# 3

## MONEY AND FINANCE

*Fiscal consolidation has substantially scaled down the Centre's dependence on net credit from Reserve Bank and also the draft of the Government on the resources of the commercial banking sector. In the current financial year the growth of money supply (M3) slowed down compared to the previous financial year despite a sizeable expansion in bank credit to the commercial sector and in particular to exporters.*

*The overall monetary policy continued to be restrictive to bring about a reduction in inflation, but there was some relaxation aimed at giving a stimulus to the productive sectors of the economy. The floor lending rate for advances of over Rs.2 lakh was brought down from 20 per cent to 18 per cent in two stages. Banks were given freedom to fix the interest rates on Non-resident External (Rupee) Accounts as also on domestic term deposits subject to caps of 13 per cent and 12 per cent respectively. Selective credit controls against cotton and kapas, vegetable seeds and oils were relaxed. A target of 10 per cent of net bank credit has been fixed for credit to exporters to be attained by banks by June 1993. Interest rates on export credit were cut across the board by one percentage point.*

*Serious irregularities and frauds were discovered in the securities transactions of certain banks which sparked a wider investigation. The investigations have revealed significant systemic weaknesses which are being corrected.*

*The year witnessed a series of financial sector reforms starting with a reduction in the incremental Statutory Liquidity Ratio (SLR) and a removal of the incremental Cash Reserve Ratio (CRR). The SLR on outstanding demand and time liabilities has also been reduced. A time schedule for attaining capital adequacy norms was announced. The branch licensing policy was liberalised. Revised formats for balance sheet and profit and loss accounts of the banks were introduced, and guidelines were issued for the setting up of new private sector banks.*

*Parallel reforms were initiated in the capital market. The Securities and Exchange Board of India (SEBI) was given statutory status by promulgation of an ordinance on 30 January 1991. The Capital Issues (Control) Act (1947) under which the Government* *exercised control on the volume and pricing of capital issues was repealed and the office of Controller of Capital Issues (CCI) was abolished. Permission was given to selected Indian companies to access the global capital market. SEBI has commenced the regulation of the capital market and the registration of brokers, sub-brokers and dealers. Foreign institutional investors are now permitted to invest in Indian companies. Mutual funds and portfolio managers have been brought under the regulatory powers of SEBI.*

*Steps were also taken to strengthen market for government securities through an upward revision in interest rates and the introduction of a system of auction of securities. A refinancing facility for these securities was also provided. Auctioning of 91-day and new 364-day treasury bills commenced. The auctioning of Government securities has reduced recourse to borrowing from RBI. A continued restraint on government's draft on bank resources is required to achieve monetary policy objectives.*

Monetary and credit policy in 1991-92 was directed primarily at curbing the growth of effective demand in order to contain inflation and ease the pressure on the balance of payments. Significant success was achieved on both counts. The annual rate of inflation, which had reached a peak of 16.7 per cent in August 1991, subsided to 13.6 per cent by the end of 1991-92. Foreign exchange reserves (excluding gold and SDRs) expanded from US$ 1.1 billion at the end of June 1991 to US$ 5.6 billion at the end of March 1992. This was in part due to the policy of credit restraint maintained during 1991-92. The expansion in net bank credit to the Government(NBCG) declined from Rs.23042 crore in 1990-91 to Rs.18101 crore in 1991-92. However, the growth of money supply (M3) at 18.5 per cent in 1991-92 was faster than the growth of 15.1 per cent in the previous year. The faster growth in money supply in 1991-92 was basically on account of the rapid build-up in net foreign exchange assets.

3.2 The stance of monetary policy in 1992-93 continued to be restrictive for most of the year, reflecting the priority attached to bringing down inflation to a single digit level. As a result, the overall expansion in money supply (M3) in 1992-93 was appreciably slower than in the previous year. However, some relaxation in the credit regime was introduced in the second half of the year with a view to stimulating domestic production and supporting exports.

3.3 The year 1992-93 was also characterised by major steps towards financial sector reforms covering both the banking sector and the capital markets. These reforms were based on the recommendations of the Narasimham Committee and took account of the shortcomings in the system revealed by the irregularities in securities trading of banks which surfaced early in the financial year.

## Money and Credit

### Monetary Programme and Policies

3.4 Monetary policy objectives in 1992-93 were conditioned by the need to reduce the rate of growth of money supply in view of the continuing inflationary pressure in the economy evident at the start of the year and the overhang of liquidity resulting from the fact that money supply growth in 1991-92 had actually accelerated. It was therefore envisaged that money supply growth in 1992-93 should be significantly slower than in 1991-92. The target for monetary expansion for 1992-93 should be kept at 10.4 per cent. The target of 10.4 per cent was associated with slower expansion in net Reserve Bank credit to the Central Government reflecting the lower level of the budget deficit in 1992-93. These elements of the monetary programme for 1992-93 were reflected in the credit ceilings agreed with the IMF as Programme targets under the standby arrangement. These targets, with the corresponding quarterly subceilings, are presented in Table 3.1.

TABLE 3.1

**Monetary Targets for 1992-93: IMF Programme**

| | Outstandings* at the end of | | | | | | |
|---|---|---|---|---|---|---|---|
| | 1992 | | | | | | 1993 |
| | June | | September | | December | | March |
| | C | A | C | A | C | A | C |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 |
| **A. Performance criteria** | (Rs. billion) | | | | | | |
| Net Domestic Assets (NDA) of RBI@ | 916 | 885 | 900 | 870 | 943 | 915 | 969 |
| Net Reserve Bank Credit to Central Government (NRCCG) | 997 | 990 | 999 | 986 | 993 | 994** | 977 |
| Net Bank Credit to the Government (NBCG) | 1677 | 1662 | 1689 | 1700 | 1697 | 1729 | 1687 |
| **B. Macro-economic Objectives** | (Growth in per cent) | | | | | | |
| Money Supply | 3.0 | 5.9 | 3.7 | 7.5 | 8.0 | 11.5 | 10.4 |
| Reserve Money | 7.1 | 7.4 | 5.9 | 6.7 | 11.0 | 7.8 | 13.8 |

* Indicative targets A = Actual C = Ceiling

** Inclusive of Rs.7.5 billion incurred on account of Reserve Asset Subscription made to the IMF towards quota increase.

@ The ceiling will be adjusted for (i) unexpected valuation effects arising from change in exchange rate and price of gold; (ii) changes in reserve requirements; and (iii) changes in the net international reserve floor.

NOTE: Compliance with the ceilings on RBI variables, i.e., NDA and net RBI credit to Central Government, will be determined by taking a simple average of four Fridays leading up to and including last reporting Friday of June, September and December. For March 1993 quarter it would be the average of four preceding Fridays and March 31, after the closure of Government accounts.For NBCG,it is on the basis of the average of the last two reporting Fridays for the first three quarters, and the average for the two reporting Fridays of March and March 31, after closure of Government accounts, for the last quarter.

3.5 As shown in Table 3.1, data on actual performance in comparison with targets are available up to December-end (25 December) 1992. It is seen that the performance criteria in respect of both net domestic assets of RBI and net RBI credit to Central Government were met for the first three quarters of 1992-93. Reserve Bank credit to Central Government on an average basis is still high, compared to the year-end levels. The indicative targets in respect of net bank credit to Government were met only for the first quarter, i.e., June 1992. For subsequent quarters net bank credit to the Government has been above the ceiling. The expansion in M3 in this period is also significantly above its quarterly projections, although it has grown more slowly than in the previous year.

### Monetary and Credit Policy in 1992-93

3.6 Monetary policy in 1992-93 was guided by the objectives of moderating the growth in Money Supply (M3) and implementing the recommendations of the Narasimham Committee on financial sector reforms. In the second half of the year, in recognition of the noticeable slowing down of inflation and the need to stimulate production, monetary policy in 1992-93 relaxed the restrictions placed in 1991-92 (Box 3.1).

BOX 3.1

**Credit Policy Measures in 1992-93**

- Lending rate structure simplified into four slabs instead of six.
- The floor interest rate for bank credit (other than export) of over Rs. 2 lakh reduced in two stages to 18 per cent.
- Interest rate on pre-shipment and post-shipment export credit reduced across the board by one percentage point.
- Banks free to fix interest rates on term deposits subject to a cap of 13 per cent (reduced later to 12 per cent).
- Banks free to set interest rates on Non-Resident External (Rupee) Accounts subject to a cap of 13 per cent.
- Interest rate on savings deposits raised to 6 per cent.
- Interest rate for export credit denominated in US Dollars reduced to 6.5 per cent and for refinance from RBI on this credit to 5.5 per cent.
- Forty-five per cent ceiling on the ratio of incremental credit (minus export credit) to deposits removed.
- Target for export credit set at 10 per cent of net bank credit to be attained by banks by June 1993.
- Restrictions on loans for consumer durables and on other non-priority sector personal loans removed.
- Selective credit controls on bank advances against stocks of oilseeds and vegetable oils, cotton and kapas relaxed.
- RBI's limits to NABARD enhanced by Rs.400 crore.
- RBI's refinance limits to IDBI for discounting bills relating to purchase of machinery, commercial vehicles etc. increased by Rs.400 crore, linked to IDBI providing Rs.200 crore from its own resources.
- Threshold limit for term loans by the banks raised to Rs.10 crore.
- Relaxations in the method of computing maximum permissible bank finance for individual borrowers in order to increase effective credit availability.

### Reduction in SLR and CRR

3.7 A start was made in implementing the Narasimham Committee recommendations to reduce the Statutory Liquidity Ratio (SLR) and Cash Reserve Ratio (CRR) which had over the years been increased to very high levels leading to a very large part of bank funds (up to 63 per cent at the margin) being locked up in low yielding assets. This distortion had the effect of lowering bank profitability and forced banks to charge high interest rates on commercial advances to the productive sectors.

### Changes in Interest rates

3.8 Table 3.2 indicates changes in interest rate structure of scheduled commercial banks in 1992-93 so far. Banks have been advised to fix their deposit rates on the basis of their perception of inflation, cost of and return on funds and inter-bank borrowing/lending status. To improve competitiveness of exports, interest rates on Rupee export credit were reduced across the board by one percentage point in October 1992. Banks are also entitled to refinance facilities from RBI against export credit denominated in both rupees and US dollars. The interest rate on refinance on dollar-denominated export credit was reduced from 9.5 per cent to 7.5 per cent on March 2,1992 and further to 5.5 per cent on April 22, 1992.

