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Statement on Developmental and Regulatory Policies

This Statement sets out various developmental and regulatory policy measures for strengthening regulation and supervision; broadening and deepening of the financial markets; payment and settlement systems; and, financial inclusion.

I. Regulation and Supervision

1. Relaxation of External Commercial Borrowing (ECB) framework for Resolution Applicants

Under the extant ECB framework, proceeds of ECB denominated in either foreign currency or Indian Rupee (INR), are not permitted to be utilised for repayment or for on-lending for repayment of domestic Rupee loans. The resolution applicants under Corporate Insolvency Resolution Process (CIRP) under Insolvency and Bankruptcy Code (IBC), 2016 may find it attractive to borrow abroad to repay the existing lenders. In view of the above, it is proposed to relax the end-use restrictions under the approval route of the ECB framework for resolution applicants under the CIRP and allow them to utilise the ECB proceeds for repayment of Rupee term loans of the target company. Such ECBs could be availed from all eligible lenders under the extant ECB framework except from overseas branches/subsidiaries of Indian banks. Guidelines in this regard will be issued by the end of February 2019.

2. Review of Instructions on Bulk Deposit

In terms of extant instructions, banks have been given discretion to offer differential rate of interest on the bulk deposits as per their requirements and Asset-Liability Management (ALM) projections. The instructions in this regard, last reviewed in January 2013, defined

“bulk deposits” as single rupee deposits of ₹1 crore and above. With a view to enhancing the operational freedom of banks in raising deposits, it is proposed

- (i) to revise the definition of bulk deposits as single rupee deposits of ₹2 crore and above; and,
- (ii) that henceforth banks shall maintain their bulk deposit interest rate cards in the core banking system for supervisory review.

Guidelines in this regard will be issued by the end of February 2019.

3. Umbrella Organisation for Urban Cooperative Banks

The structure, size, lack of avenues for raising capital funds and limited area of operation of the Primary (Urban) Co-operative Banks (UCBs) add to their financial vulnerabilities. A long-term solution to make the UCB sector financially resilient and to enhance the depositors’ confidence is to set up an Umbrella Organization (UO) as prevalent in many countries. The UO, apart from extending liquidity and capital support to its member UCBs, would also be expected to set up Information and Technology (IT) infrastructure for shared use of members to enable them to widen their range of services in the wake of advances in information and communication technology at a relatively lower cost. The UO can also offer fund management and other consultancy services.

The idea of setting up of UO for the UCB sector was first mooted in the year 2006 by the Working Group (Chairman: Shri N S Vishwanathan) set up by the Reserve Bank on Augmentation of Capital of UCBs. It was examined in greater detail by the Working Group on Umbrella Organization and Constitution of Revival Fund for Urban Cooperative Banks (Chairman: Shri V S Das) in 2009 and the Expert Committee on Licensing of New Urban Co-operative Banks (Chairman: Shri Y H Malegam) in the year 2011. The need for UO has also been stressed by the High Powered Committee on UCBs (Chairman: Shri R Gandhi) in the year 2015.

The Reserve Bank has received a proposal for setting up an UO from the National Federation of Urban Cooperative Banks and Credit Societies Ltd. (NAFCUB). A decision on the specifics of the UO proposal will be taken by the Reserve Bank shortly.

4. Risk Weights for rated exposures to Non-Banking Financial Companies (NBFCs)

Under extant guidelines on Basel III Capital Regulations, exposures/claims of banks on rated as well as unrated Non-deposit Taking Systemically Important Non-Banking Financial Companies (NBFC-ND-SIs), other than Asset Finance Companies (AFCs), Non-Banking Financial Companies – Infrastructure Finance Companies (NBFCs-IFC) and Non-Banking Financial Companies – Infrastructure Development Fund (NBFCs-IDF), have to be uniformly risk-weighted at 100%. With a view to facilitating flow of credit to well-rated NBFCs, it has now been decided that rated exposures of banks to all NBFCs, excluding Core Investment Companies (CICs), would be risk-weighted as per the ratings assigned by the accredited rating agencies, in a manner similar to that for corporates. Exposures to CICs will continue to be risk-weighted at 100%. Guidelines in this regard will be issued by the end of February 2019.

5. Harmonisation of NBFC Categories

Various categories of NBFCs have evolved over time pertaining to specific sector/asset classes. Regulations put in place for each NBFC category have also been somewhat different. At present, there are twelve such categories. The Committee on Comprehensive Financial Services for Small Businesses and Low Income Households (chaired by Dr. Nachiket Mor) and Internal Committee (Chairman: Shri G. Padmanabhan), which submitted their reports in January 2014 and April 2014 respectively, had recommended harmonisation of the various categories of NBFCs. The Reserve Bank is committed to such harmonisation and to move towards activity-based regulation replacing the current entity-based regulation for the NBFC sector. As a first step in this direction, deposit acceptance regulations were harmonised in November 2014. Further, with the recent rationalization and liberalization of ECB norms, differential rules applicable to various categories of NBFCs stand harmonised.

It has now been decided to harmonise major categories of NBFCs engaged in credit intermediation, viz., Asset Finance Companies (AFC), Loan Companies, and Investment Companies, into a single category. The proposed merger of existing categories would reduce to a large extent the complexities arising from multiple categories and also provide the NBFCs greater flexibility in their operations. It will cover 99% of the NBFCs by number. Guidelines in this regard will be issued by the end of February 2019.

