CHAPTER 7

MONETARY AND CREDIT DEVELOPMENTS

In the last financial year money supply (M3) recorded a fairly modest growth, which along with various supply management measures, helped in containing the rate of inflation in the face of a very severe drought. Among the important credit measures adopted by monetary authorities were upward revisions of the Statutory Liquidity Ratio (SLR) and the Cash Reserve Ratio (CRR) and reintroduction/tightening of selective credit control measures on a number of price-sensitive essential commodities. These measures were aimed at preventing excess liquidity growth and speculative use of bank advances. To improve supply conditions in the economy, the banks extended financial assistance including conversion of loans (from short term to medium term) and credit rescheduling facilities to the drought-hit farmers to help them in undertaking a second sowing or raising an alternative crop, and also increased the flow of credit to the non-food commercial sector to support productive activity.

7.2 In the current year so far (i.e. upto January 13, 1989), the growth of money supply (M3) has been slightly higher than in the corresponding period of the last financial year, inspite of a much lower expansion in currency. This is because there has been a significantly higher growth in deposits with commercial banks (particularly demand deposits). Net RBI Credit to Central Government has recorded a much faster growth this year, reflecting substantial fiscal strains on Government finances. The commercial banks have also been able to accommodate a much larger volume of non-food commercial credit because of a decline in food credit this year so far, though this decline has been much smaller in size than in the last year.

7.3 The Reserve Bank of India (RBI) released on April 23, 1988 the entire remaining cash balance of the scheduled commercial banks impounded under incremental CRR during January 14, 1977 to October 31, 1980 to enable them to meet the anticipated seasonal increase in food credit. Since the Rabi 1988 food procurement credit requirements turned out to be substantially lower than expected and the return-flows of food credit were also higher, CRR was raised from 10 per cent to 11 per cent in two stages in July 1988, to contain the banks' liquidity growth. Furthermore, RBI also asked these banks to terminate all buy-back arrangements with non-bank clients in Government and other approved securities on or before July 1, 1988 since these arrangements were not only likely to affect the profitability of the banks but also could put them in a liquidity bind. Selective credit controls were reintroduced in the case of wheat and tightened in the case of other essential commodities like paddy, rice, oilseeds and vegetable oils. However, effective February 10, 1989, such credit controls against oil seeds and vegetable oils were relaxed in view of improved output of these commodities.

7.4 A number of developments in the prevailing interest rate structure are particularly noteworthy. Interest rates on short-term agricultural loans upto Rs. 15,000 sanctioned to farmers by the scheduled commerical banks, were brought down with effect from March 1, 1988, benefitting a large number of farmers, particularly small and marginal farmers. Effective April 4, 1988 the deposit rate for 91 days and above but less than six months was raised by 1.5 percentage points to 8 per cent to provide a better return on short-term surplus funds. While interest rates on all other deposits including Non-Resident (External) Rupee Account and small saving schemes were left unaltered, separate rates of interest came to be provided for Foreign Currency (Non-Resident) Account deposits denominated in US dollar, Pound sterling, DM and Yen. In a major move aimed at imparting greater flexibility to the interest rate structure, the ceiling on interest rates on bank advances, fixed earlier at 16.5 per cent, was replaced effective October 10, 1988 by a floor rate of 16 per cent. This should benefit bank borrowers with a good track record and also give banks some flexibility in their lending rates.

7.5 To facilitate the flow of bulk non-food commercial advances the requirement of prior authorisation by the RBI of such credit limits sanctioned by commercial banks under the Credit Authorization Scheme (CAS), was dispensed with in October, 1988. Henceforth, there will be only post sanction scrutiny by RBI of proposals beyond stipulated levels. The scheme has been renamed as Credit Monitoring Arrangement. In a separate initiative, all borrowers are permitted to transfer their accounts from one bank to another without obtaining a no-objection letter from the former provided the latter bank takes up the entire liabilities of the borrower from the transferer bank.

7.6 Among significant institutional developments, housing finance benefitted from the establishment of the new apex National Housing Bank by RBI and also from the liberalization of housing advances by the commercial banks. An important development in the money market was the setting up of Discount and Finance House of India Limited by Reserve Bank jointly with public sector banks and other financial institutions to impart liquidity to money market instruments; it commenced operations from April 25, 1988. The Securities and Exchange Board of India was established on April 12, 1988 to promote an orderly and healthy growth of securities market and protect investor's interest. The Unit Trust of India, the Industrial Credit and Investment Corporation of India, the Asian Development Bank and some other institutions jointly set up the first credit rating agency of the country viz., Credit Rating and Information Services of India Limited (CRISIL) which will assess the debt obligations of companies and assign credit ratings. Such ratings will improve financial discipline among companies, help individual investors and financial institutions in making correct investment decisions and encourage steady flow of funds to the corporate sector.

7.7 As indicated in last year's Economic Survey, exercises were taken up in the last financial year to set up indicative monetary targets and monitor them periodically in the Ministry of Finance in consultation with the Reserve Bank. These targets were revised in the light of drought conditions. Appropriate and timely policy actions taken both by the Government and the RBI helped in containing the growth of the key monetary variables well within targetted levels during last year. For the current financial year also, similar exercises of monetary targeting were conducted.

Monetary Trends in 1987-88

7.8 Significant deceleration in the rate of growth in both narrow money (M1) and broad money (M3) was witnessed in 1987-88. On 31st March basis, as against an increase of 16.8 per cent in 1986-87, M1 grew at a lower rate of 13.7 per cent in 1987-88. Similarly, M3 also expanded at a substantially lower rate of 15.9 per cent, compared to expansion by 18.6 per cent in 1986-87. The lower growth of M3 in 1987-88 can be attributed mainly to a noticeably smaller increase of bank deposits in that year which can be further attributed to a lower growth in income and certain institutional factors. The growth in demand deposits was smaller not only in absolute terms (Rs. 1774 crores as against Rs. 4078 crores in 1987-88) but also in percentage terms (7.8 per cent as against 21.8 per cent) As pointed out in last year's Economic Survey, this deceleration in the growth rate of demand deposits in 1987-88 may be attributed, in part, to buy-back arrangements in Government and other approved securities by banks with their non-bank clients. Time deposit salso recorded a somewhat smaller percentage growth of 17.2 per cent as against 19.6 per cent increase in 1986-87; the lower growth of time deposits may, in part, be attributed to the loss of agricultural incomes because of the drought. The smaller growth in bank deposits more than compensated for the upward pressure on money supply growth exerted by the much faster expansion in currency at 18.2 per cent in 1987-88 as compared with a growth of 13.3 per cent in 1986-87.