### Selective Credit Controls

3.9 The levels of credit ceiling applicable to advances against paddy/rice and wheat were reduced from 85 per cent to 70 per cent of the peak level of credit maintained in the three year base period (1988-89 to 1990-91), with effect from 22 April 1992. The selective credit controls which were tightened against cotton and kapas through higher minimum margins against bank advances with effect from this date, were later on relaxed in two stages on 11 December 1992 and 19 Januray 1993 by reducing minimum margins by 15 percentage points in each stage. From 19 January 1993 the minimum margins on bank advances have been reduced across the board by 15 percentage points, for oilseeds and vegetable oils (including vanaspati).

3.10 From 22 April 1992 RBI removed the ceiling of 45 per cent on the incremental non-food (minus export) credit-deposit ratio and banks were advised to normalise credit facilities to support the revival of productive activity. Further, restrictions imposed in October 1991 on (a) loans for consumer durables and (b) other non-priority sector personal loans were withdrawn from the same date.

### Special Measures for Credit to Agriculture and Industry

3.11 On January 19,1993 several special measures as noted below were initiated to boost the flow of credit to agriculture and industry:

(a) The limits given to National Bank of Agriculture and Rural Development (NABARD) under its General Line of Credit were enhanced by Rs.400 crore so that it can provide larger credit to finance short-term agricultural operations.

(b) Reserve Bank of India would provide short-term accommodation of Rs.400 crore by way of refinance limits to Industrial Development Bank of India (IDBI) to supplement Rs.200 crore of IDBI's own funds for augmenting credit flow to the manufacturers of commercial vehicles, machinery manufacturers, hire purchase/equipment leasing companies and road transport corporations, through the IDBI's schemes of bill rediscounting and direct discounting and assistance to hire purchase/leasing companies.

TABLE 3.2

**Selected Interest Rates of Scheduled Commercial Banks**

(Per cent per annum)

| | Rates @ as on 31 March 1992 | Rates @ as on 9 October 1992 |
|---|---|---|
| A. Bank deposits | | |
| (a) Domestic term deposits | | |
| i) 46 days and above but less than one year | 11.00 | |
| ii) One year and above but less than two years | 12.00 | Not exceeding |
| iii) Two years and above but less than three years | 12.00 | 12.00 |
| iv) Three years and above | 13.00 | |
| (b)Non-Resident (External) Rupee Accounts | | |
| i) 46 days and above but less than one year | 8.50 | |
| ii) One year and above but less than two years | 10.50 | |
| iii) Two years and above but less than three years | 11.00 | Not exceeding |
| iv) Three years and above but less than five years | 13.00 | 13.00 |
| v) Five years and above | 14.00 | |
| (c) Savings deposits | 5.00 | 6.00 |
| B Bank credit (other than export credit) | | |
| i) Up to and including Rs. 7500 | 11.50 | 11.50 |
| ii) Over Rs.7500 and up to Rs.15000 | 13.00 | |
| iii) Over Rs. 15000 and up to Rs.25000 | 13.50 | 13.50 |
| iv) Over Rs. 25000 and up to Rs.50000 | 15.50 | |
| v) Over Rs. 50000 and up to Rs. 2 lakh | 16.50 | 16.50 |
| vi) Over Rs. 2 lakh (Minimum) | 19.00 | 18.00 |
| I. Export credit (Rupee) | | |
| i) Credit against duty drawback receivable up to 90 days | 0.00 | 0.00 |
| ii) Pre-shipment credit up to 180 days | 15.00 | 14.00 |
| iii) Post-shipment credit | 15.00 | 14.00 |
| (a) Demand bills | | |
| (b) Usance bills 46 to 90 days | | |
| iv) Credit against Govt. incentives | 15.00 | 14.00 |
| v) Pre-shipment credit for 181 to 270 days * | 17.00 | 16.00 |
| vi) Post-shipment credit | | |
| (a) Usance Bills 91 to 180 days | 19.00 | 18.00 |
| (b) beyond six months from date of shipment | 24.00 | 23.00 |
| vii) All other export credit not listed (Minimum)) | 20.00 | 18.00 |
| II. Post-shipment export credit (US Dollar) (Demand bills in transit period specified by FEDAI and usance bills for a period specified by FEDAI plus grace period, up to six months from date of shipment) | 8.50 | 6.50 |
| C DRI advances | 4.00 | 4.00 |
| D Term loans(to agriculture,SSI and transport operators owning up to two vehicles) | | |
| i) Over Rs. 25000 and up to Rs. 50000 | 14.00 | 14.00** |
| ii) Over Rs. 50000 | 15.00 | 15.00** |

@ The rates are exclusive of interest tax imposed effective 1 October 1991.
* With prior approval of RBI ** New limits since October 9,1992 : (i) Over Rs.25,000/- and up to Rs.2 lakh (ii) Over Rs. 2 lakh

TABLE 3.3

**Selective Credit Controls on Bank Advances (Effective 19 January 1993)**

(Per cent)

| | Mills/ processors | Others | Warehouse receipts | credit ceiling Nov.1990- Oct.1991** |
|---|---|---|---|---|
| 1 | 2 | 3 | 4 | 5 |
| 1 Paddy and rice | 60 | 75 | 60 | 70 |
| 2 Wheat | 60 | 75 | 60 | 70 |
| 3 Pulses | 60 | 75 | 60 | 85 |
| 4 Other foodgrains | 60 | 75 | 60 | 85 |
| 5 Oilseeds (oil of groundnut,rapeseed/ mustard, cottonseed, linseed, castorseed and all imported oilseeds) | 45 | 60 | 45 | 85 |
| 6 Vegetable oils (viz. groundnut oil, rapeseed/mustard oil, cottonseed oil linseed oil, castor oil,vansapati and all imported oils) | 45@ | 60 | 45 | 85 |
| 7 Sugar | | | | |
| a) Buffer | 0 | - | - | - |
| b) Unreleased stock | 20 | - | - | - |
| c) Released | 75 | 75 | 60 | - |
| 8 Gur and khandsari | 45 | 75 | 60 | - |
| 9 Cotton and kapas | x | 45 | 30 | 85+ |

** Percentage to peak level of credit of a party during three years ending 31 March 1991.
@ Applicable to registered oil mills.
- Not applicable.
+ Applicable to other than mills/processors.
x Exempt from margin requirement.

(c) The threshold limit for term loans by the scheduled commercial banks which had remained unchanged since 1985 at Rs.3 crore has also been extended to Rs.10 crore so that banks can provide term loans for larger number of projects in participation with State Finance Corporations (SFC) and State Industrial Development Corporations (SIDC), irrespective of the paid-up capital and reserves of the borrowing company.

(d) Credit availability from the banks for individual borrowers has been enhanced by modifying the maximum permissible bank finance (MPBF)limits currently applicable for each borrower. The method of calculating the limits will include only two-thirds of the term loan instalments falling due for repayment during the next twelve months (instead of the full amount) as items of current liabilities by banks, thus increasing the MPBF limit.

## Monetary and Credit Trends

### Reserve Money

3.12 High-powered or reserve money provides the base for overall monetary growth. In the current financial year up to January 8, 1993 reserve money grew at 8.7 per cent which is significantly lower than the growth of 15.0 per cent in the corresponding period of 1991-92. The slow-down in reserve money expansion was primarily because the expansion of Net RBI Credit to the Central Government was much slower at Rs.8724 crore compared with Rs.14980 crore in 1991-92. This in turn reflects the lower budgetary deficit in 1992-93. Growth of reserve money in the current year has also been moderated by the decline in net foreign exchange assets of RBI by Rs.3275 crore compared with an expansion by Rs.6092 crore in 1991-92.

3.13 The growth of reserve money in the current financial year would have been even slower had it not been for the expansion in the borrowing of commercial and co-operative banks from RBI. As shown in Table 3.4, this item expanded by Rs.2565 crore in 1992-93 compared with a decline of Rs.3612 crore in 1991-92. In the last financial year, the restrictive credit policy had kept bank credit growth at a very low level. The banks with surplus liquidity could repay their debts to the RBI and also add to their balances with RBI by a large margin. In contrast, faster growth in bank credit in 1992-93, and particularly export credit, following relaxation in credit controls and liberalisation of RBI's export credit refinance in the current financial year, has led to a reversal of the last year's trend. Banks have been providing more export credit by making use of refinance facilities from the Reserve Bank.

TABLE 3.4

**Sources of Change in Reserve Money**

| | | Variations+ | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | Outstanding on March 31, 1990 | 1990-91 Mar.31 to Mar.31 | 1991-92 Mar.31 to Mar.31 | 1991-92 Mar.31 to Jan.10 | 1992-93 Mar.31 to Jan.8 | 1990-91 Mar.31 to Mar.31 | 1991-92 Mar.31 to Mar.31 | 1991-92 Mar.31 to Jan.10 | 1992-93 Mar.31 to Jan.8 |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 |
| | | | (Rs. crore) | | | | (Per cent) | | |
| 1 Net RBI credit to Government $ | 73683 | 15165 | 5168 | 13022 | 7491 | 20.6 | 5.8 | 14.7 | 8.0 |
| 2 RBI credit to banks@ | 7472 | 2535 | -4905 | -3612 | 2565 | 33.9 | -49.0 | -36.1 | 50.3 |
| 3 RBI credit to commercial sector* | 6349 | -7 | 918 | -821 | -1240 | -0.1 | 14.5 | -12.9 | -17.1 |
| 4 Net foreign exchange assets of RBI # | 6068 | 1915 | 10855 | 6092 | -3275 | 31.6 | 136.0 | 76.3 | -17.4 |
| 4a Excluding revaluation of gold | | -4633 | 9141 | 3430 | -3173 | -76.4 | 114.5 | 43.0 | -16.8 |
| 5 Government's currency liabilities to the public | 1555 | 66 | 75 | 60 | 62 | 4.2 | 4.6 | 3.7 | 3.7 |
| 6 Net non-monetary liabilities of RBI | 17536 | 9486 | 381 | 1614 | -3017 | 54.1 | 1.4 | 6.0 | -11.0 |
| 7 Reserve Money (1+2+3+4+5-6) | 77591 | 10188 | 11730 | 13127 | 8620 | 13.1 | 13.4 | 15.0 | 8.7 |

+ Variations are worked out on the basis of March 31 data after closure of Government accounts. All figures except for 1990-91 are provisional

@ Includes claims on NABARD.

