



## MRUNAL'S ECONOMY WIN20CSP UPDATE PACK FOR 19'S BATCHES PILLAR#1

- ⇒ The advantage of buying Iphone, Oneplus, Nokia or AndroidOne series of phones is they provide (free) operating system updates/security patches for 2-3 years. I believe coaching industry too needs to adopt similar business practice.
- ⇒ So, this 'Win20CSP update patch/handout' is for my old batch students who had joined my economy classes anywhere between Jan-2019 to Jan 2020. It contains updates since the end of last year's UPSC Prelim-2019, including Full Budget 2019 (that came in July after election), (SkyBlue cover) Economic Survey 2018-19, (Purple cover) Economic Survey 2019-20, Budget-2020 and other Current Affairs Updates from newspapers

Take printout → fill up the blanks through my (FREE) lectures for this purpose → don't staple but punch them & add in your existing handout file, after appropriate pillars.

## 10: PILLAR#1A1: MONEY-BARTER TO BITCOIN KE UPDATES

### 10.1 🏠 COINS AND NOTES

#### 10.1.1 🏠 🧑🏻 🧑🏻 🧑🏻 RBI's App to help the blind identify currency notes

80 lakh people in India are blind (नेत्रहीन). To help them identify currency notes:

- Old series of Gandhi notes have square (50), triangle (100), circle (500) ~~diamond (1000)~~
- New series of Gandhi notes have bleed lines, raised printing of Gandhi etc.
- But, so many varieties of notes, difficult for them to remember size & shapes so,
- IIT Ropar developed Roshni App.
- 2020-Jan: RBI launched '\_\_\_\_\_ ' App. Mobile camera scan & identifies the note (Even if it's half folded), gives audio notification in Hindi/English, also works offline. But can't validate whether note is genuine or fake (Counterfeit). by \_\_\_\_\_ Software company has developed it for RBI. If a user is both blind and deaf, the app will identify note by giving different set of vibrations.

#### 10.1.2 🏠 Budget-2020: A museum for coins

- a museum on numismatics and trade (सिक्काशास्त्र और व्यापार का संग्रहालय) will be built at the historic 'Old Mint Building' in \_\_\_\_\_.

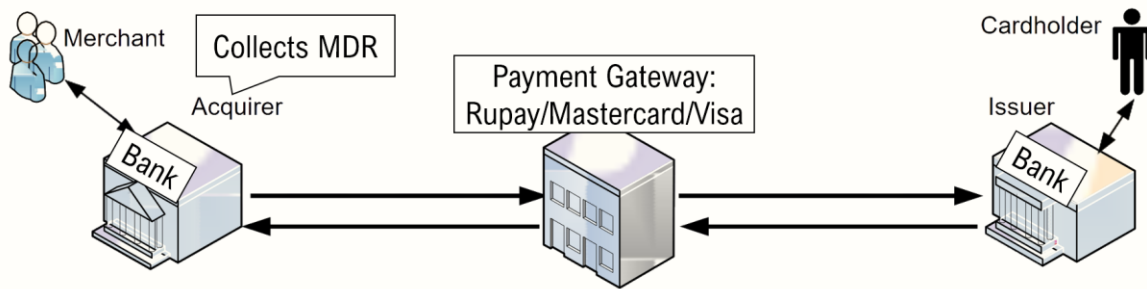
### 10.2 🏠 DIGITAL PAYMENTS / LESS CASH ECONOMY

#### 10.2.1 🏠 🏠 NEFT becomes free & available 24/7

	NEFT	RTGS	IMPS
Who runs	RBI	RBI	NPCI
Timing	- originally: not on holidays, not 24/7 - From 2019-Dec: 24/7 on all days. Although settlement at 30-30 min	Not on holidays Not 24/7	24/7 on all days
Fees?	- 2019-Jul: RBI waived the charges on NEFT and RTGS, & asked banks to pass benefit to customers.		Not free, though SBI & others gives free upto "₹.x"



### 10.2.2 📁 Digital Payment → MDR developments



- ⇒ Merchant Discount Rate (MDR: व्यापारिक छूट दर) is the fees that a merchant must pay to his (acquirer) bank for every credit / debit card transaction. MDR fees is shared among 3 parties
  - ✓ 1) customer's card issuing bank
  - ✓ 2) merchant's acquiring bank
  - ✓ 3) payment gateway provider e.g. Mastercard, Visa, Rupay
- ⇒ 2020: RBI allowed RRBs to act as acquiring banks. This will help expanding card network in rural areas.
- ⇒ **2019: Nirmala.S's Full Budget:** If biz.firm turnover > ₹ 50 crore → It must provide facility to accept Rupay debit card and UPI QR code. (Else penalty under Income Tax Act) → NO MDR on such transaction. RBI and Banks will absorb this 'burden' as a benefit of not handling so much cash. (Payments and Settlement Systems Act, 2007 rules amended for this part).

### 10.2.3 📁 New Umbrella Entity (NUE) for Retail Payments System (2019)

- ⇒ Presently, Paytm has rival companies like Mobikwick, Phonepe; Mastercard X Visa; SBI X Axis Bank; but there is no rival company against NPCi.
- ⇒ NPCi is an umbrella entity for retail payments system - it operates in card payment (RuPay), Money transfer (IMPS), Mobile Apps (UPI, BHIM), ATM Network (NFS) etc.
- ⇒ 2020-Feb: RBI issued a draft proposal, "if any Indian company interested to compete in this (NPCi-like) retail payment segment, we'll license them as new umbrella entity (NUE: खुदरा भुगतान के लिए नई छतरी इकाई). Subject to these technical "XYZ" eligibility requirements."
- ⇒ **Benefits?** More companies like NPCi → more competition → more Innovation and cheaper services for users. But, still in the draft stage, so **#DONT-LOSE-SLEEP**

### 10.2.4 📁 National Common Mobility Card (NCMC, 2019)

**Ministry of Housing & Urban Affairs (MoHUA)** got India's 1st indigenously developed 'One Nation One Card Model' with the help of NPCi, Bharat Electronics Limited (BEL), CDAC and some banks. It has 3 components:

- ⇒ **1) NCMC Card:** To be issued by banks. Nature can be Debit/Credit/Prepaid. Can be used for metro, bus, suburban railways, toll, parking, smart city payments and retail shopping.
- ⇒ **2) SWEETKAR:** Automatic Fare Collection System.
- ⇒ **3) SWAGAT:** Swachalit / Automated Gate.



### 10.2.5 🚗💳 FASTag for paying toll fees at highways (2017)

FASTags are prepaid rechargeable tags that allow for automatic toll collection at electronic toll collection gates Radio-frequency Identification (RFID) technology.

- ✓ 2013 onwards Govt required vehicle manufactures to install RFID tags on windscreens.
- ✓ 2017: National Highways Authority of India (NHAI, a statutory body under Highways ministry) launched 2 mobile apps **MyFASTag** and **FASTag Partner** to facilitate Electronic Toll Collection (इलेक्ट्रॉनिक पथकर/टोल वसूली).
- ✓ Persons loads up ₹ ₹ in his mobile app → activates RFID tag in his car → when it passes through highway toll-booth, the money is automatically deducted = faster traffic movement. (and **hidden benefit**: tracking of vehicle theft, criminal's movement etc)
- ✓ FASTag is vehicle specific and once it is affixed to a vehicle, it cannot be transferred to another vehicle.
- ✓ NPCi's has **National Electronic Toll Collection (NETC)** provides technological support.
- ✓ Highways Ministry is also trying to bring **inter-operability (आंतरसंचालनीयता)** of the FASTags i.e. single FASTag can be used for paying ₹
  - at State Highways Toll Plaza (under State Governments' purview) as well as
  - at National Highways Toll Plaza (under Union Government's purview).
- ✓ From 15<sup>th</sup> January 2020, it shall be mandatory for all vehicles passing through tolls to have FASTags. Vehicles without FASTags will have pay up 2x normal rates at toll gates.

### 10.2.6 🏦💳 RBI's Nandan Nilekani Panel (2019: Jan to May)

Nilekani (Ex-chairman of UIDAI) gave total 70+ suggestions. Notable among them are:

#### Suggested Reforms @Government

- ⇒ Under Direct Benefit Transfer (DBT: प्रत्यक्ष लाभ अंतरण) mechanism, Government transfers subsidies and payments directly to beneficiaries account such as MGNREGA or Pahal-LPG subsidy. But poor people withdraw cash from bank account entirely because local merchants not accepting digital payments. So, raise awareness about BHIM-UPI and its adoption.
- ⇒ Government's MDR subsidy expires on 2019-Dec. Extend it for another 2 years.
- ⇒ Give companies tax incentives (कर प्रोत्साहन) for using digital payments. Reduce the taxes on the devices required for digital payments.
- ⇒ Government organizations should not charge **convenience fees (सुविधा शुल्क)** from citizens while accepting digital payments. GSTN portal should allow card payments.
- ⇒ **National Common Mobility Card (NCMC)**: Allow its usage in all transit routes and PoS. Future mobiles may have NFC technology, then cards may become redundant anyways.
- ⇒ Setup **Computer Emergency Response Team** for finance (FIN- CERT: आपातकालीन प्रतिक्रिया टीम).



#### Nilekani's Suggested Reforms @RBI

- ⇒ RBI should prepare area wise '**Digital Financial Inclusion Index**' (डिजिटल वित्तीय समावेशन सूचकांक) to monitor progress & take remedial steps. Ensure no user is more than 5 kms away from a banking access point. Local vendor should be made Banking Correspondent (BC: बैंकमित्र).



- ⇒ Setup an **Acceptance Development Fund** (डिजिटल भुगतान स्वीकृति विकास निधि) to develop digital payment infrastructure in poorly served areas e.g. subsidy on PoS devices. RBI and Banks should co-contribute ₹ ₹ in this fund.
- ⇒ Reduce the MDR / card payment fees. Allow customer to do “x” no. of digital payment transactions per month with no charges.
- ⇒ RBI should make NEFT available 24/7 and review charges on its usage. (2019-June: RBI removed charges on both NEFT and RTGS and asked the banks to pass on the benefits to customers.)



#### **Nilekani's Suggested Reforms @NPCi**

- ✓ NPCI should offer RuPay and BHIM UPI in other countries to facilitate remittance to India.
- ✓ Encourage local language apps/ software for digital payments.

Nilekani also suggested many technical reforms but not imp4exam

**MCQ. Who among the following was the Chairman of the Committee on Deepening Digital Payments appointed by the RBI ? (Asked in CDS2019-II-Q116)**

- (a) H.R.Khan      (b) Nandan Nilekani      (c) N.R.Narayana Murthy      (d) Sanjay Jain

#### **10.2.7 Payment and Settlement Systems in India: Vision 2019 - 2021**

RBI published this document in 2019-May. it repeated most of the points that Nilekani report said. As such not much IMP unless preparing for RBI exams, then

[rbi.org.in/Scripts/PublicationVisionDocuments.aspx?Id=921](https://rbi.org.in/Scripts/PublicationVisionDocuments.aspx?Id=921)

### **10.3 MONEY'S EVOLUTION → CRYPTOCURRENCY**

#### **10.3.1 Cryptocurrency & India → RBI ban revoked by SC**

Since 2013, RBI had been warning Indians not to get involved in cryptocurrency due to frauds, tax evasion and terror finance.

