*		Per cent of total	
		SC	ST	SC	ST
1	2	3	4	5	6
Class I	182	27	13	14.8	7.1
Class III	120	15	7	12.5	5.8
Class IV					
(a) Maintenance Attendant	365	81	5	22.2	1.4
(b) Others	117	12	4	10.3	3.4
Total	**784**	**135**	**29**	**17.2**	**3.7**

SC: Scheduled Castes; ST: Scheduled Tribes.

year ago, the category-wise details of which are presented in Tables X.4 and X.5.

X.30 The Reserve Bank's management and representatives of the All India Reserve Bank Scheduled Castes/Scheduled Tribes and the Buddhist Federation met on four occasions in 2014 to discuss issues relating to the implementation of reservation policy in the Reserve Bank. The total number of Other Backward Classes (OBCs) (recruited after September 1993) in the Reserve Bank as on December 31, 2014, stood at 1,870, of which 533 were in Class I, 604 in Class III and 733 in Class IV.

X.31 The total strength of ex-servicemen in the Reserve Bank as on December 31, 2014, was 1,005. Out of these, 200 were in Class I, 147 in Class III and 658 in Class IV. The total number of physically handicapped employees in Class I, Class III and Class IV cadres stood at 234, 89 and 105 respectively, as on December 31, 2014. The cadre-wise composition of the staff strength as on June 30, 2015, is presented in Table X.6.

X.32 The Reserve Bank's offices in Mumbai (including the Central Office departments) continued to have the maximum share of total staff strength at 29.2 per cent (Table X.7).

Prevention of Sexual Harassment of Women at the Workplace

X.33 A new comprehensive set of guidelines was issued in 2014-15 in accordance with the Sexual Harassment of Women at Workplace (Prohibition, Prevention and Redressal) Act and Rules, 2013. The guidelines prescribe, among others, strict timelines for handling complaints and bestow significant powers, including levy of penalty to internal complaints committees. While no sexual harassment complaints were received in the Reserve Bank in 2014, awareness/orientation programmes at periodic intervals were conducted to sensitise staff/members of complaint committees on the legal provisions and the Reserve Bank's new guidelines in the matter.

Table X.5: Staff Strength of the Reserve Bank

Category	Category-wise strength						Per cent to total strength	
	Total Strength		SC		ST		SC	ST
	2013	2014	2013	2014	2013	2014	2014	
1	2	3	4	5	6	7	8	9
Class I	7,864	7,565	1,133	1,128	499	479	14.9	6.3
Class III	3,916	3,573	586	499	252	193	14.0	5.4
Class IV	5,580	5,656	1,764	1,740	463	446	30.8	7.9
Total	**17,360**	**16,794**	**3,483**	**3,367**	**1,214**	**1,118**	**20.0**	**6.7**

Note: Position as on December 31.

Table X.6: Reserve Bank's Staff Strength
(as on June 30, 2015)

Grade	Staff Strength
1	2
Grade A	4,077
Grade B	1,552
Grade C	1,025
Grade D	271
Grade E	353
Grade F	101
Total in class I	**7,379**
Special Assistant	815
Senior Assistant	247
Assistant	2,381
Word Processor Assistant	173
Secretarial Assistant	32
Others	272
Total in class III	**3,920**
Maintenance Staff	1,395
Technical Staff	135
Service Staff	3,127
Others	715
Total in class IV	**5,372**
Total Staff Strength	**16,671**

Right to Information (RTI)

X.34 The Reserve Bank received 8,044 requests for information and 1,021 first appeals under the RTI Act during 2014-15, all of which were attended to. Effective February 27, 2015, the Reserve Bank has aligned with the RTI online portal of the Government enabling the public to file online RTI applications and first appeals with the Reserve Bank. Four training programmes on the RTI Act for employees were conducted at the Reserve Bank's training centres.

Samadhan and Other Initiatives

X.35 The Reserve Bank has undertaken a HR transformation project, named *Samadhan*, to deliver uniform, automated and rule-based HR services to its employees, including payroll and employee benefits. The *Samadhan* application, based on SAP will be available to employees on desktop, mobile and tablet platforms on a 24x7x365 basis irrespective of location. The workflows of *Samadhan* will have minimum human intervention for expeditious delivery of services. With the launch of *Samadhan,* an HR Operations Unit has been set up at Bengaluru to centrally process establishment

Table X.7 : Reserve Bank's Office-wise Staff Strength
(As on June 30, 2015)

Office (including sub-offices)	Class I	Class III	Class IV	Total
1	2	3	4	5
Agartala	10	5	0	**15**
Ahmedabad	275	168	231	**674**
Belapur	132	53	178	**363**
Bengaluru	460	185	220	**865**
Bhopal	153	126	123	**402**
Bhubaneswar	148	115	170	**433**
Chandigarh	195	105	117	**417**
Chennai	433	340	354	**1,127**
Dehradun	19	6	2	**27**
Gangtok	8	0	0	**8**
Guwahati	195	136	187	**518**
Hyderabad	311	158	243	**712**
Jaipur	216	148	181	**545**
Jammu @	97	56	59	**212**
Kanpur	215	164	267	**646**
Kochi	33	34	29	**96**
Kolkata	482	427	442	**1,351**
Lucknow	150	106	146	**402**
Mumbai	609	325	959	**1,893**
Nagpur	240	205	234	**679**
New Delhi	501	236	294	**1,031**
Panaji, Goa	16	3	3	**22**
Patna	181	144	218	**543**
Pune-CAB-CRDC-ITP	66	37	69	**172**
Raipur	20	6	0	**26**
Ranchi	16	7	0	**23**
Shillong	9	5	0	**14**
Shimla	14	6	0	**20**
Thiruvananthapuram	209	115	131	**455**
Total	**5,413**	**3,421**	**4,857**	**13,691**
CODs #	**1,966**	**499**	**515**	**2,980**
Grand Total	**7,379**	**3,920**	**5,372**	**16,671**

CAB : College of Agricultural Banking;
CRDC: Central Records and Documentation Centre;
ITP : IMF Training Programme, Pune.
@ : Includes Srinagar Sub-Office.
\# : Central office departments including DICGC.

transactions of all employees. It has also been decided to set up a business continuity site in New Delhi. With a view to rationalising administrative costs, a Centralised Administrative Unit in Mumbai has been established to cater to the needs of all Central Office departments in Mumbai.

Performance Management System (PMS) and Job Profiles

X.36 Key Result Area (KRA)-based PMS is in vogue from 2013-14 coupled with a ranking model from the first cycle of review. Further, job profiles across work areas are being compiled for identifying required competencies, developing these competencies and standardising for similar positions across regional offices. The job profiles for senior officers will be finalised by September 2015 and for officers in Grade 'B' and 'C' by March 2016.

Senior Management Retreat and Other Developments

X.37 The Reserve Bank's Senior Management Retreat for 2014 was held in Mussoorie with the broad theme, '*RBI @80: Looking Back, Looking Ahead'*. As part of inter-institutional arrangement for knowledge sharing, a joint international seminar, 'Financial Stability: Issues and Concerns' was held in collaboration with the European Central Bank (ECB) at the College of Agricultural Banking, Pune in May 2015.

Agenda for 2015-16

X.38 Taking forward the efforts to evaluate capabilities available within the organisation, HRMD plans to work in 2015-16 on all associated HR areas like recruitment, placement mechanisms, fine-tuning the internal processes post organisational restructuring, talent spotting, talent management and continuous capacity building. These initiatives are likely to contribute towards more open and transparent HR and administration processes and procedures.

RBI Academy

X.39 The Reserve Bank plans to set up an Academy as a residential facility with state-of-the-art infrastructure in Navi Mumbai, primarily for integrated learning and development of its staff including e-learning. Going forward, the Academy will also conduct training for foreign central banks including those from South Asian Association for Regional Cooperation (SAARC) and other regions to promote external cooperation and cross learning.

A Competency based HR Framework

X.40 Going forward, the HR framework is envisaged to be competency based for career planning, placement, targeted learning and succession planning, leading to integrated HR processes. Therefore, a functional and behavioural competency set for each job role needs to be assessed coupled with the evaluation of competencies of the available human resources. Assessment centres will be set up for assessing the behavioural competency mapping of the staff.

Structured e-learning

X.41 The Reserve Bank is introducing structured e-learning for its staff. In the first phase, e-learning modules will primarily be umbrella courses targeted at larger groups of staff members and specific courses positioned as complementary to classroom courses. In addition, webinars will be used for wider dissemination of knowledge.

Common Cadre Recruitment

X.42 There will be a common recruitment process for officers in Grade B from 2015 onwards. For this purpose, a new scheme of selection is being framed in consultation with the Reserve Bank of India Services Board and the Institute of Banking Personnel Selection. The recruitment cycle is expected to shorten with the forthcoming new scheme of selection. Phase I examination for common recruitment is likely to be held in November 2015.

ENTERPRISE-WIDE RISK MANAGEMENT IN THE BANK

X.43 The adoption of the Enterprise-wide Risk Management (ERM) framework in February 2012 by the Reserve Bank marked a move from a 'silo-based' approach to a 'whole-of-business' perspective to risk management. Accordingly, the Risk Monitoring Department (RMD) envisaged a three-phased ERM rollout plan for the Reserve Bank.

X.44 As per the *three-lines-of-defence* approach to ERM adopted by the Reserve Bank, the Business Areas (BAs) represent the first line of defence as the BAs identify and manage their respective risks, while the Risk Monitoring Department (RMD) as the second line supports all BAs in the identification of significant risks, formulates risk policies, provides a risk assessment methodology, reports the risks to the Risk Governance Structure (RGS) and works to foster a risk culture in the Reserve Bank (Box X.3). Finally, the Internal Audit function which constitutes the third line of defence provides risk assurance to RGS through the risk-based audit process.

Agenda for 2014-15: Implementation Status

X.45 The risk-reporting structure was put in place in 2013-14 with the development of guidelines and

Box X.3
Operational Risk Monitoring Framework in Central Banks

The Basel Committee on Banking Supervision defines operational risk (OR) as 'the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events'. Central banks too are exposed to operational risks and, being risk-sensitive institutions, closely monitor their actual and potential operational risk exposures. However, there are no international benchmarks for monitoring operational risks in central banks. The International Operational Risk Working Group (IORWG) of over 61 central banks, including the Reserve Bank of India and the Bank for International Settlements acts as a centre of competence on Operational Risk Management (ORM). The ORM framework adopted by most of the central banks typically includes a risk assessment methodology, risk repositories and heat map(s), apart from incident reporting systems and periodic risk surveys.

Risk assessment methodology generally uses a combination of the likelihood of occurrence and severity of impact of a risk event to rate its riskiness on a graduated scale (say, high, significant or acceptable). The likelihood of occurrence of a risk event could be derived from both quantitative and qualitative factors. The impact of occurrence of an operational risk event on an organisation could be classified as financial impact, disruption in business operations / customer service, (negative) impact on reputation of the entity, or a combination of any of the three.

Risk Repository, also called Risk Register, contains the enumeration of each process/activity of an entity, the description of its associated risks at the inherent level, the controls in place to mitigate the inherent risks and the remaining, that is, Residual Risk after taking the controls into account.

Heat Map is a visual representation of the risk profile of a business area as it provides a colour-coded presentation of various risks. The heat map also depicts the migration of processes across risk zones on account of application of controls. The Incident Reporting System creates institutional memory on OR incidents with a view to promoting organisational learning and quantification of OR for building capital buffers. Risk surveys, on the other hand, enable on-going updating of the risk profile of the organisation by capturing existing as well as emerging risks in the operating environment.

As the risk culture of an organisation impacts the very identification and, thus, the articulation of its risks, a campaign has been launched by the Reserve Bank to enhance risk awareness among its staff so as to deepen and widen the risk culture in the institution. This will be reinforced by providing a computerised environment for risk monitoring to enable access to a risk database by Business Areas. Also, work is underway for implementing a consistent approach to rating of risks in the Reserve Bank. Risk surveys will continue to be used as a tool for identification and monitoring of emerging risks in Business Areas as well as for the Reserve Bank as a whole.

templates for preparation of risk registers for generating risk profiles of the BAs along with the establishment of an Incident Reporting System for building an institutional memory of actual and near-miss incidents. Five of the identified BAs have completed the Risk Registers and work is in progress in 27 other BAs. A vigorous risk management awareness campaign for strengthening the risk culture in the Reserve Bank was initiated during the year.

X.46 A draft Economic Capital Framework (ECF) for the Reserve Bank was formulated during the year to assess the Reserve Bank's capital and internal reserves position in a structured and systematic manner (Box X.4). Besides, designing and implementing a Risk Appetite Framework

Box X.4
Risk Management and Economic Capital in Central Banks

The public policy mandate of central banks makes the context of their risk management materially different from that of commercial entities, and necessitates the focus of their risk management to be on preserving and facilitating their policy efficacy, rather than profit maximisation. This principle of 'policy predominance' in pursuit of public interest often requires central banks to assume considerable financial risks on their balance sheets. For instance, the Reserve Bank of India maintains national forex reserves, constituting almost three-fourth of its balance sheet, in fulfilling its core purpose of fostering confidence in the external value of the rupee. While the reserves do buffer the country against external shocks, they also expose the Reserve Bank to considerable exchange rate risks. Such risks, which cannot be hedged, have to be carried by the Reserve Bank.

A central bank's role in fostering monetary and financial stability also exposes it to a wider range of risks, including losses arising from market interventions, lender of last resort (LOLR) role, market maker of last resort (MMLR) role and quasi-fiscal operations. Importantly, these mandates can at times require central banks to adopt a counter-intuitive approach to risk and assume increased risk on to their balance sheet, during times of systemic financial stress in order to de-risk the financial system.

A central bank's risks can be substantial and, consequently, its losses are neither as rare nor insignificant as is usually assumed. In the recent period, while a number of central banks in developed economies have suffered losses, central banks in emerging/developing economies suffered losses through the 1980s and 1990s also. Interestingly, this happened despite the seigniorage income accruing all along to these central banks, which is an important source of their financial strength.

Given these unique challenges, the general approach towards financial risk management in central banks is that while they do not actively manage risks arising from policy actions, they seek to ensure that their balance sheets have sufficient financial resilience to absorb these risks. Thus, they maintain sufficient economic capital, supplemented by risk-transfer/dividend-smoothening mechanisms.

Central banks as providers of domestic liquidity require capital not to remain going concerns but to ensure policy efficacy and credibility with regard to the ability to achieve their objectives. Weak finances can move central banks to either rely on generating excessive seigniorage income, which may come in conflict with their price-stability objective, or seek recapitalisation from the government, which could impact their autonomy.

The capital requirements of a central bank can vary considerably depending on a number of factors, *inter alia*:

- *The size of shocks and scope of a central bank's mandate*: The wider the area of responsibilities of a central bank, greater the risks and, hence, higher the requirement of capital.
- *The accounting policy framework adopted by central banks*: Central banks which periodically recognise changes in valuation of assets will see greater variability in their financial positions, which increases capital requirements.
- *Institutional arrangements*: Statutory provisions for a central bank's recapitalisation as well as risk transfer mechanisms can reduce its capital requirements, though not eliminate them.
- *The fiscal space available with the sovereign*: A central bank may require recapitalisation, precisely at a time when the fiscal position is under strain, say, due to a financial crisis. This strengthens the case for *ex ante* capitalisation of a central bank, rather than *ex post* recapitalisation.

The European Central Bank and the central banks of Australia, Austria, Belgium, France, Finland, Germany,

(Contd....)

Italy, Netherlands, Norway, New Zealand, Singapore and Sweden use methodologies, such as value-at-risk, expected shortfall, stress tests and other risk models to determine their adequacy of reserves/risk provisions. The central bank of New Zealand has in place a well-developed economic capital framework to model its capital requirements. The Reserve Bank of India is also seeking to put in place an economic capital framework. The exercise is a challenging one as the Reserve Bank plans to cover not only the risks in its balance sheet but also its 'contingent risks' which arise from its public policy role in fostering monetary and financial stability.

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(RAF) for the Reserve Bank was also envisaged during the year.

Agenda for 2015-16

X.47 In the coming year, ECF is expected to be refined and implemented in the Reserve Bank. RAF, which is under development, is also planned for induction. The finalisation of risk registers of all BAs will bring out the risk profile/heat map of each BA, regional office and the organisation as a whole. The Incident Reporting System will help identify patterns across incidents with a view to effectively preventing/managing such events in the future. Risk surveys will be conducted to support the monitoring of the emerging risks as also to review top risks. Efforts for creating risk awareness at all levels and across all locations will continue to be pursued for deepening the risk culture in the organisation.

INTERNAL AUDIT/INSPECTION IN THE RESERVE BANK

X.48 Internal audit/inspection undertaken by the Inspection Department of the Reserve Bank examines and reports on the adequacy and reliability of its risk management, internal controls and governance processes under a robust risk based internal audit (RBIA) framework and provides regular feedback to the Audit and Risk Management Sub-Committee (ARMS) of the Central Board.

Agenda for 2014-15: Implementation Status

X.49 The audit plan for January-December 2014 was fully implemented. A panel of information system (IS) auditors was prepared, training imparted and IS audits are being carried out by these empanelled auditors as part of RBIAs. A seminar on 'Internal Audit and Enterprise-wide Risk Management for Central Bankers in the SAARC Region' was held in February 2015. The plan for a comprehensive Audit Management System (AMS) could not materialise as the risk registers were being prepared in various central office departments (CODs). As regards vulnerability assessment and penetration testing (VAPT), a Technical Advisory Group (TAG) has been constituted to empanel external auditors for carrying out VAPT.

Agenda for 2015-16

X.50 For 2015-16, the department will focus on: i) ensuring a smooth and seamless transition from a largely compliance based audit to RBIA on the basis of risk registers in CODs/regional offices (ROs); ii) identifying an appropriate AMS application suitable for the Reserve Bank which will provide an integrated solution for audit process; iii) undertaking VAPT of corporate e-mail and real time gross settlement (RTGS) applications; iv) appointing concurrent auditors as per the revised procedure / parameters; and v) developing appropriate guidelines for project audits with respect to all new estate, IT related and other projects and also assisting the respective user departments in their implementation.

INTERNATIONAL RELATIONS

X.51 In the aftermath of the global financial crisis and growing engagement with multilateral institutions, the Reserve Bank constituted a dedicated International Department as in many other central banks. The department acts as the nodal point for international financial diplomacy to further India's national interests and seeks to play a pivotal role in international macroeconomic coordination and global regulatory standard-setting.

Agenda for 2014-15: Implementation Status

Central Bank Swap Arrangements

X.52 The department carried forward the background work on the BRICS (Brazil, Russia, India, China and South Africa) Contingent Reserve Arrangement (CRA). This contributed to the signing of the CRA Treaty on July 15, 2014 in Fortaleza, and the Inter-Central Bank Agreement (ICBA) on July 7, 2015 in Moscow. The Reserve Bank provided US$ 400 million support to the Central Bank of Sri Lanka under the SAARC swap arrangement and a further US$ 1.1 billion facility under a special/ad hoc swap agreement.

Engagement with Multilateral Institutions

X.53 As the nodal agency, the department coordinated the work relating to the Basel Committee of Banking Supervision (BCBS), Committee of Global Financial System (CGFS) and Committee on Payments and Market Infrastructures (CPMI). The department also coordinated with various standing committees/groups of the Financial Stability Board (FSB). In the G20 forum, work relating to the Framework Working Group (FWG) and the Investment and Infrastructure Working Group (IIWG) were attended to. The department coordinated the Article IV consultation with International Monetary Fund (IMF) and has also been engaged in issues of the General Review of Quotas.

SAARCFINANCE (SF)

X.54 Amongst the SF initiatives, the Reserve Bank and the State Bank of Pakistan have initiated, along with other SAARC countries, a collaborative study on capital flows. The SF scholarship scheme, implemented through the department, awarded four scholarships for the academic year 2015-16. In the second half of 2014-15, after the constitution of the department, it handled visits by 23 foreign groups/ delegations to the Reserve Bank.

Agenda for 2015-16

X.55 In 2015-16, the department will work towards operationalisation of CRA, creation of a SF database, preparing position papers on key issues of negotiations in the global fora, coordination of the FSB Peer Review, Financial Sector Assessment Programme (FSAP) by the Fund-Bank and Article IV consultations with IMF. India will be assuming the BRICS chairmanship in 2016. Working out meetings, agendas and plans for this in coordination with the Government, will also occupy the attention of the department.

GOVERNMENT AND BANK ACCOUNTS

X.56 The Department of Government and Bank Accounts (DGBA) looks after the accounts of the governments as well as the Reserve Bank. In the area of accounting and its presentation, the Reserve Bank has been moving towards greater transparency through its annual accounts/financial statements. For transparent conduct of government banking business and its own internal accounting processes, the Reserve Bank has been leveraging on IT resources to provide better and more efficient services.