* Excludes, since the establishment of NABARD, its refinance to banks.

$ Includes special securities.

# Variations are inclusive of appreciation in the value of gold following its revaluation close to the international market price since 17 October 1990. Such appreciation has a corresponding effect on RBI's net non-monetary liabilities

TABLE 3.5

## Sources of Change in Money Stock

| 1 | 1990-91 Mar.31 to Mar.31<br>2 | 1991-92 Mar.31 to Mar.31<br>3 | 1991-92 Mar.31 to Jan.10<br>4 | 1992-93 Mar.31 to Jan.8<br>5 | 1990-91 Mar.31 to Mar.31<br>6 | 1991-92 Mar.31 to Mar.31<br>7 | 1991-92 Mar.31 to Jan.10<br>8 | 1992-93 Mar.31 to Jan.8<br>9 |
|---|---|---|---|---|---|---|---|---|
| | Variations during $ | | | | | | | |
| | | (Rs. crore) | | | | (Per cent) | | |
| 1 M1 (Money supply with the public) | 11832 | 21219 | 18463 | 5085 | 14.6 | 22.8 | 19.9 | 4.5 |
| II M3 (Aggregate monetary resources) (1+2+3+4) | 34878 | 49256 | 40727 | 38643 | 15.1 | 18.5 | 15.3 | 12.3 |
| i) Currency with the public | 6748 | 8184 | 7800 | 4755 | 14.6 | 15.4 | 14.7 | 7.8 |
| ii) Demand deposits with banks | 5008 | 12813 | 9253 | -1314 | 14.7 | 32.7 | 23.6 | -2.5 |
| iii) Time deposit with banks | 23046 | 28037 | 22264 | 33558 | 15.4 | 16.2 | 12.9 | 16.7 |
| iv) Other deposits with RBI | 76 | 222 | 1410 | 1644 | | | | |
| III Sources of change in Money stock (M3)(1+2+3+4-5) | | | | | | | | |
| 1 Net bank credit to Government (A+B) | 23042 | 18101 | 23888 | 16392 | 19.7 | 12.9 | 17.0 | 10.4 |
| A) RBI's net credit to Government (i+ii)@ | 15165 | 5168 | 13022 | 7491 | | | | |
| i) Central Government | 14745 | 5508 | 14980 | 8724+ | | | | |
| ii) State Governments | 420 | -340 | -1958 | -1233 | | | | |
| B) Other banks' credit to Government | 7877 | ·12933 | 10866 | 8901 | | | | |
| 2 Bank credit to commercial sector(A+B) | 20065 | 19296 | 7135 | 21012 | 13.2 | 11.2 | 4.2 | 11.0 |
| A) RBI's credit to commercial sector * | -7 | 918 | -821 | -1240 | | | | |
| B) Other banks' credit to commercial sector | 20072 | 18378 | 7956 | 22252 | | | | |
| 3 Net foreign exchange assets of the banking sector# | 1854 | 10855 | 6092 | -3275 | 27.2 | 125.2 | 70.2 | -16.8 |
| 3a Excluding revaluation of gold | -4694 | 9141 | 3430 | -3173 | -68.8 | 105.4 | 39.6 | -16.2 |
| 4 Government's currency liabilities to the public | 66 | 75 | 60 | 62 | 4.2 | 4.6 | 3.7 | 3.7 |
| 5 Banking sector's net non-monetary liabilities other than time deposits (a+b) | 10149 | -929 | -3552 | -4452 | 21.9 | -1.6 | -6.3 | -8.0 |
| a) Net non-monetary liabilities of RBI | 9486 | 381 | 1614 | -3017 | | | | |
| b) Net non-monetary liabilities of other banks (residual) | 663 | -1310 | -5166 | -1435 | | | | |

* Excludes, since the establishment of NABARD, its refinance to banks.

@ Includes special securities.

$ Variations in respect of scheduled commercial banks are based on data for the last reporting Friday of March. data for the RBI and others are for March 31.

\# Inclusive of appreciation in the value of gold following it revaluation close to international market price since 17 October 1990. Such appreciation has a corresponding effect on RBI's net non-monetary liabilities.

\+ Includes Rs.751.64 crore (equivalent of SDRs 211.95 million) incurred on account of Reserve Asset subscription to the IMF towards the quota increase.

### Money Supply (M3)

3.14 Money supply (M3) expansion, which had accelerated in 1991-92, slowed down in the course of the current financial year. In 1992-93 up to 8 January 1993 it was 12.3 per cent, compared with 15.3 per cent in the corresponding period of the previous financial year. The annual rate of growth (point-to-point basis) has also fallen from 18.8 per cent on 10 January 1992 to 15.4 per cent on 8 January 1993.

3.15 The lower rate of growth in M3 may be attributed to substantiallly lower growth in net RBI credit to Central Government and also in net bank credit to Government (Table 3.5). Fiscal consolidation, and particularly reduced recourse to RBI for financing the fiscal deficit because of the sale of 364-day treasury bills in the market, have made it possible to keep the growth in net Reserve Bank credit to the Central Government at a modest level. The other contributory factor to the lower growth in M3 is the decline in the net foreign exchange assets of the banking sector. This in turn is primarily because of (a) refund of deposits under Foreign Currency (Banks and Others) Deposits scheme and (b) higher rate of growth in imports than exports. However, there was upward pressure on the growth of money supply on account of (a) increase in bank credit to commercial sector and (b) decline in non-monetary liabilities of the banking sector.

3.16 The growth of bank credit to the commercial sector in the current year has been very substantial, reflecting to some extent the conscious decisions of the Government to reduce the SLR and withdraw the incremental cash reserve ratio. Up to 8 January 1993, the growth of bank credit to the commercial sector had reached Rs.21012 crore compared with only Rs.7135 crore in the same period of the preceding year. Net non-monetary liabilities of the banking sector, expansion of which is a moderating factor on money supply growth, have declined in the current financial year.

3.17 The lower growth in M3 in the current financial year is reflected in lower growth in both currency with public and a fall in demand deposits with banks, which were partly offset by larger growth in time deposits.

### Scheduled Commercial Banks

3.18 The remarkable shift from demand to time deposits was induced by (a) high interest rate of 11 per cent offered on short-term time deposits (i.e. deposits from 46 days up to one year) and (b) removal of tax deduction at source (TDS) on interest income (Table 3.6). Another factor which boosted time deposit growth, particularly up to July 1992, was the large inflow of foreign currency deposits under Foreign Currency (Banks and Others) Deposit (FC(BO)D) scheme to invite deposits from foreign citizens (not just from NRIs), banks and corporations. Under the scheme, which was in effect up to 31 July 1992, there was an inflow of US$ 1615 million in 1992-93 as against US$ 302 million in 1991-92 as a whole. Since August 1992 this scheme has been closed and repayments have started, which has somewhat moderated time deposit growth.

3.19 The lending capacity of the banks has been substantially augmented in the current financial year because of the removal of the incremental CRR and reduction in SLR, and the refund of one-third of incremental CRR cash balances held by RBI. This is reflected in the sharp increase in scheduled commercial bank credit in the period up to 8 January 1993. Total bank credit increased by Rs.19934 crore in this period compared with Rs.5013 crore in the previous year. If food procurement credit is excluded, the increase is even more dramatic - from Rs.4984 crore in 1991-92 to Rs.19110 crore in 1992-93. Demand for bank credit by the commercial sector got a boost from the reduction in interest rates on bank advances, availability of attractive refinance facilities for export credit and removal of the ceiling on incremental non-food (excluding export) credit-deposit ratio.

TABLE 3.6
**Scheduled Commercial Banks - Selected Indicators**

| | | Variations during | | |
|---|---|---|---|---|
| | 1990-91 March 23 1990 to March 22 1991 | 1991-92 March 22 1991 to March 20 1992 | 1991-92 March 22 1991 to Jan.10 1992* | 1992-93 March 20 1992 to Jan.8 1993* |
| 1 | 2 | 3 | 4 | 5 |
| | | (Rs. crore) | | |
| 1 Aggregate deposits (a+b) | 25583 | 38217 | 28290 | 31256 |
| a) Demand deposits | 4337 | 11896 | 8704 | -1446 |
| b) Time deposits | 21246 | 26321 | 19586 | 32702 |
| 2 Borrowings from R.B.I. | 1069 | -2891 | -1346 | 2536 |
| 3 Cash in hand and balances with R.B.I. | 554 | 10522 | 10977 | 2036 |
| a) Cash in hand | 156 | 204 | 104 | 180 |
| b) Balances with R.B.I. | 398 | 10318 | 10873 | 1856 |
| 4 Net Balances with R.B.I. (3(b)-2) | -671 | 13209 | 12219 | -680 |
| 5 Money at call and short notice | -489 | 904 | 965 | 1328 |
| 6 Bank Credit (a+b) | 14848 | 9291 | 5013 | 19934 |
| a) Public food procurement credit | 2500 | 164 | 29 | 824 |
| b) Non-food bank credit | 12348 | 9127 | 4984 | 19110 |
| Of which to Priority Sector | 2532 | 2554 | 633@ | 853@ |
| 7 Investments in Government and other approved securities | 10696 | 15131 | 12144 | 10957 |
| a) Government securities | 7706 | 12729 | 10713 | 8741 |
| b) Other approved securities | 2990 | 2402 | 1431 | 2216 |
| 8 Balances with other banks in current account | 276 | 621 | 574 | 200 |
| | | (per cent) | | |
| 9 Credit-deposit ratio | 60.4 | 54.4 | 54.9 | 55.5 |
| 10 Non-food credit-deposit ratio | 58.1 | 52.4 | 52.9 | 53.4 |
| 11 Investment-deposit ratio | 39.0 | 39.9 | 39.5 | 38.6 |

* Provisional.
@ Data available up to June of respective years.

