Daily Banking Digest

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'RBI plans tokenisation of assets, bonds under wholesale CBDC pilot'

The Reserve Bank of India (RBI) is expanding its wholesale Central Bank Digital Currency (CBDC) pilot to include tokenization of assets and government bonds. The focus is on testing technology rather than generating large transaction volumes. RBI Deputy Governor T Rabi Sankar also discussed the impact of Artificial Intelligence (AI) and quantum computing on banking and cybersecurity.

Key Points:

- **Tokenization Exploration:** The RBI will experiment with tokenized assets and government bonds in the wholesale CBDC pilot.
- **Technology Focus:** The primary goal is to evaluate the technology's capabilities, not to drive high transaction volumes.
- **CBDC Transaction Levels:** While initial CBDC pilot transactions reached 1 million, volumes have since decreased.
- **AI and Quantum Computing:** The RBI recognizes the significant impact of AI and quantum computing on encryption and cybersecurity, requiring potential overhauls to existing systems.
- **Adapting to Change:** Bankers must prioritize adapting to these rapid technological advancements to remain competitive.
- **Cybersecurity Challenges:** Changing requirements necessitate updates to cybersecurity systems and potentially relevant laws.

RBI conducts two VRR auctions to infuse liquidity.

The Reserve Bank of India (RBI) conducted two variable rate repo (VRR) auctions to address a widening liquidity deficit in the banking system. This action follows previous reverse repo auctions aimed at absorbing excess liquidity.

Key Points:

- **Liquidity Management:** The RBI uses VRR auctions to inject liquidity when there is a deficit and reverse repo auctions (VRRR) to absorb excess liquidity.
- **Auction Results:** Banks exhibited strong demand for funds in the 14-day VRR auction, with bids significantly exceeding the notified amount. The RBI also conducted a 3-day VRR auction.
- **Widening Liquidity Deficit:** The banking system's liquidity deficit increased substantially.
- **RBI Stance:** RBI Governor Shaktikanta Das emphasized that the current focus is on managing inflation through interest rate adjustments, while liquidity will be managed through various tools to ensure market stability.

HUDCO looks to increase its exposure to infra projects

HUDCO, traditionally focused on housing finance, is shifting its emphasis towards financing urban infrastructure projects to drive growth. This strategic shift reflects the evolving needs of the Indian economy.

Key Points:

- **Infrastructure Focus:** Infrastructure projects increasingly dominate HUDCO's loan book, while the housing segment's share decreases.
- **RBI Application:** HUDCO has applied to the RBI for registration as an Infrastructure Finance Company, further solidifying its commitment to the sector.
- **Financial Performance:** HUDCO's December quarter net profit doubled, and revenue saw significant growth.
- **Loan Activity:** While loan sanctions decreased compared to the previous year, disbursements increased.
- **Portfolio Composition:** Urban infrastructure projects now represent 49% of HUDCO's total loan portfolio.
- **Exposure in Maharashtra:** HUDCO has significant exposure to projects in Maharashtra and is planning to increase its financing in the state further.
- **Increased Borrowing:** HUDCO plans to nearly double its borrowing program to support its expansion into infrastructure financing.

PM Modi announces Bharat Ratna for Charan Singh, Narasimha Rao, and MS Swaminathan

Chaudhary Charan Singh, former Prime Minister of India, is to be posthumously awarded the Bharat Ratna, India's highest civilian honor, as announced by Prime Minister Narendra Modi. This award is to honor Singh's dedication to farmers' rights and welfare throughout his political career. Additionally, agricultural scientist MS Swaminathan and another former Prime Minister, PV Narasimha Rao, will also receive the Bharat Ratna. This selection signifies the government's focus on agriculture and is a nod to contributions from non-BJP leaders and the southern part of India. Charan Singh's long political journey included various key roles, reflecting his commitment to democracy and the agricultural sector.

EV subsidy cut to 15 per cent given the inroads made in the market: Ministry

The Indian government has revised its electric vehicle (EV) subsidy program to focus on consumer incentives and boost domestic manufacturing. These changes aim to promote wider EV adoption and accelerate India's transition to clean mobility.

Key Points:

- **Reduced Subsidies:** The subsidy for electric two-wheelers (e-2Ws) has been reduced from 40% to 15% of the ex-factory price.
- **Consumer Focus:** Instead of directly subsidizing manufacturers, the government will now provide incentives to buyers, lowering the upfront cost of EVs.
- **Production-Linked Incentives (PLI):** Two PLI schemes are being implemented to boost domestic EV manufacturing and increase exports.
- **Increased FAME II Outlay:** The budget for the FAME India scheme phase-II has been increased to ₹11,500 crore to support clean mobility initiatives.
- **Positive EV Sales:** As of February 6, 7,34,760 units of e-2Ws were registered in the current fiscal year, demonstrating growing EV adoption.

