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Banks get ₹3.7 tn lending boost with RBI-govt truce

CREDIT POLICY Deferment of capital reserve norms by a year to boost liquidity

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MUMBAI: The Reserve Bank of India (RBI) board's decision to extend the timeline for full implementation of Basel III rules for bank capital by a year will free up as much as ₹3.7 lakh crore for potential lending, a person with direct knowledge of the matter said on condition of anonymity.

The central bank's board on Monday decided that Indian banks will have to meet the capital conservation buffer norms under Basel III regulations by March 31, 2020, instead of the earlier deadline of March 2019.

The capital requirements rule is designed to ensure that banks build up capital buffers at times when credit is growing, which can be drawn down as losses are incurred during a stressed period. The capital conservation buffer in the form of common equity is being uniformly phased-in over a period of four years, or 0.625% a year, starting January 1, 2016.

The government and the RBI were locked in a bitter public stand-off on a host of issues, including a liquidity squeeze in the banking system. While the finance ministry holds the view that there is a shortage of liquidity, the central bank is of the view that the situation is much better.

The issue also came up for discussion during the Financial Stability and Development Council meeting chaired by finance minister Arun Jaitley. During that meeting, ministry officials asked the RBI not to let the liquidity issue faced by non-banks get out of hand, as there was a risk of it spilling over to other sectors. RBI officials, however, said there was robust credit growth, and it did not have any data which suggests that non-banking financial companies (NBFCs) were facing a liquidity crunch.

A decision on creating a special liquidity window for NBFCs may be taken in the next RBI board meeting on December 14. The RBI board also advised the central bank to let banks recast loans up to ₹25 crore given to micro, small and medium enterprises (MSMEs). However, two contentious issues on the transfer of surplus reserves and relaxing norms for weak banks were referred to committees.

Madan Sabnavis, chief economist at Care Ratings said the measures relating to MSMEs and capital adequacy will help small businesses as well as weaker banks. "The weaker banks will gain from the capital adequacy relaxation for sure. In a way, these two measures will also help the liquidity situation as banks will be able to lend more while restructuring stressed loans."

Moody's Investors Service said the decision to extend the timeline for the full implementation of Basel III guidelines by a year is credit negative for state-run banks. "It was our expectation that all public sector banks would have a core equity tier 1 (CET1) ratio of at least 8% by the end of March 2019, based on the government's commitment that it would capitalize all these banks to a level sufficient to meet the minimum regulatory capital norms. With the regulatory timelines now extended, it may be a case that at least some of the rated public sector banks' CET1 ratios over the next 12 months would be lower than what we currently expect," Srikanth Vadlamani, VP, financial Institutions group at Moody's said in the report.

Turning on the liquidity tap

- The decision to extend the implementation of capital conservation buffer will free up as much as ₹3.7 trillion for potential lending
- The extension of deadline will give the government breathing space on bank recapitalization, according to analysts
- Moody's says the extension of deadline for the implementation of Basel III norms is credit negative for state-run banks
- Recast of MSME loans will have a negative implication for the credit profile of banks, says the rating agency