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Development

- HDI by UNDP
  - summary measure of average achievement in key dimensions of human development: a long and healthy life, being knowledgeable and have a decent standard of living
  - geometric mean of normalized indices for each of the three dimensions.
  - health dimension is assessed by life expectancy at birth, the education dimension is measured by mean of years of schooling for adults aged 25 years and more and expected years of schooling for children of school entering age. The standard of living dimension is measured by gross national income per capita. The HDI uses the logarithm of income, to reflect the diminishing importance of income with increasing GNI
  - does not reflect on inequalities, poverty, human security, empowerment, etc
  - Devised in 1990 by Mahbub ul Haq
  - Latest is 2016 HDI; Norway at top with 0.949 HDI
  - India’s HDI was 0.624 – medium human development category; ranked 131
  - UNDP head is Achim Steiner; headoffice in New York

- Inequality Adjusted HDI by UNDP (IHDI)
  - IHDI combines a country’s average achievements in health, education and income with how those achievements are distributed among country’s population by “discounting” each dimension’s average value according to its level of inequality
  - Norway at top
  - India’s value 0.454; rank 135

- Gender Development Index by UNDP
  - GDI is the ratio of the HDIs calculated separately for females and males using the same methodology as in the HDI
  - GDI for India is 0.819

- Gender Inequality Index by UNDP
  - measures gender inequalities in three important aspects of human development—reproductive health, measured by maternal mortality ratio and adolescent birth rates; empowerment, measured by proportion of parliamentary seats occupied by females and proportion of adult females and males aged 25 years and older with at least some secondary education; and economic status, expressed as labour market participation and measured by labour force participation rate of female and male populations aged 15 years and older
  - India’s GII is 0.53 and rank is 125

- Multidimensional poverty index by UNDP
  - Published first time in 2010
  - index identifies deprivations across the same three dimensions as the HDI and shows the number of people who are multidimensionally poor (suffering deprivations in 33% or more of the weighted indicators) and the number of weighted deprivations with which poor households typically contend with
  - Indicators – nutrition, child mortality for health; children enrolled and headcount ratio for education and cooking fuel, toilet, water, electricity, floor and assets for standard of living
  - India MDPI is 0.282

Measurement of growth

- GDP provides one single number that represents the monetary value of all the finished goods and services produced within a country's borders in a specific period
- Real GDP or Gross Domestic Product (GDP) at constant (2011-12) prices in the year 2017-18 is likely to attain a level of `129.85 lakh crore
- GDP is derived by adding taxes on products net of subsidies on products to GVA at basic prices. GDP at current prices in the year 2017-18 is likely to attain a level of `166.28 lakh crore – Nominal GDP
- nominal Net National Income (NNI), also known as national income (at current prices) is likely to be `147.11 lakh crore during 2017-18
- per capita net national income during 2017-18 is estimated to be `111,782
• per capita income in real terms (at 2011-12 prices) during 2017-18 is likely to attain a level of `86660
• Real GVA, i.e, GVA at basic constant prices (2011-12) is anticipated to increase from `111.85 lakh crore in 2016-17 to `118.71 lakh crore in 2017-18
• Sectors reported upon
  o Agriculture, forestry and fishing
  o Mining and quarrying
  o Manufacturing
  o Electricity, gas, water supply and other utility services
  o Construction
  o Trade, hotels and transport & communication and services related to broadcasting
  o Financial, insurance, real estate and professional services
  o Public administration and defence and other services