3.20 There has been a large expansion in export credit in the current financial year. Up to 27 November 1992, export credit increased by Rs.2314 crore (21.6 per cent) accounting for 9.2 per cent of the total net bank credit, as against 8.6 per cent on 20 March 1992 and 7.6 per cent on 22 March 1991.

3.21 Expansion in export credit may be attributed to attractive facilities of refinance provided by RBI on export credit. On 27 November 1992 export credit refinance reached a high level of Rs.8,064 crore (62.0 per cent of total export credit) from Rs. 5594 crore on 20 March 1992 (52.3 per cent of total export credit). Refinance limits for export credit denominated in US dollars, increased from only Rs.30 crores on 20 March 1992 to Rs.3,018 crore on 27 November 1992.

3.22 RBI also constituted an expert committee to examine the various issues relating to export credit. Banks have been advised to reach a level of export credit equivalent to 10 per cent of net bank credit by June 1993 and meet full credit requirements of exporters, even if it exceeds the maximum permissible bank finance (MPBF) limits for individual borrowers. Failure to reach the stipulated level of export credit or to show distinct improvement in export credit performance could invite bank-specific policy response (a higher CRR or withdrawal of refinance facility) from RBI.

### Sectoral Distribution of Bank Credit

3.23 Data on the sectoral distribution of gross bank credit are available for April-July 1992 (Table 3.7). Both gross bank credit and non-food credit have recorded faster growth in this brief period (6.3 per cent and 6.7 per cent as against 0.7 per cent and 0.4 per cent respectively in April-July, 1991). There has been a substantial expansion in credit flow to large and medium industries (10.6 per cent as against 0.8 per cent last year). However, credit to small-scale industries expanded at a slower pace.

### Financial Results of Commercial Banks

3.24 As mentioned earlier, the formats of financial statements of the scheduled commercial banks were revised on the basis of new norms and principles regarding income recognition, asset classification and provisioning. The revised financial statements show that total profits were 64.3 per cent higher in 1991-92 than in 1990-91 for the State Bank of India (SBI) and its seven associates, 71.8 per cent higher for 20 other public sector banks, 120 per cent higher for private sector banks and 37.9 per cent higher for foreign banks. The increase is 61.5 per cent for all scheduled commercial banks.

3.25 However, a better indicator of the performance of the banks is their profits as a percentage of their working funds (Table 3.8). They were the highest for the foreign banks in both 1990-91 and 1991-92 because of their larger non-interest income. The ratio of total expenditure to working funds is also higher for foreign banks (relative to other groups of banks) but less so than their income ratio.

3.26 Between 1990-91 and 1991-92, profits as a percentage of working funds increased for public and private sector banks but declined for the foreign banks. Expenditure as a percentage of working funds increased for all categories of banks except the private sector banks.

3.27 Twenty four foreign banks with 140 branches earned Rs.2799.74 crore of interest income with a total outstanding bank credit of Rs.9144.03 crore, while all other commercial banks including SBI Group and private sector banks with nearly 46000 branches earned a total interest income of Rs.21910 crore with a total outstanding credit of Rs.118626 crore at the end of March 1992. However, interest costs of the foreign banks were also relatively higher. The average interest paid on working funds was 7.3 per cent for foreign banks against 6.9 per cent for other banks. Thus the foreign banks spend more to earn more on their working funds. Table 3.9 presents published profits of the public sector banks for accounting years ended 31 March 1991 and 1992.

## Term Lending Institutions

3.28 Aggregate assistance sanctioned by term lending financial institutions (also called development finance institutions (DFIs)) registered a growth rate of over 25.1 per cent in 1991-92 over the previous year, and disbursements grew by 33.5 per cent. In the three-year period from 1989-90 to 1991-92, assistance sanctioned and disbursed recorded average annual growth rates of 20.5 per cent and 21.4 per cent respectively.

3.29 Provisional data for the first nine months of 1992-93 for all-India DFIs shows a sharp growth of around 70 per cent in sanctions and a 47 per cent growth in disbursements over corresponding period of the previous year (Table 3.10). The financial institutions, in response to the emerging environment, have started accessing market sources for funds in a big way. Industrial Development Bank of India (IDBI) made a bond issue of over Rs.486

TABLE 3.7

## Sectoral Deployment of Gross Bank Credit

| On the last reporting Friday | 1989-90 | 1990-91 | April-July 1991-92 | 1991-92 | 1992-93 | 1989-90 | 1990-91 | April-July 1991-92 | 1991-92 | 1992-93 |
|---|---|---|---|---|---|---|---|---|---|---|
| | Variations during* | | | | | | | | | |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | 11 |
| | (Rs.crore) | | | | | (Per cent) | | | | |
| I Gross bank credit | 16943 | 15348 | 7987 | 790 | 7949 | 19.8 | 14.9 | 6.8 | 0.7 | 6.3 |
| 1.Public food procurement | 1237 | 2500 | 164 | 357 | -189 | 160.9 | 124.6 | 3.7 | 7.9 | -4.0 |
| 2. Gross non-food credit (a+b+c+d) | 15706 | 12848 | 7823 | 433 | 8138 | 18.5 | 12.8 | 6.9 | 0.4 | 6.7 |
| a) Priority sector (i+ii+iii) | 6164 | 2532 | 2554 | 617 | 1189 | 18.0 | 6.3 | 6.0 | 1.4 | 2.6 |
| i) Agriculture | 2576 | 224 | 1437 | 602 | 660 | 18.5 | 1.4 | 8.6 | 3.6 | 3.6 |
| ii) Small-scale industry | 2408 | 1638 | 977 | 47 | 348 | 18.3 | 10.5 | 5.7 | 0.3 | 1.9 |
| iii) Other priority sectors | 1180 | 670 | 140 | -32 | 181 | 16.5 | 8.1 | 1.6 | -0.4 | 2.0 |
| b) Medium & large industry | 6077 | 6246 | 2822 | 366 | 4998 | 18.9 | 16.3 | 6.3 | 0.8 | 10.6 |
| c) Wholesale trade (excluding food procurement (i+ii+iii+iv) | 705 | 438 | 284 | 199 | 740 | 14.8 | 8.0 | 4.8 | 3.5 | 11.9 |
| i) Cotton Corporation of India | 103 | -49 | 117 | -90 | -144 | 278.4 | -35.0 | 128.6 | -98.9 | -69.2 |
| ii) Food Corporation of India (Fertilizers) | 28 | -18 | -191 | -14 | 3 | 13.9 | -7.8 | -90.1 | -6.6 | 14.3 |
| iii) Jute Corporation of India | -44 | 8 | 8 | -24 | -2 | -44.9 | 14.8 | 12.9 | -38.7 | -2.9 |
| iv) Other trade | 618 | 497 | 350 | 327 | 883 | 14.0 | 9.8 | 6.3 | 5.9 | 15.0 |
| d) Other sectors | 2760 | 3632 | 2163 | -749 | 1211 | 20.0 | 21.9 | 10.7 | -3.7 | 5.4 |
| II. Export credit+ | 2104 | 941 | 1075 | 778 | 954 | 34.3 | 11.4 | 11.7 | 8.5 | 9.3 |
| Priority sector advances as proportion of net bank credit @ | | | | | | 42.40 | 39.20 | 38.50 | 39.70 | 36.60 |

* All figures after 1990-91 are provisional.

@ In the last month of each period; advances include inter-bank participations.

\+ Also included in non-food credit above.

Note: Data relate to 50 scheduled commercial banks which account for about 95 per cent of the credit of all scheduled commercial banks. Net bank credit data are exclusive of bills rediscounted with RBI, IDBI, Exim Bank and other approved financial institutions.

TABLE 3-8

## Working Results of Scheduled Commercial Banks for 1990-91 and 1991-92

| | SBI group | | Other public sector banks | | Private sector banks | | Foreign banks | | All Banks | |
|---|---|---|---|---|---|---|---|---|---|---|
| | 1990-91 | 1991-92 | 1990-91 | 1991-92 | 1990-91 | 1991-92 | 1990-91 | 1991-92 | 1990-91 | 1991-92 |
| | | | | A Rupees crore | | | | | | |
| A.Income | 10019 | 13428 | 17134 | 21018 | 1151 | 1528 | 2278 | 3674 | 37361 | 39659 |
| i)Interest | 9061 | 11775 | 15695 | 18975 | 1056 | 1380 | 1880 | 2829 | 34250 | 34970 |
| ii) Other income | 958 | 1653 | 1439 | 2043 | 94 | 147 | 398 | 845 | 3111 | 4689 |
| B.Expenditure | 9869 | 13184 | 16808 | 20458 | 1114 | 1446 | 2046 | 3354 | 36605 | 38452 |
| i)Interest | 5673 | 7392 | 11436 | 13630 | 632 | 810 | 1307 | 1845 | 22944 | 23684 |
| ii)Other operating expenses | 2556 | 2864 | 4327 | 5020 | 358 | 424 | 395 | 570 | 10509 | 8881 |
| iii)Provisions and contingencies | 1640 | 2928 | 1045 | 1809 | 124 | 212 | 344 | 939 | 3152 | 5888 |
| C.Profit | 150 | 246 | 315 | 499 | 38 | 81 | 348 | 495 | 1058 | 1320 |
| D. Working Funds | 93012 | 115081 | 166296 | 186636 | 10552 | 14069 | 15985 | 25103 | 361565 | 340984 |
| | | | | B Per cent of working funds | | | | | | |
| A.Income | 10.77 | 11.67 | 10.30 | 11.26 | 10.91 | 10.86 | 14.25 | 14.64 | 10.33 | 11.63 |
| i)interest income | 9.74 | 10.23 | 9.44 | 10.17 | 10.01 | 9.81 | 11.76 | 11.27 | 9.47 | 10.26 |
| ii) other income | 1.03 | 1.44 | 0.87 | 1.09 | 0.89 | 1.04 | 2.49 | 3.37 | 0.86 | 1.38 |
| B.Expenditure | 10.61 | 11.46 | 10.11 | 10.96 | 10.56 | 10.28 | 12.80 | 13.36 | 10.12 | 11.28 |
| i)interest expenses | 6.10 | 6.42 | 6.88 | 7.30 | 5.99 | 5.76 | 8.18 | 7.35 | 6.35 | 6.95 |
| ii)other operating expenses | 2.75 | 2.49 | 2.60 | 2.69 | 3.39 | 3.01 | 2.47 | 2.27 | 2.91 | 2.60 |
| iii)provisions and contingencies | 1.76 | 2.54 | 0.63 | 0.97 | 1.18 | 1.51 | 2.15 | 3.74 | 0.87 | 1.73 |
| C.Profit | 0.16 | 0.21 | 0.19 | 0.27 | 0.36 | 0.58 | 2.18 | 1.97 | 0.29 | 0.39 |