Agenda for 2014-15: Implementation Status

X.57 Some of the accounting policy changes as suggested by statutory auditors and Technical

Committees (I and II) were implemented. Accordingly, repo and reverse repo transactions are now being treated as lending and deposit transactions respectively as against sale and purchase transactions earlier. Further, changes in policies on capitalisation/depreciation of building and machinery, impaired assets and recognition of accrued dividend were effected.

Agenda for 2015-16

X.58 In line with the recommendations of Technical Committee-I, the formats of weekly accounts, balance sheet and profit and loss account were revised with effect from July 17, 2015, in consultation with the Government, by amending the RBI Act, 1934 and the RBI General Regulations, 1949. Technical Committee-I had recommended that rupee securities be carried at fair value and any unrealised gain or loss be transferred to the Investment Revaluation Account. This will be made applicable from 2015-16.

X.59 A Working Group constituted in February 2015 to review the system of inspection of government business in agency banks is expected to submit its report by end-August 2015. Accordingly, inspection of government business in agency banks is set to be revamped. A Working Group on Business Process Reengineering (BPR) of government business comprising members from concerned government agencies, the Reserve Bank and agency banks is expected to submit its report by October 2015. BPR for government business will be undertaken subsequently.

MANAGING FOREIGN EXCHANGE RESERVES

X.60 The Department of External Investments and Operations (DEIO) manages the country's foreign exchange reserves. With its increasing size, it has become imperative to strengthen the accounting, valuation methods, risk management practices and IT infrastructure including disaster management for the purpose of managing the foreign exchange reserves.

Agenda for 2014-15: Implementation Status

X.61 During the year, market and asset class diversification was pursued within the over-arching framework of safety, liquidity and returns, under the overall guidance of the high level and internal strategy committees. In line with Technical Committee-II's recommendations, the accounting refinements were carried out by June 30, 2014, for forward contracts, entered into by the Reserve Bank for intervention operations, and swaps at off-market rates that are in the nature of repos. The existing treasury system was replaced by a new state-of-the-art system in October 2014 and integrated into the Reserve Bank's Core Banking Solution. Certain international best practices for managing credit, market and operational risks were implemented during the year and documented. A more robust disaster recovery mechanism with a focus on regular drills has been put in place.

Agenda for 2015-16

X.62 The remaining recommendations of Technical Committee-II, particularly relating to valuation changes in foreign currency assets (FCA) and gold, are on the agenda for 2015-16. The Reserve Bank aims to stabilise live operations from alternate locations towards mitigating the impact of disaster induced disruptions. The Reserve Bank will continue its efforts at refining the strategy and tactics of portfolio management to enhance returns in a low earning environment without sacrificing the objectives of liquidity and safety.

ECONOMIC AND POLICY RESEARCH

X.63 Research is a critical activity in central banks. In the Reserve Bank, the Department of Economic and Policy Research (DEPR) is entrusted with the task of providing research inputs and MIS (management information system) services in economic and policy related issues. The department is envisaged to evolve and establish itself as a knowledge centre in policy-oriented research in macroeconomics and monetary policy issues. The department pursues an issue-based medium-term research agenda.

Agenda for 2014-15: Implementation Status

X.64 The department brought out its flagship publications - Annual Report, Study on State Finances and RBI Bulletin. Four outreach seminars were held at various centres, mostly universities, during the year to disseminate the main messages of the Annual Report 2013-14 of the Reserve Bank. The print-version of the Weekly Statistical Supplement (WSS) was discontinued from January 2015 while ensuring its online availability. There was regular compilation and dissemination of primary statistics on monetary aggregates, balance of payments, external debt, household financial savings and flow of funds. During the year, work relating to the Reserve Bank's history Volume V covering the period 1997-2007 was initiated.

X.65 During 2014-15, 40 research papers were completed, of which nine were published in external domestic and foreign journals. Besides, the Reserve Bank Occasional Papers (the research journal of the Reserve Bank) carried seven research papers. The research papers covered multiple areas of interest: inflation dynamics, exchange rate, asset quality in the banking sector, monetary policy transmission, financial stability and impact of taper talk. Towards promoting research, several initiatives were undertaken in 2014-15, such as instituting best research paper award, allowing co-authorship by the Reserve Bank staff with outside researchers/ experts for the Reserve Bank Working Papers and Occasional Papers and outlining a code of conduct for the researchers.

X.66 Notable events organised by the department included a seminar on 'Economic Outlook and Monetary Policy in the United States' by Mr Stanley Fischer, Vice Chairman, US Federal Reserve on February 11, 2015. Another significant event, 'Conversation with Ms Christine Lagarde, MD, International Monetary Fund (IMF)' was organised on March 17, 2015. The 3rd RBI Chair Professors' and DEPR Researchers' Joint Conference was held during the year, which involved presentations of papers on a range of issues under the broad theme 'Managing Risks and Macro-imbalances'. Besides, several seminars on diverse themes were organised as part of the DEPR study circle with the participation of external experts.

Agenda for 2015-16

X.67 Going forward, the research areas envisaged to be covered during 2015-16 include growth and investment, exchange rate, monetary policy transmission lags, issues in financial markets, potential output, optimal monetary policy rule, pass-through of international prices to domestic prices and pass-through of food and fuel inflation to core inflation. The department proposes to organise a number of seminars/ lectures during 2015-16. MIS is proposed to be modified and the publications will be rationalised. The drafting of history Volume V will be taken up with the constitution of a full fledged History Cell.

STATISTICS AND INFORMATION MANAGEMENT

X.68 The Department of Statistics and Information Management (DSIM) makes available macro-financial statistics to the public and provides statistical support and analytical inputs to the policy and operational needs of the Reserve Bank by managing comprehensive statistical systems relating to banking, corporate and the external sectors, undertaking structured surveys, maintaining the Reserve Bank's data warehouse, engaging in statistical analyses and forecasting.

Agenda for 2014-15: Implementation Status

Data Management, Dissemination and Publications

X.69 The department released statistics relating to banking, corporate and external sectors as per the time schedule and with reduction in time-lag wherever possible. Data from corporate regulatory filing with the Ministry of Corporate Affairs was used for estimating saving and capital formation and private corporate performance analyses. The periodicity of the Co-ordinated Portfolio Investment Survey (CPIS) was increased from annual to bi-annual. Banks were involved in implementation of Stage-2 enhancements in international banking statistics (IBS) through workshops and a pilot survey.

X.70 Quarterly BSR-1 data covering individual bank accounts was released for the first time. The scope of eXtensible Business Reporting Language (XBRL)-based return submission was broadened with 23 new returns and developmental work for another 23 returns is at an advanced stage. Harmonisation of banking statistics, guiding banks in proper implementation of the automated data flow (ADF) system and linking the XBRL system to it was taken up during the year. A Credit Repository has been developed on the basis of the Report on Large Credit, wherein as part of system-wide standardisation efforts, Income Tax-Permanent Account Number (IT-PAN) has been introduced for borrower identification.

Surveys and Research

X.71 The periodicity of a few surveys designed for providing inputs to monetary policy formulation was synchronised with the policy announcement cycle. Efforts were made to impart methodological improvements in surveys under the guidance of the Technical Advisory Committee on Surveys (TACS). An article based on the salient results of the Residential Asset Price Monitoring Survey was also released. The framework for forecasting has been updated and a quarterly macro-econometric model has been operationalised. Several research studies were contributed to the Reserve Bank Working Paper Series/other publications/ academic conferences.

Agenda for 2015-16

X.72 DSIM will move towards the implementation of Bank for International Settlements-Committee on the Global Financial System recommended Stage-2 enhancements to IBS. A comprehensive guide for the current statistics section of the Reserve Bank of India Bulletin will be released. Phase III of the XBRL project will be launched to ensure standardised reporting for more returns where banks will be persuaded to orient their ADF systems to XBRL reporting. Work relating to harmonisation of banking statistics will be pursued. The database on Indian economy (DBIE) infrastructure will be used for developing a SAARCFINANCE regional statistical database and compilation of 'Handbook of SAARCFINANCE'. Research studies will be undertaken in the area of corporate sector performance, expectation channel and forecasting of macro variables.

LEGAL MATTERS

X.73 The Legal Department of the Reserve Bank provides counsel and support to other departments ensuring that the policy decisions, actions and position taken by the Reserve Bank in various fora are legally sound and defensible. The department also guides the Reserve Bank in matters relating to the RTI Act.

Agenda for 2014-15: Implementation Status

X.74 During the year, a large number of appeals and writ petitions were filed before the Supreme Court against the judgments rendered by the Gujarat and Madras High Courts, challenging the constitutional validity of Section 2(1) (o) of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 relating to classification of non-performing assets. The Supreme Court has since declared the provision as constitutionally valid.

X.75 The High Court of Gujarat in the case of Ionic Metalliks *vs.* Union of India had to deal with a case which, *inter alia*, challenged the Reserve

Bank's Master Circular on Wilful Defaulters and the action taken by certain banks on the basis of that circular. While upholding the authority of the Reserve Bank to issue the circular, the Court, however, held that making the circular applicable to all directors, irrespective of their involvement and responsibility, would neither be appropriate nor reasonable.

Agenda for 2015-16

X.76 Going forward, issues pertaining to the recommendations of Financial Sector Legislative Reforms Commission (FSLRC) and the enactment of the Indian Financial Code (IFC) are likely to be focused. Besides, certain amendments to the various Acts administered by the Reserve Bank need to be pursued in order to meet certain international commitments and standards and to clarify and clean up some provisions.

CORPORATE STRATEGY AND BUDGETING

X.77 The Corporate Strategy and Budget Department (CSBD) was carved out of the erstwhile Department of Expenditure and Budgetary Control as part of organisational restructuring in 2014. A key function of CSBD is formulating the budget of the Reserve Bank by adopting activity based and zero based budgeting, as also the need for allocating resources optimally. Expenditure is monitored through a quarterly review to the CCB. During 2014-15, CSBD held several rounds of interaction with Regional Directors (RDs), budget officers of ROs and CODs to sensitise them to use the budget process as a tool for expenditure monitoring and to focus on activities planned.

Agenda for 2015-16

X.78 The remit of the department going forward, is to identify the Reserve Bank's strategic priorities and allocate resources accordingly. With respect to funded external institutes, CSBD's focus will be to minimise funding of their revenue expenditure over a period of three years while supporting their research and capital expenditure. CSBD is formulating a business continuity management (BCM) policy by June 2016. Payment of salaries and staff-related payments, a core function of the department, is in the process of being taken over by HRMD.

CORPORATE SERVICES

X.79 With a view to enabling the specialised departments to focus on their core functions, the Department of Corporate Services (DCS) has been set up as part of the reorganisation. It has a mandate to provide corporate support services by way of management of events/meetings/hospitality; framing guidelines for award of rate contracts; centralised procurement of office stationery, electronic document management; and protocol services to the top management.

RAJBHASHA

X.80 The Reserve Bank continued to ensure compliance of statutory provisions of the Official Language Act to promote the use of Hindi in its working during 2014-15. The Rajbhasha Department of the Reserve Bank acts as the nodal department for this purpose.

Agenda for 2014-15: Implementation Status

X.81 All the Regional Offices obtained membership of the Town Official Language Implementation Committee (TOLIC) during the year. Six offices of the Reserve Bank were notified in terms of Rule 10(4) of The Official Languages Rules, 1976. A number of Hindi competitions as well as functions in Hindi were organised during the year, including a two-day conference of *Rajbhasha* Officers in May 2015. Towards enhancing the use of Hindi in a computerised environment, intensive Hindi typing training programmes were conducted for officers and staff and 156 trainees passed the examination conducted by the Government.

X.82 Besides statutory publications, other publications were also brought out in a bilingual form. *Banking Chintan-Anuchintan,* the quarterly

Hindi magazine dedicated to banking and finance, is being published. The first issue of a half yearly e-newsletter *Rajbhasha Samachar* was released in January 2015.

X.83 The Parliamentary Committee on Official Language visited the Reserve Bank's Kochi office in 2015 and released the e-Banking Glossary. The glossary has since been uploaded on the Reserve Bank's website with various advanced features, such as search options in both Hindi and English. The Parliamentary Committee also visited the Delhi and Kolkata offices of the Reserve Bank. The committee suggested a few corrective actions for furthering the use of Hindi in the Reserve Bank like increasing the number of workshops and increasing the expense on Hindi advertisements.

Agenda for 2015-16

X.84 The work plan for 2015-16 has taken on board the concerns expressed by the Parliamentary Committee on Official Language. It has been decided to celebrate 2015-16 as the *Rajbhasha* Golden Jubilee Year in the Reserve Bank for which an action plan has been prepared covering various activities to be held during the year. A Hindi workshop for Regional Directors and heads of Central Office departments, region-wise seminars, various Hindi functions marking important linguistic events like Translation Day and International Mother Language Day have been planned to raise the level of implementation of the *Rajbhasha* policy.

PREMISES

X.85 The Premises Department is engaged in creating and maintaining the Reserve Bank's building infrastructure. In 2014-15, the department brought some of the stalled projects on track. Projects under the design and build (DB) mode were taken up for residential colonies at Anna Nagar, Chennai; Dadar-Parel, Mumbai and Ameerpet, Hyderabad; additional hostels at the Indira Gandhi Institute of Development Research (IGIDR), Mumbai and the Reserve Bank Staff College (RBSC), Chennai. The process of acquisition of land for a sub-office and residences in Imphal was initiated. The existing physical infrastructure for dealing room for financial market operations in Mumbai and for comprehensive human resource system (CHRS) in Bengaluru was upgraded.

Green Initiative

X.86 As part of its Green Policy, grid interactive solar power plants are under installation at all Reserve Bank's offices. To utilise the waste generated, organic waste convertors have been installed in Kanpur, Thiruvananthapuram, New Delhi, Bengaluru and CAB, Pune.

Swachh Bharat - Sanitation Audit

X.87 A third party sanitation audit was carried out on a pilot basis for the Central Office Building (COB), Fort and Bandra Kurla Complex offices, Mumbai and Mumbai Central Colony. The findings have been taken up for rectification and redressal.

Agenda for 2015-16

X.88 The focus during 2015-16 will be on consolidating the existing physical resources of land and buildings, so as to ensure optimum utilisation and reduction in maintenance costs over the next two to three years. It is proposed to take up construction of the Reserve Bank's offices in Dehradun and Raipur. The redevelopment of Hauz Khas Colony, New Delhi; Chembur Colony, Mumbai under the DB mode, and construction of the CAFRAL building in Mumbai were impeded due to delays in securing requisite statutory approvals. With closer follow-up, the projects are expected to commence in 2015-16.

X.89 The Internet Protocol CCTV project is being implemented replacing the existing analog CCTV systems in 20 offices and is likely to be completed by October 2015. The provision of an integrated security system in the COB is expected to be completed by December 2015. The access control card based turnstile system installed at COB, is being replicated in the Regional Offices.

XI THE RESERVE BANK'S ACCOUNTS FOR 2014-15

The balance sheet size of the Reserve Bank increased by 10.09 per cent for the year ended June 30, 2015 primarily due to increase in foreign currency assets on the asset side which rose by 21.50 per cent and increase in notes in circulation and deposits which rose by 9.57 per cent and 37.60 per cent respectively on the liability side. While gross income for the year 2014-15 increased sharply by 22.66 per cent, the total expenditure increased by 11.92 per cent. The year ended with an overall surplus of ₹658.96 billion as against ₹526.79 billion in the previous year, representing an increase of 25.09 per cent.

XI.1 The balance sheet of the Reserve Bank is largely a reflection of the activities carried out in pursuance of its currency issue function as well as monetary policy and reserve management objectives. The key financial results of the Reserve Bank's operations during the year 2014-15 along with comments are set out in the following paragraphs.

XI.2 The year 2014-15 witnessed an overall increase in the size of the balance sheet by ₹2,647.92 billion, *i.e.*, 10.09 per cent from ₹26,243.67 billion as on June 30, 2014 to ₹28,891.59 billion as on June 30, 2015. The increase on the asset side was mainly due to increase in Foreign Currency Assets (FCA). The increase on the liability side was mainly due to a rise in notes in circulation and deposits. As on June 30, 2015 domestic assets (including gold) constituted 26.07 per cent while the FCA constituted 73.93 per cent of total assets as against 33.0 per cent and 67.0 per cent, respectively as on June 30, 2014.

XI.3 As in the previous year, no amount has been transferred to the Contingency Fund. An amount of ₹10.00 billion has been provided for and transferred to the Asset Development Fund specifically towards capital contribution to the National Housing Bank (NHB) and the surplus of ₹658.96 billion has been transferred to the Central Government. The balances in the Contingency Fund and the Asset Development Fund and the surplus transferred to the Central Government during the last five years have been given in Tables XI.1 & XI.2 respectively.

XI.4 For better comparability and transparency, the Reserve Bank has been progressively moving towards greater disclosures in its financial statements. A Technical Committee constituted in 2012-13 to review the Form of Presentation of the Balance Sheet and Profit & Loss Account [Chairman: Shri Y.H. Malegam (Technical Committee I)] had made several recommendations relating to the format and contents of the Balance Sheet and Profit & Loss Account of the Reserve Bank and also to change the nomenclature of the Profit and Loss Account to Income Statement. Further, the

Table XI.1: Balances in Contingency Fund (CF) and Asset Development Fund (ADF)

(₹ billion)

As on June 30	Balance in CF	Balance in ADF	Total	CF and ADF as percentage to total assets
1	2	3	4=(2+3)	5
2011	1707.28	158.66	1865.94	10.3
2012	1954.05	182.14	2136.19	9.7
2013	2216.52	207.61	2424.13	10.1
2014	2216.52	207.61	2424.13	9.2
2015	2216.14*	217.61	2433.75	8.4

* The decline in the CF is due to adjustment of the debit balance in the FCVA on account of MTM loss on forward contracts on June 30, 2015.

Table XI.2:Trends in Gross Income, Expenditure and Net Disposable Income

(₹ billion)

Item	2010-11	2011-12	2012-13	2013-14	2014-15
1	2	3	4	5	6
a) Gross Income	370.70	531.76	743.58	646.17	792.56
b) Transfers to Internal Reserves (i+ii)	134.02	270.25	287.94	0.00	0.00
(i) Contingency Fund	121.67	246.77	262.47	0.00	0.00
(ii) Asset Development Fund@	12.35	23.48	25.47	0.00	0.00
c) Net Income (a-b)	236.68	261.51	455.63	646.17	792.56
d) Total Expenditure	86.55	101.37	125.49	119.34	133.56
e) Net Disposable Income (c-d)	150.13	160.14	330.14	526.83	659.00
f) Transfer to funds*	0.04	0.04	0.04	0.04	0.04
g) Surplus transferred to the Government (e-f)	150.09	160.10	330.10	526.79	658.96
Transfer of Surplus to Government as per cent of Gross Income less Total Expenditure	52.8	37.2	53.4	99.99	99.99

*: An amount of ₹10 million each has been transferred to the National Industrial Credit (Long Term Operations) Fund, the National Rural Credit (Long Term Operation) Fund, the National Rural Credit (Stabilisation) Fund and the National Housing Credit (Long Term Operations) Fund during each of the five years.

@For 2014-15 not shown as it is included in total expenditure.

Committee had also recommended a few changes in the accounting policy. The Board of the Reserve Bank has accepted these recommendations for implementation. In order to effect the change relating to the format and contents of the Balance Sheet and Profit and Loss Account, Government of India has notified the format of weekly accounts of the Bank on July 15, 2015 in the Gazette of India and amendments in relevant sections of RBI General Regulations, 1949 have been notified by the Bank on July 6 and July 15, 2015 in the Gazette of India for changes in the format of the Balance Sheet and Profit and Loss Account of the Bank. Accordingly, the accounts of the Bank for the year 2014-15 have been drawn up in the new format.

XI.5 The major changes in the format and contents of the Balance Sheet and the Profit and Loss account are as under:

- Balance Sheets of Issue and Banking Departments have been merged and each item of asset and liability is shown as line items supported by schedules.
- 'Gold Coin and Bullion' which earlier formed part of 'Other Assets', and 'Investment in Subsidiaries and Associates', which formed part of 'Investments' in the Banking Department balance sheet, are now shown as distinct balance sheet heads.
- The Profit and Loss Account has been renamed as 'Income Statement' and the income head has been bifurcated into two major sub heads *viz*. 'Interest' and 'Others' supported by schedules.
- A new head 'Provisions' has been added under expenditure for accounting of transfers to the Contingency Fund (CF) and the Asset Development Fund (ADF).
- The unit of reporting has been changed from 'Rupee Thousands' to 'Rupee billions'.

XI.6 For better readability and presentation, investments have been bifurcated into four major categories. 'Balances Held Abroad' and 'Investments' held as part of Banking Department balance sheet are shown as 'Investments–Foreign-BD' and 'Investments- Domestic-BD', respectively. 'Foreign Securities' and 'GoI Rupee Securities' forming part of 'Issue Department Assets' have been shown as 'Investments- Foreign-ID' and 'Investments-

Domestic-ID' respectively. Contingency Reserve and Asset Development Reserve have been renamed as 'Contingency Fund' and 'Asset Development Fund'.