Poverty lines
• First devised by Y K Alagh in 1979
  o The estimated calorie norm was 2400 kcal per capita per day in rural areas and 2100 kcal per capita per day in urban areas
  o consumer expenditure (food and non-food) of Rs.49.09 per capita per month was associated with a calorie intake of 2400 per capita per day in rural areas and Rs.56.64 per capita per month with a calorie intake of 2100 per day in urban areas. This Monthly Per Capita Expenditure (MPCE) was termed as poverty line
  o application of a single poverty line for all the states (though separate in rural and urban areas) implicitly, and dubiously assumes absence of price differential across the states. The estimate of poverty based on this methodology also assumed a fixed consumption basket of the poor overtime, and a uniform consumption basket for all the states
• Improved by Lakdawala expert group in 1993
  o The national rural and urban poverty lines of Task Force (Alagh) were disaggregated into state-specific poverty lines using inter-state price differentials measured by Fisher’s Index
  o All India urban poverty ratio = 25.7% (for 2004-05)
  o All India rural poverty ratio = 28.3% (for 2004-05)
• Further improved by Tendulkar expert group in 2009
  o did not construct a poverty line. It adopted the officially measured urban poverty line of 2004-05 based on Expert Group (Lakdawala) methodology and converted this poverty line (which is URP-consumption based) into MRPconsumption
  o URP-consumption = consumption data are collected from the households using 30 day recall period for all the items. MRP-consumption = consumption data for five non-food items viz., clothing, footwear, durable goods, education, and institutional medical expenses are collected using 365-day recall period and 30-day recall period for the remaining items.
  o The national urban poverty ratio in 2004-05 as per the Expert Group (Tendulkar) methodology is identical to the one estimated by the Expert Group (Lakdawala) methodology, which is 25.7 percent
  o Shift from URP to MRP significantly raised all India Urban poverty line level of MPCE (Monthly Per Capita Expenditure) from 538.6 to 578.8
  o Expenditure per month in 2011-12 – rural = Rs. 816; urban = Rs. 1000
  o Poverty ratios (2011-12)
    • Rural – 25.7%
    • Urban – 13.7%
    • Total – 21.9%
• Latest by C Rangarajan
  o Used Modified Mixed Recall Period (MMRP) - consumer expenditure data is gathered from the households using the recall period of: (a) 365-days for clothing, footwear, education, institutional medical care, and durable goods, (b) 7-days for edible oil, egg, fish and meat, vegetables, fruits, spices, beverages, refreshments, processed food, pan, tobacco and intoxicants, and (c) 30-days for the
remaining food items, fuel and light, miscellaneous goods and services including non-institutional medical; rents and taxes

- **New food basket** –
  - New calorie requirement - 2155 kcal per capita per day in rural areas and 2090 kcal per capita per day in urban areas
  - Also added are protein and fat requirements
    - Protein – 48 gms in rural areas and 50 gms in urban areas
    - Fat – 28 gms in rural areas and 26 gms in urban areas

- **Non food component of poverty line basket added** –
  - Based on education, clothing, shelter and mobility

- **Monthly Per-capita Consumption Expenditure (MPCE) of Rs 972 in rural areas and Rs 1407 in urban areas** constitute the new poverty lines at the all-India level; Rs.1106 for all India

- This translates to $ 2.14 per capita per day for Rural India, $ 3.10 per capita per day for Urban India and $ 2.44 per capita per day for the country as a whole in PPP terms

- **Poverty ratios (2011-12)**
  - Rural – 30.9%
  - Urban – 26.4%
  - Total – 29.5%

  - According to World Bank
    - Poverty headcount ratio in India in 2011 at $1.9 a day = 21.2%

**Poverty alleviation programmes**

- **1952** – Community development programmes; later modified into the form of sectoral approach through Intensive Agricultural District Programme in the 70s
- **1970** – resource based development approach, Drought Prone Area Programme
- **1970** – Small Farmer Development Agency and Marginal Farmers and Agricultural Labourers; later both these schemes were combined and renamed as District Rural Development Agency
- **1970** – Hill Area Development Programme and Tribal Area Development Programme
- **1978** – Integrated Rural Development Programme (later Swarnajayanti Gram Swarozgar Yojana) is the single largest anti-poverty programme for small and marginal farmers, agricultural and non-agricultural labour, rural artisans and craftsmen and SCs and STs – main thrust was to transfer assets and resources to broaden production base; to raise BPL families above the poverty line by creation of sustainable opportunities for self employment in rural sector
- **Command Area Development Programme** – to maximize utilization of the limited resources of land and water through reduction of loss of water through seepage, extend areas under irrigation, increase cropping intensity etc
- **1977** – Desert Development Programme
- **1977** – Minimum Needs Programme for providing social services like elementary education, community health services, rural water supply, rural roads, rural electrification
- Food for Work programme aimed at improving nutritional status, income and living standards through generation of additional gainful employment and creating community assets – wage employment in drought affected areas
- **1999** – Jawahar Gram Samriddhi Yojana; restructured version of Jawahar Rojagar Yojana
- **1995** – National Old Age Pension Scheme
- **1995** – National Family Benefit Scheme; provides 20k to a person of family who become the head of the family after the death of its primary breadwinner
- **1999** – Annapoorna to provide 10 kg of free food grains to eligible senior citizens
- **2006** – MGNREGA; 100 days of paid work guaranteed (150 days for tribals); employment on demand; under MGNREGA entitled to unemployment allowance if employment not provided within 15 days
- **2001** – Valmiki Ambedkar Awas Yojana (VAMBAY) – facilitates construction and upgradation of dwelling units of slum dwellers; community toilets under Nirmal Bharat Abhiyan
Five Year Plans