TABLE 3.9

**Published Profits of Public Sector Banks**

| | | (Rs. crore) Year ended March 31 1991 | 1992 |
|---|---|---|---|
| A | STATE BANK OF INDIA GROUP | | |
| 1 | State Bank of India | 107.01 | 175.05 |
| 2 | State Bank of Bikaner & Jaipur | 5.50 | 9.50 |
| 3 | State Bank of Hyderabad | 8.51 | 12.75 |
| 4 | State Bank of Indore | 2.94 | 3.23 |
| 5 | State Bank of Mysore | 2.87 | 3.85 |
| 6 | State Bank of Patiala | 14.59 | 29.78 |
| 7 | State Bank of Saurashtra | 4.50 | 6.00 |
| 8 | State Bank of Travancore | 4.00 | 5.09 |
| B | NATIONALISED BANKS | | |
| 1 | Allahabad Bank | 19.84 | 28.11 |
| 2 | Bank of Baroda | 56.66 | 95.10 |
| 3 | Bank of India | 19.49 | 56.63 |
| 4 | Bank of Maharashtra | 3.10 | 4.04 |
| 5 | Canara Bank | 136.04 | 156.59 |
| 6 | Central Bank of India | 9.48 | 30.49 |
| 7 | Dena Bank | 7.26 | 9.10 |
| 8 | Indian Bank | 31.84 | 36.50 |
| 9 | Indian Overseas Bank | 6.74 | 9.05 |
| 10 | Punjab National Bank | 73.69 | 112.44 |
| 11 | Syndicate Bank | 2.84 | 4.46 |
| 12 | United Bank of India | 5.78 | 6.68 |
| 13 | Union Bank of India | 10.05 | 29.45 |
| 14 | UCOBank | -42.96 | -20.99 |
| 15 | Andhra Bank | 8.21 | 8.42 |
| 16 | Corporation Bank | 4.65 | 5.20 |
| 17 | New Bank of India | -45.00 | -41.52 |
| 18 | Oriental Bank of Commerce | 22.83 | 26.78 |
| 19 | Punjab & Sind Bank | -5.45 | 0.68 |
| 20 | Vijaya Bank | 0.25 | 1.84 |

crore, besides raising significant amounts from certificates of deposits. Similarly, Industrial Credit and Investment Corporation of India (ICICI) broadened its equity base with a public issue. Small Industries Development Bank of India (SIDBI) has also accessed the market directly for resources.

3.30 A major problem facing the financial institutions is the mobilisation of resources especially since access to low-cost funds from the Reserve Bank of India is expected to shrink. It is expected that the financial institutions will increasingly rely upon mobilisation of resources from the capital markets through issue of both debt and equity. The Government has decided to convert Industrial Finance Corporation of India (IFCI) into a company; an ordinance to this effect was promulgated on 1 October 1992. This will allow IFCI access to the capital market. SEBI has issued guidelines to regulate and facilitate the raising of resources by financial institutions from the market. The salient features of the guidelines are outlined in Box 3.2.

### Money Market Trends

3.31 Discount and Finance House of India (DFHI) continued its efforts towards developing an active secondary market for money market instruments and integrating various segments of market. For the first time during the current financial year DFHI was entrusted with an additional role of activating a secondary market for dated government securities.

TABLE 3.10

**Financial Assistance Sanctioned and Disbursed by All-India Financial Institutions**

(Rs.crore)

| | April-December (P) | | | |
|---|---|---|---|---|
| | Sanctioned | | Disbursed | |
| | 1991 | 1992 | 1991 | 1992 |
| 1 | 2 | 3 | 4 | 5 |
| IDBI | 4592.6 | 6482.0 | 3369.8 | 4392.3 |
| IFCI | 1255.3 | 1486.2 | 821.8 | 1059.6 |
| ICICI | 2231.5 | 4576.5 | 1505.4 | 2403.1 |
| SIDBI | 1888.9 | 1749.0 | 1430.9 | 1324.4 |
| IRBI | 151.3 | 167.4 | 112.7 | 110.3 |
| RCTC | 7.8 | 5.5 | 5.5 | 5.5 |
| TDICI | 14.1 | 21.9 | 12.8 | 15.5 |
| SCICI | 297.0 | 448.8 | 104.0 | 346.1 |
| TFCI | 67.1 | 62.2 | 28.3 | 27.3 |
| LIC | 802.6 | 1006.6 | 532.3 | 453.5 |
| UTI | 1797.3 | 6327.6 | 1660.4 | 4055.6 |
| GIC | 338.2 | 385.4 | 175.1 | 295.7 |
| TOTAL | 13039.9 | 22152.1 | 9355.2 | 13776.8 |

P Provisional

Note: Totals are adjusted for inter-institutional flows, namely IDBI's resource support to IFCI and UTI's special deposits with IDBI, IFCI and ICICI.

3.32 Total turnover of DFHI in the call money market in 1991-92 expanded by 47 per cent over 1990-91 level to reach a figure of Rs.297000 crore (a daily average of Rs.546 crore). In the current financial year up to December 11, 1992 its total lending in the call money market stood at Rs.328000 crore as against Rs.235000 crore in the

BOX 3.2

**SEBI Guidelines for Financial Institutions' Capital Issues**

* No promoters' contribution.
* Underwriting not mandatory.
* Free pricing of issues permitted subject to track record of consistent profitability for minimum three years.
* Maximum debt-equity ratio 2:1; minimum debt service coverage ratio 1:2.
* Disclosure requirements to include accounting policies, bad and doubtful debt provisions and a standard classification for assets.
* Credit rating compulsory for debentures and bonds of more than 18 months' maturity.

period of 1991. There has, however, been a significant decline in the turnover of DFHI in commercial bills, commercial papers (CP) and certificates of deposit (CD). Up to 27 November 1992 there was a small turnover of Rs.28 crore in CPs and a very negligible turnover in CDs.

3.33 The volume of CDs issued by the scheduled commercial banks rose from Rs.5682 crore on 20 March 1992 to Rs.8469 crore on 2 October 1992. Banks pay a high interest rate on CDs. Hence holders of CDs prefer to hold them till maturity and an active secondary market has not developed.

3.34 From 2 May 1992, the limit for issue of CDs was raised from 5 per cent to 7 per cent of the banks' fortnightly average aggregate deposits in 1989-90. Thus these limits were enhanced by Rs. 2994 crore. The enhanced limit will not be subject to CRR. It was further raised to 10 per cent from 17 October 1992.

3.35 The primary market in CPs has made significent progress; the outstanding amount raised from Rs.64.70 crore on 30 June 1991 to Rs.681.75 crore on 30 November 1992. The working capital (fund-based) limit for a company for issue of CP was reduced to Rs.5 crore from Rs.10 crore and the rating requirement relaxed from P1 to P2 in the case of Credit Rating Information Services of India (CRISIL) ratings and from A1 to A2 in the case of Investment Information and Credit Rating Agency of India Limited (ICRA) ratings. Due to easy conditions in the market, holders of CPs could fund their holdings without any need to access the secondary market. Easy conditions in the call money market and lower call money rates also explain the lower turnover of Rs.565 crore in commercial bills this year as against Rs.6151 crore during the corresponding period of last year.

3.36 Excess short-term liquidity in the financial system generated by foreign inward remittances and counterpart funds of Indian Development Bonds and sluggish demand for non-food credit explain the easy conditions in the money market in the first quarter of 1992. The rates flared up in April 1992 as the banks tried to cover their enhanced CRR requirements on the increased deposits at the end of March 1992 (Figure 3.1). Another exceptional factor was uncertainty in the market created by the irregularities in the management of funds by commercial banks and financial institutions described in the next section. For most part of 1992, call money rates were lower than those in 1991.

3.37 The 182-day treasury bill was the first security sold by auction for financing the fiscal deficit of the Central Government. The DFHI developed a secondary market in these bills. They were popular with the banks.

3.38 In the credit policy for the first half of 1992-93 it was decided to introduce 364-day Treasury Bills. Auctions were held for these bills in 1992-93. Like 182-day treasury bills, whose actions have been discontinued, these bills can also be held for meeting the SLR. Between 26 April and 1 January 1993, the outstanding amount of 364-day treasury bills rose to Rs.8419 crore. The cut-off yield rate ranged between 11.17 per cent and 11.42 per cent. As these bills cannot be rediscounted with RBI, they have helped the Central Government limit its recourse to borrowing from RBI.

### Money Market Mutual Funds (MMMF)

3.39 Following the report of the Task Force on Money Market Mutual Funds, RBI announced full details of the scheme. The scheduled commercial banks and public financial institutions or their existing mutual fund subsidiaries can now set up Money Market Mutual Funds(MMMF). In the case of MMMFs set up by scheduled commercial banks or their subsidiaries, the limit for raising resources under various schemes should not exceed two per cent of the sponsoring bank's fortnightly average aggregate deposits during 1991-92. For those set up by public financial institutions, the limit should not exceed two per cent of their long-term domestic borrowings.

**Irregularities and Fraudulent Transactions in Securities Trading**

3.40 In April 1992 investigations conducted by RBI into certain aspects of securities trading by some banks led to the exposure of serious irregularities and frauds in the securities transactions of several banks. Unscrupulous brokers, colluding with some bank officials, were found to be violating established rules and guidelines in a manner designed to siphon off bank funds to brokers for speculative transactions in shares. These irregularities and frauds, popularly termed the "securities scam", revealed serious weaknesses of internal control and supervision in banks which need to be urgently corrected.