XI.7 Based on the recommendations made by the Technical Committee I certain changes in accounting policies were also effected in 2014-15. Repo and Reverse Repo transactions, were earlier treated as purchase and sale of securities. As the substance of the transaction is lending and deposit of funds and securities only represent the collateral for the transaction, Repo under Liquidity Adjustment Facility (LAF) and Marginal Standing Facility (MSF) is now being treated as lending and Reverse Repo being treated as deposit of funds with RBI. The Technical Committee I had also recommended that rupee securities be carried at fair value and any unrealised gain or loss may be transferred to the Investment Revaluation Account (IRA). This will be implemented in 2015-16.

XI.8 Another Technical Committee [Chairman: Shri Y.H.Malegam (Technical Committee II)] was constituted during 2013-14 to review the Level and Adequacy of Internal Reserves and Surplus Distribution Policy of the Reserve Bank of India. Based on the recommendations of the Technical Committee II, the forward contracts entered into by the Bank as part of its intervention operations are being marked to market on yearly basis as on the balance sheet date from the year 2013-14. Further, as against the earlier policy of ignoring gain and accounting for loss only, now both gain or loss are accounted for.

XI.9 The other major recommendations of the Technical Committee II, which will be implemented in 2015-16 are: (i) change in the method of revaluation of the rupee securities from Lower of Book or Market Value (LOBOM) to fair valuation, and (ii) bifurcation of Currency and Gold Revaluation Account (CGRA) into Gold Revaluation Account (GRA) and Foreign Currency Revaluation Account (FCRA).

XI.10 The Balance Sheet and the Income Statement prepared for the year 2014-15 in the new formats along with the schedules, statement of significant accounting policies and supporting notes to the accounts are furnished below:

RESERVE BANK OF INDIA
BALANCE SHEET AS ON JUNE 30, 2015

(Amount in ₹ billion)

Liabilities	Schedules	2013-14	2014-15	Assets	Schedules	2013-14	2014-15
Capital		0.05	0.05	**Assets of Banking Department (BD)**			
Reserve Fund		65.00	65.00	Notes, rupee coin, small coin	5	0.11	0.11
Other Reserves	1	2.20	2.22	Gold Coin and Bullion	6	590.24	578.84
Deposits	2	3769.45	5186.86	Investments-Foreign-BD	7	4,796.21	7,276.29
Other Liabilities and Provisions	3	8961.70	8905.03	Investments-Domestic-BD	8	6,684.68	5,174.97
				Bills Purchased and Discounted		0.00	0.00
				Loans and Advances	9	370.83	802.32
				Investment in Subsidiaries	10	13.20	13.20
				Other Assets	11	343.13	313.43
Liabilities of Issue Department				**Assets of Issue Department (ID)**			
Notes issued	4	13,445.27	14,732.43	Gold Coin and Bullion (as backing for Note issue)	6	649.78	637.23
				Rupee coin		1.72	1.99
				Investment-Foreign-ID	7	12,783.31	14,082.75
				Investment-Domestic-ID	8	10.46	10.46
				Domestic Bills of Exchange and other Commercial Papers		0.00	0.00
	Total Liabilities	**26,243.67**	**28,891.59**		**Total Assets**	**26,243.67**	**28,891.59**

RESERVE BANK OF INDIA
INCOME STATEMENT FOR THE YEAR ENDED JUNE 2015

(Amount in ₹ billion)

INCOME	Schedules	2013-14	2014-15
Interest	12	636.88	744.82
Others	13	9.29	47.74
Total		**646.17**	**792.56**
EXPENDITURE			
Printing of Notes		32.14	37.62
Expense on Remittance of Currency		0.71	0.98
Agency Charges	14	33.25	30.45
Interest		0.04	0.01
Employee Cost		43.24	40.58
Postage and Telecommunication Charges		0.84	0.91
Printing and Stationery		0.21	0.34
Rent, Taxes, Insurance, Lighting, etc.		1.22	1.14
Repairs and Maintenance		1.04	1.04
Directors' and Local Board Members' Fees and Expenses		0.03	0.03
Auditors' Fees and Expenses		0.02	0.03
Law Charges		0.05	0.04
Miscellaneous Expenses		4.93	7.97
Depreciation		1.62	2.42
Provisions		0.00	10.00
Total		**119.34**	**133.56**
Available Balance		**526.83**	**659.00**
Less:			
a) Contribution to:			
i) National Industrial Credit (Long Term Operations) Fund		0.01	0.01
ii) National Housing Credit (Long Term Operations) Fund		0.01	0.01
b) Transferable to NABARD:			
i) National Rural Credit (Long Term Operations) Fund [1]		0.01	0.01
ii) National Rural Credit (Stabilisation) Fund[1]		0.01	0.01
Surplus payable to the Central Government		**526.79**	**658.96**

1 *These funds are maintained by the National Bank for Agriculture and Rural Development (NABARD).*

Madhumita S.Deb	S. S. Mundra	R. Gandhi	Urjit R. Patel	Harun R. Khan	Raghuram G. Rajan
Chief General Manager	Deputy Governor	Deputy Governor	Deputy Governor	Deputy Governor	Governor

SCHEDULES FORMING PART OF BALANCE SHEET AND INCOME STATEMENT

(Amount in ₹ billion)

		2013-14	2014-15
Schedule 1:	**Other Reserves**		
	(i) National Industrial Credit (Long Term Operations) Fund	0.23	0.24
	(ii) National Housing Credit (Long Term Operations) Fund	1.97	1.98
	Total	**2.20**	**2.22**
Schedule 2:	**Deposits**		
	(a) Government		
	(i) Central Government	1.00	1.01
	(ii) State Governments	0.42	0.43
	Sub total	**1.42**	**1.44**
	(b) Banks		
	(i) Scheduled Commercial Banks	3,469.16	3,711.94
	(ii) Scheduled State Co-operative Banks	37.29	32.22
	(iii) Other Scheduled Co-operative Banks	63.31	69.97
	(iv) Non-Scheduled Co-operative Banks	4.81	10.71
	(v) Other Banks (RRB, LDB, etc)	102.67	122.01
	Sub total	***3,677.24***	***3,946.85***
	(c) Others		
	(i) Administrators of RBI Employee PF A/c	38.62	40.75
	(ii) Depositors' Education and Awareness Fund	27.95	78.75
	(iii) Balances of Foreign Central Banks	10.13	14.71
	(iv) Balances of Indian Financial Institutions	2.53	4.33
	(v) Balances of International Financial Institutions	1.43	1.45
	(vi) Mutual Fund	0.01	0.01
	(vii) Others	10.12	1098.57
	Sub total	***90.79***	***1,238.57***
	Total	**3,769.45**	**5,186.86**
Schedule 3:	**Other Liabilities and Provisions**		
	(i) Gratuity and Superannuation Fund	123.10	140.05
	(ii) Contingency Fund (CF)	2,216.52	2,216.14
	(iii) Asset Development Fund (ADF)	207.61	217.61
	(iv) Currency and Gold Revaluation Account (CGRA)	5,721.63	5,591.93
	(v) Investment Revaluation Account (IRA)	37.91	32.14
	(vi) Foreign Exchange Forward Contracts Valuation Account (FCVA)	42.98	0.00
	(vii) Provision for Forward Contracts Valuation Account (PFCVA)	0.00	0.39
	(viii) Provision for Payables	16.55	16.81
	(ix) Surplus Transferable to the Government of India	526.79	658.96
	(x) Bills Payable	0.37	0.17
	(xi) Miscellaneous	68.24	30.83
	Total	**8,961.70**	**8,905.03**
Schedule 4:	**Notes Issued**		
	(i) Notes held in the Banking Department	0.11	0.11
	(ii) Notes in Circulation	13,445.16	14,732.32
	Total	**13,445.27**	**14,732.43**

		2013-14	2014-15
Schedule 5:	**Notes, Rupee Coin, Small Coin (with RBI)**		
	(i) Notes	0.11	0.11
	(ii) Rupee coin	0.00	0.00
	(iii) Small coin	0.00	0.00
	Total	**0.11**	**0.11**
Schedule 6:	**Gold Coin and Bullion**		
	(i) Banking Department	590.24	578.84
	(ii) Issue Department (as backing for Note issue)	649.78	637.23
	Total	**1,240.02**	**1,216.07**
Schedule 7	**Foreign Currency Assets**		
	(i) Investments - Foreign - BD	4,796.21	7,276.29
	(ii) Investments - Foreign - ID	12,783.31	14,082.75
	Total	**17,579.52**	**21,359.04**
Schedule 8:	**Investments-Domestic**		
	(i) Investments - Domestic -BD	6,684.68	5,174.97
	(ii) Investments - Domestic - ID	10.46	10.46
	Total	**6,695.14**	**5,185.43**
Schedule 9:	**Loans and Advances**		
	(A) Loans and Advances to :		
	(i) Central Government	0.00	0.00
	(ii) State Governments	6.66	25.77
	Sub total	***6.66***	***25.77***
	(B) Loans and Advances to:		
	(i) Scheduled Commercial Banks	294.17	732.03
	(ii) Scheduled State Co-operative Banks	0.00	0.00
	(iii) Other Scheduled Co-operative Banks	1.34	0.45
	(iv) Non-Scheduled State Co-operative Banks	0.00	0.00
	(v) NABARD	0.00	0.00
	(vi) Others	68.66	44.07
	Sub total	***364.17***	***776.55***
	(C) Loans, Advances and Investments from National Industrial Credit (Long Term Operations) Fund:		
	(a) Loans and Advances to:		
	(i) Industrial Development Bank of India	0.00	0.00
	(ii) Export Import Bank of India	0.00	0.00
	(iii) Industrial Investment Bank of India Ltd.	0.00	0.00
	(iv) Others	0.00	0.00
	(b) Investments in bonds/ debentures issued by:		
	(i) Industrial Development Bank of India	0.00	0.00
	(ii) Export Import Bank of India	0.00	0.00
	(iii) Industrial Investment Bank of India Ltd.	0.00	0.00
	(iv) Others	0.00	0.00
	Sub total	***0.00***	***0.00***
	(D) Loans, Advances and Investments from National Industrial Credit (Long Term Operations) Fund:		
	(a) Loans and Advances to National Housing Bank	0.00	0.00
	(b) Investments in bonds/debentures issued by National Housing Bank	0.00	0.00
	Sub total	***0.00***	***0.00***
	Total	**370.83**	**802.32**

		2013-14	2014-15
Schedule 10:	**Investment in subsidiaries**		
	(i) Deposit Insurance and Credit Guarantee Corporation	0.50	0.50
	(ii) National Housing Bank	4.50	4.50
	(iii) National Bank for Agriculture and Rural Development	0.20	0.20
	(iv) Bhartiya Reserve Bank Note Mudran (P) Ltd	8.00	8.00
	Total	**13.20**	**13.20**
Schedule 11:	**Other Assets**		
	(i) Fixed Assets (net of accumulated depreciation)	5.22	3.92
	(ii) Accrued income (a + b)	**225.90**	**206.26**
	a. on loans to employees	3.09	3.16
	b. on other items	222.81	203.10
	(iii) Swap Amortisation Account	59.30	94.33
	(iv) Revaluation of Forward Contracts Account (RFCA)	42.85	0.00
	(v) Miscellaneous	9.86	8.92
	Total	**343.13**	**313.43**
Schedule 12:	**Interest**		
	(i) Domestic Sources		
	a. Interest on holding of Domestic Securities	470.53	436.30
	b. Net Interest on LAF Operations	59.02	28.29
	c. Interest on MSF Operations	17.45	1.88
	d. Profit on Sale of Domestic Securities	331.37	139.15
	e. Depreciation	(-)480.45	(-)98.28
	f. Interest on Loans and Advances	37.46	14.06
	(ii) Foreign Sources		
	a. Interest on holding of Foreign Securities	201.50	223.42
	Total	**636.88**	**744.82**
Schedule 13:	**Income-Others**		
	(i) Discount from foreign assets	6.81	4.40
	(ii) Exchange from Foreign Exchange Transactions	(-)10.61	29.62
	(iii) Commission	12.57	13.38
	(iv) Rent Realised	0.05	0.05
	(v) Profit/loss on sale of Bank's property	0.01	0.02
	(vi) Provision no longer required	0.46	0.27
	Total	**9.29**	**47.74**
Schedule 14:	**Agency Charges**		
	(i) Agency Commission on Government Transactions	27.81	29.63
	(ii) Underwriting Commission paid to the Primary Dealers	4.81	0.33
	(iii) Sundries (Handling charges paid to banks for Relief/Savings Bonds subscriptions)	0.00	0.00
	(iv) Fees paid to the External Asset Managers, Custodians, etc.	0.63	0.49
	Total	**33.25**	**30.45**

INDEPENDENT AUDITORS' REPORT

TO THE PRESIDENT OF INDIA

Report on the Financial Statements

We, the undersigned Auditors of the Reserve Bank of India (hereinafter referred to as the "Bank"), do hereby report to the Central Government upon the Balance Sheet of the Bank as at June 30, 2015 and the Income Statement for the year ended on that date (hereinafter referred to as "financial statements"), which have been audited by us.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation of these financial statements that give a true and correct view of the state of affairs and results of operations of the Bank in accordance with the requirements of the provisions of the Reserve Bank of India Act, 1934 and Regulations framed thereunder and the accounting policies and practices followed by the Bank. This responsibility includes the design, implementation and maintenance of internal control relevant to the preparation and presentation of the financial statements that give a true and correct view and are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with the Standards on Auditing issued by the Institute of Chartered Accountants of India. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the Bank's preparation and correct presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of the accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion and to the best of our information and according to explanations given to us and as shown by the books of account of the Bank, the Balance Sheet read with Significant Accounting Policies is a full and fair Balance Sheet containing all necessary particulars and is properly drawn up in accordance with the requirements of the provisions of the Reserve Bank of India Act, 1934 and Regulations framed there under so as to exhibit true and correct view of the state of affairs of the Bank.

Other Matters

We report that we have called for information and explanation from the Bank which was necessary for the purpose of our audit and such information and explanation have been given to our satisfaction.

We also report that the financial statements include the accounts of nineteen accounting units of the Bank which have been audited by Statutory Branch Auditors and we have relied on their report in this regard.

For Haribhakti & Co. LLP
Chartered Accountants
(ICAI Firm Registration No. 103523W)

Rakesh Rathi
Partner
Membership No. 045228

For CNK & Associates LLP
Chartered Accountants
(ICAI Firm Registration No. 101961W)

Manish Sampat
Partner
Membership No. 101684

Place: Mumbai
Date: August 13, 2015

STATEMENT OF SIGNIFICANT ACCOUNTING POLICIES FOR THE YEAR ENDED JUNE 30, 2015

1. General

1.1 The Reserve Bank of India was established under the Reserve Bank of India Act, 1934 (the Act) "to regulate the issues of Bank notes and the keeping of reserves with a view to securing monetary stability in India and generally to operate the currency and credit system of the country to its advantage".

1.2 The main functions of the Bank are:-

a) Issue of Bank notes.

b) Management of the monetary system.

c) Regulation and supervision of banks and Non –Banking Finance Companies (NBFCs).

d) Acting as the lender of last resort.

e) Regulation and supervision of the Payment and Settlement Systems.

f) Maintaining and managing the country's foreign exchange reserves.

g) Acting as the banker to banks and the Governments

h) Acting as the debt manager of the Governments.

i) Regulation and development of foreign exchange market.

j) Developmental functions including in the areas of rural credit and financial inclusion.

1.3 The Act requires that the issue of Bank notes should be conducted by the Bank in the Issue Department which shall be separate and kept wholly distinct from the Banking Department and the assets of the Issue Department shall not be subject to any liability other than the liabilities of the Issue Department. The Act requires that the assets of the Issue Department shall consist of gold coins, gold bullion, foreign securities, rupee coins and rupee securities to such aggregate amount as is not less than the total of the liabilities of the Issue Department. The Act requires that the liabilities of the Issue Department shall be an amount equal to the total of the amount of the currency notes of the Government of India and Bank notes for the time being in circulation.

2. Significant Accounting Policies

2.1 Convention

The financial statements are prepared in accordance with the Reserve Bank of India Act, 1934 and the notifications issued thereunder and in the form prescribed by the Reserve Bank of India General Regulations, 1949. These are based on historical cost except where it is modified to reflect revaluation. The accounting policies followed in preparing the financial statements are consistent with those followed in the previous year unless otherwise stated.

2.2 Revenue Recognition

(a) Income and expenditure are recognised on accrual basis except penal interest which is accounted for only when there is certainty of realisation. Policy on dividend income on shares has been revised during the year and is now recognised on accrual basis when the right to receive the same is established as against the earlier policy of recognising it on cash basis.

(b) Balances unclaimed and outstanding for more than three clear consecutive years in certain transit accounts including Drafts Payable Account, Payment Orders Account, Sundry Deposits Account, Remittance Clearance Account and Earnest Money Deposit Account are reviewed and written back to income.

Claims, if any, are considered and charged against income in the year of payment.

(c) Income and expenditure in foreign currency are recorded at the exchange rates prevailing on the last business day of the week/month/ year as applicable.

2.3 Gold & Foreign Currency Assets and Liabilities

Transactions in gold and foreign currency assets are accounted for on settlement date basis.

(a) Gold

Gold is revalued on the last business day of the month at 90 per cent of the daily average price quoted by the London Bullion Market Association (LBMA) for the month. The rupee equivalent is determined on the basis of the exchange rate prevailing on the last business day of the month. Unrealised gains/ losses are credited/debited to the Currency and Gold Revaluation Account (CGRA).

(b) Foreign Currency Assets and Liabilities

All foreign currency assets and liabilities (excluding foreign currency received under the swaps that are in the nature of repos and contracts where the rates are fixed contractually) are translated at the exchange rates prevailing on the last business day of the week/month/ year as applicable. Gains and losses arising from such translation of foreign currency assets and liabilities are accounted for in CGRA and remain adjusted therein. Foreign securities other than Treasury Bills, Commercial Papers, and certain "held to maturity" securities (such as investments in notes issued by the International Monetary Fund and bonds issued by India Infrastructure Finance Company (IIFC), UK) which are valued at cost, are marked to market as on the last business day of each month. Appreciation or depreciation is recorded in the Investment Revaluation Account (IRA). Credit balance is carried forward to the subsequent year. Debit balance, if any, at the end of the year in IRA is required to be charged to the Contingency Fund and the same is to be reversed to the credit of the Contingency Fund on the first working day of the succeeding financial year. Till 2013 -14, the policy was to charge such debit balance in the IRA to the Profit and Loss Account. Foreign Treasury Bills and Commercial Papers are carried at cost as adjusted by amortisation of discount. Premium or discount on foreign securities is amortised daily. Profit/loss on sale of foreign currency assets is recognised with respect to the book value. On sale/redemption of foreign dated securities valuation gain/loss in respect of the securities sold, lying in IRA, is transferred to the Income account.

(c) Forward/Swap Contracts

Forward contracts entered into by the Reserve Bank as part of its intervention operations are revalued on a yearly basis on June 30. While the marked to market gain is credited to the 'Foreign Exchange Forward Contracts Valuation Account' (FCVA) with contra debit to Revaluation of Forward Contracts Account (RFCA), marked to market loss is debited to the FCVA with contra credit to the Provision for Forward Contracts Valuation Account (PFCVA). Debit balance in FCVA, if any, on June 30, is required to be charged to the Contingency Fund and reversed on the first working day of the following year. On maturity of the contract, the actual gain or loss is required to be recognised in the Income Account and the unrealised gains/losses previously recorded in the FCVA, RFCA and PFCVA are required to be reversed. The balance in the RFCA and PFCVA represent the net unrealised gains and losses on valuation of such forward contracts respectively.

In the case of swaps entered at off-market rates that are in the nature of repo, the difference between the future contract rate and the rate at which the contract is entered into is amortised over the period of the contract and recorded in the Income Account with contra entry in the Swap Amortisation Account (SAA). The amounts recorded in the SAA are reversed on maturity of the underlying contracts. Further, the amounts received under these swaps are not subject to periodic revaluation.

While FCVA and PFCVA form part of 'Other Liabilities', RFCA and SAA form part of 'Other Assets'.

2.4 Domestic Investments

(a) Rupee Securities

Rupee securities, held as part of Bank's domestic investments, are valued at lower of book value or market value (LOBOM). Where the market price for such securities is not available, the rates are derived based on the yield curve prevailing on the last business day of the month as notified by the Fixed Income Money Market and Derivatives Association of India (FIMMDA). Depreciation, if any, is adjusted against current year's interest income. Non- interest bearing rupee securities held as backing for note issue and securities which are earmarked against funds, such as, Gratuity and Superannuation, Provident Fund, Leave Encashment, Medical Assistance Fund, and Depositors' Education and Awareness (DEA) Fund are, however, categorised as held to maturity (HTM) and therefore not marked to market.