TABLE 7.1

Sources of Change in Money Stock

(Rs. crores)

	Variations during			
	1986-87 March 31 to March 31	1987-88 March 31 to March 31	1987-88 March 31 to January 15, 1988 (P)	1988-89 March 31 to January 13, 1989 (P)
1	2	3	4	5
I. M1 (Money Supply with the public) .	7421 (16.8)	7039 (13.7)	5310 (10.3)	6281 (10.7)
II. M3 (Aggregate monetary resources) .	22041 (18.6)	22422 (15.9)	20384 (14.5)	24415 (15.0)
(*i*) Currency with the public .	3323 (13.3)	5177 (18.2)	3974 (14.0)	3332 (9.9)
(*ii*) Demand deposits with banks .	4078 (21.8)	1774 (7.8)	1369 (6.0)	3136 (12.7)
(*iii*) Time deposits with banks .	14620 (19.6)	15383 (17.2)	15074 (16.9)	18134 (17.3)
(*iv*) 'Other' deposits with RBI .	20	88	–33	–187
III. Sources of change in M3 (1+2+3+4–5)				
(1) Net Bank Credit to Government (a+b) . .	13699 (23.5)	12350 (17.1)	11991 (16. 6)	14958 (17.7)
(*a*) RBI's net credit to Government (i+ii) . .	7607	6402	6761	8974
(*i*) To Central Government	7091	6559	7553	9679
(*ii*) To State Governments . .	516	–157	–792	–705
(*b*) Other Banks' Credit to Government . .	6092	5948	5230	5984
(2) Bank Credit to Commercial Sector (a+b)	11938 (14.4)	12746 (13.5)	6696 (7.1)	11554 (10.7)
(*a*) RBI's credit to Commercial Sector* .	342	396	413	601
(*b*) Other Banks' Credit to Commercial Sector	11596	12350	6283	10953
(3) Net Foreign Exchange Assets of the Banking Sector . .	943 (24.4)	795 (16.5)	–59 (-1.2)	–300 (-5.3)
(4) Government's Currency Liabilities to the Public . .	252 (26.8)	188 (15.8)	94 (7.9)	36 (2.6)
(5) Banking Sector's Net Non-monetary Liabilities other than Time Deposits (a+b)	4791 (17.6)	3657 (11.4)	–1662 (-5.2)	1833 (5.1)
(*a*) Net non-monetary liabilities of RBI	2737	781	100	2195
(*b*) Net non-monetary liabilities of other banks (residual)	2054	2876	–1762	-362

P—Provisional.

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

NOTES : 1. Figures may not add up to totals because of rounding.

2. Figures in brackets are percentage variations.

3. Reserve Bank data are on the basis of closure of Government accounts.

7.9 If the change in M3 in 1987-88 is analysed from the sources angle, the deceleration in the growth of money supply (M3) was principally accounted for by significantly lower growth in both net bank credit to Government and in net foreign exchange assets of the banking system. In 1987-88 net bank credit to Government increased by Rs. 12350 crores (17.1 per cent) as against Rs. 13699 crores (23.5 per cent) in 1986-87, because of a smaller increase mainly in net RBI Credit to Government and to some extent also in other banks' credit to Government. The increase in net RBI Credit to Central Government was of the order of Rs. 6559 crores in 1987-88 as compared with a rise of Rs. 7091 crores in 1986-87. Significantly, RBI credit to State Governments registered a decline of Rs. 157 crores in 1987-88 in sharp contrast to an increase of Rs. 516 crores in 1986-87. Lower increase in other banks' credit to Government, despite an upward revision in the statutory liquidity requirement, was mainly due to slower growth of bank deposits. Net foreign exchange assets of the banking sector registered not only a lower expansion in absolute terms but also in percentage terms i.e. Rs. 795 crores (16.5 per cent) in 1987-88 than Rs. 943 crores (24.4 per cent) in 1986-87. There was also a slight deceleration in the growth rate of bank credit to commercial sector to 13.5 per cent (Rs. 12746 crores) in 1987-88 as compared with the growth rate of 14.4 per cent (11938 crores) in 1986-87.

7.10 The most important trend in the scheduled commercial banks sector in 1987-88 was the deceleration both in the growth rate of aggregate deposits and in the rate of expansion of credit. Aggregate deposits of the scheduled commercial banks recorded a lower rate of growth in 1987-88 (14.9 per cent as against 20.1 per cent in 1986-87), mainly becuase of a significant decline in the growth of demand deposits to 5.3 per cent from 22.6 per cent in 1986-87. This was largely attributable to buy-back arrangements in Government and other approved securities by banks with non-bank clients. Time deposits also recorded a lower rate of growth of 17.2 per cent in 1987-88 compared with 19.5 per cent in 1986-87. This may have been due to an adverse impact of the drought on household savings in 1987-88. Bank credit also recorded a lower growth of Rs. 7492 crores (11.6 per cent) in 1987-88 as compared with that of Rs. 7715 crores (13.5 per cent) in 1986-87. The principal reason for this deceleration is the large decline of Rs. 2349 crores in food credit (compared with that of Rs. 1295 crores in 1986-87) due to a massive draw-down of foodgrains stocks held by Pubic Sector agencies in the wake of unprecedented drought last year as also the release of the subsidy. The growth of non-food credit to the commercial sector was lower at 16.4 per cent during 1987-88 as against 17.6 per cent in 1986-87.

Monetary Trends during 1988-89

7.11 In the current year so far (i.e. upto January 13, 1989) money stock (M3) has grown at a somewhat higher rate of 15 per cent compared with 14.5 per cent growth in the corresponding period of 1987-88. Unlike in 1987-88, expansion in currency with public has been modest this year so far, at 9.9 per cent as against 14 per cent expansion in that year. Both, demand and time deposits with banks have registered higher increase. While the increase in demand deposits with banks by Rs. 3136 crores (12.7 per cent) was more than double the increase of Rs. 1369 crores (6 per cent) during the corresponding period of 1987-88, the growth in time deposits with the banks has also been somewhat faster this year at 17.3 per cent as against 16.9 per cent growth recorded in the corresponding period last year.

7.12 Higher rate of growth in M3 this year so far can be attributed principally to a larger expansion of 17.7 per cent (Rs. 14958 crores) in net bank credit to Government as against an increase of 16.6 per cent (Rs. 11991 crores) in the corresponding period of 1987-88. This was supplemented by a higher growth rate of bank credit to commercial sector in 1988-89 so far than in the comparable period of last year (10.7 per cent as against 7.1 per cent, respectively). The accelerating effect of higher rates of expansion in net bank credit to Government and bank credit to commercial sector was partly moderted by a larger decline in the net foreign exchange assets of the banking system by Rs. 300 crores (5.3 per cent) in 1988-89 so far compared with a decline of Rs. 59 crores (1.2 per cent) in 1987-88.

7.13 In 1988-89 so far, the growth of RBI's net credit to Government has been substantially higher than the growth in the last year (Rs. 8974 crores as against Rs. 6761 crores, respectively). Between March 31, 1988 and January 13, 1989 while States' net indebtedness to RBI declined by Rs. 705 crores (as against a decline of Rs. 792 crores in 1987-88), net RBI Credit to Central Government rose by Rs. 9679 crores which is significantly higher than the increase of Rs. 7553 crores in the corresponding period of 1987-88.

7.14 Table 7.2 presents selected indicators relating to financial operations of the scheduled commercial banks. In the current year so far, i.e. between March 31,1988 and January 13, 1989 the aggregate deposits of these banks have grown by Rs. 20639 crores (17.5 per cent) as against increase of Rs. 15401 crores (15 per cent) in the corresponding period last year (i.e. March 31, 1987 to January 15, 1988). Demand deposits have risen by Rs. 2963 crores as compared with a rise of Rs. 1068 crores in the comparable period

TABLE 7.2

Scheduled Commercial Banks: Variations in Selected Indicators

(Rupees crores)

	Variations during@			
	1986-87	1987-88	1987-88 Upto Jan. 15, 1988*	1988-89 Upto Jan. 13, 1989*
1	2	3	4	5
1. Aggregate Deposits (a+b) . . .	+17234	+15315	+15401	+20639
(*a*) Demand Deposits .	+3641	+1040	+1068	+2963
(*b*) Time Deposits	+13593	+14275	+14333	+17676
2. Borrowings from R.B.I.	+348	+847	−14	−659
3. Cash in hand and balances with R.B.I. (a+b) . . .	+3231	+3348	+3761	+3633
(*a*) Cash in hand	+24	+4	+65	+269
(*b*) Balances with R.B.I. . .	+3207	+3344	+3696	+3364
4. Net balances with R.B.I. [3 (b) −2] .	+2859	+2497	+3710	+4023
5. Money at call and short notice . .	+1723	−865	−948	−21
6. Bank Credit (a+b)	+7715	+7492	+4144	+8347
(*a*) Public food procurement credit	−1295	−2349	−1791	−1187
(*b*) Non-food bank credit . .	+9010	+9841	+5935	+9534
Of which : to priority sector	£+3484	+4020	..	..
7. Investments in Government and other approved securities (a+b) . .	+8276	+8118	+7292	+7846
(*a*) Government securities .	+5984	+5815	+5153	+5881
(*b*) Other approved securities .	+2292	+2303	+2139	+1965
8. Balances with other banks in current account . .	−370	−266	−21	+188
9. Credit-deposit ratio†	62.9	61.1	58.2	58.0
10. Non-food credit-deposit ratio† .	58.4	59.2	55.8	57.3
11. Investment-deposit ratio† . .	37.8	39.7	39.0	39.5

@Based on March 31 data.