3.41 A high-level enquiry committee known as the Janakiraman Committee was set up by RBI. It has submitted three reports in May, July and August 1992. It identified several types of irregularities in securities transactions which were used to siphon funds out of the banking system:

(i) Purchases were made by banks and their subsidiaries of securities and other instruments where the counter-party was ostensibly another bank but when in reality the proceeds were directly or indirectly credited to brokers' accounts;
(ii) Ready-forward (sale and repurchase) transactions were entered into either on their own or on clients' accounts by banks with brokers who used these funds for speculative activity;
(iii) Brokers were directly financed by banks by discounting bills not supported by genuine transactions;
(iv) Banks and other institutions showed large payments as call money with other banks. However, in the books of the receiving banks there was no record of call money acceptances but instead the amounts were credited to the accounts of individual brokers. On the due date, these alleged call loans were repaid by payment out of the brokers' accounts in the name of other banks;
(v) Banks and institutions rediscounted bills of exchange held by other banks and institutions but the proceeds and repayments were routed through brokers' accounts; and
(vi) Sums received as inter-corporate deposits and under portfolio management schemes (PMS) and similar schemes by merchant banking subsidiaries of public sector and other banks were passed on to brokers through ready-forward deals.

3.42 The extent of unreconciled amounts as estimated by the detailed investigation made by the Janakiraman Committee has been estimated at Rs.3543 crore. These irregularities have been detected in some banks in each of the three segments of the banking industry, viz. public sector banks, private sector banks and foreign banks.

3.43 The government took early action to identify and punish those responsible for the fraudulent transactions and to recover the money lost by the banks. A special court was appointed to try all matters relating to the scam and legislation has been passed providing powers to attach the assets of notified persons involved in the scam. A special judge of the Bombay High Court has been appointed for trial of scam-related cases. The government has appointed a custodian for prompt disposal of the attached assets. The Central Bureau of Investigation (CBI) has been asked to take over investigation of all the frauds and underhand dealings exposed by RBI's investigations. Finally, in recognition of the seriousness of the fraudulent transactions exposed and of the need for thorough examination of all aspects of the matter, a Joint Parliamentary Committee (JPC) was set up to enquire into all aspects of the scam, to fix responsibility and to make suggestions about future reform of the system. The JPC has examined a number of persons including bank and government officials and brokers. Its enquiry is in progress.

3.44 The scam has brought into focus serious weaknesses in the country's financial system which need to be corrected. At one level the scam reflects deliberate and criminal violation of rules and procedures with intent of defrauding the banks. This was done through criminal collusion between brokers and some bank officials. However, there are also systemic weaknesses which made it possible. These are:

(i) Weaknesses in the internal control mechanism within the commercial banks themselves. More effective internal control mechanism could have ensured that such manipulations even if they did occur would have been detected much earlier;
(ii) There have also been weaknesses in the supervisory mechanism which need to be removed. The proposed new Board of Financial Supervision to be set up under the aegis of RBI will rectify this;
(iii) The prevalence of a very high level of pre-emption of bank resources at low rates of interest has also put pressure on banks to find various mechanisms for earning higher rates of return to supplement their income from non-fund-based activities;
(iv) It is also important to recognise that these irregularities to some extent reflect the difficulty in running an overregulated financial system in which administered interest rates in one part of the system co-exist with market-determined rates of return in the capital market. Rigid control over interest rates which takes them too far away from market-determined rates of interest is not workable and only leads to attempts to by-pass regulations in search of available high rates of interest.

3.45 The Government has been successful in minimising the adverse effects of the scam on the economy and on the working of the financial sector. Steps are being taken to improve internal control mechanisms in the banks and to strengthen the supervisory system so that such problems will not recur in future. Structural reforms envisaged in the banking sector (outlined in the next section) will also overcome some of the systemic pressures on the system which led to the evolution of practices which were deliberately misused by unscrupulous persons. The confidence in the country's banking system remains strong. The expansion in commercial credit, increase in the volume of stocks traded in the market and continued interest on the part of foreign investors bear testimony to this. It is, however, also true that such irregularities badly affect the small investor and create uncertainties in the investment environment. Therefore, it is necessary to prevent the recurrence of such irregularities in future.

## Financial Sector Reforms

3.46 The current year witnessed the initiation of major financial sector reforms based on the report of the Narasimham Committee which was submitted in November 1991. The report was placed before Parliament in December 1991 and its recommendations have been extensively discussed in the Consultative Committee of Parliament for the Finance Ministry. (Box 3.3)

### Reductions in SLR and CRR

3.47 One of the problems facing our banking system is that levels of SLR and CRR have been progressively increased over the past several years. In the case of the SLR this happened because of the desire to mobilise even larger resources through so-called market borrowings (at below-market rates) in support of the Central and State budgets. In the case of the CRR this happened because of the need to counter the expansionary impact on money supply of large budget deficits. Together, the SLR and CRR stipulation pre-empted a large part of bank resources into low-income-earning assets thus reducing bank profitability and pressurising banks to charge high interest rates on their commercial sector advances. These high interest rates paid by the corporate sector in turn encourage disintermediation from the banks since better corporate clients have an incentive to raise funds directly from the market by paying higher interest rates than the banks can offer to pay. The high SLR and CRR are in effect a tax on financial savings in the banking system

BOX 3.3

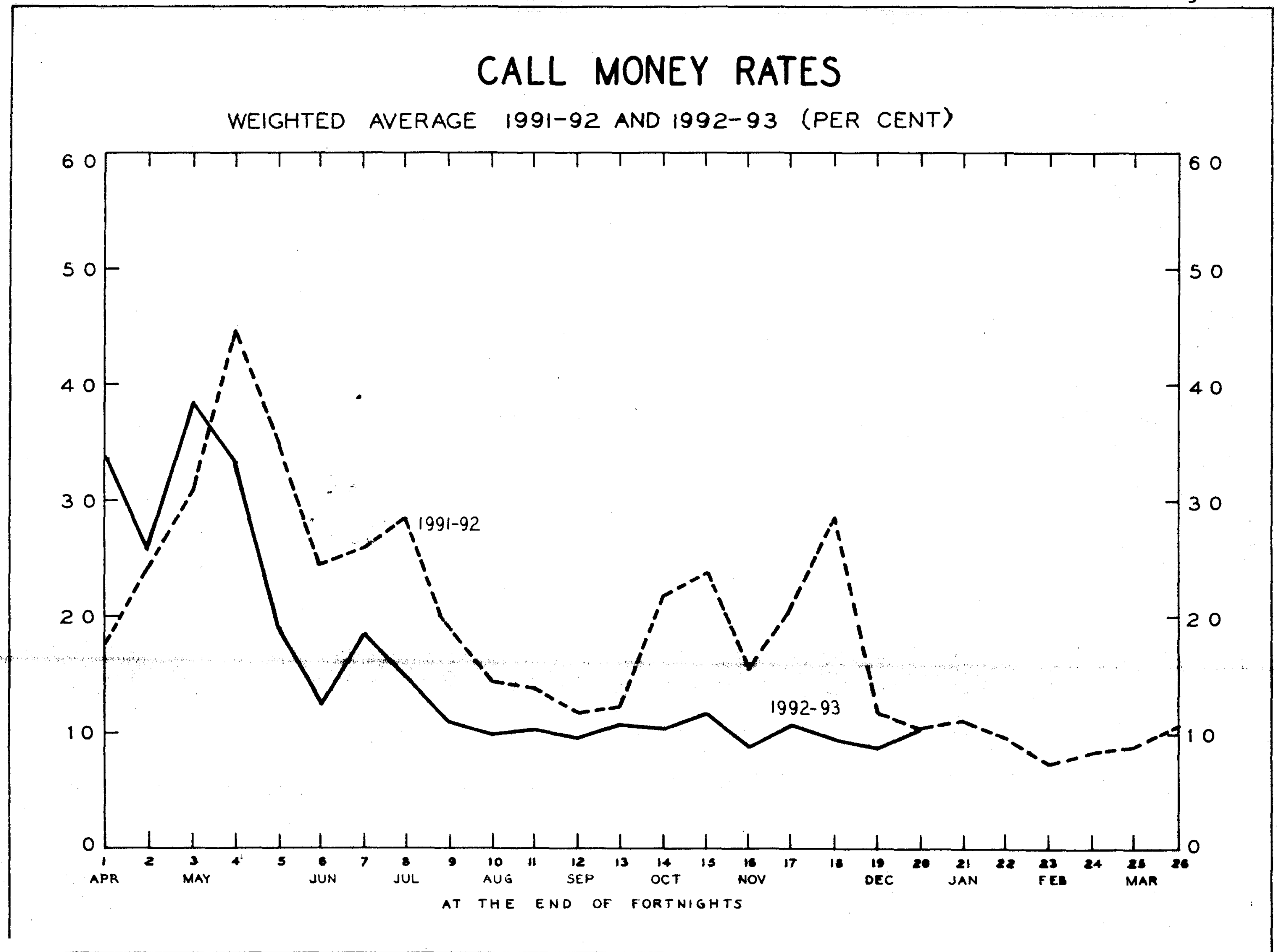
**Banking Sector Reforms**

- Statutory Liquidity Ratio (SLR) on increment in net demand and time liabilities (DTL) over 3 April 1992 level reduced to 30 per cent from 38.5 per cent.
- Phased reduction in SLR on net DTL as on 3 April 1992 to 37.75 per cent by 6 March 1993.
- Incremental Cash Reserve Ratio (ICRR) of 10 per cent on increase in net DTL over 3 May 1991 level removed from 17 April 1992.
- Number of lending and deposit interest rates reduced.
- New prudential norms relating to income recognition, classification of assets and provisioning for bad debts introduced.
- Time schedule for capital adequacy norms announced - a) 8 per cent to be attained by foreign banks operating in India by 31 March 1993, b) 8 per cent to be attained by Indian banks with branches abroad, by 31 March 1994 and c) 4 per cent to be attained by other banks by 31 March 1993 and 8 per cent by 31 March 1996.
- Revised format for balance sheet and profit and loss account reflecting actual financial health of the scheduled commercial banks introduced from the bank accounting year 1991-92 and the accounts for 1990-91 to be reformatted.
- Banks attaining capital adequacy norms and prudential accounting standards given freedom to open new branches and upgrade branches or extension counters; other banks given freedom to rationalise existing branch network.
- Guidelines finalised for objective selection procedures for non-official directors of the banks.
- New Board of Financial Supervision to be set up in Reserve Bank of India.
- New RBI guidelines to govern entry of new private sector banks.

and serve to encourage flows in market where this tax does not apply. It is therefore essential in the interest of a healthy financial system to phase out this distortion. The Government has therefore decided to reduce the SLR in stages over a three-year period from 38.5 per cent to 25 per cent and to reduce the CRR over a four-year period to a level below 10 per cent.