PLI textiles: Govt considering adding more items, extending gestation period.

The Indian government is considering changes to the Production Linked Incentive (PLI) scheme for textiles to make it more appealing to investors. These changes aim to address industry concerns and boost investment in the sector.

Key Points:

- **Expansion of Product Coverage:** The government may include additional manmade fibre (MMF) garments and fabrics in the PLI scheme to broaden its scope.
- **Extended Gestation Period:** The time allowed for investors to set up operations may be extended from two to three years, providing more flexibility.
- **Stakeholder Input:** The Department for Promotion of Industry and Internal Trade (DPIIT) has considered recommendations from the Textile Ministry and industry stakeholders to improve the PLI scheme's effectiveness.
- **Surplus Funds:** The PLI scheme for textiles initially had unallocated funds, indicating room for adjustment to attract more investment.
- **PLI Scheme Goals:** The broader PLI scheme, covering various sectors, aims to create manufacturing champions, generate jobs, and increase revenue.

RBI ups remuneration ceiling of pvt sector banks' Non-Executive Directors by ₹10 lakh to ₹30 lakh per annum

The Reserve Bank of India (RBI) has increased the maximum allowable compensation for Non-Executive Directors (NEDs) in private sector banks to attract and retain qualified individuals.

Key Points:

Increased Remuneration Ceiling: The RBI has raised the annual compensation limit for private sector bank NEDs (excluding the Chair of the Board) from ₹20 lakh to ₹30 lakh.

- **Scope of Applicability:** The revised limit applies to private sector banks, Small Finance Banks, Payment Banks, and wholly-owned subsidiaries of Foreign Banks.
- **Rationale:** The increase recognizes the important role of NEDs in ensuring strong bank governance and oversight.
- **Approval Process:** Banks must establish appropriate criteria for fixed remuneration of NEDs, subject to Board approval.
- **Disclosure Requirements:** Banks must disclose director remuneration annually in their financial statements.

RBI discourages public deposits for NBFCs as norms not at par with banks.

RBI Deputy Governor M. Rajeshwar Rao defended the RBI's restrictive approach towards allowing NBFCs (Non-Banking Financial Companies) to accept public deposits. He emphasized that such restrictions are necessary to maintain financial stability and that NBFCs benefit from less stringent regulations compared to banks.

Key Points:

- **Deposit Acceptance and Safety Nets:** Allowing NBFCs to accept public deposits would necessitate increased regulation, supervision, and the creation of safety nets like deposit insurance, adding complexity and risks.
- **NBFCs as Niche Players:** Rao argues that NBFCs thrive as specialized entities and becoming more bank-like would be counterproductive. The RBI aims to discourage deposit-taking NBFCs.
- **Regulatory Differences:** While regulations for upper-layer NBFCs have been strengthened, significant differences remain compared to banks. NBFCs have lower capital requirements, less rigorous licensing scrutiny, and greater flexibility in their operations.
- **Limited Deposit-Taking NBFCs:** The RBI has not issued any new certificates for NBFCs to accept public deposits since 1997, reflecting its restrictive policy stance.

Paytm appoints advisory group headed by former SEBI chairman M. Damodaran.

One 97 Communications, Paytm's parent company, establishes a Group Advisory Committee led by former SEBI Chairman M. Damodaran to improve compliance and address regulatory concerns. This move follows RBI sanctions against Paytm Payments Bank for regulatory violations.

Key Points:

- **Advisory Committee Formation:** One 97 Communications creates a committee to strengthen compliance and regulatory adherence.
- **Expert Guidance:** The committee includes former SEBI Chairman M. Damodaran, alongside other seasoned financial professionals.

- **Response to RBI Action:** This initiative is likely a response to recent RBI sanctions imposed on Paytm Payments Bank.
- **Commitment to Compliance:** One 97 Communications expresses its commitment to sustainable growth within a framework of regulatory compliance.

Gautam Adani secures ore for world's largest single-location copper smelter in Gujarat

Gautam Adani's conglomerate secures contracts for copper concentrate supply to fuel its new, large-scale copper smelter in India. This move aims to meet growing domestic demand and positions Adani as a significant player in the global copper market.