- Planning Commission formed on 15th March 1950; arm of Central Govt
  - First Dy Chairman was Gulzarilal Nanda
  - Last was Montek Singh Ahluwalia
- National Development Council set up on 6th August 1952
  - Comprises of PM, Cabinet Ministers, State CMs, reps of UTs and members of NITI Aayog
  - Extra constitutional, non statutory body
- Bombay Plan was published by 8 Indian industrialists in 1944-45 for post Independence planning roadmap
- Sarvodaya Plan by JP Narayan in 1950
- 1st – 1951-56
  - Harrod Domer Model
  - Main focus on agriculture
- 2nd – 1956-61
  - Mahalanobis model
  - Main focus on industrial development
- 3rd – 1961-66
- Plan holiday – 1966-69
- 4th – 1969-74
  - Gadgil Yojana
  - Nationalisation of 14 banks in 1969
  - Smiling Buddha nuclear test at Pokhran
- 5th – 1974-79
  - Top priority given to agriculture, employment and poverty alleviation (garibi hatao)
  - Prepared by D P Dhar
  - Terminated in 1978
  - Minimum Needs Programme in 1974
  - Twenty Point Programme launched in 1975
- 2 Rolling plans from 1978-80
- 6th – 1980-85
  - Poverty eradication and technological self reliance
  - Beginning of economic liberalization
  - Price controls eliminated and ration shops closed
  - NABARD established
  - Family planning expanded
- 7th – 1985-90
  - Objective of self sufficient economy
  - Pvt sector got priority over public sector for the first time
- 2 annual programs between 1990-92
- 8th – 1992-97
  - Top priority to HR – employment, education, public health
  - Narasimha Rao govt launched New Economic Policy of India
  - LPG reforms
  - Decentralization
- 9th – 1997-02
  - ‘growth with justice and equity’
- 10th – 2002-07
  - Twenty point programme reintroduced with modifications in 2006
- 11th – 2007-12
  - Prepared by C Rangarajan
  - Theme was Faster and more inclusive growth
- 12th – 2012-17
  - Faster, more inclusive and sustainable growth
**Industrial policy 1991**

- Govt monopoly
  - number of industries reserved for public sector was reduced from 17 (as per 1956 policy) to only 8 industries viz. Arms and Ammunition, Atomic Energy, Coal, Mineral Oil, Mining of Iron Ore, Manganese Ore, Gold, Silver, Mining of Copper, Lead, Zinc, Atomic Minerals and Railways
  - currently only 2 of above – atomic energy and railways are reserved for the public sector
- abolition of industrial licensing except those included in a small specified negative list
  - currently license is required only in 6 industries, namely, cigars and cigarette on the tobacco, industrial explosives, electronic, aerospace and defence equipment, industrial explosives and hazardous chemicals, drugs and pharma, alcoholic drinks
- approval for direct foreign investment upto 51% of equity in high priority sectors known as Appendix I industries was provided
  - currently around 90% of total FDI inflows are now through the automatic route.
  - Foreign Investment Promotion Board set up in 1990 was abolished in 2017; now there is a Foreign Investment Facilitation Portal under DIPP
  - The eleven notified sectors/activities requiring government approval are Mining, Defence/cases relating to FDI in small arms, Broadcasting, Print media, Civil Aviation, Satellites, Telecom, Private Security Agencies, Trading(Single, Multi brand and Food Products), Financial services not regulated or regulated by more than one regulator/ Banking Public and Private and Pharmaceuticals.
- automatic approval of technology agreement related to high priority industries within specified parameters. Indian companies were made free to negotiate the terms of technology transfer with their foreign counterparts according to their commercial judgement
- decided that MRTP (Monopolies and Restrictive Trade Practices ) Act, 1969 will be amended to remove threshold limits of assets in respect of MRTP companies and dominant undertakings. It also abolished the requirement of prior approval of the Central Government for establishing new undertaking
  - Currently, MRTP act is replaced by Competition Act 2002.

**SEZ Act 2005**

- Board of Approval is apex decision making body, headed by Secy, Dept of Commerce
- Duty free import/domestic procurement of goods for development, operation and maintenance of SEZ units
- 100% Income Tax exemption on export income for SEZ units under Section 10AA of the Income Tax Act for first 5 years, 50% for next 5 years thereafter and 50% of the ploughed back export profit for next 5 years.
- Supplies to SEZs are zero rated under IGST Act 2017
- Single window clearance
NIMZ (National Investment and Manufacturing Zones)

- conceived as large integrated industrial townships with state-of-the-art infrastructure; land use on the basis of zoning; clean and energy efficient technology; necessary social infrastructure; skill development facilities, etc., to provide a conducive environment for manufacturing industries
- These NIMZs would be managed by a Special Purpose Vehicle (SPV)
- To enable the NIMZ to function as a self government and autonomous body, it will be declared by the State Government as a Industrial Township under Article 243 Q (I) (c) of the Constitution
- Each NIMZ to have 5000 ha
- Envisioned in National Manufacturing Policy
- No Act of Parliament
- First NIMZ in Prakasam district of AP