3.48 As a first step in the pursuit of this objective, downward adjustments were made in the SLR in April 1992 to October 1992 (Box 3.3). These changes would have the effect of releasing Rs.1650 crore of lendable resources to the commercial banks. The incremental CRR of 10 per cent was rescinded with effect from 17 April 1992. In the last quarter of 1992, it was decided to release one-third of the cash balances earlier impounded under the

Figure 3-1


CALL MONEY RATES
WEIGHTED AVERAGE 1991-92 AND 1992-93 (PER CENT)
60
50
40
30
20
10
0
1991-92
1992-93
1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25 26
APR MAY JUN JUL AUG SEP OCT NOV DEC JAN FEB MAR
AT THE END OF FORTNIGHTS

incremental CRR. The increment to lendable resources on account of these balances is Rs.1280 crore.

### Norms for Income Recognition, Provisioning and Capital Adequacy

3.49 In pursuance of the recommendations of the Narasimham Committee, the Reserve Bank of India issued new prudential norms relating to income recognition, classification of assets and provisioning for bad debts. The new income recognition norms ensure that interest not actually paid cannot be shown as accrued, a practice which exaggerates profitability of the banks. Norms have also been specified for categorising non-performing accounts and for making provisions for substandard, doubtful and loss-making assets. Minimum capital standards have been prescribed in accordance with the internationally accepted Basle Committee norms under which banks have to maintain unimpaired minimum capital funds equivalent to eight per cent of the aggregate of the risk-weighted assets and other off-balance sheet exposures. For Indian banks which have branches abroad, the norm of eight per cent should be achieved as early as possible and in any case by 31 March 1994. Other banks should achieve a capital adequacy norm of four per cent by 31 March 1993 and eight per cent by 31 March 1996.

3.50 In light of concerns expressed about the difficulty in implementing provisioning norms, some relaxations have been announced allowing phasing in the provisioning for bad debts. However, there would be strict adherance to the norm for categorisation of non-performing accounts. An account is deemed non-performing if interest cannot be collected within one month after it is due. The concerned borrower in such non-performing accounts will be subject to corrective steps for all the facilities availed from the banks, including other accounts in which the borrower may have been regular in making all payments due.

### Revision of Balance Sheet and Profit and Loss Accounts Formats for Banks

3.51 The balance sheet and profit and loss account formats were revised to reflect the true financial health of the banks. These formats have been made effective from the bank accounting year 1991-92. Banks were directed to reformat their 1990-91 accounts also for publication with 1991-92 accounts in new format.

### Branch Licensing

3.52 As of April 1992 banks attaining capital adequacy norms and prudential accounting standards can set up new branches without the prior approval of RBI. Banks have the freedom now to rationalise their existing branch network by relocating branches, opening of specialised branches, spinning off business, setting up of controlling offices/ administrative units etc.

### Permission to Set Up New Private Sector Banks

3.53 Reserve Bank of India has announced guidelines for setting up of private banks as public limited companies. The guidelines have stipulated that the banks in the private sector should be financially viable. They should avoid shortcomings such as unfair preemption and concentration of credit, cross-holdings with industrial groups, etc. They will be required to observe priority sector lending targets as applicable to other domestic banks.

### Other Reform Measures

3.54 Special Recovery Tribunals will be set up to expedite the loan recovery process and necessary legislation to establish such tribunals is being drafted. Guidelines providing for objective selection procedures for non-official directors on the board of the banks were finalised.

### Developments in Capital Market

3.55 Along with banking system reforms, it was necessary to undertake a bold programme of reform of the capital market. Recommendations to this effect had been made by the Narasimham Committee as well as by other committees and groups. The Government has taken a series of initiatives in this area in the course of 1991-92 and 1992-93.

#### Capital Market Reforms

3.56 The need for reforms in the capital market has been evident for some time. As in the case of banks there has been an impressive expansion in quantity but without adequate improvement in quality. The functioning of the stock exchanges shows many shortcomings with long delays, lack of transparency in procedures and vulnerability to price rigging and insider trading. To counter these deficiencies it had been announced in the Budget Speech of 1987-88 that the Government would establish a Securities and Exchange Board of India (SEBI) to regulate the capital markets. The SEBI was set up as a non-statutory board in 1988 with the intention of giving it statutory powers but this was not done at that time. The Government gave high priority to achieving this objective; an ordinance establishing SEBI as a Statutory body was promulgated on 30 January1992. With this, SEBI acquired necessary powers to perform its functions.

3.57 The Capital Issues (Control) Act, 1947 was repealed in May 1992 , and the office of the Controller of Capital Issues (CCI), was subsequently abolished. With the abolition of CCI, prior government permission was no longer needed by companies to access the capital markets. Companies were free to approach the capital markets without prior government permission subject to getting offer documents cleared by SEBI. Control over price and premium fixation has also been removed and most issuing companies are free to fix the price of their securities for public as well as rights issues.

3.58 Indian companies have been permitted to access international capital markets through Euro-equity issues aimed at mobilising capital for modernisation and import requirements. Several companies have been given such permission. Up to the end of January 1993, two companies have raised around $ 250 million from the Euro-market.

3.59 A number of steps have been taken in the course of 1991-92 and 1992-93 by the Government and SEBI to introduce improved practices and greater transparency in the capital markets in the interest of healthy capital market development.

(i) SEBI was authorised to conduct inspections of various mutual funds. These inspections have been conducted and SEBI has submitted a report on each inspection which brings out various deficiencies of individual mutual funds. Corrective steps are being taken to set right these deficiencies.

(ii) SEBI has also drawn up a programme of inspecting stock exchanges. Eight stock exchanges have been inspected. Reports of SEBI in each case, and the recommendations therein, are under the consideration of the stock exchanges.

(iii) The process of registration of intermediaries such as stockbrokers and sub-brokers has been provided under the provisions of the Securities and Exchange Board of India Act,1992. The registration is on the basis of certain eligibility norms such as capital adequacy, infrastructure etc.

(iv) Companies issuing capital in the primary market are now required to disclose all material facts and specific risk factors associated with their projects. Proposals are under consideration to improve the disclosure of information regarding the basis of calculation of premium while leaving companies free to fix the premium.

(v) Merchant banking has been statutorily brought under the regulatory framework of SEBI. The merchant bankers are now to be authorised by SEBI. They will have to adhere to stipulated capital adequacy norms. Merchant bankers have to abide by a code of conduct which specifies a high degree of responsibility towards investors in respect of the pricing and premium fixation of issues, and disclosures in the prospectus or offer letter for issues.

(vi) The Government has given formal approval for the setting up of the National Stock Exchange of India (NSEI) by financial institutions and banks with IDBI as the nodal agency. The NSEI is expected to serve as a model exchange integrating the stock markets all over the country by providing nation-wide stock trading facilities and electronic clearing and settlements.

(vii) In order to induce companies to exercise greater care and diligence for timely action in matters relating to the public issue of capital, SEBI has advised the stock exchanges to collect from companies making public issues, a deposit of one per cent of the issue amount which could be forfeited in case of non-compliance with the provisions of the listing agreement and, non-despatch of refund orders and share certificates by registered post within the prescribed time.

(viii) Regulations on insider trading under the provisions of the SEBI Act have been notified. Such regulations will help in protecting and preserving the market's integrity, and in the long run help inspire investor confidence in the market.

(ix) RBI has liberalised the investment norms evolved for NRIs by allowing companies to accept capital contributions and issue shares or debentures to NRIs or overseas corporate bodies without prior permission.

(x) The Government has allowed foreign institutional investors(FIIs) such as pension funds, mutual funds, investment trusts, asset or portfolio management companies etc.to invest in the Indian capital market provided they register with SEBI.

(xi) To make the governing body of a stock exchange more broad based SEBI has issued guidelines for its composition. According to these guidelines the governing body of the stock exchanges should have five elected members, not more than four members nominated by the Government or SEBI and three or fewer members nominated as public representatives, besides its executive director.

(xii) The trading in stock exchanges is now for three hours instead of two-and-a-half hours.

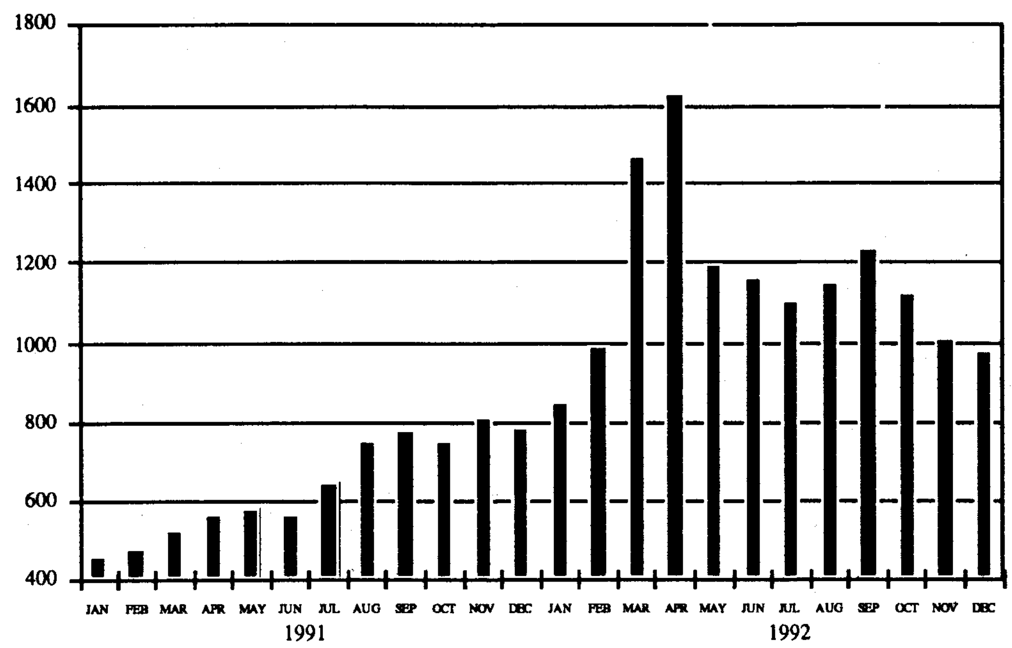
(xiii) SEBI has set up an advisory committee for primary and secondary capital markets to provide wider consultation with the investors etc.

