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Monetary and Banking Developments

The current financial year has been characterised by measures designed to create an enabling environment for further progress in the move towards a more flexible interest rate regime. Reduction in the administered interest rates on contractual savings already effected by the Government has contributed to downward flexibility in the interest rate regime. The reduction in the Bank Rate to 6.5 per cent, the lowest since May 1973, has been supplemented by a reduction in the Cash Reserve Ratio (CRR) to 5.5 per cent, which has further strengthened the liquidity position of the banking system.

3.2 The year-on-year growth in broad money (M3) as on November 2, 2001 was 16.9 per cent, compared with the projected rate of 14.5 per cent indicated in the Monetary and Credit Policy (MCP) for the current financial year. However, it dropped to 15.2 per cent after a fortnight, and further down to 14.4 per cent on January 11, 2002, reflecting the rise in M3 on November 17, 2000, on account of the proceeds of Rs. 25,662 crore from the India Millennium Deposits (IMDs). Despite some softening of interest rates, the flow of credit to the commercial sector this year has been much lower than that in the previous year. The most important source of growth in money supply so far in the current financial year has been expansion in bank credit to Government by way of investment in Government securities.

3.3 There has been a significant slowdown in the growth of non-food credit from commercial banks during the current fiscal year. The flow of non-food credit from commercial banks to the commercial sector registered a growth of only 8.7 per cent till January 11, 2002 compared with 12.1 per cent in the corresponding period last year. Banks' investment in the debt and equity instruments of public and private sector units (non-SLR investment), including bills rediscounted with financial institutions, also decelerated to 4.2 per cent during this period from 13.6 per cent in the corresponding period last year. Commercial banks' non-food credit to the commercial sector, including non-Statutory Liquidity Ratio (SLR) investments, was lower at 8.1 per cent till January 11, 2002 than that at 12.3 percent in the corresponding period last year. During April- December 2001, sanctions by All-India Financial Institutions (AIFIs) declined by 32.1 per cent compared with an increase of 18.3 per cent in the corresponding period last year. Disbursements by them also declined by 16.9 per cent during the same period in contrast to an increase of 16.1 per cent last year.

3.4 The process of financial sector reforms has been carried forward in the current financial year with a focus on banking and financial institutions. The salient measures in this regard included the following:-

- Banks given freedom to offer loans over Rs.2 lakh at rates below the Prime Lending Rates (PLRs) to exporters and other creditworthy borrowers (including public enterprises) and to formulate deposit schemes with higher and fixed rates of interest for senior citizens.
- Banks given flexibility in the composition of working capital loans.
- Guidelines for investment by banks in non-SLR securities issued.
- Prudential guidelines issued to ensure greater security for depositors of urban cooperative banks.

- The measures pertaining to financial institutions included operational and regulatory issues concerning transition to universal bank, a transparent mechanism for corporate debt restructuring, coordination between banks and the Financial Institutions (FIs), amended guidelines for Asset-Liability Management and classification and valuation of investments.
- As regards the non-banking financial companies (NBFCs), major policy measure related to reduction in the maximum interest rates on public deposits from 14 per cent to 12.5 per cent, effective from November 1, 2001.