- 2018: RBI directed all banks/NBFCs/PPI/mobile-wallet companies to stop relations with any Cryptocurrency company.
- Then certain cryptocurrency exchange website companies like CoinDCX etc went to SC alleging that
  - o Parliament has not made any law declaring this activity as illegal (unlike possession cocaine / narcotics.)
  - o Even Japan, USA, Singapore etc has not completely banned investment in cryptocurrency but imposed regulations to control its misuse/fraud.
  - o Anekantavada philosophy of Jainism: 4 blind men try to describe an elephant but end up describing only one physical feature of the elephant.
  - o Similarly, without fully studying the nature/impact of cryptocurrency, a blanket ban was placed, which has killed their business since no bank is opening their bank accounts.
- 2020-March: SC revoked the RBI ban because:
  - o Article \_\_ \_\_ \_\_ \_\_: All citizens have the right to practise any profession (व्यवसाय का हक)- including those companies dealing with cryptocurrency.



- o Same objective (financial fraud protection) could be achieved by imposing a less drastic ban.
- o So, RBI ban did not pass the test of \_ \_ \_ \_ \_ (अनुपातिकता की परीक्षा).

**What next?** 🐼 RBI may release a calibrated regulation on cryptocurrency e.g. PAN card required, can't invest more than ₹"x" lakh per month etc. topic is still developing.

### 10.3.2 🌐🔗🔒 Cryptocurrency & India → 🏛️ Banning of Cryptocurrency Bill, 2019

- ⇒ Ministry of Finance → Department of Economic Affairs has proposed a draft bill called the 'Banning of Cryptocurrency & Regulation of Official Digital Currency Bill, 2019' (क्रिप्टोक्यूरेंसी पर प्रतिबंध और आधिकारिक डिजिटल मुद्रा का विनियमन विधेयक, 2019).
- ⇒ It aims to ban the use of all types of cryptocurrencies issued by private operators. Non-bailable offense (गैर-जमानती अपराध), jail upto 10 years.
- ⇒ However, (if and when) RBI launches a blockchain-based digital currency, it'll be permitted. Anyways, the Bill still in the draft stage, so #DONT-LOSE-SLEEP

### 10.3.3 🌐🔗🔒 Cryptocurrency & world → Stable-coins

Stablecoin is a type of cryptocurrency whose price is backed by a reserve asset like gold / dollar / fiat currency e.g. Facebook's proposed \_ \_ \_ , Tether, Basecoin, and TrueUSD.

- ⇒ But, stablecoins also have challenges: 1) money laundering (धनशोधन / काले धन को वैध बनाना) 2) terror financing (आतंकी वित्तपोषण) 3) lack of consumer protection (उपभोक्ता संरक्षण की कमी) 4) financial frauds (वित्तीय धोखाधड़ी).
- ⇒ 2019-Dec: **European Union** announced, "No stable coins shall be allowed in the EU until we frame law for it."
- ⇒ 2019-Jun: G20 summit at **Osaka, Japan**. The leaders announced similar precautions.

### 10.3.4 🌐🔗🔒 Cryptocurrency & world → UNICEF's Crypto Donation Fund

- UN International Children's Emergency Fund (UNICEF, HQ- New York, USA; 1946)
- 2019-Oct: UNICEF setup a Cryptocurrency Fund to accept donations in cryptocurrencies. It has become the first UN organization to accept cryptocurrency



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## 11 PILLAR#1A2: MONETARY POLICY

### 11.1 ES20 DATA ON MONEY SUPPLY

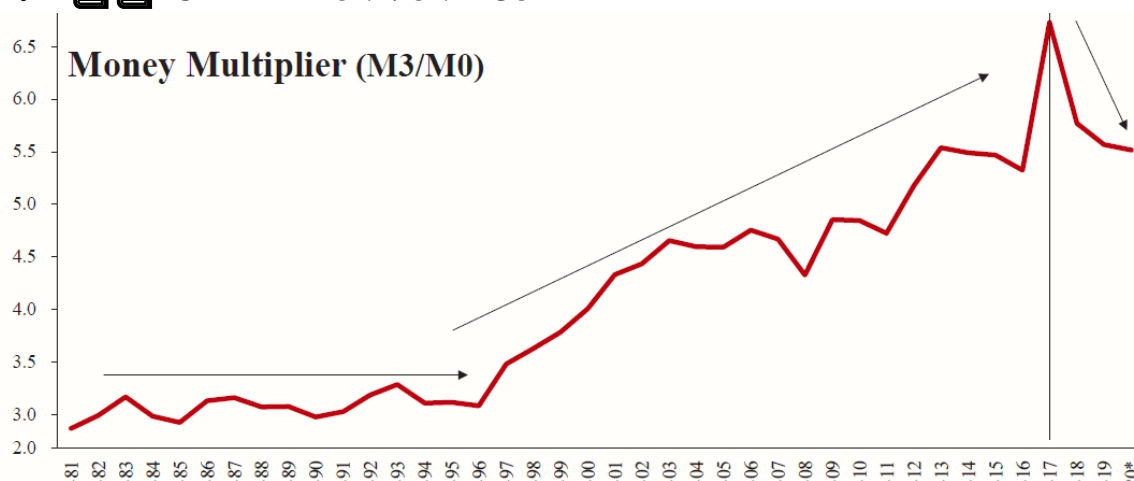



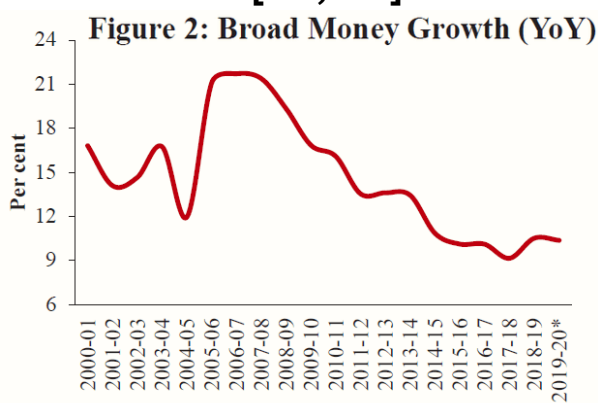
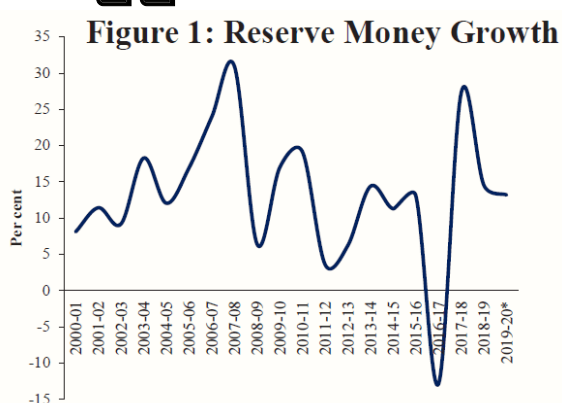
Figure 1: zigzag pattern means 'not increasing steadily'.

 ES20: Between mid-1990's to 2016-17: Money multiplier (measured as a ratio of M3/M0) was mostly increasing. But 2017-18 onwards: Money Multiplier is declining. Could be attributed to the lack of growth in loaning activities & slowdown in economy.

 ? Money Multiplier in an economy increases with \_\_ \_\_? (Asked in Pre-2019)

- A. Increase in the cash reserve ratio
- B. Increase in the banking habit of the population
- C. Increase in the statutory liquidity ratio
- D. Increase in the population of the country

### 11.2 ES20: DATA ON MEASURES OF MONEY SUPPLY [M1, M3]



Sufficient of remember that Broad money (M3) growth has declined but not in a steady manner. Beyond that, how/why rise/fall ...all that PHD poor cost-benefit.





## 11.3 🐼 RBI's MONETARY POLICY TOOLS: UPDATES

### 11.3.1.1 🐼📄✂️📅 CRR Exemption for 5 years (सीआरआर में छूट)

- ⇒ CRR: first suggested by the British economist J.M. Keynes & first introduced in US Federal Reserves (=Central Bank of USA).
- ⇒ Banks must keep this much deposits (or balance) with RBI. RBI doesn't pay interest on it usually.
- ⇒ 2020-Feb: RBI announced following to Scheduled Commercial Banks (SCB)
- ⇒ Whatever new (retail) loans you give for 1) automobiles 2) residential housing / home mortgages. 3) MSMEs [After 31/Jan/2020 upto 31/Jul/2020]
- ⇒ You can subtract that much loaned ₹ amount from deposits while computing cash reserve ratio (CRR) for the next five years (from the date when the loan was given or other technical norms, which are not important).
- ⇒ In other words, if a bank gives more loans to the above 3 sectors, it'll have to keep ↓ CRR → ↑ loanable funds → profit to the bank. And more loans → more business activity → economic growth.

### 11.3.2 🐼🔪📅 Long Term Repo Operations (LTROs)

- ⇒ Usually, Repo loans are for short term borrowing from overnight to 14-days.
- ⇒ But, 2020-Feb: RBI announced to conduct Long Term Repo Operations (LTROs: दीर्घ अवधि के रेपो ऋण) of \_\_\_\_\_ tenors.
- ⇒ RBI will loan total ₹ 1,00,000 crore, in various rounds through E-Kuber platform.
- ⇒ RBI's clients can apply to borrow a minimum ₹1 crore or higher.
- ⇒ Interest rate: prevailing repo rate. Interest rate will be compounded annually.
- ⇒ This will increase loanable funds with banks → economic growth can be revived.
- ⇒ MSF and (short term) repo lending will also be continued separately as per their own existing norms. LTRO doesn't aim to eliminate / replace them.

~~Further operational guidelines, how it impacts the bond yields etc. = poor cost: benefit~~

## 11.4 🐼📢📦🔪 MONPOLICY: QUANTITATIVE TOOLS → OPERATION TWIST

*Before that, you've to be aware of ~~some~~ many basic concepts:*

### 11.4.1 🐼📦: Security → Debt → G-Sec & Bonds

A 'Security' means a certificate/document indicating that its holder is eligible to receive a certain amount of money at a particular time. This could be a...

Borrower	🐼 Government	👤 Corporate
Short term (less than 1 year) →	Treasury bills, Cash Management bills	Bill of Exchange, Commercial Papers, Promissory Notes.
Long term (1 year/>) →	G-Sec, Sovereign Bonds	Bonds / Debentures
Interest rate	Usually lower than Corporates' because risk is low	Depends on following factors →





#### 11.4.2 📌📦👤: Corporate Bonds: factors that determine its interest rate

If companies want to borrow money, they may issue bonds to investors. e.g. “Whoever buys this Reliance Bond worth ₹1000, we will pay him 9.40% interest rate per year and return the principal after 15 years.” Usually the interest rate offered on such bonds depends on

Factor	How it determines corporate bond interest rate
(Risk) Credit rating of company	Lower credit rating (e.g. CCC or D) → higher interest rate needs to be offered because risk of default is high.
Inflation	why/how: Ans. Ref: Pillar1C → Inflation Indexed Bonds
Bank deposit interest rates	Higher the (Bank) deposit interest rate, higher bond interest rate needs to be offered to attract households to shift money from bank savings/FD to corporate bonds.
Yield on G-Sec	If G-Sec yield increases, then corporate will have to offer even higher bond interest rate to attract the investors from G-Sec investment towards C-Bond investment. <b>(This was primary motive for Operation Twist)</b>

#### 11.4.3 📌📦👤: Bond Yield

- ⇒ Bond yield is the profit an investor earns on a bond investment.
- ⇒ Suppose, Government issues a G-Sec or Bond: 8% annual interest, tenure: 1 year
- ⇒ Bhide Master invests ₹ 100. So, upon 1 year maturity he'll get ₹ 8 Interest + ₹ 100 Principal = ₹ 108. So his profit or yield will be= 8%
- ⇒ But suppose, before maturity of 1 year, Bhide Master urgently needs cash. So he sells ₹ 100 facevalue bond to Jethalal at a discounted price of ₹90
- ⇒ Jethalal keeps the it till maturity → Government pays him ₹ 108. So, for Jethalal the profit OR current bond yield to maturity is....

$$= \left( \frac{108-90}{\text{original investment of ₹ 90}} \right) * 100 = 20\%$$

