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TOPICS

» Prudential Guidelines on Restructuring of Advances by Banks

Special regulatory treatment for asset classification had been made available to all categories of advances except consumer and personal loans, capital market exposures and commercial real estate exposures pursuant to the RBI circular dated August 27, 2008. This treatment permitted treating standard accounts as standard after restructuring, provided certain conditions are met such as the restructuring not being a repeated restructuring, dues to the bank are fully secured etc. Certain modifications to these stipulations were made vide RBI circular dated December 8, 2008 whereby special regulatory treatment was extended to Commercial Real Estate Exposures restructured for the first time as well as to exposures (other than commercial real estate, capital markets and personal/ consumer loans) which were viable but were facing temporary cash flow problems and needed a second restructuring.

Since the spillover effects of the global downturn have also started affecting the Indian economy particularly from September 2008 onwards creating stress for the otherwise viable units/activities, it was important that swift action is taken for detection of the weaknesses and restructuring package is put in place for viable accounts to preserve the economic and productive value of the affected assets. Hence RBI vide circular dated January 2, 2009 provided that -

(a) All accounts covered under the circular dated December 8, 2008 which were standard accounts on September 1, 2008 would be treated as standard accounts on restructuring provided the restructuring is taken up on or before January 31, 2009 and the restructuring package is put in place within a period of 120 days from the date of taking up the restructuring package.

(b) The period for implementing the restructuring package would stand extended from 90 days to 120 days in respect of accounts covered under the circular dated August 27, 2008 as well.

(c) The value of security is relevant to determine the likely losses which a bank might suffer on the exposure should the default take place. This aspect assumes greater importance in the case of restructured loans. However, owing to the current downturn, the full security cover for the Working Capital Term Loan (□WCTL□) created by conversion of the irregular portion of principal dues over the drawing power, may not be available due to fall in the prices of security such as inventories. In view of the extraordinary situation, this special regulatory treatment will also be available to 'standard' and 'sub-standard accounts', covered under circulars dated August 27, 2008 and December 8, 2008 even where full security cover for WCTL is not available, subject to the condition that provisions are made against the unsecured portion of the WCTL are as under:

- Standard Assets: 20%.
- Sub-standard Assets: 20% during the first year and to be increased by 20% every year thereafter until the specified period (one year after the first payment is due under the terms of restructuring)
- If the account is not eligible for upgradation after the specified period, the unsecured portion will attract provision of 100%
- These provisions would be in addition to the usual provisions as per the current regulation
- All the modifications indicated in (a), (b) and (c) above are one time measure and would be available for restructuring packages implemented till June 30, 2009

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» Reduction in CRR, Repo & Reverse Repo Rates

In response to the evolving global and domestic developments, the Reserve Bank of India (RBI) has taken a number of measures since mid-September 2008. In our Banking Newsflash dated November 17, 2008 and December 8, 2008 we had summarized the steps taken by RBI to augment the domestic and forex liquidity and to enable banks to continue to lend for productive purposes while maintaining the credit quality so as to sustain the growth momentum. On a review of current global and domestic macroeconomic situation, RBI vide it□s Press Release dated January 2, 2009 has decided to take the following further measures which are summarized as under:

Repo Rate
To reduce the repo rate under the liquidity adjustment facility (LAF) by 100 basis points from 6.5 per cent to 5.5 per cent with immediate effect.

Reverse Repo Rate
To reduce the reverse repo rate under the LAF by 100 basis points from 5.0 per cent to 4.0 per cent with immediate effect.

Cash Reserve Ratio (CRR)
To reduce the CRR of scheduled banks by 50 basis points from 5.5 per cent to 5.0 per cent from the fortnight beginning January 17, 2009.

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» External Commercial Borrowings (ECB) Policy □ Liberalizations by RBI

The RBI has vide its circular A.P. (DIR Series) Circular No. 46 dated January 2, 2009 modified some aspects of the present ECB policy as indicated below:

(i) **All-in-cost ceilings.** As per extant ECB policy, the all-in-cost ceilings for ECBs, in respect of both Automatic as well as Approval routes are as under:

Average Maturity Period	All-in-Cost ceilings over 6 Months LIBOR*
Three years and up to five years	300 bps
More than five years	500 bps

* for the respective currency of borrowing or applicable benchmark.

RBI has now decided to dispense with the requirement of all-in-cost ceilings on ECB until June 30, 2009. Accordingly, eligible borrowers, proposing to avail of ECB beyond the permissible all-in-cost ceilings specified above may approach the Reserve Bank under the Approval Route.

(ii) **Relaxation in end-use restrictions.** In May 2007, RBI had withdrawn the exemption accorded to the 'development of integrated township' as a permissible end-use of ECB. It has now been decided to permit corporates, engaged in the development of integrated township, as defined in Press Note 3 (2002 Series) dated January 04, 2002, issued by Department of Industrial Policy and Promotions, Ministry of Commerce & Industry, Government of India to avail of ECB under the Approval Route. The policy will be reviewed in June 2009.

In an effort to boost the cash- starved realty sector, this move will allow the developers of integrated townships to borrow funds from overseas.

(iii) **NBFCs in infrastructure sector can access ECBs.** Non-Banking Financial Companies (NBFCs) are permitted to avail of ECB for a minimum average maturity period of five years to finance import of infrastructure equipments for leasing to infrastructure projects in India

It has now been decided to allow NBFCs, which are exclusively involved in financing of the infrastructure sector, to avail of ECBs from multilateral / regional financial institutions and Government owned development financial institutions for on-lending to the borrowers in the infrastructure sector under the Approval route. While considering the applications, Reserve Bank will take into account the aggregate commitment of these lenders directly to infrastructure projects in India. The direct lending portfolio of the above lenders vis-à-vis their total ECB lending to NBFCs, at any point of time should not be less than 3:1. This facility will be reviewed in June 2009.

(iv) **Relaxation in ECB norms for certain services sectors**. At present, entities in the services sector viz. Hotels, Hospitals and Software sector are allowed to avail of ECB up to USD 100 million per financial year for import of capital goods, under the Approval route. It has now been decided to permit the corporates in the Hotels, Hospitals and Software sectors to avail of ECB up to USD 100 million per financial year, under the Automatic Route, for foreign currency and / or Rupee capital expenditure for permissible end-use. However, the proceeds of the ECBs should not be used for acquisition of land.

The modifications to the ECB guidelines will come into force with immediate effect. All other aspects of

ECB policy, such as USD 500 million limit per company per financial year under the Automatic Route, eligible borrower, recognized lender, end-use, all-in-cost ceiling, average maturity period, prepayment, refinancing of existing ECB and reporting arrangements remain unchanged.

In case of any clarifications please contact our Knowledge Management Team.

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