(b) Treasury Bills

Treasury bills are valued at cost.

(c) Shares

Investments in shares are valued at cost.

2.5 Liquidity Adjustment Facility (LAF) Repo/ Reverse Repo and Marginal Standing Facility (MSF)

From the year 2014-15 onwards Repo under LAF and Marginal Standing Facility (MSF) is being treated as lending and is being shown under 'Loans and Advances' whereas 'Reverse Repo' is being treated as deposits and is being shown under 'Deposit-Others'. Till last year, Repo under LAF and MSF were being accounted for as purchase of rupee securities and Reverse Repo as sale of rupee securities.

2.6 Fixed Assets

a. Fixed Assets are stated at cost less depreciation.

b. Depreciation on computers, microprocessors, software (costing ₹0.1 million and above), motor vehicles, furniture, *etc.* is provided on straight-line basis at the following rates.

Asset Category	Rate of Depreciation
Motor vehicles, Furniture, *etc.*	20 per cent
Computers, Microprocessors, Software, *etc.*	33.33 per cent

c. Amortisation of premium on leasehold land and depreciation on building is provided on written-down value basis at the following rates.

Asset Category	Rate of Depreciation/ Amortisation
Leasehold Land and Building(s) constructed thereon	Proportionate to lease period but not less than 5 per cent
Building(s) constructed on Freehold Land	10 per cent

d. Fixed Assets, costing less than ₹0.1 million (except easily portable electronic assets) are charged to income in the year of acquisition. Easily portable electronic assets, such as laptops, etc. costing more than ₹10,000 are capitalised and depreciation is calculated at applicable rates.

e. Individual items of computer software costing ₹0.1million and above are capitalised and depreciation is calculated at the applicable rates.

f. Depreciation is provided on year-end balances of the Fixed Assets.

g. For assessment of impairment/ re-statement of carrying value, buildings are classified into two categories as under:

   (i) *Buildings which are in use but have been identified for demolition in future/will be discarded in future:* The value in use of such buildings is the aggregate of depreciation for the future period up to the date it is expected to be discarded/ demolished. The difference between the book value and aggregate of depreciation so arrived at is required to be charged as depreciation.

   (ii) *Buildings which have been discarded/ vacated:* These buildings are to be shown at realisable value (net selling price, if the asset is likely to be sold in future) / scrap value less demolition cost (if it is to be demolished). If the amount is negative, then the carrying value of such buildings has to be shown at ₹1. The difference between the book value and realisable value (*i.e.*, the net selling price) / scrap value less demolition cost is required to be charged as depreciation. The asset is required to be shown under the head "Other assets" - "Miscellaneous".

2.7 Employee Benefits

The liability on account of long term employee benefits is provided based on an actuarial valuation under the 'Projected Unit Credit' method.

NOTES TO THE ACCOUNTS

XI.11 Liabilities and Assets of the Bank

XI.11.1 LIABILITIES

i) Capital

The Reserve Bank was constituted as a private shareholders' bank in 1935 with an initial paid-up capital of ₹0.05 billion. The Bank was nationalised with effect from January 1, 1949 and its entire ownership remains vested in the Government of India. The paid-up capital continues to be ₹0.05 billion as per section 4 of the Reserve Bank of India Act,1934.

ii) Reserve Fund

The original Reserve Fund of ₹0.05 billion was created in terms of section 46 of the Reserve Bank of India Act,1934 as contribution from the Central Government for the currency liability of the then sovereign government taken over by the Reserve Bank. Thereafter, an amount of ₹64.95 billion was credited to this Fund from out of gains on periodic revaluation of gold up to October 1990, taking it to ₹65 billion. The fund has been static since then and gain/loss on account of valuation of gold and foreign currency is booked in the Currency and Gold Revaluation Account (CGRA) which is part of the balance sheet head 'Other Liabilities' and provisions.

iii) Other Reserves

This includes National Industrial Credit (Long Term Operations) Fund and National Housing Credit (Long Term Operations) Fund.

a. National Industrial Credit (Long Term Operations) Fund

This fund was created in July 1964, under section 46C of the Reserve Bank of India Act, 1934 with an initial corpus of ₹100 million. The fund witnessed annual contributions from the Reserve Bank for financial assistance to eligible financial institutions. Since 1992-93, a token amount of ₹10 million is being contributed each year to the Fund from the Bank’s income. The balance in the fund stood at ₹0.24 billion as on June 30, 2015.

b. National Housing Credit (Long Term Operations) Fund

This fund was set up in January 1989 under section 46D of the Reserve Bank of India Act,1934 for extending financial accommodation to the National Housing Bank. The initial corpus of ₹500 million has been enhanced by annual contributions from the Reserve Bank thereafter. From the year 1992-93, only a token amount of ₹10 million is contributed each year from the Bank’s income. The balance in the fund stood at ₹1.98 billion as on June 30, 2015.

c. Contribution to other Funds

There are two other Funds constituted under section 46A of the Reserve Bank of India Act,1934 *viz*., National Rural Credit (Long Term Operations) Fund and National Rural Credit (Stabilisation) Fund which are maintained by the National Bank for Agriculture and Rural Development (NABARD) for which a token amount of ₹10 million each is transferred to NABARD every year.

iv) Deposits

These represent the balances maintained with the Reserve Bank by banks, the Central and State Governments, All India Financial Institutions, such as, Export Import Bank of India (EXIM Bank) and NABARD, Foreign Central Banks, International Financial Institutions, balance in different accounts relating to the Employees’ Provident Fund, and balance in the Depositors’ Education and Awareness Fund (DEA Fund). DEA Fund was created in the year 2013-14 for promotion of depositors’ interest and for such other related purposes. Total deposits stood at ₹5,186.86 billion as on June 30, 2015 as compared with ₹3,769.45 billion as on June 30, 2014, registering an increase of 37.60 per cent.

a. Deposits – Government

The Reserve Bank acts as banker to the central government in terms of sections 20 and 21 and as banker to the state governments by mutual agreement in terms of section 21(A) of the Reserve Bank of India Act, 1934. Accordingly, the central and the state governments maintain deposits with the Reserve Bank. The balances held by the central and state governments were ₹1.01 billion and ₹0.43 billion respectively as on June 30, 2015, totalling ₹1.44 billion.

b. Deposits – Banks

Banks maintain balances in their current accounts with the Reserve Bank to provide for the Cash Reserve Ratio (CRR) requirements and for working funds to meet payment and settlement obligations. The amount of deposits in the current account of banks as on June 30, 2015 stood at ₹3,946.85 billion as compared with ₹3,677.24 billion as on June 30, 2014, registering an increase of 7.33 per cent during the year.

c. Deposits - Others

‘Deposits- Others’ consists of balances of Administrator of the RBI Employees’

Provident Fund, balance in the Depositors' Education and Awareness Fund (DEA Fund), balances in accounts of Foreign Central Banks, Indian and International Financial Institutions and outstanding Reverse Repo. From 2014-15, Reverse Repo transactions are being treated as deposit of funds with the Bank and therefore the outstanding Reverse Repo now forms part of 'Deposit-Others'. The amount under Deposits-Others increased by 1264.21 per cent from ₹90.79 billion as on June 30, 2014 to ₹1,238.57 billion as on June 30, 2015 primarily due to amounts held by the Bank under reverse repo transactions.

v) Other Liabilities and Provisions

The major components of 'Other Liabilities and Provisions' are provisions under different heads and Gratuity and Superannuation Fund. Till 2013-14 balances held in Gratuity and Superannuation Funds were shown under 'Deposits'-Others'. These are now shown under 'Other Liabilities and Provisions'. While Contingency Fund and Asset Development Fund represent provisions made for unforeseen contingencies and internal capital expenditure respectively, the remaining components of 'Other Liabilities and Provisions', such as, Currency and Gold revaluation account (CGRA), Investment Revaluation Account (IRA) and Foreign Exchange Forward Contracts Valuation Account (FCVA), represent unrealised marked to market gains/losses. Other Liabilities and Provisions declined by 0.63 per cent from ₹8,961.70 billion as on June 30, 2014 to ₹8,905.03 billion as on June 30, 2015, primarily due to decline in the balance held in CGRA.

a. Contingency Fund

The Contingency Fund (formerly Contingency Reserve) represents the amount set aside on a year-to-year basis for meeting unexpected and unforeseen contingencies, including depreciation in the value of securities, risks arising out of monetary/exchange rate policy operations, systemic risks and any risk arising on account of the special responsibilities enjoined upon the Bank.

b. Asset Development Fund

The Asset Development Fund (formerly Asset Development Reserve) created in 1997-98, represents the amounts provided out of income each year to meet internal capital expenditure and make investments in subsidiaries and associated institutions. During the year, there has been an addition of ₹10 billion to provide for further investment as capital in the National Housing Bank.

c. Currency and Gold Revaluation Account (CGRA)

Following the best international practices, unrealised gains/losses on valuation of Foreign Currency Assets (FCA) and Gold are not taken to the Income Account but instead recorded under a balance sheet head named as the Currency and Gold Revaluation Account (CGRA). CGRA represents accumulated net balance of unrealised gains arising out of valuation of FCA and Gold and, therefore, its balance varies with the size of the asset base, movement in the exchange rate and price of gold. During 2014-15, the balances in CGRA decreased by 2.27 per cent from ₹5,721.63 billion as on

June 30, 2014 to ₹5,591.93 billon as on June 30, 2015 mainly due to appreciation of US Dollar against other major currencies and fall in the price of Gold.

d. Investment Revaluation Account (IRA)

The foreign dated securities are marked to market on the last business day of each month and the unrealised gains/ losses arising therefrom are transferred to the IRA. The balance in the IRA as on June 30, 2015 was ₹32.14 billion as compared with ₹37.91 billion as on June 30, 2014.

e. Foreign Exchange Forward Contracts Valuation Account (FCVA) & Provision for Forward Contracts Valuation Account (PFCVA)

MTM of outstanding forward contracts as on June 30, 2015 resulted in a net loss of ₹0.39 billion, which was debited to the FCVA with contra credit to the PFCVA. As per the extant policy, the debit balance of ₹0.39 billion in FCVA was adjusted against the Contingency Fund on June 30, 2015 and reversed on July 1, 2015. Accordingly, the balance in FCVA and PFCVA as on June 30, 2015 was nil and ₹0.39 billion respectively, as against a balance of ₹.42.98 billion and nil respectively as on June 30, 2014.

The position of balances in CGRA, IRA, FCVA and PFCVA for the last five years is given in Table XI.3.

Table XI.3: Balances in Currency and Gold Revaluation Account (CGRA), Foreign Exchange Forward Contracts Valuation Account (FCVA), Provision for Forward Contracts Valuation Account (PFCVA) and Investment Revaluation Account (IRA)

(₹ billion)

As on June 30	CGRA	FCVA#	PFCVA@	IRA
1	2	3	4	5
2011	1,822.86	0.01	--	42.69
2012	4,731.72	24.05	--	122.22
2013	5,201.13	16.99	--	24.85
2014	5,721.63	42.98	0.00	37.91
2015	5,591.93	0.00	0.39	32.14

\# The equivalent account was Exchange Equalisation Account (EEA) till 2012-13.

@ Opened during 2013-14.

f. Surplus transferable to the Government of India

Under Section 47 of the Reserve Bank of India Act, 1934 after making provisions for bad and doubtful debts, depreciation in assets, contribution to staff and superannuation fund and for all matters for which provisions are to be made by or under the Act or that are usually provided by bankers, the balance of the profits of the Bank is required to be paid to the Central Government. Under Section 48 of the Reserve Bank Act, 1934 the Bank is not liable to pay income tax or super tax or any other tax on any of its income, profits or gains and is also exempt from payment of wealth tax. Accordingly, after adjusting expenditure, the contribution of an amount of ₹0.04 billion to the statutory funds, and necessary provisions, the surplus transferable to the Government of India for the year 2014-15 amounted to ₹658.96 billion, (including ₹11.46 billion as against ₹12.69 billion in the previous year payable towards the difference in interest expenditure borne by the Government consequent on conversion of special securities into marketable securities).

g. Bills Payable

The Reserve Bank provides remittance facilities for its constituents and also meets its own payments requirements through issue of Demand Drafts (DDs) and Payment Orders (POs) (besides electronic payments mechanisms). The balance under this head represents the unclaimed DDs/ POs . The total amount outstanding under this head decreased from ₹0.37 billion as on June 30, 2014 to ₹0.17 billion as on June 30, 2015 mainly due to lesser use of DDs/POs.

h. Miscellaneous

This is a residual category representing items such as interest earned on earmarked securities, amounts payable on leave encashment, etc. Till 2013-14 this category included margin maintained on Repo transactions, which has since been discontinued following the change in accounting treatment of Repo under LAF and MSF. The decrease in balance under this category from ₹68.24 billion as on June 30, 2014 to ₹30.83 billion as on June 30, 2015 was mainly on account of discontinuation of accounting of margins in respect of Repo under LAF and MSF.

vi Liabilities of Issue Department- Notes Issued

The liabilities of the Issue Department reflect the quantum of currency notes in circulation. Section 34 (I) of the Reserve Bank of India Act requires that all bank notes issued by the Reserve Bank since April 1, 1935 and the currency notes issued by the Government of India before the commencement of operations of the Reserve Bank be part of the liabilities of the Issue Department. The currency notes in circulation increased by 9.57 per cent from ₹13,445.16 billion as on June 30, 2014 to ₹14,732.43 billion as on June 30, 2015.

XI.11.2 ASSETS

11.2.1 Assets of Banking Department (BD)

The assets comprise Notes, Rupee Coin and Small Coin, Gold Coin and Bullion, Foreign Currency Assets, investments in Rupee Securities, Bills Purchased and Discounted, Loans and Advances, Investment in Subsidiaries, Other Assets. The details are as under:

i) Notes, Rupee Coin and Small Coin

This is the balance of bank notes, one rupee notes, rupee coins of ₹1, 2, 5 and 10 and small coins kept in the vaults of the Banking Department to meet the day to day requirements of the banking functions conducted by the Reserve Bank. The balance as on June 30, 2015 was ₹0.11 billion, which was the same as on June 30, 2014.

ii) Gold Coin and Bullion

Bank holds 557.75 metric tonnes of gold, of which 292.26 metric tonnes are held as backing for notes issued and shown separately as an asset of Issue Department. The balance 265.49 metric tonnes is treated as an asset of Banking Department. The value of gold held as asset of Banking Department declined by 1.93 per cent from ₹590.24 billion as on June 30, 2014 to ₹578.84 billion as on June 30, 2015 on account of decline in international gold prices.

iii) Bills Purchased and Discounted

Though the Reserve Bank can undertake purchase and discounting of commercial bills under the Reserve Bank of India Act,1934, no such activity has been undertaken in 2014-15;

consequently, there was no such asset in the books of the Reserve Bank as on June 30, 2015.

iv) Investments Foreign –BD

The Foreign Currency Assets (FCA) of the Reserve Bank are shown under two heads in the Balance Sheet: (a) 'Investments-Foreign-BD', shown as a distinct item under the assets of the Banking Department and (b) 'Investments-Foreign-ID' as Issue Department assets.

Investments-Foreign-BD include (i) deposits with other central banks, (ii) deposits with the Bank for International Settlements (BIS), (iii) balances with foreign branches of commercial banks, (iv) investments in foreign treasury bills and securities and (v) Special Drawing Rights (SDR) acquired from the Government of India. Investments-Foreign-ID comprises Deposits, T-bills and dated securities. The position of FCA of the Bank for the last two years is given in Table XI.4.

v) Investments- Domestic-BD

Investments comprise dated Government Rupee Securities, Treasury Bills and Special

Table XI.4: Details of Foreign Currency Assets (FCA)

(₹ billion)

	Particulars	As on June 30	
		2014	2015
	1	2	3
I	Assets of Issue Department Investments-Foreign-ID (Foreign securities under Issue Department balance sheet till 2013-14)	12,783.31	14,082.75
II	Assets of Banking Department		
	(a) Included in 'Investments' (*Till 2013-14*)	1,069.45	0.00*
	(b) Investment-Foreign-BD	3,726.76	7,276.29@
	Total	17,579.52	21,359.04

* : Foreign Securities and Shares in BIS and SWIFT held under this head have been moved under Investments-Foreign-BD during the year.

@ : including SDRs valued at ₹99.08 billion.

Notes:

1. Uncalled amount on partly paid shares of the Bank for International Settlements (BIS) as on June 30, 2015 was ₹1.08 billion (SDR 12,041,250). The amount was ₹1.12 billion (SDR 12,041,250) in the previous year.
2. The Reserve Bank has agreed to make resources available under the IMF's New Arrangements to Borrow (NAB) [which subsumes the earlier commitment of US$ 10 billion (₹637.55 billion) under the Note Purchase Agreement] up to a maximum amount of SDR 8.74 billion (₹783.74 billion /US$12.29 billion). As on June 30, 2015, investments amounting to SDR 0.84 billion (₹75.22 billion/US$ 1.18 billion) have been made under the NAB.
3. The Reserve Bank has agreed to invest up to an amount, the aggregate of which shall not exceed US$ 5 billion (₹318.77 billion), in the bonds issued by the India Infrastructure Finance Company (IIFC), UK. As on June 30, 2015, the Reserve Bank has invested US$ 2.10 billion (₹133.89 billion) in such bonds.
4. In terms of the Note Purchase Agreement (NPA) 2012 entered into by the Reserve Bank with IMF, Reserve Bank would purchase SDR denominated Notes of the IMF for an amount up to the equivalent of US$ 10 billion (₹637.55 billion).
5. During the year 2013-14, the Reserve Bank and the Government of India (GoI) entered into a MoU for transfer of SDR holdings from GoI to the Reserve Bank in a phased manner. During the year ending June 30, 2015, SDR 0.57 billion (₹51.16 billion; US$ 0.82 billion) was transferred to the Reserve Bank. The SDR balance held by the Reserve Bank as on June 30, 2015, was SDRs 1.1 billion (₹99.08 billion; US$ 1.55 billion).
6. With a view to strengthening regional financial and economic cooperation, the Reserve Bank has agreed to offer an amount of US $ 2 billion both in foreign currency and Indian rupee under the SAARC Swap Arrangement to SAARC member countries. During the year ending June 30, 2015, Sri Lanka (Central Bank of Sri Lanka) has availed of US$ 0.4 billion (₹25.50 billion) under this arrangement.

Oil bonds. However, as on June 30, 2015 the Bank did not hold any treasury bills. The Reserve Bank's holdings of domestic securities held as part of Bank's investments came down by 22.58 per cent, from ₹6,684.68 billion as on June 30, 2014 to ₹5174.97 billion as on June 30, 2015.The decrease was on account of (a) change in accounting treatment of Repo/ Reverse Repo under LAF and MSF (b) liquidity management operations conducted by the Bank, and (c) GoI securities maturing during the year 2014-15.

vi) Loans and Advances

a) Central and State Governments

These loans are extended in the form of Ways and Means Advances (WMA) in terms of Section 17(5) of the Reserve Bank of India Act and the limit in case of central government is fixed from time to time in consultation with them and in case of state governments, the limits are fixed based on the recommendations of Advisory Committee/Group constituted for this purpose. No loans and advances to the central government were outstanding as on June 30, 2015 and June 30, 2014. Loans and advances to the state governments as on June 30, 2015 stood at ₹25.77 billion as compared with ₹6.66 billion as on June 30, 2014.

b) Loans and advances to Commercial and Co-operative banks

These mainly include refinance availed from the Reserve Bank under the export credit refinance (ECR) facility against eligible outstanding export credit and amounts outstanding under Repo under Liquidity Adjustment facility (LAF)and Marginal Standing Facility (MSF). From the year 2014-15, Repo under LAF and MSF are being treated as lending and reflected under this head, as a result of which, the balance under this head, increased by 147.87 per cent from ₹295.51 billion as on June 30, 2014 to ₹732.48 billion as on June 30, 2015.

c) Loans and advances to NABARD

The Reserve Bank can extend loans to NABARD under section 17 (4E) of the Reserve Bank of India Act,1934. As on June 30, 2015 no loan is outstanding.

d) Loans and advances to others

The balance under this head represents loans and advances to National Housing Bank (NHB), Small Industries Development Bank of India (SIDBI), liquidity support provided to Primary Dealers (PDs) and outstanding Repo/ Term Repo conducted with the PDs amounting to ₹44.07 billion. The balance under this head decreased by 35.81 per cent from ₹68.66 billion as on June 30, 2014 to ₹44.07 billion as on June 30, 2015 primarily on account of repayment of loans by SIDBI.

vii) Investment in Subsidiaries

The details of holdings in subsidiaries institutions as on June 30, 2015 are given in Table XI.5.