#### 11.4.4 📌📦👤: Bond Yield $\propto$ 1/Price

- Bhide bought @100, his yield is 8%; Jetha bought @90, his yield is 20%.
- Thus, Bond yield is **inversely related** to the current selling price of the bond in the secondary market.
- If a bond's demand increases → its selling price will increase → bond yield decrease (Because of inverse relation)

#### 11.4.5 📌📦👤: Bond yield: other factors affecting it

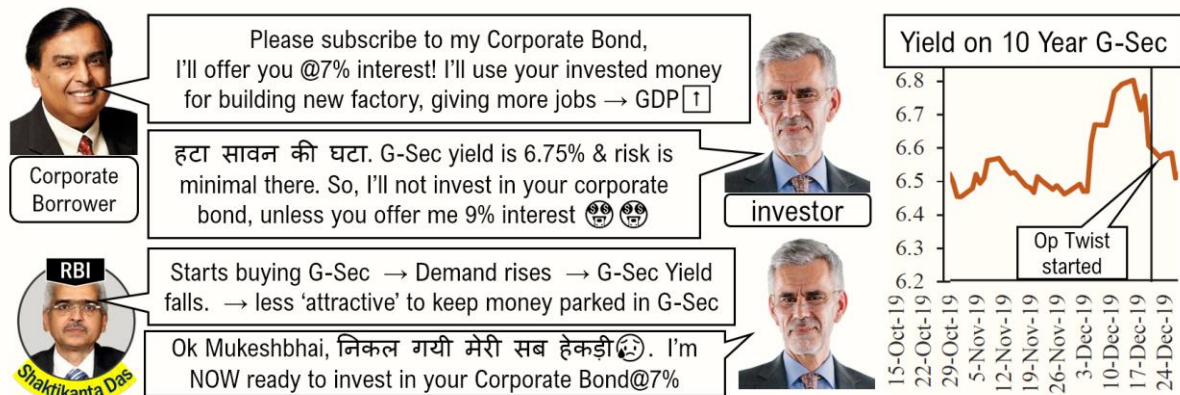
- If the economy is booming, companies are making great profit, investors may sell bonds at lower prices in a hurry to unlock their money to invest it in shares of companies, because they think it'll get them more dividend. Then bond's current selling price in the secondary market falls → yield increases.
- If the economy is facing **recession** (Continuous decline in growth rate) → companies will NOT make great profit → investors sell shares, and prefer to buy bonds hoping they'll get secured fixed interest. Then bond's demand increases in the secondary market → selling price increases → yield **declines**.

#### 11.4.6 📌📦👤👉: Operation Twist: why?

- Commercial banks were reluctant to lend money to private sector companies because of the problem of Bad Loans /Non Performing assets (NPA: More in Pillar1B-2).



- If such companies could borrow money by issuing corporate bonds (at cheaper interest rate) → more factories, more jobs, more production, more GDP.
- RBI decided to attack the third factor: “If the yield on long term G-Sec decreased, then automatically Corporate Bond interest rates could also decrease.”



#### 11.4.7 🗣️📊🔗 RBI's Operation Twist: methodology (2019-Dec)

Since RBI's existing monetary policy tools had failed to make loans cheaper for corporates / boost the economy. So in 2019-Dec, RBI started a “special OMO” wherein:

RBI _ _ _ _ →	shorter -term G-Sec (of 1 year & higher tenor) worth ₹10,000 crore
RBI _ _ _ _ →	bought longer -term G-Sec (of 10-14 years tenor) worth ₹10,000 crore (i.e. equal amount as above, so as to keep money supply neutral)

- Since RBI started buying long-term G-Sec, their demand will rise → price will rise → yield is lowered. The 10YearGSec's yield lowered from 6.75% to 6.60%
- And we've already learned, Corporate bonds are priced (benchmarked) keeping G-sec yields in mind.

**So, Op Twist → Lower G-Sec yield means →**

- ✓ Private companies can borrow money by issuing their (long term) C-Bonds at much cheaper interest rate than before.
- ✓ When a private company meets a bank manager to borrow money, it can negotiate the loan price, “If your bank does not lend me money at this cheaper interest% then I will issue my own corporate bonds.” → Even the bank lending rates for corporate loans could be reduced.
- ✓ Investor of long term G-Sec will feel discouraged to hold the G-Sec till maturity (10-14 years), He will try to sell it to another party/RBI and pull out his money, then he may park ₹₹ it a Corporate Bond / Bungalow / car / Goa-vacation etc. Thus, it helps boost the consumption → economy grows.

**समज में आ गया हो तो बढ़िया है, नहीं तो रट्टा मारो जिंदाबाद:**

1. 1961: "Operation Twist" was first used by the \_ \_ \_ \_ \_ .
2. 2019: RBI used also done it. Officially called “Special Open Market Operation (OMO) wherein the Central bank simultaneously buys and sells G-sec of varying maturities to adjust their yields. Which helps reduce interest rates on corporate bonds/debentures → easier to mobilize investment → factory expansion → jobs, GDP growth.
3. Primary objective of Op-Twist-2019 was to borrowing cheaper for corporates through bond market. It was NOT MEANT For fighting inflation.
4. It ensures better Monetary Policy transmission for economic growth. (because simply reducing the repo rate has not helped much in making loans cheaper, for corporates.)



5. Net liquidity remains unchanged because ₹10,000 crore goes in and the same amount comes out of the market.

~~Beyond this, further PHD on what/why/how – poor cost:benefit for MCQs. For example “The simultaneous sale of short-term bonds, on the other hand, helps push up short-term rates which had fallen below RBI’s benchmark rate. This would not only correct the anomaly in the short and long-term rates” .... All this is not important for the scope of competitive exams.~~

#### 11.4.8 Bond Yield: Related Concepts

*Following concepts are **not related to monetary policy** topic. But I’m shifting them from Handout Pillar: 1C (SEBI-Sharemarket-Bonds) to here for faster revision, since you’ve just learnt the bond yield topic:*

#### 11.4.9 Inverted Yield Curve = recession is coming

- ⇒ Yield graph measures the yields of short term and long-term bonds.
- ⇒ Normally, the Yield on short term bonds << (lower than) Yield on long term bonds.
- ⇒ But, if the Yield on short term bonds >> (greater than) Yield on long term bonds, then it is said “Yield Curve has become inverted.”
- ⇒ Inverted Yield Curve hints that **economic recession is coming**. This has happened in the USA. e.g. in 2007 just before the subprime crisis led recession.
- ⇒ 2019: Again, Inverted Yield Curve seen in USA, so investors are selling companies’ shares fearing that recession will come = companies’ profit / dividend will decline.
- ⇒ Then such scared investors prefer to park money in safe assets like gold → gold demand rises → gold price increases.

~~Why/How/What are the other 500 type ke implications? Ans. That M.com/PhD beyond the scope of UPSC exam.~~

#### 11.4.10 Negative Bond Yield

- ⇒ 2002: Italy switched its official currency from **Italian \_ \_ \_** to **Euro** currency.
- ⇒ 2019: Italy is undergoing great political and economic crisis. ~~(why/how: Not IMP)~~
- ⇒ So, Italian mutual funds and pension funds panicked, and began parking clients’ money in German Governments’ bonds (currency denomination: Euro) thinking it is much safer investment.
- ⇒ Ultimately, a German bond which will return total 108 Euro as principal+maturity, is being sold at 110 Euro in the secondary market because of this high demand. (Numbers are hypothetical).
- ⇒ Here, investor’s yield will be  $((108-110)/110) \times 100 = \text{MINUS } -0.02\%$  = This is Negative Bond Yield = Investor will make losses.
- ⇒ But Italian mutual funds and pension funds feel this is still better than investing in Italian banks, companies or Italian G-Sec where they’ll be making **EVEN BIGGER** losses. (Then why don’t they invest in gold or real estate to be more safer!?? Because Italian regulatory norms don’t permit it.)

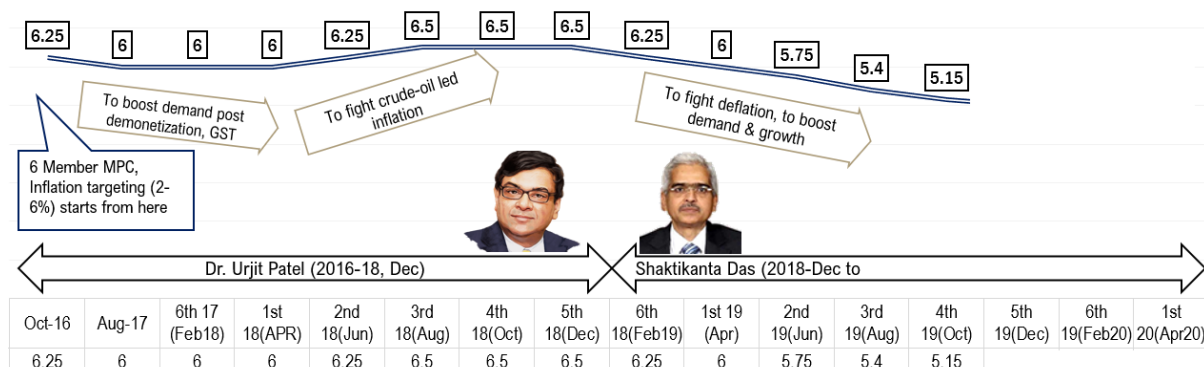
~~Beyond that, Why/How/What are the other 500 type ke cause and consequences? Ans. That Italian M.com/PhD beyond the scope of UPSC exam.~~



## 11.5 🐼🔊 RBI's BI-MONTHLY MONETARY POLICIES

Table 1: Monetary Policy Committee members replaced:

🐼 RBI side (3 members)	👤 Govt. Side (3 members)
1. RBI Governor, as the Ex-officio Chairman. 2. Dy. Governor responsible for Monetary Policy. <b>Michael Patra</b> (from 2020-Jan). <del>Earlier Viral Acharya.</del> 3. One person nominated by RBI Central Board: <b>Janak Raj</b> (Executive Director, RBI). <del>Earlier it was Michael Patra.</del>	1. Dr. Chetan Ghate, Indian Statistical Institute 2. Dr. Pami Dua, Delhi School of Economics 3. Dr. Ravindra H. Dholakia, IIM-A



	Upto Feb-2019 updates should be in your existing handout. Afterwards:
Apr-2019	<ul style="list-style-type: none"> <li>- <b>Repo cut 25bps</b> (6.25% → 6.00%), <b>stance</b> kept at <b>Neutral</b>.</li> <li>- Decision not <b>unanimous</b>. Dy. Gov. Viral Acharya fears inflation due to Oil &amp; El Nino. But, Gov. Shaktikanta Das feels the declined sale of vehicles, air &amp; sea traffic is pointing to deflationary trend ahead, so rate cut necessary.</li> <li>- Loan interest rates: External Benchmark mechanism was to be implemented from 1/4/2019 but decision deferred after bankers' feedback.</li> </ul>
Jun-2019	<ul style="list-style-type: none"> <li>- <b>Repo Cut 25bps</b> (6.00% → 5.75%), Consequently, the reverse repo rate @5.50%. MSF and Bank Rate @6%</li> <li>- <b>Stance</b>: changed from Neutral to <b>accommodative</b> = next time Committee may decrease the repo rate or keep it unchanged, but, no chances of rate hike.</li> <li>- <b>Committee voted unanimously</b> for rate cut because, IMD has predicted 96% normal monsoon, so high level of food inflation seems unlikely. Fuel prices rose but overall inflation is offset by falling of other commodities prices. Thus, CPI inflation remained unchanged at around 3%. Slowdown in trade and manufacturing due to US-China trade war, and other geopolitical issues. So cheaper loans required to boost demand and mfg.</li> <li>- <b>measures to promote digital economy</b></li> <li>- RBI waives <b>NEFT &amp; RTGS charges</b>. Banks will be required, in turn, to pass these benefits to their customers.</li> </ul>
Aug-2019	<ul style="list-style-type: none"> <li>- Repo cut _ _ _ (5.75-0.35=5.40). This is largest ever cut in a single time; <b>accommodative</b> stance.</li> <li>- RBI's NEFT will function 24/7 basis on all days, from 2019-December.</li> <li>- Banks lending to NBFC (who is lending to agro, MSME, housing) will be counted under Bank's PSL quota achievement.</li> <li>- <b>External Benchmark for loans</b> from 1/10/2019.</li> </ul>