*Provisional.

. . Not available.

†Percentage at the end of the period.

£Data relate to 50 banks which account for 95 per cent of gross bank credit. Variations are based on last Friday data.

last year. Time deposits have also recorded a much faster growth by Rs. 17676 crores this year so far against the growth of Rs. 14333 crores in the corresponding period last year. Non-food credit has grown by Rs. 9534 crores (13.6 per cent) as against Rs. 5935 crores (9.9 per cent) last year. Food credit registered a decline of Rs. 1187 crores as against the decline of Rs. 1791 crores in the corresponding period last year. As a result, bank credit by the scheduled commercial banks has recorded a rise of Rs. 8347 crores as compared with the rise of Rs. 4144 crores in the corresponding period of 1987-88. The credit-deposit ratio has, however, declined marginally to 58 per cent on January 13, 1989 as against 58.2 per cent a year ago. However, non-food credit-deposit ratio has risen by 1.5 percentage points i.e. 57.3 per cent compared to 55.8 per cent in the previous year.

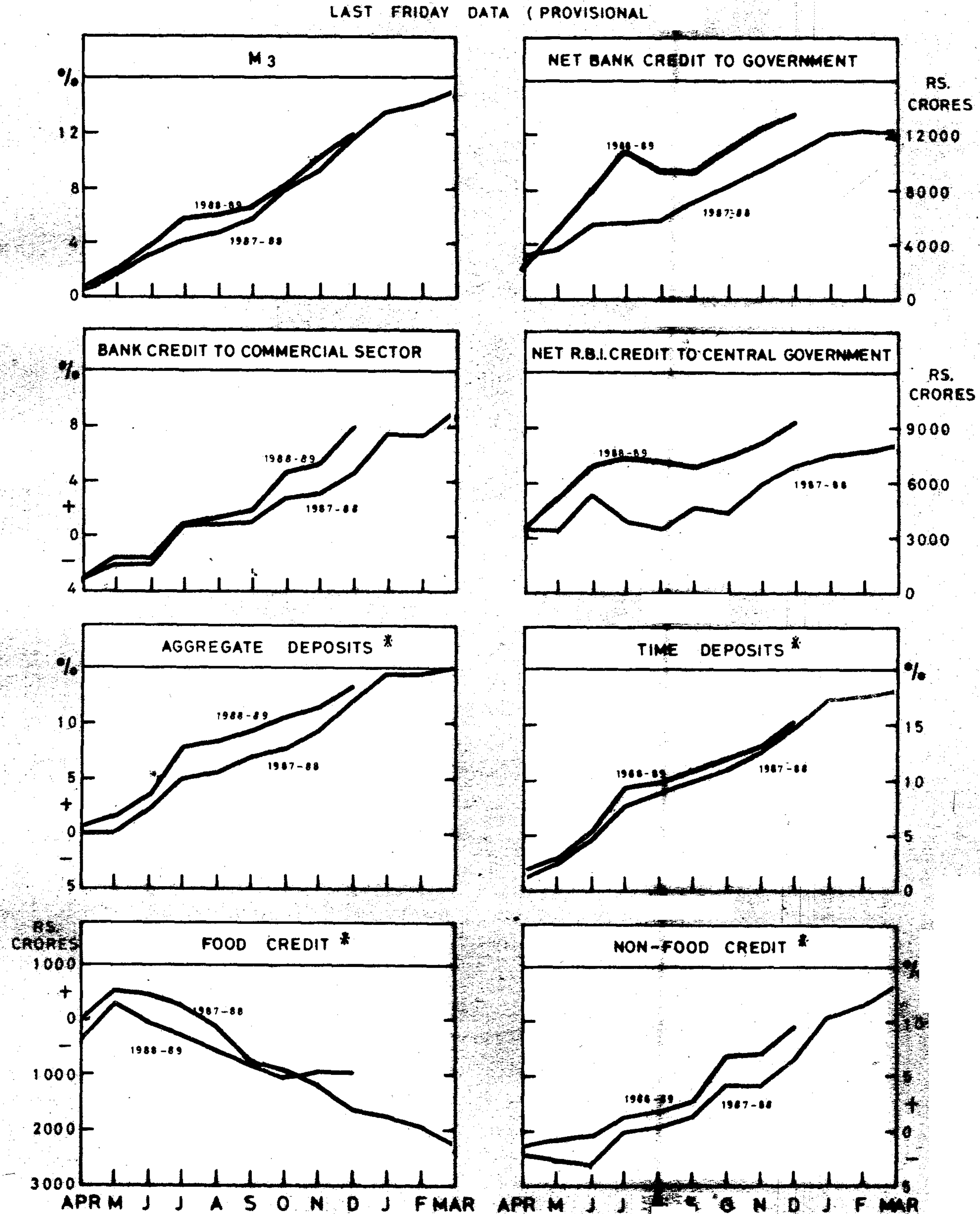
Reserve Money

7.15 It is well recognised that variations overtime in reserve money or base money adjusted for changes in the cash reserve ratio have a strong influence on changes in money supply. Net RBI credit to Government is the most important source of reserve money. As a percentage of the total reserve money it had been steadily rising since March 1978 and reached high level of 103.3 per cent on 31st March 1987 but declined significantly to 98.5 per cent at the end of last financial year.

7.16 There was, however, a large expansion in reserve money to the tune of 19.4 per cent in 1987-88 as against expansion of 17.4 per cent in 1986-87. Among the sources of reserve money, net RBI credit to Government accounted for Rs. 6402 crores out of the total expansion of Rs. 8681 crores in the reserve money in 1987-88. However, compared with the previous year, the expansion in net RBI credit to Government was lower in 1987-88 in both absolute and percentage terms (Rs. 6402 crores and 13.8 per cent as against Rs. 7607 crores and 19.7 per cent in 1986-87). It may further be pointed out that larger expansion in RBI credit to banks including claims on NABARD (Rs. 1681 crores as against Rs. 298 crores in 1986-87), also contributed significantly to the faster expansion of reserve money in 1987-88.

