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INDIA

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Status quo on rate; no dividend payout; review NBFC regulatory framework

RBI's MPC has once again voted unanimously for status quo. Moreso, it has indicated continuance of its accommodative stance as long as necessary (at least in FY20 as well as into FY21) to revive growth and contain inflation in the targeted range (though increased for H2FY21). MPC remains committed to ensure ample liquidity and credit flow into the system and support sectors identified as 'stressed'. Measures for deepening financial markets, beefing up supervision and conserving capital has also taken precedence. In its regulatory policies, it has made clear its intent to review the regulatory framework for NBFCs taking cognisance of their changing risk profile, increasing size and interconnectedness to the sector. MPC thereby proposes a scale-based regulatory approach and strengthened supervision through audit. Intention to reduce regulatory arbitrage and operational flexibility will be an interim overhang for large NBFCs.

- **Scale-based regulatory framework for NBFCs – a way forward:** RBI proposes a scale-based regulatory approach linked to the systemic risk contribution from NBFCs – a discussion paper in this regard is to be issued before 15th Jan'21. With sheer increase in size of NBFCs and their changing risk profile, there is a need to review the regulatory framework for them. We believe the intention would be to narrow down regulatory arbitrage and operational flexibility given NBFCs' interconnectedness to the financial system. This will likely lead to interim overhang for large NBFCs till a final framework evolves. Further, introduction of risk-based internal audit for UCBs / NBFCs will widen the scope of financial audit to system and process audit.

- **Extending TLTRO scope to synergise with ECLGS 2.0; liquidity management facility for RRBs:**

  RBI highlighted two important trends:

  - Recovery in rural demand is expected to strengthen further and surge in economic activity, employment, demand in urban areas due to unlocking.
  - Fiscal stimulus is now extended further to growth-generating investments beyond merely being supportive of consumption and liquidity.

  To sustain the current growth momentum and to ensure credit flow in the system, MPC proposes the following measures:

  - ***Extending scope of on-tap TLTRO funding to 26 identified stressed sectors*** and encouraging banks to synergise availing of funds from RBI with guarantee under ECGLS 2.0 to provide credit support to stressed sectors.
  - ***Allowing regional rural banks to participate in LAF/MSF window and call/notice money market.***

- **Conserve capital; defer dividend payout:** To shore up balance sheet and to support lending, it is imperative to conserve capital. ***RBI has decided that SCBs and cooperative banks shall not make any dividend payout for FY20.*** Different categories of NBFCs would be allowed to declare dividend as per a matrix of parameters, subject to a set of generic conditions. Banks can therefore look to upfront stress and absorb credit cost in FY21 itself to smoothen earnings momentum for FY22.

- **Digital push continues:** RBI proposes, at the user's discretion, to increase the limits for contactless card transactions and ***e-mandates for recurring transactions through cards (and UPI) to Rs5,000 from Rs2,000 effective Jan'21.*** The move clearly indicates RBI's intention to encourage the digital transaction platform. Recently, it disabled contactless feature on cards and empowered customers to control the limits on their cards, thereby adding safety for users.

Research Analysts:

Kunal Shah
kunal.shah@icicisecurities.com
+91 22 6637 7572

Renish Bhuva
renish.bhuva@icicisecurities.com
+91 22 6637 7465

Chintan Shah
chintan.shah@icicisecurities.com
+91 22 6637 7658

- **Promote inclusive growth and financial literacy:** Centres for financial literacy (CFL) were set up as pilot projects in 80 blocks (further extended to 100 blocks) to spread financial literacy. Now, to ensure ***its implementation at a grassroot level in a sustainable manner, RBI plans to expand it to every block in the country by 2024.***

- **Focus on financial inclusion and customer safety.** With increasing financial penetration and continued focus on further financial inclusion, customer service and resolution of customer complaints becomes an important aspect for the regulator. Notably, the regulator mandates banks to put in place a comprehensive framework comprising enhanced disclosures on customer complaints. Further, it announces a monetary disincentive in the form of recovery of cost of redress of complaints from banks when maintainable complaints are comparatively high.

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