Foreign Trade Policy 2015-20 introduces 2 new schemes in place of a plethora of schemes earlier

- Merchandise Exports from India Scheme for export of specified goods to specified markets and Services Exports from India Scheme
- There would be no conditionality attached to any scrips issued under these schemes
- Duty credit scrips issued under MEIS and SEIS and the goods imported against these scrips are fully transferable
- For grant of rewards under MEIS, the countries have been categorized into 3 Groups, whereas the rates of rewards under MEIS range from 2% to 5%. Under SEIS the selected Services would be rewarded at the rates of 3% and 5%.
- government has now decided to extend benefits of both the reward schemes (MEIS and SEIS) to units located in SEZs
- government has reduced the number of mandatory documents required for exports and imports to three, which is comparable with international benchmarks
- ‘Niryat Bandhu Scheme’ has been galvanized and repositioned to achieve the objectives of ‘Skill India’ – Niryat Bandhu is handholding scheme for entrepreneurs in export import
- Government aims to increase India’s exports of merchandise and services from USD 465.9 billion in 2013-14 to approximately USD 900 billion by 2019-20 and to raise India’s share in world exports from 2 percent to 3.5 percent.

World Development Report 2018 highlights

- Released by IBRD of WB
- Theme – LEARNING to realize education’s promise
- First ever report dedicated entirely to education

WTO issues

- Headquarters at Geneva
- Founded 1995
- DG – Roberto Azevedo
- 1948-1994 : GATT (General Agreement on Tariffs and Trade)
- Uruguay Round – final round before GATT ended and WTO came into effect (next round was Doha Round in 2001); Marrakesh Agreement marked the culmination of Uruguay Round and led to establishment of WTO
- Ministerial Conference – highest authority; 12th Conference to be hosted by Kazakhstan in Astana in 2020; MC11 was at Buenos Aires in 2017
- General Council is WTO’s highest level decision making body in Geneva, meeting regularly to carry out functions of WTO. It has reps (usually Ambassadors) from all member countries and have authority to act on behalf of ministerial conference; J S Deepak is India’s ambassador
- Subsidies in agriculture are identified by boxes
o Green box - in order to qualify, green box subsidies must not distort trade, or at most cause minimal distortion; They have to be government-funded (not by charging consumers higher prices) and must not involve price support. They tend to be programmes that are not targeted at particular products, and include direct income supports for farmers that are not related to (are “decoupled” from) current production levels or prices. They also include environmental protection and regional development programmes.

o Amber box - Nearly all domestic support measures considered to distort production and trade (with some exceptions) fall into the amber box; all domestic supports except those in the blue and green boxes; include measures to support prices, or subsidies directly related to production quantities.
  ▪ These supports are subject to limits: “de minimis” minimal supports are allowed (generally 5% of agricultural production for developed countries, 10% for developing countries)

o Blue box - This is the “amber box with conditions” — conditions designed to reduce distortion. Any support that would normally be in the amber box, is placed in the blue box if the support also requires farmers to limit production

Current issues facing Indian economy

RBI tussle with govt
  • Reasons
    o Govt insisting RBI stick to Basel norms on capital adequacy so that banks can lend more
      ▪ The Board, while deciding to retain the CRAR at 9%, agreed to extend the transition period for implementing the last tranche of 0.625% under the Capital Conservation Buffer (CCB), by one year, i.e., up to March 31, 2020
    o Govt seeking relaxation in PCA norms allowing banks to lend more
      ▪ banks under PCA, it was decided that the matter will be examined by the Board for Financial Supervision (BFS) of RBI
      ▪ Board also advised that the RBI should consider a scheme for restructuring of stressed standard assets of MSME borrowers with aggregate credit facilities of up to ₹ 250 million, subject to such conditions as are necessary for ensuring financial stability
    o Govt insisting that NBFCs are facing liquidity crunch and RBI should step in to resolve this
    o Govt eyeing RBI’s reserves
      ▪ Board decided to constitute an expert committee to examine the Economic Capital Framework of the RBI, the membership and terms of reference of which will be jointly determined by the Government of India and the RBI
      ▪ This is wrong because it weakens the balance sheet of the central bank and provides the wrong incentive to the govt as it weakens the incentive to control expansion of spending
  • Governments have sparred with the RBI before on the issue of autonomy, but the NDA government went one step further by starting consultations under Section 7 of the RBI Act, which gives the Centre the power to direct the RBI to act in specific ways
  • This was not a right measure since RBI’s autonomy is crucial in public interest because
    o Govt’s horizon of decision making is short term as there are always upcoming elections of some sort and govt needs to resort to populist alternatives where manifestos have not been delivered upon. by virtue of being nominated rather than elected, central bankers have horizons of decision-making that tend to be longer than that of governments, spanning election cycles. by their mandate central banks are committed to stabilise the economy over business and financial cycles, and hence, have to peer into the medium to long term. Unsurprisingly, central banks strive to build credibility through a series of difficult choices that reflect sacrificing short-term gains for long-term outcomes such as price or financial stability
PSBs constitute a major portion of India’s banking system. PSBs are owned by govt and regulated by RBI. If govt has influence over RBI, there will be a conflict of interest.