GROWTH IN SELECTED MONETARY INDICATORS

LAST FRIDAY DATA (PROVISIONAL

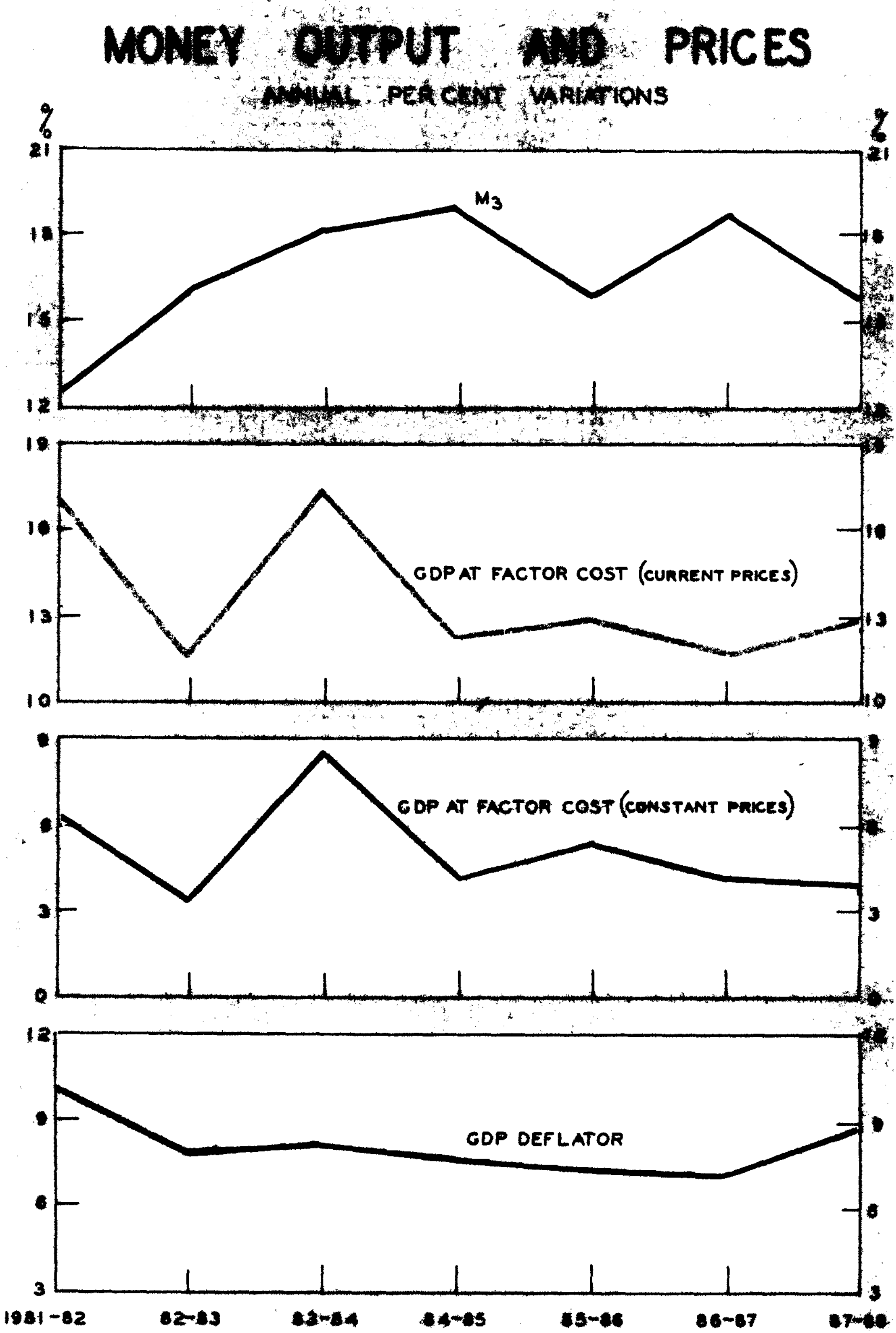


MINISTRY OF FINANCE, ECONOMIC DIVISION.

* DATA RELATE ... COMMERCIAL BANKS.

NOTE- BASE YEAR ... MARCH 31ST.

MGIP(PLU)MRND-449/VEc.Affair/88-89



MINISTRY OF FINANCE, ECONOMIC DIVISION.

MGIP(PLU)MRND-449/1/Ec.Affair/88-89

TABLE 7.3

Sources of Change in Reserve Money

(Rupees crores,

1	Outstanding as on March 31, 1985 (2)	Variations during† 1985-86 (3)	1986-87 (4)	1987-88 (5)	1987-88 March 31, 1987 to January 15, 1988@ (6)	1988-89 March 31, 1988 to January 13, 1989@ (7)
1. Net RBI credit to Government	34236	4442 (13.0)	7607 (19.7)	6402 (13.8)	6761 (14.6)	8974 (17.0)
2. RBI credit to banks£	3174	—712 (—22.4)	298 (12.1)	1681 (60.9)	612 (22.2)	—331 (—7.5)
3. RBI credit to commercial sector*	2752	300 (10.9)	342 (11.2)	396 (11.7)	413 (12.2)	601 (15.9)
4. Net foreign exchange assets of RBI	2899	842 (29.0)	880 (23.5)	795 (17.2)	—59 (—1.3)	—300 (—5.5)
5. Government's currency liabilities to the public	777	163 (21.0)	252 (26.8)	188 (15.8)	94 (7.9)	36 (2.6)
6. Net non-monetary liabilities of RBI	8622	2085 (24.2)	2737 (25.6)	781 (5.8)	100 (0.7)	2195 (15.4)
7. Reserve Money (1+2+3+4+5 -6)	35216	2950 (8.4)	6642 (17.4)	8681 (19.4)	7721 (17.2)	6785 (12.7)

† Variations are worked out on the basis of March 31 data after closure of Government accounts.

@ Provisional.

£ Includes claims on NABARD.

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

NOTE : Figures may not add up to totals because of rounding.

7.17 In the current year so far (i.e. between March 31, 1988 and January 13, 1989) reserve money has registered a lower growth of Rs. 6785 crores (12.7 per cent) compared to the growth of Rs. 7721 crores (17.2 per cent) in the corresponding period of last year. The relatively smaller expansion in reserve money this year, in spite of the larger growth in net RBI credit to Government (Rs. 8974 crores as against Rs. 6761 crores in the corresponding period of 1987-88, can be attributed principally to (a) a decline of Rs. 331 crores in RBI credit to banks as against an increase of Rs. 612 crores a year ago; (b) a larger decline in net foreign exchange assets of RBI (Rs. 300 crores as against Rs. 59 crores last year); and (c) a larger increase in net non-monetary liabilities of RBI (Rs. 2195 crores as against Rs. 100 crores).

Trends in Sectoral Deployment of Credit

7.18 As early as in 1974 banks were directed to extend at least one-third of the total credit to priority sectors consisting of agricultural and allied activities, small scale industries and other socially urgent areas/groups like scheduled castes and tribes, small business and beneficiaries of the Integrated Rural Development Programme. The target was latter on raised to 40 per cent in October 1980 to be reached by March 1985 and it was also stipulated that within the priority sector 16 per cent of the total bank advances should be earmarked for agricultural sector. Further, in the current year's budget, it was announced that the target for direct finance to agriculture by public sector banks would be raised from 16 per cent to 17 per cent of their total outstanding advances by the end of 1988-89.

TABLE 7.4

Sectoral Deployment of Gross Bank Credit

(Rs. crores)