Oct-2019	<ul style="list-style-type: none"> <li>- Repo cut 25bps (<math>5.40 - 0.25 = 5.15</math>); <b>accommodative stance</b>. <b><u>measures to promote digital economy</u></b></li> <li>- We'll set up an <b>Acceptance Development Fund</b> (ADF: डिजिटल भुगतान स्वीकृति विकास निधि) as recommended by the Nandan Nilekani <b>Committee</b> on digital payments.</li> <li>- We shall identify one district per State/UT, &amp; develop it as 100% digital payment enabled.</li> <li>- Large sized Prepaid Payment Instrument (PPI) companies such as Amazon Pay, Mobikwick etc. will be required to setup <b>Internal Ombudsman</b> (आंतरिक शिकायत निवारण अधिकारी) to reduce workload of RBI's digital ombudsman.</li> </ul>
Dec-2019	<ul style="list-style-type: none"> <li>- No changes in Repo Rate or Stance. ( _ _ _ _ _ stance)</li> <li>- heavy unseasonal rains → onions &amp; other vegetables supply disrupted → price rise.</li> <li>- Pulses' area under cultivation is declining → supply declining → price rise.</li> <li>- Milk became more expensive due to rise in fodder prices.</li> <li>- 13 states' Electricity distribution companies (DISCOMs) have increased Electricity prices.</li> <li>- So, if repo reduced → inflation problem may worsen.</li> <li>- At the same time, the economy is facing slowdown, sales are down so, if repo increased → slowdown may worsen. So, the MPC Committee unanimously decided to keep repo unchanged.</li> <li>- <b>Regulatory updates</b> related: Urban Co-operative Banks (UCB), Small Finance Banks, Semi-closed PPI etc in respective pillars.</li> </ul>
Feb-2020	<ul style="list-style-type: none"> <li>- No changes in Repo Rate or Stance because of reasons similar to Dec-2019.</li> <li>- CPI Inflation rose to 7.4% in december-2019 (which is outside the statutory limit of 2-6%) &amp; this inflation rate is highest since 2014-July. So, ideally, RBI should have increased repo rate to combat inflation but               <ul style="list-style-type: none"> <li>o 1) December-2019 policy had kept Accommodative stance = repo couldn't be increased. It could only be kept same/reduced.</li> <li>o 2) Union Budget-2020 announced various measures to boost economic growth so Committee preferred to wait &amp; watch how those measures impact inflation and growth, before changing repo rate.</li> </ul> </li> </ul> <p><b><u>RBI announces Measures to promote economic growth::</u></b></p> <ol style="list-style-type: none"> <li>1. LTRO: _ _ _ _ _</li> <li>2. _ _ _ _ Exemption based on (new) loans given for 1) automobiles, 2) residential housing and 3) MSMEs</li> </ol> <p><b><u>RBI announces measures to promote digital economy</u></b></p> <ol style="list-style-type: none"> <li>1. Regional Rural Banks (RRBs) will be allowed to operate as 'merchant Acquiring Banks' (Ref: 1A).</li> <li>2. RBI to construct a "Digital Payments Index" (DPI) to capture the growth of digital payments across India.</li> </ol>

### 11.5.1 🏠🏦 Bank's loan interest rate: External Benchmark (बाहरी बेंचमार्क, 2019)

Earlier, commercial banks decide their lending rates as per RBI's Marginal Cost of Funds based Lending Rate (MCLR). But it did not function effectively in passing the repo rate cuts to end-borrowers. So, RBI ordered following from 1<sup>st</sup> October 2019.



1. Banks must link their loan interest rates with “\_\_\_\_\_ Benchmark + Spread + Risk premium” system.
2. Individual bank free to pick any one External Benchmark such as
  - 1) RBI repo rate or
  - 2) \_\_\_\_\_T-bill yield or
  - 3) \_\_\_\_\_T-bill yield or
  - 4) any other benchmarks by Financial Benchmarks India Ltd.
3. Banks must feed the latest data of external benchmark in above formula, atleast once **every three months**.
4. **Benefits?** Same benefits which MCLR couldn't fully deliver.
5. It's applicable to the new loans given to
  - 1) personal loans (taken for any sudden emergency expenditure)
  - 2) retails loans (home, vehicle, electronics etc)
  - 3) Loans to micro & small enterprises
  - 4) Loans medium enterprises (this 4<sup>th</sup> category is to be added from 1/April/2020).

■ ■ ES20: The growth of credit to Micro, Small and Medium Enterprises and Textiles has been negative in 2019. (In other words, banks have loaned less amount of money to them compared to the previous year). Only in personal loans, there has been a slight growth.





## 12: PILLAR#1B1-CLASSIFICATION OF BANK-NBFC

### 12.1 🎉 GOLDEN ANNIVERSARY OF NATIONALIZATION- 📄📄ES20

Economic Survey 2019-20 (released on 31/01/2020) Vol1Ch.07 observed:

- First round of bank nationalisation was done in 1969 wherein 14 Private banks with ₹ 50 cr/> deposits were nationalized e.g. Bank of Baroda, PNB, Dena, Canara etc.
- so, 2019-1969=50 years Golden anniversary of the bank nationalisation. (निजी बैंकों के राष्ट्रीय करण की स्वर्ण जयंती)

👍 Positive	👎 Negative
<ul style="list-style-type: none"> <li>✓ After nationalisation, the number of Bank branches in India, the amount of loan given to farmers and villagers= has increased.</li> <li>✓ This greatly contributed to the agriculture production and poverty removal in the rural areas.</li> <li>✓ PSBs account for 70% of the banking business in India.</li> </ul>	<ul style="list-style-type: none"> <li>❖ From 1960s to 80s: The Government had launched 1) "green revolution" 2) focused on poverty removal through five year plans.</li> <li>❖ RBI had initiated selective credit control tools &amp; moral suasion to channelize more loans to farmers.</li> <li>❖ So, those actions were responsible for boosting agriculture &amp; reducing poverty.</li> <li>✓ Bank nationalization itself has not helped in it much.</li> </ul>

#### 12.1.1 🐼 > 🐼: Private sector banks are better than PSBs

📄📄ES20 gave tonnes of depressing data about PSBs such as

Indicators	🐼:😞 PSBs =losers	🐼:😄 PvBs= winners
Total NPA in Indian Banks	Majority of NPA here	less
Total Bank frauds in India	>90% occur in PSBs	Hardly 7%
Return on Equity	For every ₹1 that the government invests as share capital in PSBs → they lose 23 paise.	They make 9.6 paise profit against every ₹1 share capital.

Even in other technical indicators such as Return on assets, Market-to- book ratio, growth of new loans, Capital adequacy norms for BASEL, etc: (new) Private sector banks (PvB)s outperform PSBs. Thus, PSBs are clearly not efficient today. If they become efficient = ₹11 lakh+ crore profit for the Government. After 2013, PSBs' credit growth has declined → GDP growth is affected. 2019: PSBs' total loss > 66,000 crore which is even double than India's budget allocation for education. And so on..

#### 12.1.2 🐼 = 🐼 PSBs: reasons for inefficiency & remedies?

🐼 Reasons why PSBs are inefficient? सार्वजनिक क्षेत्र के बैंक प्रभावहीन हैं क्योंकि →	Solutions by 📄📄ES20 (More details in handout part 1B-2)
PSB staff's salary does not depend on the profitability of the bank. Employee unions frequently engage in strikes/hartals. →	<ul style="list-style-type: none"> <li>- Allow campus recruitment, lateral entry in higher management positions</li> <li>- Make employees 'part owners' through employee stock ownership plan (ESOP)</li> </ul>





They've apathetic attitude (उदासीन रवैया) towards the use of artificial intelligence, computer technology, marketing, and customer satisfaction. →	<ul style="list-style-type: none"> <li>- Use Artificial Intelligence (AI), Machine Learning (ML), Big Data Analytics, geotagging of mortgaged assets etc.</li> <li>- setup an organization PSBN Network to implement above ICT-solutions.</li> </ul>
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Further, Since the government is the majority shareholder in PSBs,

- 1) 🤖 Usually the persons favored by the present-day ruling party become the Board of directors, irrespective of merit or qualification. Thus, political considerations have significant control/influence over bank's business operations.
- 2) 🏠👤:🤖 PSBs are subjected to Right to Information (RTI) act, Central Vigilance Commission (CVC), Comptroller Auditor General (CAG), Central Bureau of Investigation (CBI), Courts and media in a more stringent manner. (बैंकर खोफ में रहते हैं की ईमानदार निर्णय की भी शक की निगाहों से जांच होगी)
- 3) Consequently, PSB officials fear harassment under the veil of vigilance investigations & media-trials. They prefer safety and conservatism over risk-taking and innovation. (रूढ़िवाद पसंद, नवाचार नापसंद)

#### 12.1.3 Merger of 10 PSBs into 4 (Announced in 2019-August)

Amalgamating Banks (एकीकृत / विलीन होनेवाली)	Anchor Bank (सहारा देनेवाली)
<ul style="list-style-type: none"> <li>– Oriental Bank of Commerce (1943, HQ: Gurugram, Haryana),</li> <li>– United Bank of India (1950, Kolkata)</li> </ul>	1) PNB. (1984, HQ: Delhi, It'll become the 2nd largest bank after SBI, in terms of business size and branch network)
<ul style="list-style-type: none"> <li>– Syndicate Bank (1925, HQ: Manipal, Karnataka)</li> </ul>	2) Canara Bank (1906, HQ: Bengaluru, Karnataka)
<ul style="list-style-type: none"> <li>– Andhra Bank (1923, Hyd)</li> <li>– Corporation Bank (1906, Mangaluru)</li> </ul>	3) Union Bank of India (1919, Mumbai)
<ul style="list-style-type: none"> <li>– Allahabad Bank (1865, Kolkata)</li> </ul>	4) Indian Bank (1907, Chennai)

After this process is over, we'll be left with only 12 PSBs (+1 India Post Payment Bank).

#### 📌📌 ES20 Vol1Ch7 on 50 years of bank nationalization also noted:

- ⇒ 2019: Global top-100 banks: China (18 banks), USA (12 Banks), Japan > France > .....India (only 1 bank: SBI at Rank#55).
- ⇒ Even Sweden and Singapore have more global banks than India, even though these countries' size of economy (GDP) is much smaller than India.
- ⇒ So, given India's size of economy (in terms of GDP), India should have 6-8 banks in the global top 100. → These large banks provide large loans → India can reach \$5 trillion GDP by 31/3/2025. (More in Pillar4C)
- ⇒ Therefore, merger of public sector banks is necessary. It'll increase the manpower, financial strength of the merged entities, then they can compete at global level.

#### 12.1.4 🏠👤🌐🚗📄 On-Tap Licenses for SFB

- 8 out of 10 Small Finance Banks (SFB) became Scheduled Banks. RBI reviewed & found they have achieved their priority sector targets and helped in financial inclusion. More competition and new players will help.
- so 2019-June, RBI announced it'll allow 'On-Tap' license for SFB soon. (i.e. no need to wait for notification unlike IAS exam, apply whenever you wish like a driving license)



### Eligibility conditions to get SFB license 'On Tap':

- Minimum 200 crore capital.
- resident individuals/professionals with ten years of experience in banking and finance;
- 5 year /> old companies owned by Indian residents
- Existing NBFCs, MFIs, local area banks and payments banks.
- Urban cooperative banks (UCB) allowed to convert into SFB but capital norms slightly different.
- 2019-Dec: Even **Payment banks can convert** into SFB, after 5 years of operation.