3.60 The process of reforms in the capital market has only just begun. It needs to be deepened to bring about speedier conclusion of transactions, greater transparency in operations, improved services to investors, and greater investor protection while at the same time encouraging the corporate sector to raise resources directly from the market on an increasing scale. Major modernisation of the stock exchanges to bring them in line with world standards in terms of transparency and reliability is also necessary if foreign capital is to be attracted on any significant scale.

**Behaviour of Stock Prices**

3.61 The behaviour of stock prices in 1992-93 was dominated by the crash which followed the exposure of the scam in April, 1992. As reported in last year's Economic Survey, stock prices were relatively stable in the third quarter of 1991-92. However, they began to rise again in January. This rise accelerated in the second half of February and especially in March. Reserve Bank of India's all-India Index Number of Ordinary Share Prices which stood at 851.4 (Base: 1980-81) in the last week of January increased to 1099.6 in the last week of February and rose sharply to 1485.4 by the last week of March. Thereafter it increased to a new peak of 1659.6 in the first week of April 1992. Between the last week of January 1992 and the peak level in April 1992 the Index had increased by 94.9 per cent, with most of the increase occuring in March (Figure 3.2).

**Figure 3.2. Ordinary share price index**
**(RBI index, 1980-81=100)**




3.62 While the increase in stock prices in January and February in anticipation of the Budget was not necessarily abnormal the increase in March and April, 1992 was very sharp. The rise in stock prices was discussed by the Government with both Reserve Bank of India and SEBI in the last quarter of 1991-92. However, there was no indication at the time of the source of funds fuelling speculation. The first indication that the source of funds may have been the siphoning of funds from the banking system came only in April 1992 with the exposure of irregularities in the State Bank of India consequent to the investigation undertaken by the Reserve Bank of India.

3.63 In the absence of any specific information on the source of speculative pressure, it was not possible to identify specific corrective measures. Credit against shares had already been tightened in the October 1991 credit policy. The Bombay Stock Exchange had taken a series of steps in February and March 1992 to curb speculative pressure, including cessation of the carry-forward facility on specified shares. These measures, which are the usual instruments for curbing speculation, were obviously not effective.

BOX 3.4

**Measures to Strengthen Government Securities Market**

- Ceiling interest rate on dated securities raised from 11.5 per cent (20-year) to 13 per cent (15-year).
- Auctions held for 5-year, 6-year, 7-year and 10-year securities.
- 364-day treasury bills sold by auction.
- 91-day treasury bills partly auctioned.
- Introduction of Repurchase Obligations auctions in securities by RBI.
- Government securities refinance facility introduced at 14 per cent interest rate.

**New Issues in the Capital Market**

3.64 Despite the difficulties experienced by the stock markets following the crash in stock prices in April 1992, the year 1992-93 is characterised by large volumes of funds raised from the capital markets. Available data for 1992-93 are summarised in Table 3.11. During April-October 1992 the total volume of new issue activity measured by approvals issued by CCI up to May and clearances of prospectuses by SEBI increased by 67 per cent in the case of non-Government companies. In the case of Government companies, there was a sharp decline in the volume of issues of bonds in 1992-93, compared to the previous year. The total capital issues planned by Government and non-Government companies in April-October 1992 were Rs.9111 crore, 25 per cent higher than in the previous year.

3.65 Data for actual issues are available only for non-Government companies and may be seen in Table 3.11. They show that the actual issues increased from Rs.1583 crore in 1991 to Rs.9846 crore in 1992, a six-fold increase in one year.

**Government Securities Market**

3.66 With the introduction of auctions in Central Government securities in the current financial year, interest rates are now being determined by market forces. The maximum rate on these securities has risen from 11.5 per cent for 20-year securities to 13 per cent for 15-year securities in April 1992. In 1992-93 so far, three auctions of Rs.1000 crore each have been held for Central Government securities with maturities of five, six and ten years.

3.67 With a view to providing liquidity to scheduled commercial banks for their excess holdings of Government and other approved dated securities, a new refinance facility called Government Securities Refinance Facility has been introduced since October, 1992. All scheduled commercial banks (excluding RRBs) are eligible for this refinance facility at a rate of interest of 14 per cent per annum.

3.68 RBI has decided to conduct, from time to time, repos (repurchase obligations) auctions for Central Government dated securities from its portfolio in order to improve short-term management of excess liquidity. These repos auctions are in the form of sales

TABLE 3.11

**Issues and Approvals for New Issues by Public Limited Companies**

| | 1990-91 | | 1991-92 | | 1991 | | 1992 | |
|---|---|---|---|---|---|---|---|---|
| 1 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 |
| | No. | Rs. cr. | No. | Rs. cr. | No. | Rs. cr. | No. | Rs. cr. |
| Approvals of which | 1105 | 12633 | 1263 | 19402 | 539 | 7306 | 567 | 9111 |
| A. Non-Government companies | 1074 | 6425 | 1243 | 12341 | 533 | 5238 | 564 | 8731 |
| (i) Equities@ | 841 | 2854 | 868 | 4291 | 351 | 1625 | 463 | 4198 |
| (ii) Debentures | 233 | 3571 | 375 | 8050 | 182 | 3613 | 101 | 4533 |
| B. Government companies | 31 | 6208 | 20 | 7061 | 6 | 2068 | 3 | 380 |
| (i) Equities@ | 14 | 201 | 3 | 76 | 1 | 53 | 2 | 330 |
| (ii) Public sector bonds | 17 | 6007 | 17 | 6985 | 5 | 2015 | 1 | 50 |
| Issues by non-Government public limited companies* of which | 365 | 4202 | 519 | 5753 | 227 | 1583 | 479 | 9846 |
| (i) Equities** | 252 | 1261 | 373 | 1733 | 159 | 486 | 383 | 3877 |
| (ii) Debentures | 113 | 2941 | 146 | 4020 | 68 | 1097 | 96 | 5969 |
| | | | Changes over the previous year (per cent) | | | | | |
| Approvals of which | | .. | | .. | | | | 25 |
| A. Non-Government companies | | -19 | | 92 | | | | 67 |
| (i) Equities@ | | 40 | | 50 | | | | 158 |
| (ii) Debentures | | -39 | | 125 | | | | 25 |
| B. Government companies | | 49 | | 14 | | | | -82 |
| (i) Equities@ | | 141 | | -62 | | | | 523 |
| (ii) Public sector bonds | | 47 | | 16 | | | | -98 |
| Issues by non-Government public limited companies* of which | | -35 | | 37 | | | | 522 |
| (i) Equities** | | 3 | | 37 | | | | 698 |
| (ii) Debentures | | -44 | | 37 | | | | 444 |

* Provisional; excluding issues privately placed with financial institutions etc, and including oversubscription retained in some cases.

** Excludes bonus issues, but includes preference shares and cumulative convertible preference shares.

@ Includes premia and bonus shares.

of Government securities by the Reserve Bank for very short periods (within the fortnightly make-up period) with a buy-back clause. Repos auctions have been introduced with effect from December 1992.

3.69 The Government has recently decided to introduce a scheme for the sale of 91-day treasury bills on an auction basis in addition to the current system of sale of these bills at pre-determined discount rate (4.6 per cent) which will continue to be available for investment on tap. Under the new scheme, RBI will hold auction sales of these bills from time to time at dates to be announced. The rate of discount and the corresponding issue price would be determined at each auction by RBI. These bills can be held by a person, firm, company, corporate body or institution (except State governments, provident and gratuity funds) in India.

**Credit Rating Agencies**

3.70 There are now two credit rating agencies in the country, viz. Credit Rating Information Services of India Limited (CRISIL) and Investment Information and Credit Rating Agency of India Limited (ICRA). Their main function is to rate debt instruments of companies. In 1991-92 CRISIL assigned ratings to 155 debt instruments of 103 companies worth Rs.5866.5 crore while ICRA rated 47 debt instruments of 34 companies worth and Rs.1161.8 crore. Guidelines issued by SEBI make credit ratings mandatory for companies issuing debentures to public.

3.71 From its inception till 12 November 1992, CRISIL rated a total of 491 debt instruments issued by 315 companies (including 5 in public sector) involving a total sum of Rs.20980 crore. During the 15 months ended 30 November 1992, ICRA rated 119 debt instruments of 81 companies involving a total sum of Rs.3537.87 crores. It has also completed two credit assessments and two general assessments during this period.

3.72 CRISIL also completed the credit assessment of 70 small companies up to November 1992. Credit assessment, a special product developed initially for the State Bank of India, is now used by other public sector banks as well, as an important input in their decision-making process on terms of lending. Besides, CRISIL has started providing technical assistance and training to foreign rating agencies.

## Outlook

3.73 Monetary expansion in this financial year so far presents a mixed trend. Bank credit to the commercial sector is growing much faster than last year while net bank credit to the Government has been rising at a slower pace. Net foreign exchange assets of the banking sector have declined. Fresh inflow of foreign exchange deposits through FC(BO)D scheme has been stopped since August 1992 and there will be only repayments now. All these factors will exert a moderating influence on the growth of money supply.

3.74 With the growth in export credit, banks' access to refinance facilities of the RBI has increased significantly and has added to the expansion in reserve money. To the extent that Government borrowing from the Reserve Bank has been reduced, there has been some moderation in reserve money growth. To revive industrial and agricultural growth, Reserve Bank has recently released resources to financial institutions which will increase reserve money. While meeting credit requirements to support the revival of activity is essential, care needs to be taken to ensure that excessive liquidity does not result in a resurgence of inflationary pressures. In this context, the Government's reliance on bank credit needs to be restrained. This is essential for attaining the objectives of monetary policy.

3.75 The programme for financial sector reforms needs to be pursued with vigour so that we can move as quickly as possible towards a dynamic, efficent and competitive financial system.