Key Points:

- **Copper Smelter Capacity:** Adani's new smelter will have an initial capacity of 500,000 tons, expanding to 1 million tons by 2029 to cater to India's projected doubling of copper demand.
- **Supply Contracts:** Adani has secured both short- and long-term copper concentrate supply agreements.
- **Global Market Dynamics:** The smelter's launch coincides with a shortage of copper concentrate globally, potentially leading to production cuts by other smelters.
- **Adani's Strategy:** Adani seeks resource security in critical minerals and positions itself as a low-cost, competitive producer in the copper market.

RBI to tap NHAI, NPCI to fix rescue plan for Paytm users

The Reserve Bank of India (RBI) is coordinating with various stakeholders, including NHAI and NPCI, to manage the migration of merchants and consumers from Paytm Payments Bank Ltd. (PPBL), which is currently facing regulatory issues. The RBI will release FAQs to address concerns arising from its recent restrictions on PPBL, which include a ban on new deposits and customer onboarding. RBI Governor Shaktikanta Das emphasized the importance of bilateral engagement and proportionate regulatory actions to maintain systemic stability and protect customer interests.

Key Points:

- RBI to hold meetings with NHAI and NPCI to finalize the transition plan for Paytm users.
- Upcoming FAQs by RBI aim to guide merchants through the transition following PPBL restrictions.
- PPBL was prohibited from accepting new deposits or onboarding customers due to non-compliance issues.
- RBI stresses the need for bilateral engagement and timely corrective actions with regulated entities.
- Paytm is working on transitioning payment interfaces and codes to other banks.
- The RBI's actions are intended to ensure financial system stability and protect customers.

Disruptions in Red Sea route likely to raise freight and forwarding cost by 25-30 pc: Report

Disruptions in the Red Sea route are expected to cause a significant increase in freight and forwarding costs for companies engaged in international trade, with a larger impact on the agriculture and textiles sectors. This will extend the working capital cycle and may lead to increased borrowing, particularly for sectors with already rising leverage.

Key Points:

- Freight and forwarding costs may surge by 25-30% due to Red Sea route disruptions.
- The working capital cycle could be prolonged by 15-20 days.
- Sectors like agriculture and textiles might face greater challenges.
- Large entities might handle the cost increase, but supply chain delays are a concern.
- Medium-sized businesses face dual challenges with costs and supply chain issues.
- Freight rates have already increased by 150% in the past 45 days.
- Significant portions of India's oil imports and exports are affected by the route change.
- Shipping lines rerouting around the Cape of Good Hope increases transit time and costs.
- Potential for further delays due to operational challenges.
- 20-25% of India's foreign trade through the Suez Canal is impacted, affecting key export and import commodities.
- The crisis leads to higher shipping costs, reduced export volumes, and inflationary pressures.

RBI deputy governor flags business risks for NBFCs

RBI Deputy Governor M. Rajeshwar Rao highlighted several risks associated with NBFCs, including their reliance on bank borrowing, questionable practices by P2P lenders, and high interest rates by microfinance institutions. Speaking at a CII summit, Rao stressed the importance of diversified funding sources for NBFCs and adherence to licensing conditions and regulatory guidelines.

Key Points:

- NBFCs show increased asset growth but face risks due to concentrated banking sector linkages and high leverage.
- Rao urged NBFCs to diversify funding sources and maintain underwriting standards.

- P2P lending practices raise concerns; Rao warns against breaches of licensing conditions.
- Microfinance institutions criticized for not passing benefits to borrowers and inflating margins.
- He referenced the high interest rates issue and loan waivers in Assam as a need for microfinance introspection.
- Concentrated business models in consumer and vehicle loans pose risks in economic stress.
- RBI calls for NBFCs to adopt risk mitigations above minimum regulatory standards.
- Regulatory disparities between banks and NBFCs noted, with the latter facing fewer restrictions.
- Rao mentioned that while the capital requirement is higher for NBFCs, it only covers credit risk as opposed to banks' coverage of multiple risk types.
- The RBI has not registered new NBFCs for public deposits since 1997, underlining a cautious approach towards deposit acceptance.

FAME II EV subsidies till March-end or until funds are available: Govt

The Indian government has extended the eligibility for electric vehicle (EV) subsidies under the FAME-II scheme until March 31, 2024, or until allocated funds are exhausted. The scheme's budget has been increased to incentivize the adoption of EVs, with a focus on electric two-wheelers, three-wheelers, and four-wheelers.

Key Points:

- FAME-II subsidies applicable for e-vehicles sold until March 31, 2024, or until funds run out.
- Budget for FAME-II has been increased from Rs 10,000 crore to Rs 11,500 crore.
- Rs 7,048 crore is designated for subsidies on electric two-wheelers, three-wheelers, and four-wheelers.
- Rs 4,048 crore allocated for capital assets grants and Rs 400 crore for the 'others' category.
- The move aims to promote clean mobility and increase the adoption of electric vehicles in India.