## 12.2 📖 (YEARBOOK) DEPT OF POST: POSB vs IPPB

Ministry of Communications has two dept: 1) Depart of Telecommunications 2) Department of Posts →

- ✓ Setup by Clive (1766), expanded by **Warren Hastings** (1774)
- ✓ 1854: **Dalhousie**- Post Office Act; 1st postal stamp, rates by weight & not by distance.
- ✓ 2008: Project Arrow for modernization.
- ✓ 2013: **Telegram** stopped by India Post, due to onset of SMS & email.
- ✓ Dept of Post sells
  - **Gangajal** sourced from Rishikesh and Gangotri.
  - UTI-Mutual funds and Sovereign Gold bonds.
- ✓ **Post Shoppe** = special outlet in big post offices for philately (stamp collection hobby)
- ✓ **RTI fees** can be submitted by buying Indian Postal Orders (IPO). **E-IPO** = overseas Indians can pay RTI fees online using this mechanism.
- ✓ **Deen Dayal SPARSH Yojana**: Students in class 6-9 given scholarship for philately.
- ✓ **Dhai Akhar Letter Writing Competition** wherein students asked to write letters to Mother Teresa, Tagore etc. 2019-20's theme "Dear Bapu, you're immortal." This theme is inspired by Albert Einstein's homage to Gandhi "Generations to come will scarce believe that such a one as this ever in flesh and blood walked upon this earth".
- ✓ **Officers' training** conducted at **Rafi Ahmed Kidwai** National Postal Academy at Ghaziabad, UP. Kidwai was India's first Minister for Communications.

Dept of Post →	Post Office Savings Bank (PoSB)	India Post Payments Bank (IPPB)
<b>foundation</b>	Govt Savings Bank Act 1873	Companies act 2013 → Public ltd company registered in 2016
<b>Accept demand deposits?</b>	Savings account only	1. Current account 2. Savings account
<b>Accept time deposits?</b>	YES	No, bcoz payment bank
<b>Can keep more than ₹1 lakh balance?</b>	YES	No, bcoz payment bank. But u can link IPPB account with PoSB account to auto-transfer (=SWEEP) excess balance to PoSB.
<b>E-Banking and online bill payment</b>	Not directly but you can do it by linking PoSB account with IPPB account	yes, UPI, BHIM, NEFT, IMPS and BBPS (Bharat Bill pay) available.



Dept of Post →	Post Office Savings Bank (PoSB)	India Post Payments Bank (IPPB)
Sukanya Smriddhi (daughter's fixed deposit account)	Can be opened	Not possible. Because time deposits are not allowed.
loans to individual?	No. ₹ goes to NSSF	Not until it becomes Small Finance Bank
Objective?	Promote savings habits among poor	Remittance & digital payments

### 12.3 🏠👤 COOPERATIVE BANKS: KERALA BANK (2019)

- 2019-Oct: RBI permitted Kerala's all 13 district co-operative banks (DCBs) to be merged with Kerala State Co-operative Bank.
- The combined entity will be called "Kerala Bank". It'll be a 'State Cooperative Bank.'

### 12.4 🏠👤 AIFI: NHB'S REGULATORY POWER SHIFTED TO RBI

- National Housing Bank (NHB, setup through act of parliament in 1988).
- Original boss: RBI (100%). But, (Full) Budget-2019:
  - o RBI sold its 100% ownership to Govt.
  - o NHB's regulatory powers over Housing Finance Cos (NBFC) handed over to RBI.

#### 12.4.1 🏠👤 NBFC → Investment and Credit Companies (new category in 2019)

- 2019: this new category created by merging previous NBFC categories viz. Asset Finance Companies, Loan Companies, Investment Companies.
- RBI will regulate these RBI added this new category of NBFCs

#### 12.4.2 🏠👤 Microfinance → Lending norms changed in 2019-Oct

- 2010: RBI's Y. H. Malegam Committee → RBI created a new NBFC category called Micro Finance Institution (MFI)
- Give small loans to poor without collateral, flexible EMI.
- Examples: Bandhan (W.Bengal, separately got PvB license), Disha (A'Bad: separately got SFB license), SKS (Andhra), Cashpor (UP), Ujjivan (Karnataka).
- 📊 ES20 appreciated the role of MFI in Helping the weaker section because Majority of its borrowers are women (97%), SC/ST(30%) and minorities (29%)
- **Who regulates them?** RBI + Ministry of Corporate Affairs
- **\*Who can borrow from MFI?** Ans. Household whose annual income is not more than ₹ 1.25 lakh (rural) or ₹ 2 lakhs (urban).
- **\*How much can one person borrow from an MFI?** Ans. Not More than ₹ 1.25 lakh.

*\*Before 2019-Oct above limits were lowers.*



## 13: PILLAR#1B-2: BURNING ISSUES IN BANKING-FINANCE

### 13.1 🏢👤😞 COOPERATIVE BANKS: NEGATIVE NEWS (2019): PMC BANK

- The Punjab and Maharashtra Cooperative (PMC, HQ-Mumbai, setup 1984) is a Multi-State Scheduled Urban Co-operative Bank. It functions in Maharashtra, Delhi, Karnataka, Goa, Gujarat, Andhra Pradesh and Madhya Pradesh.
- PMC bank loaned large amount to a weak company HDIL, because of its cozy relations with bank directors. Company who couldn't repay it. NPA became so large, bank might collapse.
- RBI imposed withdrawal limits on the depositors using the powers of Banking Regulation Act. Because 'bank run' would have been so high even CRR-SLR can't fulfill it, if there was no withdrawal limit.
- Merger / closing / liquidation of a cooperative bank requires approval by Government's registrar of cooperatives so RBI alone can't do much action.
- RBI's Y.H. Malegam Committee (2011) had suggested many reforms on UCBs, but they're not yet implemented until Government amends the laws.
- Therefore, RBI offered Urban Cooperative Banks to convert their license into Small Finance Bank (SFB) then RBI alone will have supervision powers without interference from Government. But UCB banks not interested, they enjoy the present loopholes.
- **Budget-2020:** Promised to amend the Banking Regulation Act to increase RBI's powers over cooperative banks.

📌 ? Recently the RBI has imposed limitations, initially for a period of six months, on the withdrawal of amount by account holders of this banks: (UPSC-CDS-i-2020)

- (a) IndusInd Bank (b) Dhanlaxmi Bank  
(c) Punjab and Maharashtra Cooperative Bank (d) South Indian Bank

### 13.2 🏢👤😞 YES BANK AND AT1 BONDS (2020)

- ⇒ 2004: Yes Bank, a Private Sector Scheduled Commercial Bank starts (HQ-Mumbai)
- ⇒ Its founder Rana Kapoor took bribes to approve loans to companies without capacity to repay loans, such HDIL (This HDIL company also borrowed from PMC bank, causing another crisis there.). By 2020 Yes bank's business became unstable.

$$\text{Equity Capital} + \text{Liabilities} + \text{NET Profit} = \text{Assets}$$

Table 2: Hypothetical figure only for illustration. B.Com/PHD NOT REQUIRED

	+Equity Capital (Shares)	+Liabilities		+NET Profit	=Assets (Loans, CRR, SLR etc)
		Bonds	Deposits		
Healthy bank	+11	+3	+78	+1	=100
Loser bank This is happening	*	*	+78	-10	=90 (assets <input type="text" value="1"/> due to bad loans)
*How to revive? (we must balance the Equation)	11 → <input type="text" value="1"/> 20 (get equity infusion from SBI etc.)	3 → <input type="text" value="1"/> 2 (by writing off AT1 bonds)	+78 (put deposit withdrawal limits to keep this stable. besides, if loans given for 10- 15 years project, bank can't return depositors' money <i>abhi</i> <i>ke abhi</i> )	-10	=90

2020-March: RBI is attempting following for Yes Bank's revival (पुनर्जीवित करना)

- ⇒ **Deposits Liability:** (temporary) withdrawal limits of ₹50,000 on depositors



### ⇒ **⬇️ Bond Liability:**

- A) Write down ~₹9000 crore worth AT1 Bonds liability from equation. (in other words, those investors will not get a single paisa. बॉन्ड की देयता को खारिज कर देना). These bonds holders are unhappy & will go to court to stop this. **OR alternatively**
- B) Convert the AT1 bonds into (lower priced) shares e.g. ₹100 Face Value ka Bond converted into ₹20 Face Value ka Share (so there is 80% loss / haircut for the bond holder)

⇒ **⬆️ Equity Capital:** Other banks to provide equity (share) capital worth >₹10,000cr into Yes Bank → future shareholding maybe SBI (45%), ICICI(6%), HDFC(6%), Axis(3-4%)

But daily ball by ball commentary / and changes in this plan so we need not lose sleep.

### 13.2.1 **BASEL-III norms: Capital Tiers**

BASEL-III norms require banks to keep capital against their risk weighted asset ratio. This capital is subdivided into:

Capital of a Bank	Instruments / subtypes: List not exhaustive
Tier1 / core capital →	⇒ <b>Common Equity Tier-1 (CET1)</b> e.g. ordinary shares. ⇒ <b>Additional Tier1 (AT1)</b> e.g.  AT1 Bonds, Preferential shares etc.
Tier2 →	⇒ Bonds/Debenture, Hybrid instruments

BASEL-III prescribed that banks must keep minimum x%, y% etc in each of these tiers, depending on their Risk Weighted Asset (RWA).

### 13.2.2 **Additional Tier 1 (AT1) Bonds**

They have no maturity date (i.e. bank has to pay interest for infinite time / perpetuity and principal will not be returned). However, bank may 'buyback' them after certain years. If / when a bank makes huge losses → AT1 Bonds' liability may be

- written off (खारिज कर देना) **OR**
- converted into shares (process called 'Bail-In').

Beyond this any what/why/how/PHD = poor cost benefit for MCQs.