On the last Friday basis	Variations during									
	1985-86		1986-87		1987-88		April-Seotember 1987		April-September 1988	
	Rs. crores	Per cent	Rs. crores	Per cent	Rs. crores	Per cent	Rs. crores	Per cent	Rs. crores	Per cent
1	2	3	4	5	6	7	8	9	10	11
I. Gross Bank Credit	7257	15.1	7356	13.3	7766	12.4	1539	2.5	4039	5.7
1. Public Food Prourcement .	–130		–431		–2914		–1353		–882	
2. Gross Non-food Credit (a+b+c+d)	7387	17.5	7787	15.7	10680	18.6	2892	5.0	4921	7.2
(*a*) Priority Sector (i+ii+iii) .	3157	17.1	3484	16.2	4020	16.0	1565	6.2	1844	6.3
(*i*) Agriculture . .	1398	18.3	1512	16.7	1439	13.6	671	6.3	760	6.3
(*ii*) Small Scale Industry .	1204	18.2	1292	16.5	1712	18.8	519	5.7	767	7.1
(*iii*) Other Priority Sectors .	555	13.4	680	14.5	869	16.2	375	7.0	317	5.1
(*b*) Industry (Medium & Large)	2483	15.6	2934	15.9	3871	18.1	1019	4.8	1706	6.8
(*c*) Wholesale Trade (other than food procurement) (i+ii+iii+iv) . . .	417	15.7	14	0.5	518	16.8	–43	–1.4	344	9.6
(*i*) Cotton Corporation of India	25	18.5	–51	–31.9	–18	–16.5	–109	–100.0	–91	–100.0
(*ii*) Food Corporation of India (Fertiliser) . .	–25	–15.1	8	5.7	22	14.8	10	6.7	17	9.9
(*iii*) Jute Corporation of India . . .	11	9.5	71	55.9	–56	–28.3	–31	–15.7	–49	–34.5
(*iv*) Other Trade . . .	406	18.2	–14	–0.5	570	21.7	87	3.3	467	14.6
(*d*) Other Sectors . . .	1330	25.1	1355	20.5	2271	28.5	351	4.4	1027	10.0
II. Export Credit (included under item 2)	74	3.2	737	30.6	771	24.5	339	10.8	476	12.2
Priority Sector Advances as percentage of Net Bank Credit (including PCs) in the last month of the period . . .		40.8		42.2		43.8		44.0		43.8

NOTES : Data are provisional and relate to 50 scheduled commercial banks which account for about 95 per cent of the bank credit. Gross bank credit data include bills rediscounted with RBI, IDBI, Exim Bank and other approved financial institutions and Participation Certificates. Net Bank Credit data are exclusive of bills rediscounted with RBI, IDBI, Exim Bank and other approved financial institutions.
PCs —Participation Certificates.

7.19 The broad sectoral pattern of the incremental credit deployed by 50 scheduled commercial banks, accounting for 95 per cent of the bank credit, is presented in Table 7.4. It will be evident from the table that credit to priority sectors as a percentage of net bank credit has risen steadily from 40.8 per cent at the end of 1985-86 to 42.2 per cent at the end of 1986-87 and reached a further higher level of 43.8 per cent at the end of the last financial year. It remained at this level at the end of September 1988.

7.20 A major share of the increase of Rs. 4020 crores in priority sector credit in 1987-88 had gone to agriculture and small scale industry. Credit to agriculture rose by 13.6 per cent (Rs. 1439 crores), while credit to small scale industry recorded a rise of 18.8 per cent (Rs. 1712 crores). The other priority sectors, inclusive of retail trade and small business, small transport operators and rural artisans, accounted for an increase of Rs. 869 crores (16.2 per cent).

7.21 As regards other non-food sectors, in 1987-88 the credit to wholesale trade recorded a significant growth of 16.8 per cent (Rs. 518 crores) as against almost no increase in 1986-87. Though credit to Jute Corporation of India and Cotton Corporation of India declined by 28.3 per cent and 16.5 per cent, respectively, it was off-set by 14.8 per cent and 21.7 per cent increase in the credit to Food Corporation of India (Fertiliser) and other trade, respectively. The growth in credit to medium and large industries was also significantly higher at 18.1 per cent as against 15.9 per cent in 1986-87 (Rs. 3871 crores as against Rs. 2934 crores, respectively). However, the rate of growth in export credit of the scheduled commercial banks declined from 30.6 per cent to 24.5 per cent (though in absolute terms growth was nominally higher at Rs. 771 crores against Rs. 737 crores).

7.22 For the current year, data for sectoral deployment of credit are available for April—September 1988. The expansion of non-food gross bank credit by Rs. 4921 crores (7.2 per cent) was higher than that of Rs. 2892 crores (5 per cent) in the corresponding period of 1987-88. Credit to medium and large industry and wholesale trade showed a much higher rise of Rs. 1706 crores (Rs. 1019 crores last year) and Rs. 344 crores (as against a decline of Rs. 43 crores), respectively. Export credit has also shown a higher rise of Rs. 476 crores (12.2 per cent) as compared with a rise of Rs. 339 crores (10.8 per cent) during the corresponding period last year.

Developments in Credit Policy

7.23 Monetary and credit policy occupies a key role in our strategy of planned economic development. On the one hand, the growth of production and trade calls for necessary monetary and credit expansion. On the other, it is imperative to ensure that such expansion in money and credit does not generate undue inflationary pressures. The stance of the monetary authority has, therefore, been to meet the genuine demands for credit of production sectors fully, while minimizing the use of credit for speculative purposes.

7.24 Apart from the objective of controlled expansion of money and credit as noted above, in 1987-88 the monetary and credit policy had also to meet another objective *i.e.* to provide financial assistance/relief to drought-hit farmers who faced acute financial hardships and to help them undertake a second sowing or raise short duration crops or fodder cultivation. As a result, the commercial banks in 1987-88 were asked to provide financial assistance to the affected farmers for cultivation, allow conversion of short-term into medium-term loan and to reschedule investment credit in case of complete loss of crops. The Credit Authorisation Scheme (CAS) was considerably liberalised to meet genuine credit demands. At the same time, in order to contain the liquidity growth in the banking system and consequent monetary expansion, the Statutory Liquidity Ratio (SLR) was revised upwards twice, from 37 per cent to 37.5 per cent effective from April 25, 1987 and again from 37.5 per cent to 38 per cent with effect from January 2, 1988. Similarly, there was an upward revision of the Cash Reserve Ratio (CRR) from 9.5 per cent to 10 per cent of the banks' net demand and time liabilities (excluding NRE and FCNR accounts) effective October 24, 1987. Furthermore, in response to price-output developments, selective credit controls were reimposed/tightened in the case of a number of price sensitive essential commodities like paddy/rice, cotton and kapas, oilseeds and vegetable oils in order to combat inflationary pressures on their prices. These monetary and credit policy initiatives helped restrain growth of broad money to 15.9 per cent last year as against 18.6 per cent expansion in 1986-87. Together with other appropriate fiscal and supply-side measures, these monetary and credit policy steps helped in containing the annual rate of inflation to 10.6 per cent which was significantly lower than that recorded in an earlier year of comparable drought.

7.25 In the current financial year the monetary authorities have adopted a cautious stance aimed at providing adequate credit for the strong recovery in agriculture and other sectors, while containing overall growth of liquidity to below the average growth rate of 17 per cent recorded in the last three years. In the light of favourable monsoon, presaging a very good kharif crop and expectations of industrial growth being maintained at a high level, the RBI advised commercial banks to plan their credit budgets so as to meet an increase in non-food credit to the tune of Rs. 2600 crores in the first half of

1988-89. Banks were also advised to plan for an increase in food credit to the tune of Rs. 1200 crores in April-June 1988 (followed, however, by a decline of around Rs. 1000 crores in July-September 1988). To help meet this credit expansion, RBI released on April 23, 1988 the entire amount of Rs. 744 crores of the remaining cash balances impounded under incremental CRR during January 14, 1977 to October 31, 1980. At the same time, in order to partially neutralise the return flow of food credit, the scheduled commercial banks were required to maintain a higher Cash Reserve Ratio of 10.5 per cent of their net demand and time liabilities (excluding FCNR/NRE deposits) as against 10 per cent earlier, with effect from the fortnight beginning July 30, 1988. With a lower than expected Rabi 1988 Food procurement and a faster return flow of food credit there was a growth of liquidity and hence the increase in the CRR from 10 percent to 10.5 per cent was preponed from July 30 to July 2, 1988 and a further increase in the CRR to 11 per cent was made effective from July 30, 1988. The CRR on FCNR deposit liability was also enhanced from 9.5 per cent to 10 per cent with effect from July 30, 1988.