Foreign exchange reserves rise to one-month high of $622.47 bn: RBI

India's foreign exchange reserves have increased for a second consecutive week, reaching a one-month peak of $622.47 billion as of February 2. The rise is partly due to the Reserve Bank of India's (RBI) interventions to stabilize the rupee and adjustments in foreign currency assets.

Key Points:

- India's forex reserves hit a one-month high at $622.47 billion.
- The reserves saw a significant increase of $5.74 billion, the largest in about two months.
- RBI's market interventions aim to control volatility in the rupee's value.
- Forex reserves include India's reserve position with the IMF.
- During the reported week, the rupee appreciated by 0.2% against the dollar but ended the week slightly down.

Adani Group may run three Sri Lankan airports.

Adani Group is in talks with Sri Lankan authorities to manage three airports, including the main international airport in Colombo. This move aligns with Sri Lanka's tourism growth and the need to improve airport infrastructure. If successful, it would mark Adani Group's first international aviation venture, expanding their already significant presence in the country's ports and renewable energy sectors.

Key Points:

- Adani Group is negotiating management contracts for Bandarnaike International Airport, Ratmalana Airport, and Mattala Airport in Sri Lanka.
- The initiative is part of Sri Lanka's plan to enhance tourism infrastructure following a tourism resurgence, with 1.48 million foreign tourists in 2023.
- The involvement of the Adani Group in Sri Lanka's airport management could help expand facilities and enhance passenger experiences.
- The Adani Group has significant interests in Sri Lanka, including port development with US backing to offset Chinese regional influence.
- India remains the largest source market for Sri Lankan tourism, and the country is aiming for 2.3 million tourists in 2024 and 4 million by 2030.
- Investments are increasing in Sri Lanka's hospitality sector, with new international hotels and a homestay policy in development.
- The Sri Lankan economy is recovering, with current reserves of $4.4 billion, and the government is focusing on public-private partnerships for economic growth.

After RBI curbs, EPFO bars use of Paytm Payments Bank for PF claims

The Employee Provident Fund Organisation (EPFO) will stop processing deposits and credits to EPF accounts associated with Paytm Payments Bank Limited (PPBL) starting February 23, following RBI's restrictions on PPBL due to non-compliance issues.

Key Points:

- EPFO halts deposits and credits to EPF accounts linked with PPBL from February 23.

- RBI has restricted PPBL from conducting deposit or credit transactions post-February 29.
- EPFO has instructed its offices to not accept claims with PPBL accounts.
- EPFO had previously allowed EPF payments into Paytm and Airtel Payments Bank accounts.
- The RBI's decision stems from PPBL's non-compliance with regulatory warnings.
- RBI Governor Shaktikanta Das emphasized entities are given ample time to comply before action is taken.
- The RBI affirms its support for the growth of the fintech ecosystem in India despite this move.

Banks have to set down the rules of the game vis-a-vis use of AI right now: RBI DG Rabi Sankar

RBI Deputy Governor T Rabi Sankar has emphasized the urgency for banks to establish regulations for Artificial Intelligence (AI) usage to avoid future complications. He stressed the need for collaboration among technology, banking, and legal experts to address potential risks, especially in light of the Digital Data Protection Act.

Key Points:

- Banks are urged to define AI usage rules promptly to manage outcomes effectively.
- The legal framework needs to advance to keep pace with rapidly evolving technology.
- AI is transforming the financial sector with new services and products, improving efficiency and customer experience.
- The RBI report acknowledges AI's benefits in banking but warns of amplified risks and the need for governance frameworks.
- AI's opaque nature poses challenges for compliance with laws, regulations, and internal controls.
- Cybersecurity is highlighted as a critical area for banks, with an inevitability of breaches necessitating robust risk management and system reconfigurations.

Retail CBDC transaction volumes have settled below 10 lakh per day

RBI Deputy Governor T Rabi Sankar reported that daily transactions of the Central Bank Digital Currency for retail (CBDC-R) have slightly decreased after hitting the 10 lakh milestone in December 2023, attributing this to scalability and banks' capacity challenges. The focus is now on resolving these issues rather than on transaction volumes.

Key Points:

- CBDC-R reached a peak of 10 lakh transactions per day in December 2023 but has since seen a minor drop.
- The RBI addressed scalability and technical issues faced by banks in handling the high volume of transactions.
- The value of CBDC-R transactions is reportedly in "some crores," and periodic data will be released publicly.
- The focus is on understanding technology adaptation and consumer behavior rather than just transaction volumes.
- For the wholesale e-rupee (CBDC-W), the RBI is exploring new use cases like tokenization of government bonds rather than increasing volumes.
- The primary benefit of CBDC-W is expected to be in cross-border transactions, but RBI is currently focusing on domestic stabilization and testing before international implementation.