## 13.3 **NBFC: SHADOW BANKING (आभासी / प्रतिछाया बैंकिंग प्रणाली)**

ES20 Vo1 Chapter 08 on 'NBFC's Financial Fragility' (वित्तीय भंगुरता) observed

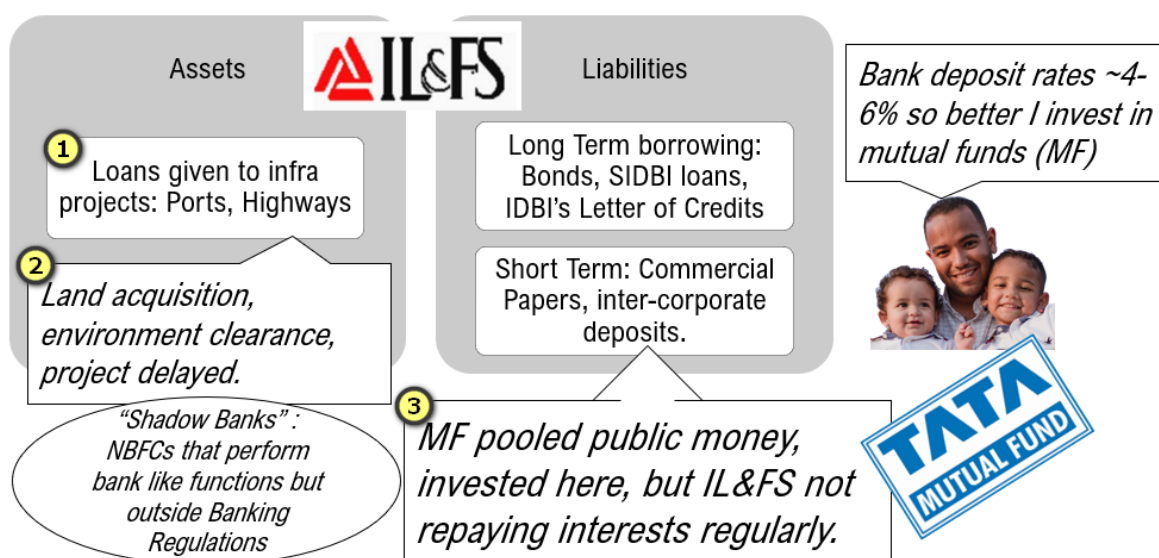
- ⇒ Shadow banking is a set of activities and institutions. They operate partially (or fully) outside the traditional commercial banking sector. They are not fully regulated by the RBI. ये संस्थाएं पारंपरिक बैंकिंग नियमों के दायरे से बाहर काम करती हैं.
- ⇒ A shadow banking system can be composed of a single institution or multiple entities forming a chain. They mobilize funds by borrowing from banks, issuing Commercial Papers (CP) and Bonds (Non-convertible debentures)



Table 3: Three important segments of the shadow banking system in India

<b>HFCs</b>	Housing Finance Companies. E.g. Dewan Housing Finance Limited (DHFL)
<b>LDMFs</b>	<ul style="list-style-type: none"> <li>- <b>Liquid Debt Mutual Funds</b> invest clients money into short term debt instruments such as T-bill (of Govt) and Commercial Papers (of companies).</li> <li>- e.g. certain schemes by UTI, Kotak, L&amp;T, Tata mutual funds</li> <li>- 2019: Some of these LDMFs had invested clients money in IL&amp;FS and DHFL, but failed to get the money back. Nearly ₹4000 crore of investors' money is stuck, triggering the NBFC crisis in India.</li> </ul>
<b>Retail-NBFCs</b>	Retail Non-Banking Financial Companies such as Gold loan companies, asset finance companies etc.

Shadow banking system's assets are risky and illiquid. If there is a 'bank run' like situation (depositors / investors demanding the money bank) these shadow banks can't honour the obligations. As seen in the ILFS crisis (2019)



- Infrastructure Leasing & Financial Services (IL&FS) is a Systemically Important Non Deposit Taking Non - Banking Finance Company (**NBFC - ND - SI**: प्रणालीगत रूप से महत्वपूर्ण- डिपॉजिट न लेनेवाली- गैर-बैंकिंग वित्त कंपनी) Setup in 1987 HQ@Mumbai.
- **Shareholders**: LIC > Japan's Orix group > Abu Dhabi's group > Central Bank of India > SBI.
- **Challenge?** 1-2-3 of above diagram. + loans given to unworthy borrowers with forged documents, bribes were paid to IL&FS board directors & auditors.

### Remedies undertaken by Government

- 1) Under Companies Act: Ministry of Corporate Affairs (MCA: कारपोरेट कार्य मंत्रालय) replaced the IL&FS's Board members. Uday Kotak made new Chairman. MCA constituted the statutory body National Financial Reporting Authority (NFRA) under Companies Act 2013 for stricter vigilance over Chartered accountants and auditors. (More in SEBI Handout)
- 2) Corporate Affairs Ministry's Serious Fraud Investigation Office (SFIO: गंभीर धोखाधड़ी जांच कार्यालय) investigating the IL&FS officials & auditors.
- 3) We'll encourage tri-party repo system. (Ref: Monetary Policy handout)





- 4) Companies Act requires all companies (incl. NBFCs) to setup a Debenture Redemption Reserve (DRR), fill it with % from profit to protect bond investors incase of default. Government exempted NBFCs, housing finance companies and, listed firms from this requirement so they can easily mobilize new funds to revive old biz.
- 5) (Full) Budget-2019: we will setup a Credit Guarantee Enhancement Corporation (CGEC: क्रेडिट गारंटी वर्धन निगम) regulated by RBI. It'll be an NBFC company. It'll provide guarantee to the lenders on behalf of borrower (by charging fees on borrowers). Then lenders may feel safer to lend ₹ ₹ to borrower at a cheaper interest rates.
- 6) We'll also give partial credit guarantee to PSBs when they loan to financially sound NBFCs
- 7) LIC says we'll not allow IL&FS to collapse (=we may use Policy holders' money to rescue it just like IDBI) = may result in "Financial Repression of households".
- 8) National Housing Bank introduced Liquidity Infusion Facility (LIFt) of ₹30,000 crore for additional liquidity to HFCs for individual affordable housing loans.
- 9) Through Finance Act, 2019, Govt amended RBI Act 1934 to increases RBI power to regulate NBFCs in following ways: RBI can remove NBFC's board of directors, debar its auditors, can inspect any NBFC or its associated group of companies, RBI can force merger/splitting of non-viable NBFCs, higher fines/penalties for violation.

#### **Remedies undertaken by RBI & SEBI**

- 10) PSBs unable to lend more to IL&FS due to PCA framework. But, RBI relaxed 'securitization norms' for NBFCs so they can use existing loan papers to issue new securities to borrow money from market, thus increasing liquidity /money supply for NBFCs' biz operations.
- 11) SEBI tightened norms for Credit Rating Agencies (CRAs). They've to disclose 'default probability' of bonds & other debt instruments. SEBI tightened norms on Mutual Funds, regarding where/how they invest clients' money.
- 12) RBI tightened norms of asset-liability management (ALM) norms for NBFCs.
- 13) 2019 July: Dy. Gov Viral Acharya Committee → RBI board approved 3 year medium term framework to improve regulation & supervision, based on global best practices = "Utkarsh-2022" roadmap.
- 14) RBI ordered certain NBFCs to implement BASEL-III norm's Liquidity Coverage Ratio (LCR) High Quality Liquid Assets (HQLA) framework in a phased manner by 1/Dec/2024.

#### **Remedies suggested by ES20**

- 15) CEA Subramanian K. has created a "Health Score for NBFCs" (स्वास्थ्य सूचकांक). It monitors given NBFC company's Asset Liability Management (ALM) problems, balance sheet strength, Operating Resilience etc. and gives them a score between -100 to +100. Higher scores indicating higher financial stability of the firm. This health score can provide early warning signals (पूर्व चेतावनी) to the Financial regulators → they can initiate appropriate measures before it's too late.

Q. How exactly do above norms work? Ans. Not-Imp. Because Prelims-word association sufficient due to technical nature of topic and for mains the maximum utility of this topic is 250 words.

#### 13.3.1 **NBFC-Negative News (2019): Thomas Cook NBFC closure in UK**

- Thomas Cook was a UK's travel-related financial services company (1841).
- They provided currency exchange, travel/luggage insurance, ticket booking, hotel accommodation, tour package etc. facilities.



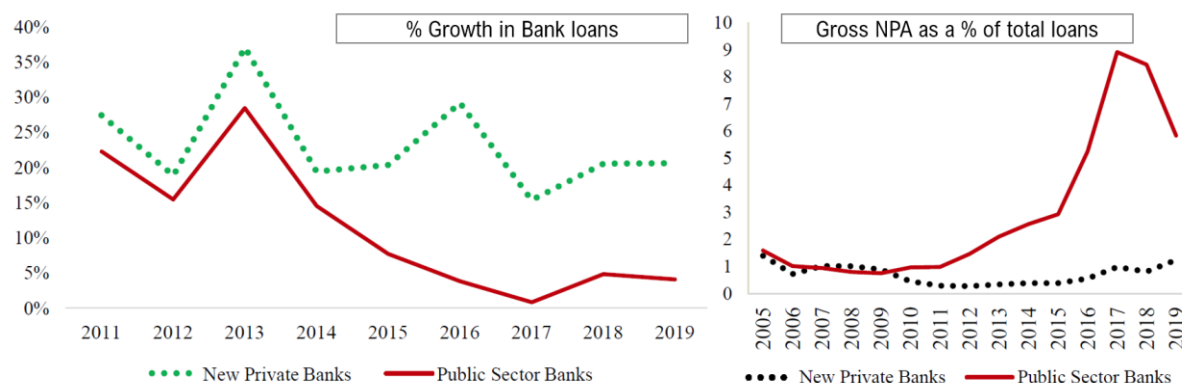


- Their business declined with the advent of Airbnb, Trivago, Makemytrip & other apps / websites in travel segment.
- 2019: Thomas Cook couldn't repay its loans, couldn't work out resolution plans with lenders, UK Government did not give bailout money → compulsory liquidation.

In September 2019, which one of the following travel giants declared itself bankrupt? (UPSC-CDS-i-2020)

- (a) Expedia (b) Cox & Kings (c) SOTC (d) Thomas Cook

### 13.3.2 NPA: Data from ES20



ES20: NPA had reached its peak in 2018 but now it appears to be declining because of various measures taken by Government and RBI.

### 13.3.3 IBC Amendments

- **Operational Creditors** (OC-कार्यसंबंधी लेनदार) = Suppliers, customers, contractors etc. They don't have voting power in IBC resolution.
- **Financial Creditors** (FC-वित्तीय लेनदार) = banks, NBFC, bond & other debt security holders + Home buyers. → they've to the voting power in IBC resolution.

### 13.3.4 Insolvency and Bankruptcy Code Amendment (2018: संहिता संशोधन)

- Permits Govt to modify norms when applying IBC for MSME.
- RERA registered building (home & office) buyers are classified as 'financial creditors'. So, if builder unable to finish project, unable to repay the loans to banks → homebuyers will have voting power in the I&B resolution process. (More RERA in Pill#6)
- It reduced the voting requirements for faster resolution:

Lenders' Voting requirements (ऋणदाताओं का प्रस्ताव के समर्थन में मतदान)	Before	After
Routine decisions (सामान्य निर्णयों के लिए)	75%	51%
Key decisions like appointing IP, extending deadlines for resolution process, approving the resolution plan	75%	66%
Withdrawing resolution plan from NCLT	NotIMP	90%

### 13.3.5 IBC Code (first) Amendment Act (2019: संहिता संशोधन)

2019-Aug: it was passed by Parliament, with following features

- Must finish entire process within 330 days, instead of earlier 180-270 days walli limit.



- If too many FCs (e.g. homebuyers): they may appoint a representative (प्रतिनिधि) for to attend the Committee of Creditors on their behalf, for smoother & systematic conduct of meeting.

### 13.3.6 🏠🔧📄 IBC Code (second) Amendment Bill 2019)

2019-Dec: introduced in parliament, with following features

- ⇒ IBC complaints can be made only if the loan amount is minimum “x” or minimum lenders are “y”. This is to **discourage frivolous complaints** by lenders. (मामूली बकाया ऋणों की शिकायतों को रोकना)
- ⇒ If the government had given any license, permit, registration etc. then it'll not be cancelled while IBC proceedings are going on. (e.g. if a liquor company's license was cancelled while ongoing case → no fresh investor would come → business can NOT be revived!).
- ⇒ **Ring-fencing from any risk of criminal proceedings:** (पुरानी आपराधिक कार्यवाही के सामने नये निवेशक की किलेबंदी/ मुक्ति) = After IBC restructuring, if a new partner joins/takes over in the business, he'll be given immunity from criminal proceedings against offences committed by previous promoters.
- ⇒ Plus, many other technical changes but poor cost-benefit chasing them.