Table XI 5: Holdings in subsidiaries

(Amount in ₹ billion)

	Cost	% holding
1	2	3
a) Deposit Insurance and Credit Guarantee Corporation (DICGC)	0.50	100
b) National Bank for Agriculture and Rural Development(NABARD)	0.20	1
c) National Housing Bank (NHB)	4.50	100
d) Bharatiya Reserve Bank Note MudranPvt. Ltd. (BRBNMPL)	8.00	100
Total	**13.20**	

viii) Other Assets

a. ‘Other Assets’ comprise fixed assets (net of depreciation), accrued income on domestic and foreign investments, balances held in Swap Amortisation Account (SAA), Revaluation of Forward Contracts Account (RFCA) and Miscellaneous Assets. Miscellaneous Assets comprise mainly loans and advances to staff, amount spent on projects pending completion, security deposit paid *etc*. The amount outstanding under ‘Other Assets’ decreased by 8.66 per cent from ₹343.13 billion as on June 30, 2014 to ₹313.43 billion as on June 30, 2015 primarily on account of marked to market loss on forward contracts as on June 30, 2015 as against marked to market gain as on June 30, 2014.

b. Swap Amortisation Account (SAA)

In the case of swaps that are in the nature of repo at off-market rates, the difference between the future contract rate and the rate at which the contract is entered is amortised over the period of the contract and held in the SAA. The balance in this account increased by 59 per cent from ₹59.30 billion as on June 30, 2014 to ₹94.33 billion as on June 30, 2015. The amounts held in this account will be reversed on maturity of the underlying contracts.

c. Revaluation of Forward Contracts Account (RFCA)

Forward contracts which are entered into as part of intervention operations are marked to market on June 30. The net gain is required to be recorded in the RFCA, and reversed on the maturity of the underlying contracts. The balance in this account as on June 30, 2015 was nil on account of marked to market loss on forward contracts.

11.2.2 Assets of Issue Department

The eligible assets of the Issue Department held as backing for notes issued consist of Gold Coin and Bullion, Rupee Coin, Foreign Currency Assets, Government of India non-interest bearing Rupee Securities and Domestic Bills of Exchange and other Commercial Papers. The Reserve Bank holds 557.75 metric tonnes of gold, of which 292.26 metric tonnes are held in India as backing for notes issued (Table XI.6). The value of gold held as backing for notes issued decreased by 1.93 per cent from ₹649.78 billion as on June 30, 2014 to ₹637.23 billion as on June 30, 2015, reflecting declining international bullion prices. Consequent upon an increase in notes issued, foreign currency assets held as backing for notes issued increased by 10.17 per cent from ₹12,783.31 billion as on June 30, 2014 to ₹14,082.75 billion as on June 30, 2015. The balance of Rupee coins held by Issue Department increased by 15.70 per cent from ₹1.72 billion as on June 30, 2014 to ₹1.99 billion as on June 30, 2015. The amount of non-interest bearing rupee securities remained unchanged at ₹10.46 billion.

XI.12 Foreign Currency Assets and Foreign Exchange Reserves

The Foreign Exchange Reserves (FER) predominantly comprises FCA, besides gold,

Table XI.6: Physical holding of Gold

	As on June 30, 2014	As on June 30, 2015
	Volume in metric tonnes	Volume in metric tonnes
1	2	3
Gold held for backing note issue (held in India)	292.26	292.26
Gold held as asset of Banking Department (held abroad)	265.49	265.49
Total	**557.75**	**557.75**

Table XI.7(a): Foreign Exchange Reserves

(Amount in ₹ billion)

	As on June 30		Variation	
	2014	2015	Absolute	Per Cent
1	2	3	4	5
Foreign Currency Assets (FCA)	17,530.21^	21,100.56#	3,570.35	20.37
Gold	1,240.02	1,216.07@	(-) 23.94	(-) 1.93
Special Drawing Rights (SDR)	268.31	259.03	(-) 9.28	(-) 3.46
Reserve Position in the IMF	103.23	83.96	(-) 19.27	(-) 18.67
Foreign Exchange Reserves (FER)	19,141.77	22,659.62	3,517.86	18.38

^ : Excludes SDR Holdings of the Reserve Bank amounting to ₹49.31 billion which is included under the SDR holdings.

: Excludes (a) SDR Holdings of the Reserve Bank acquired from GOI, amounting to ₹99.08 billion, which is included under the SDR holdings, (b) Investment of ₹133.89 billion in bonds issued by IIFC (UK) and (c) ₹25.50 billion lent to Sri Lanka under a Currency Swap arrangement made available for SAARC countries.

@ : Of this, Gold valued at ₹637.23 billion is held as an asset of Issue Department and Gold valued at ₹578.84 billion is held under asset of Banking Department.

Table XI.7(b): Foreign Exchange Reserves

(Amount in US $ billion)

	As on June 30		Variation	
	2014	2015	Absolute	Per Cent
1	2	3	4	5
Foreign Currency Assets (FCA)	289.32*	331.55**	42.23	14.59
Gold	20.63	19.07	(-) 1.56	(-) 7.56
Special Drawing Rights (SDR)	4.47	4.06	(-) 0.41	(-) 9.17
Reserve Position in the IMF	1.72	1.32	(-) 0.40	(-) 23.26
Foreign Exchange Reserves (FER)	316.14	356.00	39.86	12.61

* : Excluding USD 1,181 million invested in bonds of IIFC (UK) and SDRs equivalent to USD 820.56 million acquired by the Reserve Bank.
** : Excludes (a) SDRs equivalent to US$ 1,554 million acquired by the Reserve Bank from GOI, which is included under the SDR holdings, (b) Investment of US$ 2,100 million in bonds issued by IIFC (UK) and (c) LKR equivalent to US$ 400 million received from Sri Lanka under a Currency Swap arrangement made available for SAARC countries.

Special Drawing Rights (SDRs) and Reserve Tranche Position (RTP). Reserve Tranche Position represents India's quota contribution to IMF in foreign currency and is not part of the Bank's balance sheet. The position of Foreign Exchange Reserves as at June 30, 2014 and June 30, 2015 in Indian Rupees and the US dollar, which is the numeraire currency for our foreign exchange reserves, have been furnished in Tables XI.7 (a) and (b).

ANALYSIS OF INCOME AND EXPENDITURE

Income

XI.13 The main components of Reserve Bank's income are Interest Receipts and Others including (i) Discount, (ii) Exchange, (iii) Commission and (iv) Rent Realised, Profit or loss on sale of Bank's property and provisions no longer required. Of these, Interest receipts forms the major portion, supplemented by relatively small amounts of income from other sources, *viz.*, discount, exchange, commission and others.

Earnings from Foreign Sources

XI.14 The income from foreign sources, increased by 30.2 per cent from ₹197.68 billion in 2013-14 to ₹257.44 billion in 2014-15 mainly on account of increase in the size of foreign currency assets which increased from ₹17,579.52 billion rupees as on June 30, 2014 to ₹21, 359.03 billion rupees as on June 30, 2015. The rate of earnings on foreign currency assets was higher at 1.36 per cent in 2014-15 as compared with 1.21 per cent in 2013-14 (Table XI.8).

Earnings from Domestic Sources

XI.15 The net income from domestic sources increased by 19.29 per cent from ₹448.49 billion in 2013-14 to ₹535.00 billion in 2014-15, mainly on account of lower depreciation on rupee securities as the prices of Government securities stayed in a narrow range throughout the year. The substantial decline in depreciation by ₹382.17 billion was offset to a large extent by lower profits realised on sales of securities as the central government is now being compensated based on the weighted average rate of the term auctions conducted by the Reserve Bank during the year as against the earlier system of investing in government securities from out of the Bank's holdings. The details of earnings from domestic sources are given in Table XI.9.

XI.16 The coupon receipts was slightly lower at ₹436.30 billion in 2014-15 as compared to ₹470.53 billion as the Reserve Bank's holding of rupee securities came down on account of Open Market Operations (OMO) sales (including the sales on NDS-OM) and redemption of securities on maturity. No OMO purchases were conducted during the year.

XI.17 The net interest income from LAF and MSF (Interest on Repo and MSF less interest paid by the Bank on Reverse Repo) decreased by 60.53 per cent from ₹76.47 billion in 2013-14 to ₹30.17 billion in 2014-15 largely on account of lower Average Daily Net Liquidity Injection through RBI windows (Repo, Reverse Repo, MSF, Term Repo & Term Reverse Repo).

XI.18 Interest income on Ways and Means Advances (WMA)/Overdraft (OD) from the Centre and States increased by 21.91 per cent from ₹3.88 billion as on June 30, 2014 to ₹4.73 billion as on June 30, 2015. The interest received on account of WMA/OD from the central government during 2014-15 was ₹3.57 billion as compared to ₹3.22 billion during 2013-14 due to higher average utilisation of OD for 19 days by the central government as compared to lower utilisation of OD for 9 days in the previous year. The interest received on WMA/OD/Special Drawing Fund (SDF) from states during the year 2014-15 was ₹1.16 billion as compared to

Table XI.8: Earnings from Foreign Sources

(₹ billion)

Item	As on June 30		Variation	
	2014	2015	Absolute	Per Cent
1	2	3	4	5
Foreign Currency Assets (FCA)	17,579.52	21,359.04	3,779.51	21.50
Average FCA	16,368.93	18,909.29	2,540.36	15.52
Earnings from FCA (interest, discount, exchange gain/loss, capital gain/loss on securities)	197.68	257.44	59.76	30.23
Earnings from FCA as per cent of average FCA	1.21	1.36	0.15	12.40

Table XI.9: Earnings from Domestic Sources

(₹ billion)

Item	Year ended		Variation	
	June 30, 2014	June 30, 2015	Absolute	Per cent
1	2	3	4	5
Domestic Assets	**8664.04**	**7656.01**	**(-)1008.03**	**(-)11.63**
Weekly Average of Domestic Assets	**8694.77**	**7828.99**	**(-)865.78**	**(-)9.96**
Earnings (I + II+III)	**448.49**	**535.00**	**86.51**	**19.29**
I. Interest and other Securities Related Income				
i) Profit on Sale of Securities	331.37	139.15	(-)192.22	(-)58.01
ii) Net Interest on LAF Operations	59.02	28.30	(-)30.72	(-)52.05
iii) Interest on MSF operations	17.45	1.88	(-)15.57	(-)89.23
iv) Interest on holding of Domestic Securities	470.53	436.30	(-)34.23	(-)7.27
v) Depreciation	(-)480.45	(-)98.28	382.17	79.54
Sub total (i+ii+iii+iv+v)	***397.92***	***507.35***	***109.43***	***27.50***
II. Interest on Loans and Advances				
i) To Government (Central & States)	3.88	4.73	0.85	21.91
ii) To Banks & Financial Institutions	33.10	8.87	(-)24.23	(-)73.20
iii) To Employees	0.48	0.46	(-)0.02	(-)4.17
Sub total (i+ii+iii)	***37.46***	***14.06***	***(-)23.40***	***(-)62.47***
III. Other Earnings				
i) Discount	0.01	0.00	(-)0.01	(-)100
ii) Exchange	0.00	0.00	0.00	0.00
iii) Commission	12.57	13.38	0.81	6.44
iv) Rent realised, Profit or Loss on sale of Bank's property and Provisions no longer required.	0.53	0.21	(-)0.32	(-)60.38
Sub total (i+ii+iii+iv)	***13.11***	***13.59***	***0.48***	***3.66***

₹0.66 billion for the year 2013 –14. This is attributable to significantly higher daily average utilisation of WMA/OD/SDF by the States at ₹14.46 billion in 2014-15 as against ₹8.51 billion during 2013-14.

Expenditure

XI.19 The Reserve Bank incurs expenditure in the course of performing its statutory functions by way of agency charges/commission, printing of notes, expenses on remittance of treasure besides staff related and other expenses. The total expenditure of the Reserve Bank increased by 11.92 per cent from ₹119.34 billion in 2013-14 to ₹133.56 billion in 2014-15.

i) Interest Payment

During 2014-15 interest of ₹0.01 billion was credited to Dr B.R.Ambedkar Fund that was set up for giving scholarship to wards of staff.

ii) Employee cost

The employee cost decreased by 6.15 per cent from ₹43.24 billion in 2013-14 to ₹40.58 billion in 2014-15. The major component of employee cost is gratuity and superannuation. The decrease is mainly due to the decrease in the contribution towards accrued liabilities of the Gratuity and Superannuation Fund and other funds based on the actuarial valuation. The contribution for the year 2014-15 was ₹14.83 billion as against ₹18.09 billion in the previous year. GoI dated rupee securities, equivalent to the balances in Provident Fund, Gratuity & Superannuation Fund, Leave Encashment Fund and Medical Assistance Fund, held by the Bank have been specifically ear-marked for these Funds.

iii) Agency Charges

a. *Agency Commission on Government Transactions*

The Reserve Bank discharges the function of banker to the government through a large network of agency bank branches that serve as retail outlets for government transactions. The Reserve Bank pays commission to these agency banks at prescribed rates which were last revised with effect from July 01, 2012. The agency commission paid to these banks on account of government business for the year 2014-15 was ₹29.63 billion as compared with ₹27.81 billion for the year 2013-14, registering an increase of 6.54 per cent. The increase in agency commission could be attributed to the growth in number of transactions and amount involved in government receipts and payments.

b. *Underwriting Commission paid to the Primary Dealers (PDs)*

Reserve Bank paid total underwriting commission of ₹0.33 billion to PDs during 2014-15 as compared to ₹4.81 billion during 2013-14. Underwriting commission was on the lower side as compared to last year due to softening of yields during the year (10 year benchmark yield decreased by around 86 bps) on account of various reasons like RBI rate cut by 75 bps, softening of crude prices; fall in CPI and WPI etc. As the market conditions were benign and risk of devolvement reduced, PDs demanded lesser underwriting commission as compared to last year when market conditions turned volatile after taper tantrum by US Fed in May 2013.

c. *Fees paid to the External Asset Managers, custodians, etc.*

Fees amounting to ₹0.49 billion were paid during the year July-June 2015 as compared to ₹0.63 billion in 2013-14 to the external asset managers who are entrusted with the management of a small portion of the Reserve Bank's foreign exchange reserves and to custodians who hold the foreign assets of the Reserve Bank.

iv) Printing of notes

The expenditure incurred on printing of notes increased by 17.05 per cent from ₹32.14 billion in 2013-14 to ₹37.62 billion in 2014-15 mainly on account of increase in the supply of banknotes.

v) Other expenses

Other expenses consisting of expenditure on remittance of treasure, printing and stationery, audit fees and related expenses, miscellaneous expenses, etc. increased by 39.74 per cent from ₹10.67 billion as on June 30, 2014 to ₹14.91 billion as on June 30, 2015. This is primarily on account of increase in expenditure on Banking Development Scheme from ₹0.53 billion in 2013-14 to ₹3.03 billion in 2014-15.

vi) Provisions

This represents an amount of ₹10 billion transferred to the ADF for the investment to be made in the share capital of NHB.

Previous Year's Figures

XI.20 Figures for the previous year have been rearranged to make them comparable with the current year.

Auditors

XI.21 The statutory auditors of the Bank are appointed by the Central Government in terms of Section 50 of the RBI Act, 1934. The accounts of the Reserve Bank for the year 2014-15 were audited by M/s Haribhakti & Co. LLP, Mumbai and M/s CNK & Associates LLP, Mumbai as the Statutory Central Auditors and M/s M Choudhury and Co., M/s Sundaram & Srinivasan and M/s V K Verma & Co. as Statutory Branch Auditors.

ANNEX	CHRONOLOGY OF MAJOR POLICY ANNOUNCEMENTS: JULY 2014 TO JUNE 2015*

Date of Announcement	Policy Initiative
Monetary Policy Department	
August 5, 2014	SLR was reduced by 50 bps to 22.0 per cent of NDTL effective August 9, 2014.
September 30	ECR liquidity was reduced from 32 per cent of eligible export credit outstanding to 15 per cent effective October 10, 2014.
January 15, 2015	Policy repo rate was reduced by 25 bps to 7.75 per cent.
February 3	SLR was reduced by 50 bps to 21.5 per cent of NDTL effective February 7, 2015. ECR facility was replaced by the system level liquidity effective February 7, 2015.
February 20	The Government and the Reserve Bank entered into an agreement on the Monetary Policy framework introducing flexible inflation targeting.
March 4	Policy repo rate was reduced by 25 bps to 7.5 per cent.
June 2	Policy repo rate was reduced by 25 bps to 7.25 per cent.
Financial Inclusion and Development Department	
August 14, 2014	The operational guidelines of the Self Employment Programme (SEP) component of National Urban Livelihoods Mission (NULM) were issued in line with restructuring of the existing Swarna Jayanti Shahari Rozgar Yojana (SJSRY) as NULM.
November 13	Guidelines were issued on financing of 0.5 million Joint Liability Groups of '*Bhoomi Heen Kisan*' through NABARD.
December 3	Instructions on credit facilities to minority communities were made applicable to the Jain community in view of its notification as minority community under Section 2(c) of the National Commission for Minorities (NCM) Act, 1992.
December 9	Revised guidelines were issued for 2014-15 on Interest Subvention Scheme under the National Rural Livelihoods Mission (NRLM).
December 10	Classification of priority sector lending shortfall and interest payable to banks falling in such categories on deposits placed by them in the Rural Infrastructure Development Fund (RIDF) and other funds, were restructured. The revised deposit rates were linked to shortfall in overall priority sector lending targets.
January 2, 2015	SLBC convenor banks and lead banks were advised to complete the process of providing banking services to unbanked villages with population below 2,000 by August 14, 2015 in line with PMJDY instead of March 2016 as prescribed earlier.
January 28	Banks were advised to dispense with obtaining 'No Due Certificate' from individual borrowers (including SHGs and JLGs) for all types of loans, including loans under Government sponsored schemes, irrespective of the amount involved unless the Government sponsored scheme itself provides for obtention of 'No Due Certificate'.
February 25	Overdrafts extended by banks up to ₹ 5,000 in PMJDY accounts were made eligible for classification under priority sector advances ('others' category) as also weaker sections, provided the borrower's household annual income did not exceed ₹ 60,000 for rural areas and ₹ 1,20,000 for non-rural areas.
March 13	Priority sector loans to persons with disabilities were made eligible for classification under the weaker sections category.

*: Indicative in nature and details available on the Reserve Bank's website.

Date of Announcement	Policy Initiative
March 25	Revised guidelines were issued for relief measures by banks in areas affected by natural calamities.
April 23	Based on the recommendations of the internal working group, priority sector lending guidelines were revised.
May 21	Reporting format for progress under the SHG-Bank Linkage programme was revised with a view to capturing data pertaining to financing of SHGs under NRLM and NULM separately.
Financial Markets Regulation Department	
July 23, 2014	FPI investment in G-secs was restricted to securities with a minimum residual maturity of three years.
September 8	FPIs were permitted to hedge currency risks on coupon receipts from debt securities in India falling due in the next 12 months.
September 30	Short sale limit for liquid G-secs was increased to 0.75 per cent of the outstanding stock or ₹ 600 crore, whichever is lower.
	Initiation of short sale was permitted in the OTC market besides NDS-OM as hitherto.
September 30	Limit for importers to book forward contracts under the past performance route was increased from 50 per cent of the eligible limit to 100 per cent (same as exporters).
December 19	Requirement of exchange of physical confirmation by counterparties of trades matched on F-TRAC was removed.
January 14, 2015	Requirement of statutory auditor's quarterly certificate for hedging under the past performance route was replaced with a declaration signed by the CFO and CS of the customer.
February 3	Bonds issued by multilateral financial institutions in India were permitted as eligible underlying for repo in corporate debt.
February 3	FPI investment in corporate debt was restricted to instruments with a minimum residual maturity of three years. FPI investment in liquid and money market mutual fund schemes was disallowed.
February 5	Scheduled commercial banks, PDs, mutual funds and insurance companies were permitted to undertake re-repo of G-secs acquired through reverse repo.
February 13	Resident entities were permitted to rebook FCY-INR swap contracts after cancellation only after the expiry of the tenor of the cancelled swap.
March 20	T+2 settlement was permitted for outright secondary market transactions in G-secs by FPIs and reported on NDS-OM.
March 31	Position limits for participation by domestic investors and FPIs in the ETCD market, without the requirement of establishing underlying exposure, were increased to US$ 15 million per exchange for USD-INR and US$ 5 million for EUR-INR, GBP-INR and JPY-INR pairs, all put together. In the ETCD market, the requirement of the statutory auditor's certificate was replaced with a signed undertaking from CFO or the senior most functionary for a company's finance and accounts and the Company Secretary.
May 14	NBFCs registered with RBI, including government companies as defined in Sub-section (45) of Section 2 of the Companies Act, 2013 which adhere to the prudential norms prescribed for NBFCs were permitted to undertake ready forward contracts in corporate debt securities.
May 21	For hedging of rupee exchange risk, overseas lenders of INR denominated external commercial borrowings (ECB) were permitted to swap with their overseas bank which shall enter into a back-to-back swap with any AD category-I bank in India.