- Govt spends money, especially so before elections, which tends to increase inflation. Inflation erodes the value of savings of common man and hence RBI, as the monetary authority, has been given the legal mandate of keeping inflation at 4 ±2%
- Relaxation in bank capital requirements can lead to greater credit creation but also leads to increased lending to sub-prime assets and can result in financial crisis.
- Allowing foreign capital to flood into the economy can temporarily ease financing pressures of the govt but a sudden stop or exodus of this capital can trigger a collapse of exchange rate.

- How is RBI’s autonomy eroded
  - Appointing govt or govt affiliated officials to senior mgmt rather than technocrats
  - Eroding statutory powers of the central bank
  - Favouring discretionary or joint decision making with direct govt interventions
  - Setting up parallel regulatory agencies with weaker statutory powers

- Although govt being the representatives of the people have been given the power to override RBI, this power is meant to be used only in exceptional circumstances, say when RBI takes a drastic step when it is not called for or when RBI takes an irrational step. In that case, to bring back normalcy, it is ok for govt to impose Sec 7. But in a business as usual scenario, and especially when steps like PCA have been taken for the benefit of the banking sector, it was not right to make such a threat.

- Regulation of PSBs – RBI is statutorily limited in undertaking the full scope of actions against public sector banks (PSBs) – such as asset divestiture, replacement of management and Board, license revocation, and resolution actions such as mergers or sales — all of which it can and does deploy effectively in case of private banks.

**IL&FS issue? Why did it cause liquidity crunch in NBFCs?**

- What
  - L&FS Ltd, or Infrastructure Leasing & Finance Services, is a core investment company and serves as the holding company of the IL&FS Group – LIC largest shareholder with 25.34%
  - Defaulted in payment obligations of bank loans and failed to meet commercial paper redemption obligations and also defaulted on inter-corporate deposits
  - Debt to equity ratio of 18.7(should ideally be 2), total debt of about Rs. 91k crore
  - Due to IL&FS crisis, banks reluctant to lend to NBFCs

- Solutions
  - NCLT granted permission to the Centre to take over the board of IL&FS
  - NCLT appointed a 6 member panel to take over the mgmt of IL&FS with immediate effect – panel headed by Uday Kotak
  - RBI allowed banks to provide Partial Credit Enhancement to bonds issued by systemically important non-deposit taking NBFCs registered with RBI and Housing FCs registered with NHB
  - RBI injected liquidity in the system through a series of OMOs
  - Banks can use g-secs as level 1 high quality liquid asset equivalent to their incremental lending to NBFCs and HFCs
  - Capital funds lending limit for banks to a single non-infra NBFC has been hiked to 15% from earlier 10%

**Payments and Settlement Systems Act 2007 proposed amendments – dissent note**

- Payment systems are a sub-set of currency which is regulated by the RBI.
- The overarching impact of Monetary policy on payment and settlement systems and vice versa provides support for regulation of payment systems to be with the monetary authority.
There is an underlying bank account for payment systems which is under the purview of banking system regulation which is vested with the RBI.

Settlement systems are finally posted in the books of account of banks with the RBI to attain settlement finality. Regulating these entities goes hand in hand with the settlement function.

In India, the payment system is bank-dominated. Regulation of the banking systems and payment system by the same regulator provides synergy and inspires public confidence in the payment instruments.

Regulation of the Payment System by the Central Bank is the dominant international model for stability consideration.

IBC, 2016

Bankruptcy Law Reforms Committee was headed by T K Vishwanathan.

Comprehensive insolvency legislation encompassing all companies, partnerships and individuals (other than financial firms).

Corporate debtors – 2 stage process: Insolvency Resolution Process and Liquidation

- Creditor initiates IRP against a corporate debtor at the NCLT (defaulting debtor can also initiate)
- NCLT orders a moratorium on the debtor’s operations for the period of the IRP
- NCLT appoints an insolvency professional or 'Resolution Professional' to administer the IRP. The Resolution Professional’s primary function is to take over the management of the corporate borrower and operate its business as a going concern under the broad directions of a committee of creditors
- Creditors committee constituted by the IP
- Each decision of the creditors committee requires a 75% majority vote. Decisions of the creditors committee are binding on the corporate debtor and all its creditors
- The creditors committee considers proposals for the revival of the debtor and must decide whether to proceed with a revival plan or liquidation within a period of 180 days (subject to a one-time extension by 90 days)
- If RP not approved within 180(+90) days or 75% majority of creditor’s committee votes for liquidation or NCLT rejects the RP – liquidation
- NCLT passes an order for liquidation
- After the costs of insolvency resolution (including any interim finance), secured debt together with workmen dues for the preceding 24 months rank highest in priority. Central and state Government dues stand below the claims of secured creditors, workmen dues, employee dues and other unsecured financial creditors.