### 13.3.7 🌐🔧📄 Cross-border Insolvency (सीमा-पार का दिवालियापन)

- Cross-border insolvency has two facets: 1) foreign creditors should be able to recover money lent to Indian corporates & VICE VERSA. 2) During Indian company's insolvency in India, the Indian lenders should be able to recover money from Indian company's foreign assets easily, AND VICE VERSA.
- IBC sections 234 & 235 have provisions for it, BUT they are not notified yet, so they are not enforced.
- 2018: Corporate Affairs Ministry's Insolvency Law (reforms) Committee headed by **Injeti Srinivas** recommended
  - We should create a separate law for Cross-border Insolvency.
  - More than 40 nations use United Nations Commission on International Trade Law (UNCITRAL)'s Model Law of Cross Border Insolvency (1997)
  - So, we can use it as a template while making our own law. Government is working on such bill.

### 13.3.8 🐼🔧📄 NPA: relief given to MSMEs in 2019

- 🐼 2019-Jan: If an MSME firm had previously taken a bank loan upto ₹25 crore but defaulted on repayment. RBI permitted banks to do one-time restructuring of such loans by 31/3/2020 (Subject to certain technical conditions). 📁 Budget-2020 asked the RBI to extend this facility till 31/3/2021.
- 🐼 2019-Sept: Government ordered PSBs that even if MSME are not repaying loans, don't treat them as NPA till 31/3/2020. This will protect MSMEs from SARFAESI/IBC proceedings, while the Govt attempts to revive their business through other measures. Government also ordered PSBs to organize Loan-Melas & give loan to 'RAM' category – retail, agriculture, and MSMEs.

### 13.3.9 🏠🔧📄 RBI's 'Feb-12' Circular (2018) & Prudential Framework (2019)

- Using the powers of RBI Act, RBI issued a circular on 12<sup>th</sup> Feb 2018. It discontinued CDR, S4A, SDR etc. henceforth IBC to be main tool. 1-day default norms, lenders to



immediately start resolution, IF resolution not finalized in 180 days then liquidation. Penalties for noncompliance.

- **2019-April:** SC declared it ultra-vires (कानूनीसीमा से बाहर) because not consistent with provisions in RBI Act.

**2019-June:** Consequently, RBI released Prudential Framework for Resolution of Stressed Assets Directions 2019 (तनावग्रस्त परिसंपत्तियों के दिशा-निर्देशों के लिए विवेकपूर्ण रूपरेखा)

- RBI applied it on Banks, AIFI and selected categories of NBFCs- using the powers under Banking Regulation Act (1949) and RBI Act (1934).
- It discontinued CDR, S4A, SDR, JLF etc. henceforth IBC to be main tool.
- If principal / interest is overdue for 1-30 days, classify loan account as SMA-0. Then, within 30 days, the lender shall review the loan account, & initiate resolution process (RP). (Previous Feb-12 circular required lenders to start RP within 1-day of SMA-0.)
- It framed rules to facilitate **Sashakt** approach #1 and #2-inter-creditor agreement (ICA).
- Lenders must upload data of ₹5 crore /> loans to RBI's **CRILC** portal on weekly basis.
- Forbids loan restructuring for borrowers who have committed frauds/willful default in past. Forbids evergreening of stressed loans.

### 13.4 **ECONOMIC SURVEY ON NPA (आर्थिक सर्वेक्षण)**

#### 13.4.1 **Economic Survey 2018-19 on NPA (released in 2019-July)**

- With I&B Code and other measures by RBI, the NPA % has declined in 2018-19, and credit growth has improved. However, banks' profitability has also declined.
- I&B code's time-bound mechanisms have prompted '**behavioural changes**' in corporate borrowers (कॉर्पोरेट देनदार के व्यवहार में परिवर्तन). Now they fear losing control of the company. This has improved corporate governance, cash and financial discipline.
- By 31/3/2018: ₹ 50,000 crores worth NPAs have been upgraded to std assets (meaning the (arrogant) borrowers have been forced to resume paying principal & interest regularly.)
- Due to IBC Code, India's rank has improved in World Bank's Ease of Doing Biz report. (*More in Pillar#4*). *However, we also need to begin more reforms:*
  - ✓ We need to increase the number of NCLT benches, number of IP Professionals, use ICT technology for faster case proceedings.
  - ✓ We should enact separate law on **cross-border insolvency**. (सीमा-पार दिवालियापन)
  - ✓ **Group Insolvency** (समूह दिवालियापन): Big Industrialists usually operate through groups of companies, each having a separate identity e.g. Tata Sons Ltd → 1) TCS 2) Tata Motors 3) Tata Steel etc. If one of these company become insolvent, it creates negative ripples on entire group's financial health. Certain legal-technical reforms are necessary to address such group-insolvency.
  - ✓ Certain legal-technical reforms to address insolvency cases involving individual proprietors and partnership firms. (*They're legally different entities than 'Companies registered under companies Act. More in SEBI handout*)

#### 13.4.2 **Economic Survey 2020 on NPA (released in 2020-Jan-31<sup>st</sup>)**

- NPA had reached its peak in 2018 but now it appears to be declining because of various measures taken by the Government and RBI.
- Nearly 3000 insolvency professionals (as on December 31, 2019).



- Appreciated that IBC proceedings take on average 340 days to complete, unlike SARFAESI legal proceedings which take 4.3 years.
- Appreciated that IBC helps recovering more amount of loan than SARFAESI in 2018-19

Approx. Amount recovered in crores	2017-18	2018-19
SARFAESI and DRT	33,000	52,000
IBC	5000	71,000

### 13.4.3 📁📁ES20: Use AI-ML Technology

In PSBs, most of the loan-information processing (=Credit analytics) happens manually (ऋण विश्लेषण हस्तचालित रूप से करते हैं). This causes inefficiency, frauds and loan default.

Tools such as \_\_\_\_\_ (कृत्रिम आसूचना और मशीन प्रशिक्षण) can help them in following ways:

- ⇒ Willful defaulters usually create fictitious companies (फर्जी कम्पनी) to transfer their assets / shares / money just before they stop paying loan installments.
- ⇒ Artificial Intelligence (AI) can alert the authorities through real time surveillance & data analytics of the borrower's NEFT/RTGS/DEMAT account transaction.
- ⇒ **Geo-tagging of assets (संपत्ति की जियो-टैगिंग)** i.e. adding longitude and latitude data with the photos & videos of the Factory building, machinery, vehicles, aeroplanes, helicopter etc. Then, →
  - Scamster can't pledge fictitious assets as collaterals for loans (फर्जी संपत्ति जिसका अस्तित्व ही नहीं)
  - Scamster can't pledge the same asset as collateral to multiple banks/NBFCs. (एक ही संपत्ति को एकाधिक लोगों के पास गिरती रखकर लोन में धांधली करना)
- ⇒ **Global Positioning System (GPS) chips** may be embedded in the factory-machines and vehicle to track their real time location →
  - If scamsters move the machinery out of the factory, the banker will be alerted.
  - Bankers can remotely disable machines/vehicles, if loans are unpaid.
- ⇒ **Blockchain Technology** can be used for storing and verifying the authenticity of the data.
- ⇒ AI can monitor **Social media activities** e.g. Borrower is not paying the loan and yet sharing the Switzerland vacation photos on Instagram = He is a wilful defaulter → Attach his assets under the SARFAESI Act.

👉 **Caution?** borrower's privacy and dignity should also be respected while doing such computerized surveillance. (उधारकर्ता की निजता का भी सम्मान रखना चाहिए)

### 13.4.4 📁📁ES20: setup PSBN Network

- ⇒ Government should create a new organization named PSBN (PSB Network), which will act as a Financial Technology Hub (FinTech: वित्तीय प्रौद्योगिकी).
- ⇒ Whenever a borrower applies for loan to a public sector bank → Details sent to PSBN.
- ⇒ PSBN will verify the creditworthiness (वित्तीय साख) and risk profile (दिवालियेपन का जोखिम) of the applicant through:
  - Artificial Intelligence (AI), machine learning (ML) and Big Data Analytics- as explained in the previous section



- E-KYC-Aadhar verification → cross checking his Aadhar number against Financial data from Corporate Affair Ministry, SEBI/share market, Income Tax Department, GST, etc.

😊 **Benefit?** fraud prevention, reduced the burden of NPAs, quicker decision making, process loan applications faster, cost saving for individual banks as all of them can use a single hub instead of spending on separate servers/technology.

#### 13.4.5 🏦 PSB Banking Personnel Reforms → 📖 ES20 Vol1Ch7 (50 years anni.)

- PSBs should be allowed to do
  - 1) \_\_\_\_\_ of atleast some specialists (कुछ विशेषज्ञों की केम्पस परिसर से सीधी भर्ती)
  - 2) \_\_\_\_\_ in higher management (उच्च प्रबंधन में पार्श्विक भर्ती).
- PSBs should give \_\_\_\_\_ (ESOP: कर्मचारी स्टॉक विकल्प योजना) to their employees.

ESOP is a type of benefit plan wherein employees are given some shares of the company (Apart from their regular monthly salary).

When/if company makes more profit →	How does employee benefit from ESOP?
1) Market price of its shares will increase.	He can sell his shares to a third party for a large gain.
2) the dividend to the shareholders will increase.	He can keep the shares with himself, and will get large dividend from the company (in addition of his regular salary)

As shareholders, some of these employees may even join as board members → help designing more realistic business policies at the apex level. Thus, ESOP changes mind-set from an “employee” to that of an “owner”. It encourages the employee to work harder with more dedication, loyalty & passion for company’s profitability and brand image.

### 13.5 🏦👥 DICGCI: DEPOSITOR’S INSURANCE HIKED BY 📖 BUDGET-2020



- 1961: Deposit Insurance and Credit Guarantee Corporation Act (निक्षेप बीमा और प्रत्यय गारंटी निगम)- mandates that all types of banks must buy insurance on their deposit accounts from DICGC (100% owned by RBI, HQ: Mumbai).
- Banks have to pay premium for this insurance.
- When a bank shuts down, DICGCI will pay upto ₹ \_\_\_\_\_ insurance to every deposit holder for his principal and interest.
- 📖 Budget-2020: raised the insurance coverage to ₹ \_\_\_\_\_

#### 13.5.1 🏦👥 RBI’s Bimal Jalan panel (2018-Nov)

- It was setup to review RBI’s economic capital framework (आर्थिक पूंजी संरचना) & decide the guiding principles for dividend transfer to Government.
- 2019- August: RBI board approved its report.
- It updated / reduced buffer related technical norms in such manner that RBI will be able to transfer more dividend / surplus to the Government.
- Accordingly for 2018-19: (1.23L dividend+52k extra)= ₹ 1.76 crore to be transferred to government. This will help the government to meet its fiscal deficit target.



### 13.5.2 RBI's Financial / Accounting Year (वित्तीय वर्ष में बदलाव)

 Before	 After
RBI's financial year - 1934 onwards: January to December - 1940 onwards: July to June	- For 2020: a smaller balancesheet will be prepared from 1/July/2020 to 31/March/2021. Then - From _____, RBI will switch to annual April-March format.
But Govt's financial year is April-March so, RBI had to give interim dividend to govt until RBI's final balancesheet was prepared, then another (full) dividend was given.	After this reform, _____

2019: Bimal Jalan panel recommended above reform → RBI's central board accepted it








## 14: PILLAR#1-C: SEBI-SHARE MARKET


### 14.1 DEBT INSTRUMENTS: SHORT TERM (लघु अवधि ऋण उपकरण)

<b>LIBOR</b>	<b>London</b> Interbank Offered Rate (LIBOR) is the average interest rate at which banks in <b>London</b> give short term loans to each other. It serves a benchmark, using which <b>Global</b> banks decide their call money /notice money rates.
<b>MIBOR</b>	In LIBOR definition, replace the word “London” → “Mumbai” and “Global” → “Indian”, and you’ll know what MIBOR is!
<b>CBLO</b>	Collateralized Borrowing and Lending Obligation. Clearing Corporation of India Ltd (CCIL) helps Financial Intermediaries (FI) to get short term loans through this instrument.