Date of Announcement	Policy Initiative
June 12	Cash settled interest rate futures (IRF) were permitted on G-secs with a residual maturity of 4-8 years and 11-15 years. Residual maturity of underlying security for 10-year cash settled IRF was relaxed to 8-11 years.
June 25	AD category-I banks were permitted to borrow from specified international/multilateral financial institutions, within the permissible limits, without a case by case approval from the Reserve Bank.
Financial Markets Operations Department	
August 7, 2014	The methodology for computation and dissemination of the rupee reference rate was revised effective September 1, 2014.
August 22	The framework for liquidity management was revised effective September 5, 2014. The revised system of conducting 14-day variable rate term repos four times during a reporting fortnight, *i.e.*, on every Tuesday and Friday, between 11.00-11.30 a.m. for an amount equivalent to one-fourth of 0.75 per cent of system-wide NDTL in each auction, was introduced.
February 20, 2015	The reverse repo and marginal standing facility (MSF) operations were introduced on all Saturdays effective February 21, 2015.
Foreign Exchange Department	
July 3, 2014	Limit on financial commitments by an Indian party for overseas direct investments (ODIs) was restored to 400 per cent of its net worth, subject to a maximum of US$ 1 billion in a financial year under the automatic route.
July 7	Clean credit was permitted for a period not exceeding 180 days from the date of shipment.
July 14	Partly paid equity shares and warrants issued by an Indian company were made eligible instruments for FDI and FPI by FIIs/RFPIs.
July 15	Issue and transfer of shares including compulsorily convertible preference shares and debentures were allowed at a price worked out as per SEBI guidelines in case of listed companies and any internationally accepted pricing methodology in case of unlisted companies on an arm's length basis.
July 17	Resident individuals were permitted to make remittance under LRS for purchasing immovable property abroad.
July 21	e-KYC service launched by the Unique Identification Authority of India (UIDAI) was accepted as a valid process for KYC verification under the Prevention of Money Laundering (Maintenance of Records) Rules, 2005.
July 22	The system of considering project/deferred service export proposals exceeding US$ 100 million by a Working Group was dispensed with and AD banks/ Exim Bank were permitted to give post-award approval without any monetary limit and also permit subsequent changes in the terms of approval within the relevant FEMA guidelines/regulations
July 23	Investment limits in G-secs for FIIs/QFIs/FPIs was enhanced by US$ 5 billion by correspondingly reducing the amount available to long term investors from US$ 10 billion to US$ 5 billion, within the overall limit of US$ 30 billion.
August 27	ADs were allowed to refinance existing ECB by raising fresh ECB at lower all-in-cost even where the average maturity period of the fresh ECB was more than the residual maturity of the existing ECB.
August 28	Eligible investors were permitted to acquire G-secs in any manner as per the prevalent/ approved market practice.

Date of Announcement	Policy Initiative
September 3	Eligible borrowers were allowed to raise rupee denominated ECBs from all other recognised ECB lenders over and above foreign equity holders allowed earlier.
September 8	FPIs were permitted to hedge coupon receipts out of debt securities in India falling due in the next 12 months provided hedge contracts should not be eligible for rebooking on cancellation.
September 17	Indian companies were permitted to issue equity shares against any funds payable by them, remittances of which did not require prior permission of the government or the Reserve Bank.
September 30	Importers were allowed to book forward contracts, under the past performance route, up to 100 per cent of the eligible limit.
November 20	Time of realisation and repatriation of export proceeds for all categories of exporters was fixed at nine months.
November 21	ADs were permitted to allow eligible ECB borrowers to park ECB proceeds in term deposits with AD category-I banks in India for a maximum period of six months pending utilisation for permitted end uses.
November 21	ADs and full-fledged money changers were allowed to release full basic travel quota (BTQ) entitlement in cash or up to the cash limit specified by the Haj Committee of India to Haj/ Umrah pilgrims.
November 28	The ‘20:80 scheme’ which stipulated that 20 per cent of the gold imported had to be exported was withdrawn.
December 2	The stipulation of an auditor’s certificate for making remittances of assets abroad was dispensed with and ADs were permitted to make remittances on payment of applicable taxes.
December 8	FDI up to 49 per cent under the government route was permitted in the defence sector.
December 8	FDI in railway infrastructure was permitted up to 100 per cent under the automatic route.
December 9	An Alternative Investment Fund registered with SEBI was allowed to invest overseas on the lines of domestic venture capital funds.
December 17	Multilateral organisations like the SAARC Development Fund (SDF), of which India is a member were allowed to open accounts with AD banks in India, without the prior approval of the Reserve Bank.
December 29	Designated AD banks were permitted to create charge/ pledge on the shares of the JV/ WOS/ SDS of an Indian party in favour of a domestic or overseas lender for securing the funded and/ or non-funded facility to be availed of by the Indian party or by its group companies/ sister concerns/ associate concerns or by any of its JV/ WOS/ SDS.
January 1, 2015	The set of eligible securities for raising ECBs was made more broad-based to include movable assets and financial securities in addition to immovable assets.
January 6	Residents who are subsidiaries of multinational companies were permitted to hedge their foreign currency exposure through permissible derivatives with an AD category-I bank in India on the strength of guarantee of non-resident group entity.
January 22	A new scheme, ‘Depository Receipts Scheme, 2014’ for investment under ADR/GDR was notified, providing for repeal of extant guidelines for Foreign Currency Convertible Bonds and Ordinary Shares (Through Depositary Receipt Mechanism) Scheme, 1993 except to the extent relating to foreign currency convertible bonds.
January 22	Facility for remittance of salaries outside India was made available to employees on deputation to a group company in India and for employees of limited liability partnerships.
January 22	Individuals were permitted to carry to Nepal or Bhutan, currency notes of the Reserve Bank, denominations above ₹100 subject to a limit of ₹25,000.

Date of Announcement	Policy Initiative
January 23	AD banks were authorised to make changes in the amount of ECB, its draw-down, repayment schedules, average maturity period and all-in-cost.
February 12	Requirement of submission in Form A-1 to ADs for making payments towards imports was dispensed with.
February 12	Filing of the following returns was enabled on the e-Biz platform: Advance Remittance Form (ARF) used by companies to report FDI inflow; and FCGPR Form for reporting the issue of instruments to the overseas investor against the above FDI inflow.
March 11	Citizens of Macau and Hong Kong were prohibited from acquiring/ transferring immovable property in India akin to the prohibition for citizens of China.
March 31	A financial institution or a branch of a financial institution set up in IFSC will be treated as a person resident outside India.
April 8	FDI in the insurance sector was allowed up to 49 per cent.
April 30	Goods consigned to the importers of Nepal and Bhutan from third countries under merchant trade from India will qualify as traffic-in-transit if the goods are otherwise compliant with the provisions of the India-Nepal Treaty of Transit and the Indo-Bhutan Treaty of Transit respectively.
May 14	Requirement of declaring export of goods/software in the statutory declaration form (SDF) in case of exports through the Electronic Data Interchange (EDI) ports was dispensed with as the mandatory statutory requirements contained in the SDF were subsumed in the shipping bill format.
May 21	ADs were advised not to insist on form A2 and physical presence of the account holder at the time of closure of FCNR (B) deposits.
May 21	Under the rupee drawing arrangements, the limit of trade transactions was increased to ₹15,00,000 per transaction from ₹5,00,000.
June 1	Limit of remittances under the liberalised remittance scheme (LRS) was increased to an umbrella limit of US$ 2,50,000/- subsuming various limits under Schedule III of the Foreign Exchange Management (Current Account Transaction) Rules, 2000.
June 11	NRIs were permitted to subscribe to chit funds, without limit, on a non-repatriation basis, provided the Registrar of Chits permitted any chit fund accordingly and the subscription was brought in through the normal banking channel, including through an account maintained with a bank in India.
June 18	From the half year ending June 2015, BEF submission will be online and bank-wise.
Department of Banking Regulation	
July 15, 2014	Banks were allowed to extend structured long term project loans with periodic refinancing option to new projects in infrastructure and core industries sectors.
July 15	Banks were allowed to issue long term bonds (minimum 7 years) for financing their infrastructure and affordable housing loans, with exemptions from CRR/SLR and computing of ANBC for priority sector obligations.
July 17	Banks were advised on the list of officially valid documents (OVD) for KYC. Procedure for opening of accounts by low risk customers was also simplified.
July 22	Banks were allowed to decide on the quantum of loans against the pledge of gold jewellery and ornaments for non-agricultural end uses with bullet repayment of principal and interest.
August 7	Banks were allowed to refinance existing project loans, even without a pre-determined agreement with other banks/ FIs, and fix a longer repayment period, and this will not be considered as restructuring in the books of the existing as well as taking over lenders.

Date of Announcement	Policy Initiative
August 14	Where the initial financial closure does not provide for a standby credit facility, banks were allowed to fund cost over-runs without treating the loan as a 'restructured asset'.
September 1	Banks were advised to clearly delineate the procedure for disposal of loan proposals, with appropriate timelines, and institute a suitable monitoring mechanism for reviewing applications pending beyond the specified period. Banks were also advised to make suitable disclosures on the timelines for conveying credit decisions.
September 1	To facilitate raising of non-equity regulatory capital instruments, certain eligibility criteria for banks' capital instruments under the Basel III framework were relaxed.
September 4	For streamlining KYC norms, client due diligence measures were further simplified, dispensing with the requirement of 'positive confirmation' and physical presence of clients at the time of periodic updation.
September 9	The upper age limit for the MD and CEO and other whole time directors of banks in the private sector was fixed at 70 years with flexibility to individual banks' boards to prescribe a lower than 70 years retirement age for WTDs, including the MD & CEO, as an internal policy.
September 9	On the guidelines on wilful defaulters, definitions of guarantor, lender and unit were spelt out.
October 16	Guidelines on advanced approaches of operational risk – standardised approach and advanced measurement approach were revised.
October 21	KYC norms were further simplified: 'low risk' customers need not furnish fresh KYC documents at the time of periodic updation; self-certification will suffice in case of no change. For non-compliant KYC accounts, after repeated reminders, banks may impose 'partial freezing' in a phased manner.
October 21	Timelines were extended for reporting an account having principal or interest overdue for more than 60 days as a special mention account (SMA 2); formation of a joint lenders forum (JLF); and for deciding a corrective action plan and evaluation of the restructuring packages by an Independent Evaluation Committee.
November 3	Final guidelines were issued on monitoring tools for intra-day liquidity management, consistent with the quantitative tools in this regard finalised by the Basel Committee on Banking Supervision (BCBS).
November 20	While levying charges for non-maintenance of minimum balance in savings bank accounts, default in maintenance of minimum balance should be notified to the customer clearly and the penal charges should be directly proportionate to the extent of shortfall observed.
November 27	For financing of infrastructure and affordable housing, the formula to decide the lower of outstanding amount of bonds issued and eligible credit was revised to take into account the outstanding credit on every reporting Friday as against the earlier requirement of outstanding credit on the date of issuance of bonds.
November 28	For computing the liquidity coverage ratio (LCR), G-secs up to another 5 per cent of NDTL within the mandatory SLR were permitted as Level 1 HQLAs. Banks were allowed to avail liquidity facility against such securities under a special facility, 'Facility to Avail Liquidity for Liquidity Coverage Ratio'.
December 15	The framework of flexible structuring and periodic refinancing of long term project loans was extended to existing loans to infrastructure and core industries projects, in which the aggregate exposure of all institutional lenders exceeded ₹5 billion.
December 22	Non-cooperative borrower was re-defined as one who does not engage constructively with the lender by defaulting in timely repayment of dues while having ability to pay, thwarting lender's efforts for recovery of dues by not providing necessary information sought, denying access to assets financed/ collateral securities, obstructing sale of securities, *etc*.

Date of Announcement	Policy Initiative
January 8, 2015	The revised framework for leverage ratio (LR) was issued for a parallel run and also for public disclosure of Tier 1 LR. Individual banks will be monitored against an indicative LR of 4.5 per cent, pending finalisation of rules by BCBS by end-2017.
January 15	Comprehensive guidelines were issued on insurance businesses undertaken by banks - insurance business with risk participation/ or distribution as agents/ brokers.
January 15	Banks/ FIs were advised to become members of all four credit information companies (CICs), and the membership and annual fee were also prescribed.
January 19	Banks were allowed to review the base rate methodology after three years instead of five years. Guidelines on spread charged to the customer were also issued to protect the interests of existing borrowers.
February 5	Final guidelines for implementation of Countercyclical Capital Buffer (CCCB) were issued. However, the activation of CCCB will take place when circumstances warrant.
March 5	Banks were permitted to add stamp duty, registration and other documentation charges to the cost of house/dwelling unit for computing the Loan to Value (LTV) ratio where the cost of the house/dwelling unit does not exceed ₹1 million.
March 11	Banks were allowed to reverse the excess provision on sale of NPAs prior to February 26, 2014 to SCs/ RCs to their profit and loss account.
March 13	For opening accounts of proprietorship concerns, banks were allowed the discretion to accept one document as activity proof, subject to carrying out contact point verification to their satisfaction that furnishing two such documents was not possible.
March 20	Banks were advised to disclose details of their holdings of security receipts in a prescribed format in Notes to Accounts of Annual Financial Statements.
March 30	Banks were allowed to utilise up to 50 per cent of the countercyclical provisioning buffer/floating provisions as at end-December 2014, for making specific provisions for NPAs, as per the policy approved by their boards.
March 31	Following the BCBS's Regulatory Consistency Assessment Programme (RCAP), guidelines on Basel III capital adequacy and liquidity regulations were revised.
April 1	A scheme for setting up of IBUs in Gujarat International Finance Tec-City (GIFT) and other IFSCs that may be set up in India was formulated. Under the scheme, IBUs will be established with a minimum capital requirement of US$ 20 million or equivalent in foreign currency.
April 1	In case of fraud, the entire amount due to the bank, or for which the bank is liable is to be provided for over a period not exceeding four quarters.
April 6	When a project is stalled primarily due to inadequacies of the existing promoters followed by a change in the ownership, banks may permit extension of date of commencement of commercial operations (DCCO) up to a further period of two years, in addition to the extension of DCCO permitted under the existing regulations, without adversely affecting the asset classification of loans to such projects.
April 6	Refinance of rupee loans with foreign currency loans (including loans obtained with support from the Indian banking system) or *vice versa* shall be treated as 'restructuring', if such refinancing is extended to a borrower who is under financial difficulty and involves concessions that the bank would otherwise not consider.
April 16	Banks were permitted to offer differential rates of interest on term deposits based on the feature of early withdrawal facility. All terms deposits of individuals of ₹1.5 million and below should necessarily have a premature withdrawal facility.
May 14	Public sector banks were advised to determine the board agenda items and the periodicity thereof, with the approval of their boards, such that there was adequate focus on matters of strategic and financial importance.

Date of Announcement	Policy Initiative
May 21	The dispensation to amortise the loss on sale of NPAs to Securitisation Companies/Reconstruction Companies (SCs/RCs) over a period of two years was extended to assets sold up to March 31, 2016.
May 28	Private sector banks were advised to adhere to the Reserve Bank's instructions of May 14, 2015 on calendar of reviews by PSB boards to the extent applicable.
May 28	Banks were advised to encourage and educate large agricultural borrowers, such as agricultural commodity processors, traders, millers and aggregators to hedge their risks related to agricultural commodity prices.
June 1	Private sector banks were advised to put in place board approved comprehensive compensation policies for the non-executive directors (other than part time chairman), covering compensation in the form of profit related commission, not exceeding ₹1 million per annum for each of the non-executive directors.
June 1	Cross holding of long-term bonds issued for financing infrastructure and affordable housing was allowed amongst banks.
June 8	A Strategic Debt Restructuring (SDR) scheme was issued, allowing conversion of bank loan dues into equity shares at a 'fair price' as per a prescribed pricing formula, which is exempted from the SEBI's related regulations.
June 11	All-India Term Lending and Refinancing Institutions were permitted to reverse the excess provision on sale of NPAs (sold prior to February 26, 2014 to SCs/RCs) to their profit and loss accounts.
June 11	For KYC purposes, banks were advised to accept from low-risk customers additional documents as OVDs for proof of address, such as utility bills, municipal tax receipt, bank account statement and pension payment orders.
Department of Cooperative Bank Regulation	
August 20, 2014	CBS-enabled UCBs having minimum assessed net worth of ₹500 million, satisfying Financially Sound and Well Managed (FSWM) criteria and having track record of regulatory compliance were permitted to open on-site/off-site/mobile ATMs without prior permission of the Reserve Bank.
September 3	The acquiring commercial banks should not incur any loss out of merger/transfer of assets and liabilities of UCBs and big depositors holding in excess of ₹0.1 million each will be required to sacrifice in proportion to the deposit erosion of the target bank.
October 13	Internet banking (view only) facility was permitted to all UCBs which have implemented CBS and migrated to IPv6.
October 13	FSWM criteria for UCBs was revised to include CBS as an additional condition for opening of on-site/off-site/mobile ATMs, approval of annual business plans (ABP), extension of area of operation and shifting of premises.
October 29	Scheduled UCBs which were CBS-enabled with 9 per cent CRAR and fully compliant with the Reserve Bank's eligibility criteria, have been extended Liquidity Adjustment Facility (LAF) with effect from November 28, 2014.
October 29	UCBs were permitted to act as PAN Service Agents (PSAs) by entering into a tie-up with any agency authorised by the Income Tax Department, Government of India.
October 30	The ceiling on quantum of gold loans granted under the Bullet Repayment Scheme by UCBs was raised from ₹0.1 million to ₹0.2 million.
October 30	UCBs were advised to prominently display the full name of the bank as authorised by the Reserve Bank wherever abbreviated/abridged version of the name of UCB is used for logo/ brand building.
November 5	For compliance with the obligations under the PML Amendment Act, 2012, UCBs could also designate a person who holds the position of senior management or equivalent as a 'Designated Director'. However, in no case, the Principal Officer should be nominated as 'Designated Director'.

Date of Announcement	Policy Initiative
November 13	UCBs were advised to review and strengthen controls in cheque presenting/passing and account monitoring.
November 27	The Supervisory Action Framework was revised to facilitate early rectification of the irregularities/ deficiencies of UCBs. The revised criteria envisages restrictions/ corrective action, if any of the trigger points is breached such as the gross NPA ratio exceeding 10 per cent, regulatory capital falling below 9 per cent, credit deposit ratio exceeding 70 per cent or when a UCB is incurring losses for two consecutive years or having accumulated losses.
January 7, 2015	UCBs were advised to constitute a special committee of the board for monitoring and follow up of frauds involving amounts of ₹10 million and above, while the Audit Committee of Board (ACB) may continue to monitor all the cases of frauds in general.
January 8	The quantum of loans granted under the Bullet Repayment Scheme by StCBs/CCBs was raised from ₹0.1 million to ₹0.2 million.
January 29	Cooperative banks were advised to become members of all four Credit Information Companies (CICs) and furnish historical data to them.
April 16	State Cooperative Banks (StCBs) meeting the stipulated norms were permitted to open on-site/off-site/ mobile ATMs as per their need and potential in their area of operation without prior permission of the Reserve Bank.
April 30	CBS-enabled FSWM scheduled UCBs having minimum net-worth of ₹1 billion were allowed to issue credit cards in affiliation with authorised entities.
May 5	CBS-enabled UCBs having capacity to build necessary modules in CBS/ hand-held devices and not operating under directions u/s 35 A of the Banking Regulation Act, 1949 (AACS) were advised to roll out the Pradhan Mantri Jeevan Jyoti Bima Yojana (PMJJBY) and Pradhan Mantri Suraksha Bima Yojana (PMSBY) by May 31, 2015 and participate in these schemes.
May 7	StCBs meeting the revised eligibility criteria were permitted to submit their applications in the prescribed format for prior approval for opening of branches/specialised branches/extension counters/ shifting of branches/upgradation of extension counters into full-fledged branches.
May 14	Uniform provisioning norms in respect of all cases of frauds were prescribed. The entire amount due to the bank or for which the bank is liable, is to be provided for over a period not exceeding four quarters. If there is a delay in reporting the fraud to the Reserve Bank beyond the prescribed time limit, the entire provision is required to be made at once.
May 25	CBS-enabled UCBs having capacity to build necessary modules in CBS/ hand-held devices and not operating under directions u/s 35 A of BR Act,1949 (AACS) were permitted to participate in Atal Pension Yojana (APY).
Department of Non-Banking Regulation	
July 10, 2014	Customers required to submit only one documentary proof of address (either current or permanent) while opening a deposit account or while undergoing periodic updation.
July 14	NBFCs were advised not to charge pre-payment penalties on floating rate term loans to individual borrowers.
July 14	It was decided to accept e-KYC service process as a valid process for KYC verification. Also, demographic details and photographs as provided for by the Unique Identification Authority of India (UIDAI) will be treated as an 'OVD' for KYC requirements under Prevention of Money Laundering (Maintenance of Records) Rules, 2005.
July 25	NBFCs were advised to obtain a Global Intermediary Identification Number (GIIN) wherever applicable.
August 1	NBFCs were advised to make available information/documents required by the special investigation team (SIT) as and when required.

Date of Announcement	Policy Initiative
August 5	SCs/RCs were required to invest minimum 15 per cent of Security Receipts (SRs) of each class and each scheme issued by them on an on-going basis till redemption of SRs. Management fees should be calculated and charged as percentage of the minimum net asset value (NAV) specified by a credit rating agency (rather than percentage of outstanding SRs at present) provided the same is not more than the acquisition value of the underlying asset. Asset Reconstruction Companies (ARCs) should also be members of a JLF. ARCs should put up on their websites at quarterly intervals the list of suit filed accounts of wilful defaulters.
August 7	Every SC/RC was required to become a member of at least one CIC and provide to the CIC periodically accurate data / history of the borrowers.
August 8	Amendments were made to the regulatory framework pertaining to Mortgage Guarantee Companies.
August 12	All non-deposit taking NBFCs with asset size of ₹10 billion and above were allowed to participate in the interest rate futures market as trading members.
September 25	NBFCs were allowed to use the ratings of SMERA for the purpose of rating their fixed deposits.
November 10	Threshold for defining systemic significance for NBFCs-ND was revised to ₹5 billion from ₹1 billion. Tighter prudential norms were prescribed for NBFCs-ND-SI and all NBFCs-D.
November 10	Principal business criteria for NBFC-Factors revised to 50:50 from 75:75, in line with the Factoring Regulation Act, 2011.
December 1	Following the Prevention of Money-Laundering (Maintenance of Records) Amendment Rules, 2013, changes were carried out in KYC/AML guidelines.
January 2, 2015	Due diligence process/updation for KYC compliance was revised for various categories of customers, allowing third party verification.
January 16	Revisions of the DCCO and consequential shift in repayment schedules will not be treated as restructuring if the revised DCCO falls within a period of two years and one year from the original DCCO for infrastructure and non-infrastructure projects respectively.
January 19	Flexible structuring and refinancing of fresh term loans were allowed to long term project loans to infrastructure and core industries.
January 28	NBFCs registered as core investment companies, primary dealers and those purely into investment activities without any customer interface were exempt from the requirement of becoming members of CIC.
February 6	Minimum investment grade for long term fixed deposit products provided by Brickwork Ratings India Pvt. Ltd. was advised to be equivalent to FBBB.
February 6	Credit institutions were mandated to become members of all CICs.
February 20	Guidelines on private placements were revised with the issue of non-convertible debentures (NCDs) categorised into two groups: (a) a subscription of ₹20,000 to ₹10 million per investor with a maximum of 200 subscribers in a financial year and the issue being fully secured; and (b) a minimum subscription of ₹10 million and above with no limit on the number of subscribers and the need for the creation of security should be as approved by their boards.
February 24	The following changes in the shareholding pattern of a SC/RC will require the Reserve Bank's prior approval: transfer of shares by which the transferee becomes a sponsor; transfer of shares by which the transfer or ceases to be a sponsor; and an aggregate transfer of 10 per cent or more of the total paid up share capital by a sponsor in five years from the date of certificate of registration.
March 16	NBFCs could also designate a person who holds the position of senior management or equivalent, as a Designated Director.

Date of Announcement	Policy Initiative
April 8	For NBFC-MFIs, limit on the total indebtedness of a borrower, excluding educational/medical expenses was raised to ₹100,000 from ₹50,000. Loans disbursed to a borrower with a rural household annual income not exceeding ₹100,000 or urban and semi-urban household income not exceeding ₹160,000 were included as qualifying assets.
April 10	NBFCs lending against collateral of listed shares were advised to maintain an LTV ratio of 50 per cent, accept only Group 1 securities (as specified by SEBI) as collateral for loans of value more than ₹0.5 million where the lending is done for investment in the capital market.
April 10	Enhanced corporate governance guidelines were made applicable to NBFCs-ND-SIs and deposit taking NBFCs.
April 30	It was decided to dispense with the requirement of prior approval from the Reserve Bank for NBFCs to distribute mutual fund products.
April 30	While opening accounts of sole proprietary firms, NBFCs were given the discretion to accept only one of the prescribed documents as activity proof.
May 7	For restructuring proposals approved / to be approved by BIFR/CDR/JLF, SC/RCs were permitted to accept a resolution period co-terminus with other secured lenders.
May 14	Directions issued to infrastructure debt funds (IDFs) were amended to allow entry of IDF-NBFCs into sectors where there is no presence of a project authority. Risk weight as applicable to bonds held by IDF-NBFCs and assets of infrastructure finance companies were made applicable to all NBFCs.
May 21	Besides the Bombay Bullion Association Ltd. (BBA), rates of a commodity exchange regulated by the Forward Markets Commission were allowed to be used for valuation of gold jewellery for computing the LTV ratio.
June 25	NBFCs-ND were permitted to act as sub-agents under MTSS without requirement of prior approval from the Reserve Bank.
Department of Banking Supervision	
July 1, 2014	Classification and reporting system for frauds was prescribed, consolidating and updating earlier instructions.
September 5	Liquidity returns were prescribed for banks to monitor their resilience to potential liquidity disruptions under stress scenarios.
November 5	Preventive measures laid down for cheque related frauds.
December 15	Banks were advised to employ ‘decoy customers’ and conduct surprise checks for compliance with KYC/AML/CFT norms.
March 4, 2015	Banks were advised to implement a comprehensive compliance plan with compliance testing and review structures in view of focus on compliance review in the Reserve Bank supervisory processes.
May 7	Banks were advised to follow a framework for fraud risk management, based on the recommendations of the Internal Working Group that looked into issues relating to prevention, early detection and reporting of fraud, penal measures for fraudulent borrowers, introducing, *inter alia*, the concepts of early warning signals and red flagged accounts.
June 4	Banks were advised that henceforth concurrent auditors, who are chartered accountants, of branches below the cut-off point will submit Long Form Audit Reports (LFARs) only to the Chairman of the bank and the bank in turn will consolidate all such LFARs and submit to the Statutory Central Auditor as an internal document of the bank.

Date of Announcement	Policy Initiative
Consumer Education and Protection Department	
December 3, 2014	A Charter of Customer Rights was issued covering five basic rights of bank customers.
February 11, 2015	The status on implementation of the charter will be monitored by the Reserve Bank in addition to a review by the bank's board.
May 11	Public sector banks, select private and foreign banks were advised to appoint chief customer service officers, *i.e.,* internal ombudsman.
Internal Debt Management Department	
December 15, 2014	The quantum of securities classified under HTM was restored to 100 per cent of audited NOF for the standalone PDs as at the end of the preceding financial year, effective December 31, 2014. It was raised to 200 per cent in September 2013 due to excessive market volatility.
Department of Currency Management	
December 31, 2014	The deadline for exchange of banknotes printed before 2005 was extended from December 31, 2014 to June 30, 2015.
February 3, 2015	The Regional Offices of the Reserve Bank were advised to continue with the Lead Bank Scheme for currency management in the identified districts on a pilot basis for one more year and guide the nodal banks suitably.
April 17	The process of approval by the Reserve Bank for opening of currency chests by banks has been rationalised / simplified from a multi-layered approval process to only one final approval subject to certain conditions.
June 26	The deadline for exchange of banknotes printed before 2005 was extended from June 30, 2015 to December 31, 2015.
Department of Payment and Settlement Systems	
August 14, 2014	The minimum number of free transactions at other banks ATMs was rationalised from five to three at six metros and for own bank ATMs to five.
August 22	Where cards issued by banks in India are used for making card not present payments within the country, such transactions have to be through a bank in India and settled only in Indian currency.
November 28	Guidelines on the Bharat Bill Payment System were issued, enabling the creation of pan-India touch points for bill payments by customers, irrespective of location.
December 3	PPI guidelines were revised, enhancing value of PPI with full KYC, increasing the validity period of gift cards, allowing issue of multiple PPIs for dependent/family members and rupee denominated PPIs for visiting foreign nationals/NRIs.
December 3	Guidelines for setting up of TReDS were issued to provide quick and efficient financing options for MSMEs.
December 4	Guidelines on mobile banking transactions were issued for adoption of best practices, such as greater degree of standardisation in procedures; registration options and timing, adoption of various channels/ methods for quickening the process of MPIN generation, and customer education and awareness programme.
December 5	WLAs were permitted to accept international credit/debit/prepaid cards, facility of dynamic currency conversion for international cards at WLAs and also to enable tie-ups with other commercial banks for cash supply.
December 15	RTGS business hours were extended: 8:00 to 20:00 hours on weekdays and 8:00 to 15:30 hours on Saturdays.

Date of Announcement	Policy Initiative
January 2, 2015	Authorised entities were advised to prominently carry the name of the entity authorised by the Reserve Bank in all the information available to the public regarding the product.
January 16	Instruction on computation of '*Net-worth*' was issued for an entity to be authorised under the PSS Act.
May 7	Effective September 1, 2015, all new cards issued – debit and credit, domestic and international should be EMV chip and pin based cards.
May 14	Requirement for additional factor of authentication was relaxed for small value card present transactions only using Near Field Communication contactless technology.

APPENDIX TABLE 1: MACROECONOMIC AND FINANCIAL INDICATORS

Item			Average 2003-04 to 2007-08 (5 years)	Average 2009-10 to 2013-14 (5 years)	2012-13	2013-14	2014-15
1			2	3	4	5	6
I.	**Real Economy**						
	I.1	Real GDP at market prices (% change)	8.8	7.0	5.1	6.9	7.3
	I.2	Real GVA at basic prices (% change)	8.7	6.7	4.9	6.6	7.2
	I.3	Foodgrains Production (Million tonnes)	213.6	248.8	257.1	265.0	252.7
	I.4	a) Food Stocks (Million tonnes at end-March)	18.6	50.1	59.8	49.5	41.3
		b) Procurement#	39.3	61.3	72.2	56.9	58.0
		c) Off-take	41.5	57.0	65.9	59.8	56.0
	I.5	Index of Industrial Production (% change)	11.2	3.5	1.1	-0.1	2.8
	I.6	Index of Eight Core Industries (% change)	5.9	5.8	6.5	4.2	3.8
	I.7	Gross Domestic Saving Rate (% of GNDI at current prices)	32.4	31.4$	31.1	30.0	...
	I.8	Gross Domestic Investment Rate (% of GDP at current prices)	33.6	35.8$	36.6	32.3	...
II.	**Prices**						
	II.1	Consumer Price Index (CPI) Combined (Average % Change)	...	...	10.2	9.5	5.9
	II.2	CPI- Industrial Workers (average % change)	5.0	10.3	10.4	9.7	6.3
	II.3	Wholesale Price Index (average % change)	5.5	7.1	7.4	6.0	2.0
III.	**Money and Credit**						
	III.1	Reserve Money (% change)	20.4	12.1	6.2	14.4	11.3
	III.2	Broad Money (M3) (% change)	18.6	14.7	13.6	13.4	10.8
	III.3	a) Aggregate Deposits of Scheduled Commercial Banks (% change)	20.2	15.0	14.2	14.1	10.7
		b) Bank Credit of Scheduled Commercial Banks (% change)	26.7	16.7	14.1	13.9	9.0
IV.	**Financial Markets**						
	IV.1	Interest rates (%)					
		a) Call / Notice Money rate	5.6	7.2	8.1	8.3	8.0
		b) 10 year G-Sec yield	7.0	8.0	8.2	8.4	8.3
		c) 91-Days T-bill yield			8.2	8.9	8.5
		d) Weighted Average cost of Central Government Borrowings			8.4	8.4	8.5
		e) Commercial Paper	7.7	8.4	9.2	9.3	8.8
		f) Certificate of Deposits##	8.9	8.2	9.0	9.2	8.7
	IV.2	Liquidity (₹ billion)					
		a) LAF Outstanding~	...	...	-1,236.4	-2,179.9	-1,938.8
		b) MSS Outstanding~~	...	...	0.0	0.0	0.0
		c) Average Daily Call Money Market Turnover	184.9	255.3	323.6	302.3	255.7
		d) Average Daily G-Sec Market Turnover$$	77.1	241.4	325.1	429.0	501.2
		e) Variable Rate Repo*				1,200.2	1,628.7
		f) MSF*			70.0	737.4	416.4
V.	**Government Finances**						
	V.1	Central Government Finances (% of GDP)@					
		a) Total Revenue Receipts	9.8	9.0	8.8	8.9	8.8
		b) Capital Outlay	1.6	1.5	1.5	1.5	1.3
		c) Total Expenditure	14.7	14.7	14.1	13.7	13.1
		d) Gross Fiscal Deficit	3.6	5.3	4.9	4.4	4.0
	V.2	State Finances@@					
		a) Revenue Deficit (% of GDP)**	0.4	0.0	-0.2	0.1	0.1
		b) Gross Fiscal Deficit (% of GDP)**	2.7	2.2	2.0	2.2	2.9
		c) Primary Deficit (% of GDP)**	0.3	0.6	0.5	0.7	1.3

APPENDIX TABLE 1: MACROECONOMIC AND FINANCIAL INDICATORS *(Concld.)*

Item	Average 2003-04 to 2007-08 (5 years)	Average 2009-10 to 2013-14 (5 years)	2012-13	2013-14	2014-15
1	2	3	4	5	6
VI. External Sector					
VI.1 Balance of Payments					
a) Merchandise Exports (% change)	25.3	12.2	-1.0	3.9	-0.6
b) Merchandise Imports (% change)	32.3	9.7	0.5	-7.2	-1.1
c) Trade Balance/GDP (%)	-5.4	-8.9	-10.7	-7.9	-7.0
d) Invisible Balance/GDP (%)	5.1	5.7	5.9	6.1	5.7
e) Current Account Balance/GDP (%)	-0.3	-3.2	-4.8	-1.7	-1.3
f) Net Capital Flows /GDP (%)	4.6	3.7	4.9	2.6	4.4
g) Reserve Changes (BoP basis) (US $ billion) [(Increase (-)/Decrease (+)]	-40.3	-6.6	-3.8	-15.5	-61.4
VI.2 External Debt Indicators					
a) External Debt Stock (US$ billion)	156.5	359.0	409.4	446.3	475.8
b) Debt-GDP Ratio (%)	17.7	20.9	22.3	23.6	23.8
c) Import cover of Reserves (in Months)	14.0	8.5	7.0	7.8	8.9
d) Short-term Debt to Total Debt (%)	14.8	21.4	23.6	20.5	17.8
e) Short-term Debt to Total Debt (%) (residual maturity)	37.6^^	41.9	44.2	39.6	38.9
f) Debt Service Ratio (%)	8.3	5.6	5.9	5.9	7.5
g) Reserves to Debt (%)	116.9	82.1	71.3	68.2	71.8
VI.3 Openness Indicators (%)					
a) Export plus Imports of Goods/GDP	30.4	40.2	44.1	41.9	37.9
b) Export plus Imports of Goods & Services/GDP	40.8	52.2	56.4	54.1	49.4
c) Current Receipts plus Current Payments/GDP	46.6	58.3	62.6	60.6	55.4
d) Gross Capital Inflows plus Outflows/GDP	36.8	49.5	46.5	52.0	49.1
e) Current Receipts & Payments plus Capital Receipts & Payments /GDP	83.5	107.7	109.1	112.6	104.4
VI.4 Exchange Rate Indicators					
a) Exchange Rate (Rupee/US Dollar)					
End of Period	43.1	51.1	54.4	60.1	62.6
Average	44.1	51.2	54.4	60.5	61.1
b) 36 - Currency REER (% change)	3.1^	0.8	-4.3	-2.2	5.5
c) 36 - Currency NEER (% change)	1.7^	-4.9	-10.4	-7.7	2.4
d) 6 - Currency REER (% change)	4.4^	1.8	-3.3	-3.7	6.4
e) 6 - Currency NEER (% change)	1.6^	-5.4	-10.5	-10.4	1.3

... : Not Available. $: Average of four years.
$$: Outright trading turnover in Central government dated securities (based on calender days).
: Procurement of rice and wheat is based on respective marketing years.
: Data for “Column 2” pertains to April 13, 2007 to March 28, 2008
~ : LAF outstanding as on March 31 (negative means injection).
~~ : Outstanding as on last Friday of the financial year.
* : Outstanding as on March 31.
** : Data from 2013-14 onwards are provisional and pertain to budgets of 25 states.
@ : Central Government figures for 2014-15 pertain to provisional accounts.
@@ : State Government figures for 2014-15 pertain to revised estimates.
^ : Average of period 2005-06 to 2007-08.
^^ : Pertains to end-March 2008.

Note : 1. In columns 2 and 3, GDP is based on the old series *i.e.*, base: 2004-05; in other columns, the new series of GDP *i.e.*, base: 2011-12 is used.
2. Real Effective Exchange Rate (REER) are based on CPI.

APPENDIX TABLE 2 : GROWTH RATES AND COMPOSITION OF REAL GROSS DOMESTIC PRODUCT
(At 2011-12 Prices)

(Per cent)

Sector	Growth Rate				Share		
	Average 2012-13 to 2014-15	2012-13	2013-14	2014-15	2012-13	2013-14	2014-15
1	2	3	4	5	6	7	8
Expenditure Side GDP							
1. Private Final Consumption Expenditure	6.0	5.5	6.2	6.3	57.9	57.5	57.0
2. Government Final Consumption Expenditure	5.5	1.7	8.2	6.6	10.8	10.9	10.9
3. Gross Fixed Capital Formation	2.4	-0.3	3.0	4.6	31.9	30.7	30.0
4. Change in Stocks	-8.0	-6.2	-21.4	3.7	2.2	1.6	1.5
5. Valuables	-6.7	3.3	-48.7	25.3	2.8	1.4	1.6
6. Net Exports	28.8	-3.3	69.0	20.7	-6.4	-1.8	-1.4
a) Exports	4.4	6.7	7.3	-0.8	24.6	24.7	22.9
b) Less Imports	-1.5	6.0	-8.4	-2.1	31.0	26.6	24.2
7. Discrepancies	-185.5	-162.9	-139.7	-253.9	0.8	-0.3	0.4
8. GDP	**6.4**	**5.1**	**6.9**	**7.3**	**100.0**	**100.0**	**100.0**
GVA at Basic Prices (Supply Side)							
1. Agriculture, forestry and fishing	**1.7**	**1.2**	**3.7**	**0.2**	**17.7**	**17.2**	**16.1**
of which :							
Agriculture	2.6*	1.2	3.9	...	15.4	15.0	...
2. Industry	**5.7**	**5.1**	**5.3**	**6.6**	**23.7**	**23.4**	**23.3**
of which :							
a) Mining and quarrying	2.5	-0.2	5.4	2.4	3.0	3.0	2.9
b) Manufacturing	6.2	6.2	5.3	7.1	18.3	18.1	18.1
c) Electricity, gas, water supply & other utility services	5.6	4.0	4.8	7.9	2.4	2.3	2.3
3. Services	**7.8**	**6.0**	**8.1**	**9.4**	**58.6**	**59.4**	**60.6**
of which :							
a) Construction	1.0	-4.3	2.5	4.8	8.6	8.3	8.1
b) Trade,hotels,transport,communication and services related to broadcasting	10.5	9.6	11.1	10.7	18.0	18.8	19.4
c) Financial, real estate & professional services	9.4	8.8	7.9	11.5	19.5	19.7	20.5
d) Public Administration, defence and other services	6.6	4.7	7.9	7.2	12.5	12.6	12.6
4. GVA at basic prices	**6.2**	**4.9**	**6.6**	**7.2**	**100.0**	**100.0**	**100.0**

... : Not available .
* : The absolute figure for the sub-sector 'Agriculture' is yet to be released by CSO for the year 2014-15; hence the average pertains to 2012-13 and 2013-14.
Source: Central Statistics Office (CSO).