Individual/Unlimited partnerships

- Two distinct processes in case of insolvencies: automatic fresh start and insolvency resolution
- Under the automatic fresh start process, eligible debtors (basis gross income) can apply to the Debt Recovery Tribunal (DRT) for discharge from certain debts not exceeding a specified threshold, allowing them to start afresh
- The insolvency resolution process consists of preparation of a repayment plan by the debtor, for approval of creditors. If approved, the DRT passes an order binding the debtor and creditors to the repayment plan. If the plan is rejected or fails, the debtor or creditors may apply for a bankruptcy order.

Creditor driven insolvency process

Institutional infra

- Insolvency and Bankruptcy Board of India as the Insolvency Regulator whose functions include (i) overseeing the functioning of insolvency intermediaries i.e., insolvency professionals, insolvency professional agencies and information utilities; and (ii) regulating the insolvency process.
- Insolvency Resolution Professionals: class of regulated but private professionals having minimum standards of professional and ethical conduct; verifies the claims of the creditors, constitutes a creditors committee, runs the debtor's business during the moratorium period and helps the creditors in reaching a consensus for a revival plan. In liquidation, the insolvency professional acts as a liquidator and bankruptcy trustee
- Information Utilities: to collect, collate, authenticate and disseminate financial information of debtors in centralised electronic databases. The Code requires creditors to provide financial information of debtors to multiple utilities on an ongoing basis. Such information would be available to creditors, resolution professionals, liquidators and other stakeholders in insolvency and bankruptcy proceedings
- Adjudicatory authorities: NCLT and DRT; appeals against their decisions lie with NCLAT and DRAT and then with SC

Why IBC, 2016
- Earlier there were several laws that dealt with insolvency for companies, such as the Sick Industrial Companies Act, the Recovery of Debt Due to Banks and Financial Institutions Act, and Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI)
- investable money locked for a long time in litigations is the least preferred situation for business partners and lender
- bank unable to loan out more due to provisioning requirements
- companies unable to access new loans
- will help to ensure confidence of banks, foreign investors, associated companies in crisis mitigation mechanism related to business entities in the country
- An early resolution with sound principles will help the related parties like banks not to suffer from the failure of the business entity

Rupee depreciation
- Rise in crude oil prices
- Widening trade deficit
- US-China trade war means that outlook for Indian exports does not look very bright
- Turkey lira crisis – investors club both countries into the emerging markets section in investment models. So when investors get rid of Lira, they get rid of the Rupee too
  - Turkish Lira has depreciated a lot this year against USD owing to
    - the country’s deteriorating ties with the US (trade war) and other western nations which are sources of capital inflows into Turkey
    - Turkish President’s increasing authoritarianism leading to quelling of free and factual reporting by financial analysts and intervention in Turkey’s central bank’s functioning
    - political instability
    - high current account deficit
  - High inflation
- Interest rates in the US are rising, which is affecting capital flows to emerging markets
- RBI policy
  - it only intervenes to reduce volatility and does not target any particular level
  - Not allowing exchange rate to adjust on the downside will only increase the dependence on foreign debt
- Pros
  - Gradually depreciating rupee would help India as imports would go down and exports become more competitive in the international markets
- Cons
Costlier imports
Higher interest costs for companies that have borrowed from abroad

Resolution of stressed assets – revised framework (12th Feb 2018)

- Before revised framework
  - Asset Quality Review report by RBI that indicated that PSBs had higher NPAs than reported
  - Joint Lenders’ Forum – at least 75% creditors by value and 60% by numbers had to agree to the restructuring plan
  - Strategic Debt Restructuring plan – banks got right to convert full or part of their loans into equity shares
  - S4A (Scheme for Sustainable Structuring of Stressed Assets) – envisages determination of the sustainable debt level for a stressed borrower, and bifurcation of the outstanding debt into sustainable debt and equity/quasi-equity instruments which are expected to provide upside to the lenders when the borrower turns around