### 14.2 DEBT INSTRUMENTS: LONG TERM (दीर्घ अवधि ऋण उपकरण)

 <b>Masala Bonds</b>	These rupee denominated bonds issued outside India, to borrow money for Indian companies. ⇒ 2019-May: Kerala became the first state to issue Masala Bonds. Its Kerala Infrastructure Investment Fund Board (KIIFB) issued Masala Bond at the London Stock Exchange. Denomination: ₹ ₹ Total Size: ₹ 21.5 billion. Tenure: 5 years. Masala Bonds are usually issued by institutions with AAA rating. Since KIIFB has BB rating, hence offered higher interest rate: ~9.7% (वरना कोई खरीदता नहीं)
 <b>(Proposed) Elephant Bonds</b>	2019-May: Commerce ministry’s Dr. <b>Surjit S. Bhalla</b> Committee ‘to improve India’s share in global trade’ suggested ‘Elephant Bonds’. <b>Tenure:</b> 25-years. People declaring Black Money will be required to invest x%. → ₹ ₹ to be used only for infrastructure projects.
 <b>Social Impact Bonds (सामाजिक प्रभाव बांड)</b>	2019-Feb: SIDBI issued ₹ 300 cr. worth Women’s Livelihood Bonds (महिला आजीविका बॉन्ड) with the help of World Bank, UN Women org etc. - These bonds will be offered to High Net worth Individuals (HNI), Impact Investors (rich people interested in ‘indirect’ social service) etc. They’ll earn 3% annual interest rate for tenure of 5 years. - Money thus collected → SIDBI → Micro Finance Institutes (MFI) → loaned to individual women entrepreneurs in sectors like food processing, agriculture, services etc. for loans

### 14.3 SHARES / EQUITY FINANCE / IPO

- ⇒ 2019: Saudi Arabia’s public sector oil company \_ \_ \_ issued world largest IPO worth >\$25 billion. It was listed at Riyadh’s Tadawul Stock Exchange.
- ⇒  **ES20: No of IPO-issuing Companies have declined:** 134 (2017) → 103 (2018) → 47 (2019). Which indicates problems like protectionism (trade war), NPA, slowdown in consumer demand are preventing some of the companies from expanding further.
- ⇒ **(Full) Budget-2019:** we’ll set up a **Social Stock Exchange** under SEBI’s regulation. It’ll help social enterprises and voluntary organizations to raise capital as equity, debt or mutual funds. Then SEBI setup **Ishaat Hussain panel** to study it.





- ⇒ **Day trading / Intra-day trading:** Individuals buy and sell shares over the Internet over a period of a single day's trading, with the speculative intention of profiting from small price fluctuations.

#### 14.4 **FORCE MAJEURE (अभेद्य शक्ति)**

- ⇒ \_ \_ \_ \_ word for 'superior force'. It refers to unexpected external circumstances (अप्रत्याशित बाहरी परिस्थितियाँ) that prevent a party to a contract from meeting their obligations. e.g. Acts of God (natural disasters, epidemics), war, terror attacks.
- ⇒ In such cases, courts may not punish party for dishonoring contract. (करारनामे के दायित्व को न निभाना)
- ⇒ E.g. **Corona ( \_ \_ \_ \_ ) Virus** → Singapore Govt put restrictions on entry of Chinese → Singapore construction firms facing labour crunch (श्रमिकों की कमी) → invoked 'Force Majeure' to clients, "we can't finish building your homes/offices in time."
- ⇒ Coronavirus: >80k people in >50 nations infected (as of 2020-Feb). Restriction on global travel and trade. Investors fear that companies will not generate much profit. Many contracts/ payments will be stuck by Force Majeure. So, large scale withdrawal / exit of share investors from stock exchanges across the world. Even the BSE \_ \_ \_ \_ \_ by 1400+ points in a single day.

### 14.5 SHARE MARKET: MISC. TERMS

#### 14.5.1 **ISIN Number**

- ⇒ International Securities Identification Number (ISIN) is a Unique 12 characters, consisting of both letters and numbers.
- ⇒ It's a serial code to identify securities e.g. Reliance Industries Limited Shares ISIN: INE002A01018; Infosys Shares: INE009A01021.
- ⇒ Prevents mistakes in buying/selling shares/bonds of companies with similar sounding names. Facilitates the digital transactions through DEMAT account.
- ⇒ RBI issues ISIN for G-sec/T-bill. NSDL issues ISIN for securities other than G-Sec/T-bill.
- ⇒ **(Full) Budget-2019:** technical reforms in ISIN for ease in issuing Corporate Bonds.

#### 14.5.2 **IOSCO**

- International Organization of Securities Commissions (IOSCO) is the international body of world's securities regulators. SEBI is a member.
- It's known for its **IOSCO Guidelines** for Investors Protection and systematic risk in global economy.

#### 14.5.3 **Initial Coin Offering (ICO)**

- ⇒ Suppose, a company wants to raise investors' money for launching new cryptocurrency, or service/app related to an existing cryptocurrency.
- ⇒ Then, it'll issue Initial Coin Offering (ICO) → Investor subscribes to it, and receives 'tokens' (and not SHARES). Investors can use the 'tokens' to buy companies coins/services or may sell it to a third party.
- ⇒ RBI has cautioned Indians not to invest in such instruments, because of the dangers which we already learned in the Handout Pillar#1A-1: Bitcoins.



## 14.6 INVESTMENT INSTRUMENTS/FUNDS

### 14.6.1 🏠🏦🏛️ Sovereign Wealth Fund (SWF: संप्रभु धन कोष)

- ⇒ State owned investment fund, wherein central bank, finance ministry and other public sector financial intermediaries park their surplus fund. → money used for investment. E.g. Singapore's GIC sovereign wealth fund, Abu Dhabi Investment Authority (ADIA)'s funds, Qatar Investment Authority (QIA) etc.
- ⇒ **Sidetopic:** What is National Investment & Infrastructure Fund (NIIF) Ans. Pillar#5: Infrastructure handout.

### 14.6.2 🏠🏦🏛️: (🏠🏦🏛️) Bharat Bond (Debt) ETF (2019-Dec)

- ⇒ Fund Manager (\_\_\_\_\_ Asset Management Ltd) → He'll issue Bharat Bond-ETF.
- ⇒ **Maturity:** \_\_\_\_\_
- ⇒ **Unit Size:** ₹1000 each. So even middle-class investors buy these Bond-ETFs.
- ⇒ Fund managers will invest this ₹ into a basket of bonds issued by Central Public Sector Enterprises, Central Public Financial Institutions (CPFIs such as public sector bank and insurance companies) and other Government organizations.
- ⇒ **ETF** will be tradable at the stock exchange.

#### 👍 **Bharat bond ETF: Benefits?**

- ✓ **For Government companies** = Easier and more efficient to borrow ₹ instead of individually launching their bonds in the market.
- ✓ **For Investors** = safety because of assured return on bonds, irrespective of Government company's profit.
- ✓ Enhanced retail participation → deepening bond markets
- ✓ In future, more fund managers may be selected, and even non-AAA rated public sector bonds may also be included.
- ✓ **Budget-2020:** given success of Bharat bond ETF, we are planning to launch another debt-ETF containing G-sec. This will help the retail investors to invest in G-sec.

### 14.6.3 🏠🏦🏛️: (🏠🏦🏛️) Govt's AIF for Real Estate Sector (2019)

- ⇒ 2019-Nov: Govt to setup an alternative investment fund (AIF Category-II) using ₹ of govt, SBI and LIC. (Total 25,000 cr)
- ⇒ AIF Fund manager: SBI Cap ventures ltd.
- ⇒ AIF Fund manager will give ₹ (as Debt finance) to builders with unfinished housing projects → demand for steel, cement, construction workers= economic growth.

## 14.7 🏠🏦🏛️ CORPORATE GOVERNANCE (कॉर्पोरेट शासन)

SPICe	⇒ Earlier, Corporate affairs ministry designed INC-29 online form to registration of new company. Later it was replaced with Simplified Proforma for Incorporating Companies ( <b>SPICe</b> ) <b>Online form</b> .
CARO Guidelines	⇒ An auditor is an authorized personnel that verifies the accuracy of financial records. Their primary objective is to protect businesses from fraud. Companies Act → Companies Auditor's Report Order ( <b>CARO</b> ) = Auditors have to annually submit reports to the Corporate affairs ministry



## 15: 1D: 🏠 INSURANCE, PENSION & FINANCIAL INCLUSION

### 15.1.1 🏠 LIC's Disinvestment (2020, विनिवेश)

- ⇒ LIC's insurance products come with a sovereign guarantee (संप्रभु गारंटी) by the Govt. So people prefer to buy it over private sector insurance policies. This hampers perfect competition (पूर्ण प्रतियोगिता).
- ⇒ If Government shareholding ↓ → LIC functioning becomes independent → less financial repression of households (e.g. how LIC bought loss making IDBI under Government's pressure. Ref Pillar#1B-1: Banks' classification).
- ⇒ So, earlier, International Monetary Fund (IMF, 2018) and Justice B.N.SriKrishna's Financial Sector Legislative Reforms Commission (FSLRC-2011: वित्तीय क्षेत्र विधायी सुधार आयोग) had also advised the same to Government of India.
- ⇒ 📅 Budget-2020: LIC Act will be amended → LIC will be converted from a statutory corporation (वैधानिक निगम) into a listed company → Initial Public Offering (IPO) → Government will sell part of its shareholding. Because of following reasons:

### 15.2 🏠 GEN INSURANCE → HEALTH INSURANCE (स्वास्थ्य बीमा योजनाएं)

Fixed Benefit Policy (निश्चित लाभ)	Indemnity Based (क्षतिपूर्ति आधारित)
<p>Fixed payment given depending on illness.</p> <p>⇒ If the Policy agreement said "if you get cancer, we'll give you ₹50 lakhs."</p> <p>⇒ So, even if a patient spends ₹10 lakh on hospitalization, still the company will pay ₹50l.</p>	<p>Upto to the "actual hospitalization cost" from the total insured sum.</p> <p>⇒ E.g. Policy covers upto ₹5 lakh annual health insurance.</p> <p>⇒ So if hospital bill = ₹1.5 lakh then insurance company will pay ₹1.5. Lakhs only.</p> <p style="text-align: center;"><b>Further Subtypes</b></p> <p>⇒ <b>Cashless policy:</b> patient simply goes to an empanelled hospital = free treatment.</p> <p>⇒ <b>Non-Cashless policy:</b> patient first pays hospital bill from own pocket → submits bills to insurance company → gets refund.</p>

### 15.2.1 🏠 Arogya Sanjeevani Policy (2020)

Too many types of health insurance policies with various features and premiums = a common man gets confused which health policy is best for him.

So, IRDAI ordered health insurance cos to launch a Standard Health Insurance Product (SHIP: आदर्श स्वास्थ्य बीमा उत्पाद) to cover the basic health insurance requirements of every person. Insurance Companies need to launch it FROM or BEFORE 1/April/2020 with following Features:

- ✓ **Name** of the policy must be "Arogya Sanjeevani Policy -<name of the company>". Any other name NOT allowed.
- ✓ **Type:** \_ \_ \_ \_ \_ Health policy insuring minimum ₹1 lakh to maximum ₹5 lakhs.
- ✓ **Validity:** minimum 1 year to lifetime
- ✓ **Entry age:** Minimum 18 to Maximum 65.
- ✓ Policy can be availed for (A) self and/or (B) Family Floater policies covering close family members such as spouse, children, parents. (स्वयं / पुरे परिवार के लिए)



- ✓ **What costs will be covered?** hospitalization cost, pre and post hospitalization cost, Ayush treatment (=Ayurveda, homeopathy etc).

### 15.3 AYUSHMAN BHARAT FUNDING

Budget-2018: Ayushman Bharat launched with two components:

- