Chapter 4 - Monetary Management and Financial Intermediation

Given the unprecedented shock of COVID-19 pandemic, monetary policy was significantly eased from March 2020 onwards. RBI undertook various conventional and unconventional measures like Open Market Operations, Long Term Repo Operations, Targeted Long Term Repo Operations etc. to manage liquidity situation in the economy.

The financial flows to the real economy however remained constrained on account of subdued credit growth by both banks and Non-Banking Financial Corporations. The higher reserve money growth did not fully translate into commensurate money supply growth due to the lower (adjusted) money multiplier reflecting large deposits by banks with RBI under reverse repo.

- Gross Non Performing Assets ratio of Scheduled Commercial Banks decreased from 8.21 per cent at the end of March 2020 to 7.49 per cent at the end of September 2020.
- Capital to risk-weighted asset ratio of Scheduled Commercial Banks increased from 14.7 per cent to 15.8 per cent between March 2020 and September 2020 with improvement in both Public and Private sector banks.
- Improvement in transmission of policy repo rates to deposit and lending rates, as reflected in the decline of 94 bps and 67 bps in Weighted Average Lending Rate on fresh rupee loans and outstanding rupee loans respectively from March 2020 to November 2020.
- The recovery rate for the Scheduled Commercial Banks through IBC (since its inception) has been over 45 per cent. However, the focus on resolution of stressed assets had to take a backseat during the year on account of the outbreak of the Covid-19 pandemic. Government had suspended the initiation of fresh insolvency proceedings.

Regulatory Measures in Banking Sector

Commercial Banks

1. Merger of PSBs: Consolidation among another 10 PSBs, with Punjab National Bank, Canara Bank, Union Bank of India and Indian Bank as anchor banks came into effect from April 1, 2020.
2. Restructuring of MSME loans: A one-time restructuring of loans to MSMEs that were in default but 'standard' as on January 1, 2019, was permitted.
3. Large exposure framework: A bank's exposure under the Large Exposure Framework to a group of connected counterparties was increased from 25 per cent to 30 per cent of the eligible capital base of the bank.
4. Export Credit: The maximum permissible period of pre-shipment and post-shipment export credit sanctioned by banks was increased from one year to 15 months for disbursements made up to July 31, 2020, in line with the relaxation granted in the period of realization and repatriation of the export proceeds to India.
5. Monetary policy transmission – external benchmarking of loans: RBI deregulated the interest rates on advances by SCBs (excluding RRBs). With a view to strengthen the transmission of monetary policy, the banks were mandated to link all new floating rate personal or retail loans and floating rate loans extended to MSMEs to external benchmarks such as repo rate, Treasury Bill Rate and any external benchmark published by Financial Benchmarks India Pvt Ltd (FBIL).

Co-operative Bank

1. Revision in the target for priority sector lending: To promote financial inclusion, the overall priority sector lending target for Urban Co-operative Banks has been increased.
2. Inclusion of co-operative banks as eligible member lending institutions under interest subvention scheme for MSMEs - issuance of guidelines: All co-operative banks have been advised of their inclusion as Eligible Lending Institutions under the "Interest Subvention Scheme (ISS) for MSMSEs 2018" of the Government.
3. Reporting of large exposures to Central Repository of Information on Large Credits (CRILC): Urban Cooperative Banks (UCBs) with assets of `500 crore and above were brought under the CRILC reporting framework. Accordingly, UCBs shall report credit information, including classification of an account as Special Mention Account (SMA), on all borrowers having aggregate exposures of `5 crore and above with them to CRILC.
4. Limits on exposure to single and group borrowers and large exposures: The exposure norms for single borrower and a group of borrowers from 15 per cent and 40 per cent of UCB's capital funds, to 15 per cent and 25 per cent, respectively, of UCB's Tier-I capital.
5. Submission of returns under Section 31 (read with section 56) of the Banking Regulation Act, 1949 - Extension of time: In view of the difficulties faced by UCBs in submission of the returns due to the ongoing COVID-19 pandemic, the timeline for the furnishing of the returns for the financial year ended on March 31, 2020, was first extended by three months, i.e., till September 30, 2020 and then further to December 31, 2020.
6. Amendments to the Banking Regulation Act, 1949: Banking Regulation (Amendment) Act, 2020: The Banking Regulation Act has been amended by the Banking Regulation (Amendment) Act, 2020.

INVESTMENT BY FOREIGN PORTFOLIO INVESTORS

There were net inflows to the tune of ` 2.1 lakh crore on account of the foreign portfolio investors (FPIs) in the Indian capital market during 2020-21 (up to December), as compared to net inflows of ` 0.81 lakh crore during the same period in 2019-20. The total cumulative investment by FPIs (at the acquisition cost) increased by 5.4 per cent to US$ 273.6 billion as on December 31, 2020 from US$ 259.5 billion as on December 31, 2019.

INSURANCE SECTOR

Insurance penetration which was 2.71 per cent in 2001 has steadily increased to 3.76 per cent in 2019. In contrast, insurance penetration in Asia, i.e., Malaysia, Thailand and China was 4.72, 4.99 and 4.30 per cent respectively in 2019. As of 2019, the penetration for Life insurance in India is 2.82 per cent, the penetration for Non-Life insurance is much at 0.94 per cent.

Some important regulatory measures undertaken due to COVID-19 are as follows:

- KYC process has been simplified with the permission granted for 54 insurers to undertake Paperless KYC process through Aadhaar Authentication Services of UIDAI.
- Guidelines were issued on introduction of short-term health insurance policies providing coverage for COVID-19 disease which are valid upto March 31,2021.
- Guidelines were issued for Corona Rakshak policy which is a standard benefit-based policy and Corona Kavach Policy, a standard health policy which will be offered on indemnity basis and insurers had been asked to launch the product from July 10, 2020.

PENSION SECTOR

The overall contribution under NPS grew by more than 30 per cent.

In view of COVID-19, various regulatory measures were taken, including:

- Issuance of an advisory for extension of timelines for submission of various compliance by the Pension Funds and Custodian.
- Extension of time limit by one month (i.e. up to 30.06.2020) for submission of annual accounts and other annual MIS due to Covid-19 for all Pension Funds, Custodian, and NPS Trust.
- The partial withdrawal from NPS has been allowed for treatment of COVID-19.
- The online functionality on NPS on-boarding through Aadhaar-based offline paperless KYC verification.
- Online registration of APY subscribers through Bank's own web-portal, without using net-banking by their Savings Bank Customers.

CHAPTER SUMMARY

- Monetary policy remained accommodative in 2020.
- The repo rate has been cut by 115 bps since March 2020.
- Systemic liquidity in 2020-21 remained in surplus so far. RBI undertook various conventional and unconventional measures like OMOs, Long Term Repo Operations, Targeted Long Term Repo Operations etc. to manage liquidity situation in the economy.
- The transmission of high reserve money growth to money supply growth was only partial, showing impaired liquidity transmission as the banks put money back with RBI under reverse repo.
- Credit growth of banks slowed down to 6.7 per cent as on January 1, 2021. The credit off-take from banking sector witnessed a broad-based slowdown.
- Gross Non Performing Assets ratio of Scheduled Commercial Banks decreased from 8.21 per cent at the end of March 2020 to 7.49 per cent at the end of September 2020. However, this has to be seen in conjunction with the asset classification relief provided to borrowers on account of the pandemic.
- The monetary transmission of lower policy rates to deposit and lending rates improved in this year.
- Nifty 50 and S&P BSE Sensex reached record high closing of 14,644.7 and 49,792.12 on January 20, 2021 respectively.
- The recovery rate for the Scheduled Commercial Banks through IBC (since its inception) has been over 45 per cent.
- In view of COVID-19 pandemic, initiation of Corporate Insolvency Resolution Process (CIRP) was suspended for any default arising on or after March 25, 2020 for a period of 6 months. This was further extended twice for 3 months on September 24, 2020 and December 22, 2020. The suspension along with continued clearance of CIRPs allowed a small decline in accumulated cases.