Rs 40,000-crore blow! FPIs dumped stocks from 7 sectors in January, but one bore the brunt of it.

Foreign portfolio investors (FPIs) reversed their bullish stance on Indian equities in January, offloading stocks worth Rs 40,300 crore ($4.8 billion) across various sectors after months of significant buying. Financial services saw the most extensive sell-off, with private banks, especially HDFC Bank, facing the biggest hit.

Key Points:

- After buying in the last quarter of 2023, FPIs sold heavily in January, particularly in the financial services sector.
- HDFC Bank experienced one of its worst monthly losses in recent times, due to disappointing earnings and subsequent downgrades.
- Other sectors like FMCG and automobiles also saw sell-offs, while media & entertainment, and metals & mining faced declines, with companies like Zee Entertainment witnessing a substantial drop.
- Despite being net sellers, FPIs continued to invest in IT, oil and gas, telecom, power, and capital goods sectors.
- FPI activities in the near term are expected to be influenced by US bond yield trends, global market dynamics, and India's potential inclusion in the JPMorgan Global Emerging Market bond index.
- While equities saw outflows, FPIs heavily invested in the Indian debt market, marking the highest inflows since June 2017.

Plan in works to compensate victims of financial frauds.

The Indian government is taking steps to combat rising cybercrime in the financial sector. Banks and financial institutions will implement new measures to protect customers, facilitate the return of stolen funds, and streamline incident reporting.

Key Points:

- **Action Plan for Fraud Victims:** Banks will develop plans to return funds to victims of fraudulent transactions.
- **Specific Phone Number Series:** Regular 10-digit phone numbers will be phased out for commercial use, replaced by designated series (e.g., '140xxx') to help identify spam.
- **Standardized Information Sharing:** Financial institutions will share data in a standardized format to aid law enforcement investigations.
- **24/7 Complaint Resolution:** Resources will be made available around the clock to address customer complaints promptly and improve fraud resolution rates.
- **Blocking Suspicious Handsets:** The Department of Telecommunications has blocked 1.4 lakh mobile numbers linked to fraud or disconnected lines.
- **Cyber Fraud Reporting Platform:** Banks will integrate with the Citizen Financial Cyber Fraud Reporting and Management System to streamline reporting.

Rich face crypto dilemma: To bet or not via foreign route.

Wealthy Indians are interested in cryptocurrency exchange-traded funds (ETFs), but face uncertainty due to regulatory concerns and banking restrictions. Some are investing using funds already held in overseas accounts, but the legality and tax implications are unclear.

Key Points:

- **ETF Appeal:** SEC-approved crypto ETFs offer legitimacy and a regulated investment option, attracting interest from Indian investors.
- **Regulatory Ambiguity:** While not explicitly banned, banks may refuse to transfer funds designated for crypto investment, reflecting the RBI's reservations about virtual digital assets (VDAs).
- **Tax Considerations:** Indian investors must report earnings from crypto ETFs within their income tax filings, regardless of regulatory ambiguity.
- **Indirect Investment:** Some residents have used existing offshore funds to invest in crypto ETFs, bypassing current restrictions.
- **Potential for Confusion:** Legal experts suggest that investment in crypto ETFs may fall under existing securities regulations, rather than specific VDA rules, creating a potential loophole.

On the cards: Automated reconciliation system to plug I-T mismatches.

The Income Tax (I-T) department in India is introducing an automated system to streamline the identification and resolution of mismatches between filed tax returns and processed information. This initiative aims to improve compliance and reduce taxpayer burden.

Key Points:

- **Automated Mismatch Detection:** The new system will flag discrepancies between taxpayer returns and information held by the I-T department.
- **Initial Focus:** The system will initially address mismatches from financial years 2021-22 and 2022-23.
- **Simplified Response:** Taxpayers will receive alerts via SMS/email and can reconcile mismatches through the compliance portal without submitting documents.
- **Potential for Updated Returns:** If unable to explain mismatches, taxpayers can file updated returns to correct any under-declarations.
- **Technology Enhancements:** The process leverages AI, ML, and NLP for efficiency and will gradually expand coverage.
- **Annual Information Statement (AIS):** The AIS plays a crucial role in driving increased tax compliance and collections.
- **E-verification and Updated Returns:** E-verification aids mismatch reconciliation, and under the I-T Act, taxpayers can file updated returns for two years with additional taxes if discrepancies remain unexplained.