7.26 As noted earlier banks were found to be entering into buy-back arrangements in Government and other approved securities with non-bank investors in 1987-88 which kept the growth of demand deposits low in that year and also led to an understatement of the liquidity growth of the banking system. It was felt that these arrangements were likely to affect the profitability position of the banks and put them into a liquidity bind. The RBI, therefore, prohibited the banks from entering into such arrangements effective from April 4, 1988 and directed them to terminate all the existing arrangements on the date they expired or on July 1, 1988 whichever was earlier.

7.27 Several measures were adopted by RBI in 1987-88 to promote bill financing and strengthen the money market in India in pursuance of the recommendations of the Working Group on the Money Market. In 1987-88 banks were informed that only 75 per cent of the eligible receivables of all parties subject to the Credit Authorisation Scheme would be taken into account for financing with effect from April 1, 1988 and all parties subject to CAS were required to attain a ratio of bill acceptance to credit purchase of 25 per cent by April 1, 1988. A specific time-bound programme was also to be drawn up by banks in consultation with borrowers and the Reserve Bank was to be advised in case of an unavoidable short-fall regarding financing of inland credit sales through bills and covering credit purchases by way of bill acceptances. With the DFHI expected to impart further liquidity to the 182 days Treasury Bills, effective April 23, 1988, refinance limits under 182 days Treasury Bills Refinance Facility were made equivalent to 50 per cent of a bank's holdings of 182 days Treasury Bills instead of 75 per cent hitherto and the interest rate on such refinance was raised from 10 per cent to 10.25 per cent.

7.28 The current financial year witnessed a major overhaul of the Credit Authorisation Scheme (CAS). It may be recalled that in the case of bulk sanction of non-food commercial credit advanced by the commercial banks, CAS was introduced in order to ensure that bank credit for large borrowers does not make a disproportionate claim on the lendable resources of the banks at the cost of other borrowers, such bank credit is optimally used and the borrowers follow necessary financial discipline. In the last few years a number of reforms/liberalizations were introduced in this scheme, on the basis of periodic reviews in order to improve its operational flexibility without compromising its basic objectives. Some of these reforms (particularly those introduced in 1987-88) have already been mentioned in last year's Economic Survey. In the early part of 1988-89 instructions were issued that proposals for term loans granted by banks in participation with all India financial institutions need not be referred to the RBI for prior authorisation provided the share of banks does not exceed 25 per cent of the aggregate financial assistance from the financial institutions and banks taken together.

7.29 After a review of the working of the CAS for about 15 months beginning from July 1987, it was found that a large majority of CAS parties were complying with the norms prescribed under this scheme. There had been substantial improvement in compliance with the inventory norms and submission of quarterly information statement as required under the scheme. Thus it became apparent that the purposes of CAS were being broadly achieved due mainly to the enforcement of the basic financial discipline. Consequently, it was also decided to dispense with the practice of prior authorisation by RBI of the sanction of working capital credit limits/term loans, even for amounts beyond the stipulated cut-off points. The RBI, therefore, advised the banks in October 1988, that working capital limits exceeding Rs. 5 crores should be sent to RBI only for post-sanction scrutiny, scheme being renamed as Credit Monitoring Arrangement. In the case of term loans also, all proposals which were currently required to be referred to RBI for prior authorisation would hereafter be subjected only to post-sanction scrutiny. However, the RBI has cautioned the commercial banks that if any particular bank is found by RBI on such post-sanction scrutiny to be not enforcing the basic discipline it may instruct such bank to refer larger cases to it even for prior authorisation.

7.30 As a further measure of reform in response to representations received from borrowers, all parties including those enjoying credit limits exceeding Rs. 5 crores were permitted, from October 1988, to transfer their accounts from one bank to another without the requirement of a no-objection letter from the existing bank. However, the transferee bank will have to take over the entire liabilities (both good and unsatisfactory accounts). Transferer bank may refuse to allow such transfer to a party if it wants to shift only good accounts, leaving unsatisfactory accounts with the existing bank, unless arrangements are made, by the party concerned to the satisfaction of the bank. Existing instructions on consortium advances restricting the number of banks to five in respect of credit limits upto Rs. 50 crores have been modified and it has been stipulated that the number of banks in formal consortium arrangements should be limited to around 10.

7.31 A new instrument called Inter-Bank Participations has been introduced with a view to facilitating the adjustment of short-term liquidity within the banking system. These Participations can be either on a risk-sharing basis or without risk-sharing. Participations on risk-sharing basis would be for 91—180 days at an interest rate to be determined between the issuing bank and the participating bank subject to a minimum of 14 per cent per annum. Participations without risk-sharing would have a tenure not exceeding 90 days at an interest rate to be determined between the concerned banks subject to a ceiling of 12.5 per cent per annum. Participations without risk-sharing will be treated as a part of the demand and time liabilities of the borrowing bank and subject to reserve requirements.

7.32 In order to provide some flexibility in the money market, the Discount and Finance House of India (DFHI) has been allowed with effect from July 28, 1988 to participate in the call and notice money market both as a lender and a borrower and it was further decided in October 1988, to exempt the operations of DFHI in the call/notice money market from the provisions of the ceiling on the rate of interest set out by the Indian Banks Association.

7.33 The development of a viable and accessible institutional system for the provision of housing finance is one of major thrust areas of the National Housing Policy recently adopted by the Government of India. The National Housing Bank (NHB) has been set up as an apex institution on July 9, 1988 with its share capital fully subscribed by the Reserve Bank. Aims and objectives of this Bank have been discussed in detail later in this Chapter. Since banks with their vast net work of branches have an important role to play in housing finance and some banks have already set up specialised housing finance institutions, the Reserve Bank in October 1988, introduced a numebr of changes in the terms for providing housing finance as detailed below :

(*a*) The maximum period of repayment for housing loans sanctioned by scheduled commercial banks has been extended from 10 years to 15 years;

(*b*) The margins for housing loans have been relaxed on a graded scale and the maximum margin has been reduced from 50 per cent to 35 per cent.

(c) Lending rates on housing finance have also been revised with effect from October 10, 1988 as follows :—

Amount of the Loan	Interest rate (per cent per annum)
(i) Upto Rs. 20,000	12.5
(ii) Above Rs. 20,000 and upto Rs. 50,000	13.5
(iii) Above Rs. 50,000 and upto Rs. 1 lakh	14.0
(iv) Above Rs. 1 lakh . . .	14.5–16.0

The rate of interest for scheduled castes and tribes on housing loan upto and inclusive Rs. 5000 will, however, remain unchanged at 4 per cent.

(d) Banks have been advised to accept other forms of security in case mortgage of property or Government guarantee is not feasible.

(e) Banks also can extend credit for additions, repairs and alterations and provide supplementary finance if individuals have raised finance from elsewhere. They can also adjust instalments keeping in view the resource position of the low income group of borrowers.

7.34 In the very beginning of the financial year selective credit controls were reintroduced/tightened to check spill-over effects of drought on the price situation. Effective from April 4, 1988 the base period for determining credit ceilings for advances subject to selective credit controls, was brought forward by one year from 1982-83, 1983-84 and 1984-85 (November—October) to 1983-84, 1984-85 and 1985-86 (November—October). Simultaneously the level of credit ceilings on advances against paddy/rice, pulses, 'other foodgrains', cotton and kapas was reduced from 100 per cent to 85 per cent of the peak level of credit maintained by the party in the base period. Credit to cotton mills, however, remained exempt from such control. Again on a review of the market situation, bank advances against wheat, fully exempt earlier from the provisions of selective credit control since October 1985, were brought back within the purview of such controls effective from April 11, 1988. Such advances came under a credit ceiling at 85 per cent of the base period noted above, in addition 60 from a margin of 30—45 per cent. However, the ceiling was not made applicable to roller flour mills. On a further review of the price-output trends minimum margins on bank advances against the stock of wheat were raised across the board by 15 percentage points with effect from June 9, 1988. However, effective from September 19, 1983 a lower minimum margin of 30 per cent was stipulated for processing units/mills in the

TABLE 7.5

Minimum Margins on Bank Advances Against Stock of Commodities covered under Selective Credit Control

(Percentages)

Commodities	Effective February 10, 1989		
	Against Stock		Against warehouse receipts
	Processing Units/ Mills	Others	
1. Paddy/Rice. . .	45	60	45
2. Wheat . . .	45@	60	45
3. Other foodgrains (other than paddy/rice) and wheat) . . .	45@	60	45
4. Pulses . . .	45	60	45
5. Oilseeds, *viz.* Groundnut, rapeseed/mustard seed, linseed, castor seed, cottonseed and all imported oilseeds .	30	45	30
6. Vegetable oil *viz.* Groundnut oil, rapeseed/mustard oil, linseed oil, castor oil, cottonseed oil, vanaspati and imported vegetable oils. .	30*	60	45
7. Cotton & Kapas . .	X	45	30
8. Sugar			
(a) Buffer . . .	0	–	–
(b) Unreleased stocks	17.5	–	–
(c) Released . .	60	60	45
9. Gur & Khandsari .	30	60	45

@30 per cent in the State of Punjab from September 19, 1988 to March 31, 1990.

XCompletely exempt from all the stipulations of selective credit control.

*Applicable to registered oil mills and vanaspati manufacturers.

— Not Applicable.

State of Punjab upto March 31, 1990 (as against 45 per cent in other States/UTs). However, in view of the improved output of oilseeds and vegetable oils, effective February 10, 1989 the minimum margins on advances against oilseeds and vegetable oils (including vanaspati) have been reduced accross the board by 15 percentage points and the level of credit ceiling in respect of bank advances against these commodities has been raised from 85 per cent to 100 per cent of the peak level of credit maintained by the party in any of the three years noted above. Table 7.5 presents the details of existing minimum margins on bank advances against stocks of commodities covered under selective credit controls.

Structure of Interest Rates

7.35 Interest rates play a very important role in the mobilisation of savings as also in the allocation of investible resources to different sectors of the economy in accordance with the socio-economic priorities. Although interest rates in India are predominantly administered, they are revised from time to time in the light of evolving trends.

7.36 Effective March 1, 1988, a reduction was made in the lending rates by one to two-and-a-half percentage points on short term agricultural loans (upto Rs. 15,000) to farmers sanctioned by the scheduled commercial banks (including Regional Rural Banks). Interest rates on loans exceeding Rs. 15,000 were, however, left unaltered. These reductions in interest rates benefitted a very large number of farmers, particularly the small and marginal farmers who were hit the hardest by the drought of 1987-88. The target for direct finance to agriculture by scheduled commercial banks was raised from 16 per cent to 17 per cent of the total bank advances; this target is to be attained by March 1989.

TABLE 7.6

Interest Rates on Short-term Loans to Farmers

(Per cent per annum)

Range of Advance	Effective upto February 29, 1988	Effective from March 1, 1988
1	2	3
(*i*) Upto Rs. 5,000 .	11.50	10.00
(*ii*) Over Rs. 5,000 and upto Rs. 7,500 .	12.50	10.00
(*iii*) Over Rs. 7,500 and upto Rs. 10,000 .	12.50	11.50
(*iv*) Over Rs. 10,000 and upto Rs. 15,000 .	12.50 – 14.00	11.50
(*v*) Over Rs. 15,000 and upto Rs. 25,000 .	12.50 – 14.00	12.50 – 14.00
(*vi*) Over Rs. 25,000 .	14.00 – 15.50	14.00 – 15.50

7.37 Another significant development in the field of interest rate policy during the current financial year was the replacement of a ceiling rate on bank advances by a floor rate specified by the RBI. Thus banks were granted greater freedom and flexibility in fixing interest rates, in line with the recommendations of the Committee on the Review of the Working of Monetary System. It may be recalled that effective April 1, 1987 the maximum lending rate of scheduled commercial banks was reduced from 17.5 per cent to 16.5 per cent. This ceiling rate of 16.5 per cent was replaced by a floor rate of 16 per cent effective from October 10, 1988. Banks were, however, advised by the RBI to use this discretion to charge differential rates judiciously. Disciplined bank borrowers with good track records and parties with good credit ratings will definitely benefit from this flexibility, though banks are expected to vary lending rates with an element of moderation, so as to ensure that the range of interest rates charged remained within reasonable limits.

TABLE 7.7

Existing Structure of Interest Rates : Some Selected Categories

(Per cent per annum)

I. Scheduled Commercial Banks Deposits :	
(*i*) 91 days and above but less than one year.	8.0
(*ii*) One year and above but less than two years	9.0
(*iii*) Two years and above . .	10.0
II. Non-Resident (External) Rupee Accounts :	
(*i*) 6 months and above but less than one year.	8.5
(*ii*) One year and above but less than two years	10.5
(*iii*) Two years and above but less than three years	11.0
(*iv*) Three years and above but less than five years	12.0
(*v*) Five years and above . .	13.0

	Pound Sterling	U.S. Dollar	Deutsche Mark	Japanese Yen
III. Foreign Currency (Non-Resident) Accounts :				
	(Rates effective from January 30, 1989)			
(*i*) 6 months and above but less than one year.	11.50	10.00	6.50	5.25
(*ii*) One year and above but less than two years	11.75	10.50	6.75	5.50
(*iii*) Two years and above but less than three years	12.00	10.50	7.25	5.75
(*iv*) Three years only	12.00	10.50	7.50	6.00
IV. Other Financial Instruments :				
(*i*) Convertible debentures :				
(*a*) FERA & MRTP COs. . .		12.5		
(*b*) Non-FERA & Non-MRTP Cos.		14.0		
(*ii*) Non-Convertible debentures .		14.0		
V. Post Office Savings Schemes				
(*i*) One year time deposits. .		9.5		
(*ii*) Two year time deposits. .		10.0		
(*iii*) Three year time deposits. .		10.5		
(*iv*) Five year time deposits. .		11.5		
(*v*) Five year recurring deposits .		11.0		
(*vi*) National Savings Certificates (vi and vii issues)		11.0		
VI. Bank Advances :		16.00* (Minimum)		

*All lending rates which were prescribed at 16.5 per cent (fixed) ceased to have a ceiling stipulation but are subject to a minimum of 16.0 per cent.

7.38 It may be added that in the case of retail trade advances of over Rs. 25000 and upto Rs. 1 lakh the earlier range of interest rates from 15-16.5 per cent has also been reduced to a range of 15-16 per cent. Similarly interest rate on advances to Central and State Government agencies entrusted with procurement and distribution of commodities for sale on a commercial basis was brought down from 16.5 per cent to 16 per cent.

7.39 On the deposit side the rate of interest on deposits of scheduled commercial banks for 91 days and above but less than six months was raised from 6.5 per cent to 8 percent with effect from April 1, 1988 (excluding NRE/FCNR Accounts), in order to yield better return on the deployment of short term surplus funds. Interest rates on other deposits of banks, company deposits, and various postal saving schemes were left unaltered.

7.40 As regards the Foreign Currency (Non-Resident) Accounts, two more currencies, *viz.*, Deutsche Mark and Japanese Yen, have been added to the Scheme with effect from August 1, 1988 and non-resident Indians are now permitted to maintain deposits in four currencies, *viz.*, Pound Sterling, US Dollar, Deutsche Mark and Japanese Yen. As such, a separate interest rate structure is prescribed for fixed deposits in each of these four currencies and the rates are changed keeping in view the corresponding interest rates prevailing for these currencies in overseas markets. The interest rates have been revised on six occasions between August 1, 1988 and January 30, 1989.

Credit by Term-lending Institutions

7.41 A variety of non-banking financial institutions, All India and State level, operate in the financial market of the country and play a useful role in providing long and medium term capital for setting up of industrial units, their expansion and modernisation. Some of them like Industrial Credit and Investment Corporation of India (ICICI) and Industrial Development Bank of India (IDBI) provide loans also in foreign currency. A large number of industries ranging from textile to electricity generation and electric machinery and fertilisers have been financially assisted by these institutions. They have been also notably active in extending assistance to industrially backward areas and states. Units assisted by them not only belong to private, public and co-operative sector but also to joint sector.

7.42 Aggregate sanctions and disbursements by all India financial institutions continued their rising trend in 1987-88. Total assistance sanctioned by all financial institutions aggregated at Rs. 9297 crores which is 16.5 per cent higher than total assistance sanctioned in 1986-87. Nearly 77 per cent of this sanction can be attributed to all India financial institutions comprising Industrial Development Bank of India (IDBI), Industrial Finance Corporation of India (IFCI), Industrial Credit and Investment Corporation of India (ICICI), Life Insurance Corporation (LIC), Unit Trust of India (UTI) and General Insurance Corporation (GIC). While sanction by way of rupee loans increased by 27.1 per cent to Rs. 7703 crores, those in foreign currency declined by 36.5 per cent to Rs. 467.7 crores. Nearly two-thirds of these rupee loans can be attributed to all India development banks. All industries excepting fertiliser, electrical machinery and electricity generation industries received higher amounts of assistance in 1987-88 than in 1986-87. Credit sanctioned to backward areas increased by 11.9 per cent to Rs. 3401 crores in 1987-88 as against Rs. 3039.1 crores in 1986-87.

7.43 During the five year period 1983-84 to 1987-88 credit sanctioned and disbursed by these institutions recorded a very significant growth. Total sanctions and disbursements by all financial institutions during this period constituted nearly 69 per cent and 65 per cent of the cumulative sanctions and disbursements respectively, by them upto end March 1988. Five industries viz. textile, services, miscellaneous chemicals, electricity generation and machinery accounted for nearly 46 per cent of the total cumulative sanctions upto end March 1988, textile industry having been allotted the highest sanction. Sanction and disbursement to backward areas constituted 40.9 per cent and 41.5 per cent of total cumulative sanctions and disbursements by all financial institutions upto end March 1988.

7.44 Data is available for the current financial year only for the six month period i.e. April to September 1988. During this period the total sanctions of all financial institutions was of the order of Rs. 7548 crores which is 80.8 per cent higher compared to Rs. 4173 crores in the corresponding period last year. However, disbursements were of the order of Rs. 4069 crores which is 28 per cent higher than disbursements of Rs.3179 crores made in April-September 1987. All India financial institutions accounted for 84.9 per cent and 81.3 per cent of total sanctions and disbursements made by all financial institutions in April-September 1988. UTI alone sanctioned assistance to the tune of Rs. 1053 crores and disbursed assistance of Rs. 568 crores in April-September 1988 as against sanctions of Rs. 352 crores and disbursements of Rs. 314 crores in April-September 1987. Institution-wise details of sanctions and disbursements are presented in Appendix Table 4.8.

Some Institutional Developments

7.45 The current financial year has witnessed significant institutional developments in the area of money and credit. As a follow-up on the recommendations of the Working Group on Money Market, the RBI, jointly with public sector banks and financial institutions, set up an apex body named as Discount and Finance House of India Ltd.(DFHI). The DFHI, which commenced its operations from April 25, 1988 deals in short-term money market instruments with the primary objective of imparting improved liquidity to such instruments. Since the commencement of its operations, DFHI has been regularly participating in the auction of 182 days treasury bills and is actively dealing in the secondary markets. The DFHI has had a cumulative turnover of Rs. 5,130 crores in 182 days treasury bills by the end of December 1988. The DFHI has been permitted by the RBI to participate also in the inter-bank call money market both as lender and borrower and act as an arranger of funds against a charge of modest fee in this market. Under the recent busy season credit policy of RBI, operations of DFHI in call and notice money market have been exempted from provisions of the ceiling rate on call and notice money as fixed by the Indian Banks Association. The DFHI's daily average business in the call money market has been around Rs. 100 crores. It may be added that the RBI has recently simplified the procedure for handling commercial bills and permitted banks to issue usance promissory notes in convenient lots and maturities on the strength of genuine trade bills discounted by them and to rediscount these promissory notes with the participants in the rediscount market. Since these usance promissory notes would attract a second round of ad-valorem stamp duty, the Government of India have remitted the stamp duty on such usance promissory notes raised by the banks. After the introduction of this revised bill rediscounting procedure, DFHI's turnover in commercial bills rediscounting has recorded significant expansion. In a short span of two months between the end of October 1988 and the end of December 1988, the DFHI achieved a turnover of business in commercial bills to the extent of over Rs. 750 crores. It may be noted here that DFHI, as a matter of policy, is interested in larger turn-over in 182 days treasury bills rather than becoming a repository of these bills.

7.46 A major development in the Indian capital market during the financial year was the establishment of the Securities and Exchange Board of India (SEBI) on April 12, 1988. The Board will function primarily to promote an orderly and healthy growth of securities market as also to protect the investors' interests. In the initial years SEBI will be financed through contributions from public financial and investment institutions and will deal with all matters relating to the development and regulation of securities market and investors' protection. It will not only report to Government periodically on various aspects of the securities markets but will also advise the Government on development and regulation of this market and on the protection of investors. It is hoped that the functioning of SEBI will not only strengthen the up-trend in equity prices from May 1988 but will also introduce discipline in the equity trading and thereby encourage large and steady flow of funds into the primary capital market.

7.47 Another institutional development which has significant implications for the growth of credit and investment in the country, has been the setting up of Credit Rating and Information Services of India Ltd. (CRISIL) jointly by Industrial Credit and Investment Corporation of India, Unit Trust of India, Asian Development Bank and some other institutions. It is the first credit rating agency in the country which functions to evaluate debt obligations of the companies, depending on their ability to service these obligations and assign ratings to them, expressed as numeric and alphabetical symbols. Ratings convey CRISIL's opinion as to future risks of a particular debt obligation or its credit quality. This rating should foster financial discipline, encourage better accounting standards and facilitate direct mobilisation of funds by the corporate sector. It is, therefore, hoped that the services of CRISIL are utilised increasingly by companies seeking to raise funds from the market. At the same time CRISIL should also endeavour to achieve and maintain the high technical competence and professional integrity necessary for making accurate assessments of credit risks.

7.48 An important landmark in the development of housing finance in the country was crossed when the Reserve Bank of India set up on July 9, 1988 National Housing Bank (NHB) as a statutory corporation and as an apex institution in the field of housing finance. The NHB would strive to promote and develop specialised housing finance institutions for mobilising resources and supply of credit for house construction. Among its other important functions will be the provision of refinance facilities to housing finance institutions and scheduled banks, provision of guarantee and underwriting facilities to them and formulation of schemes for the mobilisation of resources and extension of credit for housing, including for economically weaker sections of society. It will also provide guidelines to housing finance institutions for ensuring their growth on sound lines and co-ordinating the working of all agencies connected with housing. NHB has been empowered by the statute to raise resources through issues of bonds and debentures, to borrow from Central Government and other institutions approved by the Central Government and also to accept deposits of a long-term nature. As and when necessary, it can also borrow in foreign currency from banks or financial institutions in India or abroad. Besides long-term loans out of the National Housing Credit (long-term operations) Fund recently established by Reserve Bank, the NHB would also be provided short-term accommodation.