II. Financial Markets

6. Foreign Exchange Derivative facilities for Residents and Non-Residents (Regulation FEMA-25)

A review of the existing facilities for hedging of foreign exchange risk by non-residents and residents was announced in the Statement on Developmental and Regulatory Policies in the Monetary Policy Statements in February 2018 and August 2018, respectively. The said review has been undertaken.

Post review, a draft of the revised directions is being put in the public domain for seeking comments. The draft directions propose to, *inter alia*, merge the facilities for residents and non-residents into a single unified facility for all users, allow users having valid underlying exposure to hedge flexibly using any instrument of their choice, introduce the ability to hedge anticipated exposure to foreign exchange risk, and simplify the procedures for authorised dealers to offer foreign exchange derivatives. The draft circular on the revised guidelines will be released by the end of February 2019.

7. Task Force on Offshore Rupee Markets

In view of offshore interest in the Indian Rupee, the Reserve Bank's policy efforts have been to align incentives for non-residents to gradually move to the domestic market for their hedging requirements. At the same time, there is a need to improve residents' access to derivatives markets to hedge their currency risks. In order to take forward the process of gradual opening up of the foreign exchange market and also to benefit from a wider range of participants and views, it is proposed to set up a Task Force on Offshore Rupee Markets. The Task Force will examine the issues relating to the offshore Rupee markets in depth and recommend appropriate policy measures that also factor in the requirement of ensuring the stability of the external value of the Rupee. Further details about the composition and terms of reference of the Task Force shall be issued separately by the end of February 2019.

8. Rationalisation of Interest Rate Derivative Directions

The Reserve Bank has, over time, issued regulations covering various interest rate derivative products such as Interest Rate Swap (IRS), Forward Rate Agreement (FRA), Interest Rate Future (IRF), Interest Rate Option (IRO) and Money Market Future (MMF). The comprehensive guidelines on derivatives was issued in 2007 to clearly define the roles and

responsibilities for users and market makers. However, except Overnight Indexed Swaps (OIS), the activity in these derivative markets has been rather thin and limited. This, among other reasons, has contributed to a limited use of interest rate derivatives in the Indian financial sector. Some of these regulations have also not been reviewed for almost two decades (IRS/FRA guideline of 1999). It is, therefore, proposed to rationalise interest rate derivative regulations to achieve consistency and ease of access with the eventual objective of fostering a thriving environment for management of interest rate risk in the Indian economy. The draft comprehensive guidelines will be issued for public feedback by the end of March 2019.

9. Regulation of Financial Benchmarks

It was proposed in the Statement on Developmental and Regulatory Policies, in the Fourth Bi-monthly Monetary Policy Statement dated October 05, 2018, to introduce a regulatory framework for financial benchmarks to improve the governance of the benchmark processes relating to financial products and markets regulated by the Reserve Bank. Draft guidelines are being issued for public consultation.

10. Investment by Foreign Portfolio Investors (FPI) in Corporate Debt

As a part of the review of the FPI investment in Corporate Debt undertaken in April 2018, it was stipulated that no FPI shall have an exposure of more than 20% of its corporate bond portfolio to a single corporate (including exposure to entities related to the corporate). FPIs were given exemption from this requirement on their new investments till end-March 2019 to adjust their portfolios. While the provision was aimed at incentivizing FPIs to maintain a portfolio of assets, further market feedback indicates that FPIs have been constrained by this stipulation. In order to encourage a wider spectrum of investors to access the Indian corporate debt market, it is now proposed to withdraw this provision. A circular to this effect will be issued by mid-February, 2019.

III. Payment and Settlement Systems

11. Regulation of Payment Gateway Service Providers and Payment Aggregators

The Reserve Bank had in November 2009 issued directions regarding maintenance of nodal accounts of intermediaries like payment gateway providers and payment aggregators. In the “Payment and Settlement Systems - Vision 2018” Document, the Reserve Bank had indicated

that given the increasing role and importance of such entities, these guidelines would be revised. Accordingly, the Reserve Bank has been examining the need and feasibility of regulating Payment Gateway Service Providers and Payment Aggregators. A discussion paper on comprehensive guidelines covering payments related activities of these entities will be placed in the public domain for consultation with the stakeholders.

IV. Financial Inclusion

12. Working Group to Review Agricultural Credit

Agricultural credit growth has been significant over the years. In spite of this, there remain issues relating to agricultural credit such as regional disparity, extent of coverage, etc. There is also the issue of deepening long-term agricultural credit for capital formation. To examine these issues and arrive at workable solutions and policy initiatives, an Internal Working Group (IWG) to Review Agricultural Credit has been constituted by the Reserve Bank.

13. Collateral-free Agriculture Loan — Enhancement of Limit.

Presently the banks are mandated to extend collateral-free agriculture loans up to ₹ 1 lakh. This limit of ₹ 1 lakh was fixed in the year 2010. Keeping in view the overall inflation and rise in agriculture input costs since then, it has been decided to raise the limit for collateral-free agriculture loans from ₹ 1 lakh to ₹ 1.6 lakh. This will enhance coverage of small and marginal farmers in the formal credit system. The circular to this effect will be issued shortly.

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