APPENDIX TABLE 3: INFLATION, MONEY AND CREDIT

(Per cent)

Inflation									
Consumer Price Index (All India)**	**Rural**			**Urban**			**Combined**		
	2012-13	**2013-14**	**2014-15**	**2012-13**	**2013-14**	**2014-15**	**2012-13**	**2013-14**	**2014-15**
1	2	3	4	5	6	7	8	9	10
General Index (All Groups)	**10.1**	**9.6**	**6.2**	**10.4**	**9.4**	**5.7**	**10.2**	**9.5**	**5.9**
Food and beverages	11.8	11.2	6.6	12.1	11.0	6.4	11.9	11.1	6.5
Housing	...	...	...	11.3	10.4	6.9	11.3	10.4	6.9
Fuel and light	7.9	7.4	5.1	9.7	7.3	2.7	8.5	7.4	4.2
Miscellaneous	7.2	6.7	4.9	7.5	7.0	4.2	7.3	6.8	4.6
Excluding Food and Fuel	8.0	7.3	5.8	9.4	8.6	5.5	8.7	8.1	5.6
Other Price Indices	**2006-07**	**2007-08**	**2008-09**	**2009-10**	**2010-11**	**2011-12**	**2012-13**	**2013-14**	**2014-15**
1. Wholesale Price Index (2004-05=100)									
All Commodities	**6.6**	**4.7**	**8.1**	**3.8**	**9.6**	**8.9**	**7.4**	**6.0**	**2.0**
Primary Articles	9.6	8.3	11.0	12.7	17.7	9.8	9.8	9.8	3.0
of which : Food Articles	9.6	7.0	9.1	15.3	15.6	7.3	9.9	12.8	6.1
Fuel and Power	6.5	0.0	11.6	-2.1	12.3	14.0	10.3	10.2	-0.9
Manufactured Products	5.7	4.8	6.2	2.2	5.7	7.3	5.4	3.0	2.4
Non-Food Manufactured Products	5.7	5.0	5.7	0.2	6.1	7.3	4.9	2.9	2.4
2. CPI- Industrial Workers (IW) (2001=100)	**6.7**	**6.2**	**9.1**	**12.4**	**10.4**	**8.4**	**10.4**	**9.7**	**6.3**
of which : CPI- IW Food	9.2	8.4	12.3	15.2	9.9	6.3	11.9	12.3	6.5
3. CPI- Agricultural Labourers (1986-87=100)	**7.8**	**7.5**	**10.2**	**13.9**	**10.0**	**8.2**	**10.0**	**11.6**	**6.6**
4. CPI- Rural Labourers (1986-87=100)	**7.5**	**7.2**	**10.2**	**13.8**	**10.0**	**8.3**	**10.2**	**11.5**	**6.9**

Money and Credit									
	2006-07	**2007-08**	**2008-09**	**2009-10**	**2010-11**	**2011-12**	**2012-13**	**2013-14**	**2014-15**
Reserve Money	23.9	31.0	6.4	17.0	19.1	3.6	6.2	14.4	11.3
Currency in Circulation	17.3	17.2	17.0	15.7	18.8	12.4	11.6	9.2	11.3
Bankers' Deposits with RBI	45.6	66.5	-11.3	21.0	20.2	-15.9	-10.0	34.0	8.3
Narrow Money (M1)	17.1	19.4	9.0	18.2	10.0	6.0	9.2	8.5	11.3
Broad Money (M3)	21.7	21.4	19.3	16.9	16.1	13.5	13.6	13.4	10.8
Currency-Deposit Ratio	17.1	16.5	16.1	15.9	16.3	16.1	15.7	15.1	15.2
Money Multiplier*	4.7	4.3	4.9	4.8	4.7	5.2	5.5	5.5	5.5
GDP/M3*$	1.3	1.2	1.2	1.2	1.2	1.2	1.2	1.2	1.2
Scheduled Commercial Banks									
Aggregate Deposits	23.8	22.4	19.9	17.2	15.9	13.5	14.2	14.1	10.7
Bank Credit	28.1	22.3	17.5	16.9	21.5	17.0	14.1	13.9	9.0
Non-food Credit	28.6	23.0	17.8	17.1	21.3	16.8	14.0	14.2	9.3
Credit-Deposit Ratio	73.9	73.9	72.4	72.2	75.7	78.0	77.9	77.8	76.6
Credit-GDP Ratio$	45.0	47.4	49.3	50.1	50.6	52.2	52.7	52.8	52.1

...: Not Available. *: Ratio. $:GDP data for 2011-12 onwards are based on new series *i.e.,* base: 2011-12.
**: Base 2010=100 for 2012-13 and 2013-14, and 2012=100 for 2014-15.
Note: Data refer to y-o-y change in per cent unless specified otherwise.

APPENDIX TABLE 4: CAPITAL MARKET - PRIMARY AND SECONDARY

(Amount in ₹ billion)

Items	2013-14		2014-15	
	No of Issues	Amount	No of Issues	Amount
1	2	3	4	5
I. PRIMARY MARKET				
A. Prospectus and Rights Issues*				
1. Private Sector (a+b)	**70**	**116.8**	**86**	**170.6**
a) Financial	26	60.6	29	83.6
b) Non-Financial	44	56.2	57	87.0
2. Public Sector (a+b+c)	**20**	**439.7**	**3**	**24.5**
a) Public Sector Undertakings	5	105.7	...	...
b) Government Companies	1	37.0	...	...
c) Banks/Financial Institutions	14	297.0	3	24.5
3. Total (1+2, i+ii, a+b)	**90**	**556.5**	**89**	**195.1**
Instrument Type				
(i) Equity	55	132.7	64	97.9
(ii) Debt	35	423.8	25	97.1
Issuer Type				
(a) IPOs	38	12.4	46	30.4
(b) Listed	52	544.1	43	164.6
B. Euro Issues (ADRs and GDRs)	**1**	**1.2**	**2**	**95.9**
C. Private Placement&				
1. Private Sector (a+b)		**1,213.3**		**2,770.2**
a) Financial		875.3		1,838.4
b) Non-Financial		338.0		931.8
2. Public Sector (a+b)		**2,778.5**		**1,694.7**
a) Financial		1,802.7		1,349.8
b) Non-Financial		975.9		344.8
3. Total (1+2, i+ii)		**3,991.8**		**4,464.8**
(i) Equity		272.1		286.0
(ii) Debt		3,719.7		3,761.4
D. Qualified Institutional Placement$	**17**	**136.6**	**51**	**291.0**
E. Mutual Funds Mobilisation (Net)#		**537.8**		**1,032.9**
1. Private Sector		488.4		1,037.0
2. Public Sector		49.4		-4.1
II. SECONDARY MARKET				
BSE				
BSE Sensex: End-Period		22,386.3		27,957.5
Period Average		20,120.1		26,556.5
Price Earning Ratio@		18.3		19.1
Market Capitalisation to GDP ratio (%) @@		65.4		80.9
Turnover Cash Segment		5,216.6		8,548.4
Turnover Derivatives Segment		92,194.3		203,627.4
NSE				
S&P CNX Nifty: End-Period		6,704.2		8,491.0
Period Average		6,009.5		7,967.3
Price Earning Ratio@		18.9		22.7
Market Capitalisation to GDP ratio (%) @@		64.1		79.2
Turnover Cash Segment		28,084.9		43,296.6
Turnover Derivatives Segment		382,114.1		556,064.5

...: Nil &: Provisional. $: Includes resource mobilisation from Institutional Placement Programme also.
#: Net of redemptions. @: As at end of the period. @@: GDP figures with new base: 2011-12.
Source: SEBI, NSE, BSE, CSO and various merchant bankers.

APPENDIX TABLE 5: KEY FISCAL INDICATORS

(As per cent to GDP)

Year	Primary Deficit	Revenue Deficit	Primary Revenue Deficit	Gross Fiscal Deficit	Outstanding Liabilities@	Outstanding Liabilities$
1	2	3	4	5	6	7
Centre						
1990-91	3.9	3.2	-0.5	7.6	53.7	59.6
1995-96	0.8	2.4	-1.7	4.9	49.4	57.3
2000-01	0.9	3.9	-0.6	5.5	53.9	59.4
2007-08	-0.9	1.1	-2.4	2.5	56.9	58.9
2008-09	2.6	4.5	1.1	6.0	56.1	58.6
2009-10	3.2	5.2	1.9	6.5	54.5	56.3
2010-11	1.8	3.2	0.2	4.8	50.5	52.1
2011-12	2.8	4.5	1.4	5.8	51.1	52.9
2012-13	1.8	3.7	0.5	4.9	50.8	52.3
2013-14	1.1	3.1	-0.2	4.4	50.0	51.7
2014-15 RE	0.8	2.9	-0.4	4.1	50.1	51.7
2014-15 PA	0.8	2.9	-0.4	4.0	...	...
2015-16 BE	0.7	2.8	-0.4	3.9	48.9	50.3
States*						
1990-91	1.7	0.9	-0.6	3.2	21.9	21.9
1995-96	0.7	0.7	-1.1	2.5	20.3	20.3
2000-01	1.7	2.5	0.2	4.0	27.3	27.3
2007-08	-0.5	-0.9	-2.9	1.5	26.6	26.6
2008-09	0.6	-0.2	-2.1	2.4	26.1	26.1
2009-10	1.2	0.5	-1.3	2.9	25.5	25.5
2010-11	0.5	0.0	-1.6	2.1	23.5	23.5
2011-12	0.4	-0.3	-1.8	1.9	22.6	22.6
2012-13	0.5	-0.2	-1.7	2.0	22.1	22.1
2013-14	0.7	0.1	-1.4	2.2	21.4	21.4
2014-15 RE	1.3	0.1	-1.4	2.9	21.8	21.8
2015-16 BE	0.8	-0.4	-1.9	2.3	21.6	21.6
Combined*						
1990-91	4.9	4.1	-0.2	9.1	62.9	68.9
1995-96	1.5	3.1	-1.7	6.3	59.4	67.3
2000-01	3.5	6.4	0.6	9.2	68.2	73.7
2007-08	-1.2	0.2	-5.0	4.0	69.5	71.4
2008-09	3.3	4.3	-0.8	8.3	69.7	72.2
2009-10	4.5	5.7	2.4	9.3	68.8	70.6
2010-11	2.4	3.2	-1.3	6.9	64.0	65.5
2011-12	3.2	4.1	-0.3	7.8	64.9	66.6
2012-13	2.3	3.4	-1.1	6.9	64.8	66.3
2013-14	1.9	3.3	-1.4	6.6	64.3	66.0
2014-15 RE	2.2	3.0	-1.7	6.9	65.3	67.0
2015-16 BE	1.5	2.4	-2.3	6.3	64.6	66.1

...: Not Available. PA: Provisional Accounts. RE: Revised Estimates. BE: Budget Estimates.
* : Data from 2013-14 onwards are provisional and pertains to budgets of 25 states.
@: Includes external liabilities of the centre calculated at historical exchange rates.
$: Includes external liabilities of the centre calculated at current exchange rates.

Note: 1. Data on combined deficit/liabilities indicators are net of inter-governmental transactions between the Centre and the State governments *viz.*, (a) NSSF investment in State governments special securities (b) Loans and advance by the Centre to States and (c) State governments' investment in Centre's treasury bills.
2. Negative sign (-) indicates surplus in deficit indicators.
3. GDP data from 2011-12 onwards are based on new base 2011-12.

Source: Budget documents of the Central and State governments.

APPENDIX TABLE 6: COMBINED RECEIPTS AND DISBURSEMENTS OF THE CENTRAL AND STATE GOVERNMENTS

(Amount ₹ billion)

Item	2010-11	2011-12	2012-13	2013-14	2014-15 (RE)	2015-16 (BE)
1	2	3	4	5	6	7
1 Total Disbursements	**21,451.5**	**24,217.7**	**26,949.3**	**29,759.8**	**35,215.1**	**38,150.9**
1.1 Developmental	12,677.0	14,209.4	15,741.6	16,982.1	20,697.0	21,897.5
1.1.1 Revenue	10,260.2	11,394.6	12,807.1	13,822.7	16,423.5	16,997.2
1.1.2 Capital	1,935.8	2,163.4	2,446.1	2,747.1	3,822.1	4,461.5
1.1.3 Loans	480.9	651.3	488.4	412.3	451.4	438.8
1.2 Non-Developmental	8,520.5	9,695.9	10,850.5	12,345.2	13,978.5	15,715.2
1.2.1 Revenue	7,765.9	8,923.6	9,991.4	11,337.0	12,939.7	14,460.2
1.2.1.1 Interest Payments	3,485.6	4,000.0	4,543.1	5,329.3	5,948.6	6,656.9
1.2.2 Capital	747.5	754.8	837.1	984.4	1,008.9	1,212.4
1.2.3 Loans	7.0	17.5	21.9	23.8	29.9	42.6
1.3 Others	254.0	312.4	357.2	432.6	539.6	538.2
2 Total Receipts	**21,535.6**	**24,540.6**	**27,690.3**	**29,767.1**	**34,835.6**	**37,976.2**
2.1 Revenue Receipts	15,788.2	16,926.8	19,716.2	21,900.7	26,098.5	28,547.3
2.1.1 Tax Receipts	12,500.7	14,427.5	16,879.6	18,413.6	20,859.2	23,206.2
2.1.1.1 Taxes on commodities and services	7,393.7	8,745.6	10,385.9	11,227.3	12,658.9	14,372.9
2.1.1.2 Taxes on Income and Property	5,087.2	5,654.1	6,462.7	7,155.0	8,165.9	8,797.6
2.1.1.3 Taxes of Union Territories (Without Legislature)	19.8	27.9	30.9	31.3	34.4	35.8
2.1.2 Non-Tax Receipts	3,287.5	2,499.3	2,836.6	3,487.1	5,239.3	5,341.1
2.1.2.1 Interest Receipts	250.8	288.7	355.4	400.4	385.4	347.9
2.2 Non-debt Capital Receipts	322.9	441.2	389.2	390.7	438.0	773.4
2.2.1 Recovery of Loans & Advances	82.1	253.7	129.3	93.5	92.8	77.1
2.2.2 Disinvestment proceeds	240.9	187.5	259.9	297.3	345.2	696.3
3 Gross Fiscal Deficit [1 - (2.1 + 2.2)]	**5,340.3**	**6,849.7**	**6,844.0**	**7,468.4**	**8,678.6**	**8,830.2**
3A Sources of Financing: Institution-wise						
3A.1 Domestic Financing	5,104.8	6,725.2	6,771.9	7,395.5	8,581.6	8,718.4
3A.1.1 Net Bank Credit to Government	3,147.1	3,898.3	3,352.8	3,358.6	-297.5	..
3A.1.1.1 Net RBI Credit to Government	1,849.7	1,391.8	548.4	1,081.3	-3,253.0	..
3A.1.2 Non-Bank Credit to Government	1,957.7	2,826.9	3,419.1	4,036.9	8,879.1	8,718.4
3A.2 External Financing	235.6	124.5	72.0	72.9	97.1	111.7
3B Sources of Financing: Instrument-wise						
3B.1 Domestic Financing	5,104.8	6,725.2	6,771.9	7,395.5	8,581.6	8,718.4
3B.1.1 Market Borrowings (net)	4,151.7	6,195.1	6,536.9	6,381.3	6,941.4	7,266.6
3B.1.2 Small Savings (net)	-545.3	190.9	-85.7	-142.8	-577.7	-327.4
3B.1.3 State Provident Funds (net)	362.4	334.3	329.9	306.7	351.3	344.0
3B.1.4 Reserve Funds	35.6	178.5	-4.1	34.6	-127.5	56.5
3B.1.5 Deposits and Advances	342.9	122.1	27.2	255.4	203.9	131.9
3B.1.6 Cash Balances	-84.2	-322.9	-741.0	-7.3	379.4	174.8
3B.1.7 Others	841.6	27.2	708.6	567.5	1,410.7	1,072.1
3B.2 External Financing	235.6	124.5	72.0	72.9	97.1	111.7
4 Total Disbursements as per cent of GDP	*27.6*	*27.4*	*27.0*	*26.2*	*28.1*	*27.0*
5 Total Receipts as per cent of GDP	*27.7*	*27.8*	*27.7*	*26.2*	*27.8*	*26.9*
6 Revenue Receipts as per cent of GDP	*20.3*	*19.2*	*19.7*	*19.3*	*20.8*	*20.2*
7 Tax Receipts as per cent of GDP	*16.1*	*16.3*	*16.9*	*16.2*	*16.6*	*16.4*
8 Gross Fiscal Deficit as per cent of GDP	*6.9*	*7.8*	*6.9*	*6.6*	*6.9*	*6.3*

..: Not Available.

Note: 1. Data for States from 2013-14 onwards are provisional and pertain to budgets of 25 State governments.
2. GDP data for 2014-15 and 2015-16 are Provisional Estimates and Budget estimates, respectively.

Source: Budget documents of Central and State governments.

APPENDIX TABLE 7: INDIA'S OVERALL BALANCE OF PAYMENTS

(US $ million)

	2010-11	2011-12	2012-13	2013-14	2014-15P
1	2	3	4	5	6
A. CURRENT ACCOUNT					
1 Exports, f.o.b.	256,159	309,774	306,581	318,607	316,741
2 Imports, c.i.f.	383,481	499,533	502,237	466,216	460,920
3 Trade Balance	-127,322	-189,759	-195,656	-147,609	-144,179
4 Invisibles, Net	79,269	111,604	107,493	115,212	116,242
a) 'Non-Factor' Services of which :	44,081	64,098	64,915	72,965	75,683
Software Services	50,905	60,957	63,504	66,958	70,400
b) Income	-17,952	-15,988	-21,455	-23,028	-24,983
c) Private Transfers	53,125	63,469	64,342	65,481	66,275
5 Current Account Balance	-48,053	-78,155	-88,163	-32,397	-27,937
B. CAPITAL ACCOUNT					
1 Foreign Investment, Net (a+b)	42,127	39,231	46,711	26,386	73,561
a) Direct Investment	11,834	22,061	19,819	21,564	32,627
b) Portfolio Investment	30,293	17,170	26,891	4,822	40,934
2 External Assistance, Net	4,941	2,296	982	1,032	1,630
3 Commercial Borrowings, Net	12,160	10,344	8,485	11,777	2,729
4 Short Term Credit, Net	12,034	6,668	21,657	-5,044	-924
5 Banking Capital of which :	4,962	16,226	16,570	25,449	11,618
NRI Deposits, Net	3,238	11,918	14,842	38,892	14,057
6 Rupee Debt Service	-68	-79	-58	-52	-81
7 Other Capital, Net @	-12,416	-6,929	-5,047	-10,761	1,426
8 Total Capital Account	63,740	67,755	89,300	48,787	89,959
C. Errors & Omissions	**-2,636**	**-2,432**	**2,689**	**-882**	**-616**
D. Overall Balance [A(5)+B(8)+C]	**13,050**	**-12,831**	**3,826**	**15,508**	**61,406**
E. Monetary Movements (F+G)	**-13,050**	**12,831**	**-3,826**	**-15,508**	**-61,406**
F. IMF, Net					
G. Reserves and Monetary Gold (Increase -, Decrease +) of which : SDR allocation	**-13,050**	**12,831**	**-3,826**	**-15,508**	**-61,406**
Memo: As a ratio to GDP					
1 Trade Balance	-7.5	-10.3	-10.7	-7.9	-7.0
2 Net Services	2.6	3.5	3.5	3.9	3.7
3 Net Income	-1.1	-0.9	-1.2	-1.2	-1.2
4 Current Account Balance	-2.8	-4.2	-4.8	-1.7	-1.3
5 Capital Net (Excld. changes in reserves)	4.5	3.0	5.1	3.4	7.4
6 Foreign Investment, Net	2.5	2.1	2.5	1.4	3.6

P: Provisional.

@: Includes delayed export receipts, advance payments against imports, net funds held abroad and advances received pending issue of shares under FDI.

Note: 1. Gold and silver brought by returning Indians have been included under imports, with a contra entry in private transfer receipts.
2. Data on exports and imports differ from those given by DGCI&S on account of differences in coverage, valuation and timing.

APPENDIX TABLE 8: FOREIGN DIRECT INVESTMENT FLOWS TO INDIA: COUNTRY-WISE AND INDUSTRY-WISE

(US $ million)

Source/Industry	2010-11	2011-12	2012-13	2013-14	2014-15 P
1	2	3	4	5	6
Total FDI	**14,939**	**23,473**	**18,286**	**16,054**	**24,748**
Country-wise Inflows					
Mauritius	5,616	8,142	8,059	3,695	5,878
Singapore	1,540	3,306	1,605	4,415	5,137
U.S.A	1,071	994	478	617	1,981
Cyprus	571	1,568	415	546	737
Japan	1,256	2,089	1,340	1,795	2,019
Netherlands	1,417	1,289	1,700	1,157	2,154
United Kingdom	538	2,760	1,022	111	1,891
Germany	163	368	467	650	942
UAE	188	346	173	239	327
France	486	589	547	229	347
Switzerland	133	211	268	356	292
Hongkong	209	262	66	85	325
Spain	183	251	348	181	401
China	2	73	148	121	505
Malaysia	40	18	238	113	219
South Korea	136	226	224	189	138
Luxembourg	248	89	34	539	204
Others	1,142	892	1,154	1,015	1,250
Sector-wise Inflows					
Manufacturing	4,793	9,337	6,528	6,381	9,613
Construction	1,599	2,634	1,319	1,276	1,640
Financial Services	1,353	2,603	2,760	1,026	3,075
Real Estate Activities	444	340	197	201	202
Electricity and other Energy Generation, Distribution & Transmission	1,338	1,395	1,653	1,284	1,284
Communication Services	1,228	1,458	92	1,256	1,075
Business Services	569	1,590	643	521	680
Miscellaneous Services	509	801	552	941	586
Computer Services	843	736	247	934	2,154
Restaurants and Hotels	218	870	3,129	361	686
Retail & Wholesale Trade	391	567	551	1,139	2,551
Mining	592	204	69	24	129
Transportation	344	410	213	311	482
Trading	156	6	140	0	228
Education, Research & Development	56	103	150	107	131
Others	506	419	43	293	232

P: Provisional.
Note : Includes FDI through SIA/FIPB and RBI routes only.