Annex

(see paragraph 15 to 25)

Sl	*Source of funds (excluding equity)*	*Rates offered on deposits on the date of review / rates at which funds raised (1)*	*Balance outstanding as a percentage of total funds (other than equity) (2) (See note below)*	*Marginal cost (1)x(2)*	*Remarks*
A	**Marginal Cost of Borrowings**				
1	**Deposits**				
a	Current Deposits				The core portion of current deposits identified based on the Reserve Bank of India (Small Finance Banks – Asset Liability Management) Directions, 2025 should be reckoned for arriving at the balance outstanding.
b	Savings Deposits				The core portion of savings deposits identified based on the Reserve Bank of India (Small Finance Banks – Asset Liability Management) Directions, 2025 should be reckoned for arriving at the balance outstanding.
c	Term deposits (Fixed Rate)				Term deposits of various maturities including those on which differential interest rates are payable should be included.
d	Term deposits (Floating Rate)				The rate should be arrived at based on the prevailing external benchmark rate on the date of review.
e	Foreign currency deposits				Foreign currency deposits, to the extent deployed for lending in rupees, should be included in computing marginal cost of funds. The swap cost and hedge cost of such deposits should be reckoned for computing marginal

					cost.
2	**Borrowings**				
a	Short-term Rupee Borrowings				Interest payable on each type of short term borrowing will be arrived at using the average rates at which such short term borrowings were raised in the last one month. For eg. Interest on borrowings from RBI under LAF will be the average interest rate at which a bank has borrowed from RBI under LAF during the last one month.
b	Longterm Rupee Borrowings				Option 1: Interest payable on each type of long term borrowing will be arrived at using the average rates at which such long term borrowings were raised. Option 2: The appropriate benchmark yield for bank bonds published by FIMMDA for valuation purposes will be used as the proxy rate for calculating marginal cost.
c	Foreign Currency Borrowings including HO borrowings by foreign banks (other than those forming part of Tier-I capital)				Foreign currency borrowings, to the extent deployed for lending in rupees, should be included in computing marginal cost of funds. The all-in-cost of raising foreign currency borrowings including swap cost and hedge cost would be reckoned for computing marginal cost of funds.
	Marginal cost of borrowings				**The marginal cost of borrowings shall have a weightage of 92 percent of Marginal Cost of Funds while return on networth will have the balance weightage of 8 percent.**
B	**Return on networth**	Amount of common equity Tier 1 capital required to be maintained for Risk Weighted Assets as per extant capital adequacy norms shall be included for computing marginal cost of funds. Since currently, the common equity Tier 1 capital is (5.5 percent +2.5 percent) 8 percent of RWA, the weightage given for this component in the marginal cost of funds will be 8 percent.			

		In case of newly set up banks (either domestic or foreign banks operating as branches in India) where lending operations are mainly financed by capital, the weightage for this component may be higher, i.e., in proportion to the extent of capital deployed for lending. This dispensation will be available for a period of three years from the date of commencing operations. The cost of equity will be the minimum desired rate of return on equity computed as a mark-up over the risk free rate. A bank could follow any pricing model such as Capital Asset Pricing Model (CAPM) to arrive at the cost of capital. This rate can be reviewed annually.

Marginal cost of funds = 92 percent x Marginal cost of borrowings + 8 percent x Return on networth

Note: A bank shall have the option to reckon the outstanding balances of deposits and other borrowings as on any day, not more than seven calendar days, prior to the date from which the MCLR becomes effective. The chosen time lag shall be maintained consistently for a period not less one year.