- After revised framework
  - Lenders shall identify incipient stress in loan accounts, immediately on default, by classifying stressed assets as special mention accounts (SMA) as per the following categories: SMA 0 for payment due between 0-30 days, SMA 1 for dues between 31-60 days, SMA 2 for dues between 61-90 days
  - Lenders shall report credit information, including classification of an account as SMA to Central Repository of Information on Large Credits (CRILC) on all borrower entities having aggregate exposure of ₹ 5 crore and above with them — defaults to be reported on weekly basis
  - All lenders must put in place Board-approved policies for resolution of stressed assets under this framework, including the timelines for resolution – called Resolution Plan
  - As soon as there is a default in the borrower entity’s account with any lender, all lenders – singly or jointly – shall initiate steps to cure the default. The resolution plan (RP) may involve any actions / plans / reorganization including, but not limited to, regularisation of the account by payment of all over dues by the borrower entity, sale of the exposures to other entities / investors, change in ownership, or restructuring
  - RPs involving restructuring / change in ownership in respect of ‘large’ accounts (i.e., accounts where the aggregate exposure of lenders is ₹ 100 crore and above), shall require independent credit evaluation (ICE) of the residual debt by credit rating agencies. For accounts over 500 crore, 2 ICEs required
  - For large accounts of Rs. 2000 crore+, RP to be implemented within 180 days. If not implemented, lenders to file insolvency application under IBC within 15 days
  - In case of restructuring, the accounts classified as ‘standard’ shall be immediately downgraded as non-performing assets (NPAs), i.e., ‘sub-standard’
  - Borrowers who have committed frauds/ malfeasance/ wilful default will remain ineligible for restructuring

- capital should be understood as the “own funds” used to create assets by banks, as against borrowed funds like deposits. The capital maintained by the bank merely shows the proportion of own funds brought in by the bank in the total funds deployed towards creating assets. There is a misconception that capital is a pile of money stacked away as some sort of “rainy-day fund”, and that the economy is deprived of that pile of money. The reality couldn’t be farther from the truth – the capital maintained by banks would have already been deployed on its balance sheet towards creating assets, including loans

PCA framework

- PCA framework was introduced in December 2002 as a structured early intervention mechanism designed to help banks regain health by preserving capital.
Revised PCA Framework was issued by the Reserve Bank on April 13, 2017
- PCA can thus be seen as first, stabilizing the banks at risk, and then, undertaking the deeper bank reforms needed for long-term viability of the business model of these banks
- Indicators to be tracked for Capital, asset quality and profitability would be CRAR/ Common Equity Tier I ratio, Net NPA ratio and Return on Assets respectively
- Leverage would be monitored additionally as part of the PCA framework
- Breach of any risk threshold (as detailed under) would result in invocation of PCA
- Currently Capital Conservation Buffer is 1.875%, addition of 0.625% delayed to 2020
- Min CET 1 capital ratio is 5.5%
- Min Tier 1 capital ratio is 7%
- Min Total capital ratio is 9%
- Based on tracked indicators crossing certain defined thresholds, banks are put under PCA and restrictions are imposed upon them for example
  - Upon crossing risk threshold 1, there is a restriction on dividend distribution/remittance of profits and promoters are required to bring in additional capital
  - Upon crossing risk threshold 2, in addition to above, there is restriction on branch expansion and higher provisions are required
  - Upon crossing risk threshold 3, in addition to above, restriction imposed on management compensation

**Basel norms**
- Basel rules are an internationally accepted regulatory framework providing minimum standards to be met by banks
- Basel II norms hinged on three pillars – capital adequacy, supervisory review, and market discipline. In particular, capital charges were to be made for credit risk, market risk and operational risk that banks faced.
- Basel III norms
  - stricter requirements for the quality and quantity of regulatory capital, in particular reinforcing the central role of common equity;
  - an additional layer of common equity - the capital conservation buffer - that, when breached, restricts discretionary pay-outs to help meet the minimum common equity requirement;
  - a countercyclical capital buffer, which places restrictions on participation by banks in system-wide credit booms with the aim of reducing their losses in credit busts;
  - a leverage ratio - a minimum amount of loss-absorbing capital relative to all of a bank's assets and off-balance sheet exposures regardless of risk weighting;
  - liquidity requirements - a minimum liquidity ratio, the Liquidity Coverage Ratio (LCR), intended to provide enough cash to cover funding needs over a 30-day period of stress; and a longer-term ratio, the Net Stable Funding Ratio (NSFR), intended to address maturity mismatches over the entire balance sheet; and
  - additional requirements for systemically important banks, including additional loss absorbency and strengthened arrangements for cross-border supervision and resolution
- Under Basel III norms, unexpected losses are a function of the cumulative default rates (CDR) observed in the credit ratings provided by the credit rating agencies (CRAs). The CDR is nothing but the probability of a non-default rating assigned by a CRA turning into a default rating within a certain period of time. Based on internationally observed CDRs and recovery rates, Basel norms have prescribed risk weights for various credit exposures. However, the CDRs and the loss given default observed in India are much higher than that observed internationally. With this kind of default behaviour, applying the Basel specified risk weights would understate
the true riskiness in the loan assets carried on the books of Indian banks. As the need for repeated recapitalisation has proved, banks in India need to aspire to have higher capital levels.

- Provisions (made from current earnings) are to cover expected losses while level of capital maintained by the bank is for covering unexpected losses. If banks don’t have adequate capital, losses erode into deposits. Banks have to maintain adequate capital to ensure that the probability of deposits being eroded is close to zero.

**Latest RBI circulars**

- decided by the Government of India to increase w.e.f. November 02, 2018 Interest Equalisation rate from 3% to 5% in respect of exports by the Micro, Small & Medium Enterprises (MSME) sector manufacturers under the Interest Equalisation Scheme on Pre and Post Shipment Rupee Export Credit.
- RBI has decided to conduct purchase of Government securities under Open Market Operations (OMOs) for an aggregate amount of ₹ 400 billion in the month of December 2018.
- Govt announced a Rs. 2.1 lakh crore recapitalization plan for PSBs – 80k crore through recap bonds, 8k crore as budgetary support (total 1.5 lakh crore from govt capital infusion).
- Latest MPC : keep the policy repo rate under the liquidity adjustment facility (LAF) unchanged at 6.5 per cent.

**Speeches**

- Capital Account Convertibility by G Padmanabhan in 2015
- PCA framework by Viral Acharya
- Banking regulator independence from govt by Viral Acharya
- Banking regulatory powers should be ownership neutral by Urjit Patel

**India’s banking sector related**

**Capital Account Convertibility**

- Capital account convertibility means the freedom to convert rupees into foreign currency and back for capital transactions. India has current account convertibility but not capital account convertibility.
- Macro-economic parameters have to be stable before it is implemented
  - The low current account deficit should be sustained
  - Fiscal deficit needs to be contained
  - The rupee as a currency should be more frequently traded internationally
- Leads to free exchange of currency at lower rates and an unrestricted mobility of capital
- Beneficial for a country because inflow of foreign investment increases, allowing companies to borrow at lower costs and fuelling growth
- The flip side, though, is that it could destabilize an economy due to massive capital flows in and out of the country.

**History of India’s banking sector?**

- In 1969 the Indian government nationalised 14 major private banks
- In 1980, 6 more private banks were nationalized
- Regional Rural Banks (RRBs) also known as Gramin banks, are Indian scheduled banks (Government banks) operating at regional level in different States of India. They have been created with a view of serving primarily the rural areas of India with basic banking and financial services
- The short-term co-operative credit structure operates with a three-tier system - Primary Agricultural Credit Societies (PACS) at the village level, Central Cooperative Banks (CCBs) at the district level and State Cooperative Banks (StCBs) at the State level.
- PACS are outside the purview of the Banking Regulation Act, 1949 and hence not regulated by the Reserve Bank of India. StCBs/DCCBs are registered under the provisions of State Cooperative Societies Act of the State concerned and are regulated by the Reserve Bank. Powers have been delegated to National Bank for Agricultural and Rural Development (NABARD) under Sec 35 A of the Banking Regulation Act (As Applicable to Cooperative Societies) to conduct inspection of State and Central Cooperative Banks.
- Primary Cooperative Banks (PCBs), also referred to as Urban Cooperative Banks (UCBs), cater to the financial needs of customers in urban and semi-urban areas.

Data from RBI doc from mains prep – critical parameters like NPAs, CAD, fiscal deficit etc
- CAD has ballooned to 2.9% of GDP in Q2 (July-Sept) of this financial year – USD 19.1bn as compared to USD 6.9bn last year
  - Due to high trade deficit of USD 50bn (half of this is due to petroleum, oil and lubricants)
  - 26% of our import is of oil
- FDI fell to USD 7.9bn in Q2 this year as against USD 12.4bn
- FPI recorded net outflow of USD 1.6bn as against inflow of USD 2.1bn last year
- Inflation was 3.3% in Oct (CPI was 140.6)
- The Reserve Bank currently has Rs 9.79 lakh crore in reserves - a sum equivalent to 28 per cent of its assets – transferred 50k crore to govt as
- Singapore banking system’s overall NPL ratio decreased from 2.1% in Q3 last year to 1.9% this year – local banks NPL ratio was 1.5%
- Forex reserves are around 393 bn USD
- GDP growth rate was 6.7% last year as per RBI annual report; expected to rise to 7.4% this financial year

FRBM Act 2003
- Act of the Parliament of India to institutionalize financial discipline, reduce India's fiscal deficit, improve macroeconomic management and the overall management of the public funds
- main purpose was to eliminate revenue deficit
- aim was to bring down fiscal deficit to 3% by 2008
- FRBM review committee – debt to GDP ratio of 60% should be targeted, fiscal deficit of 3% to be targeted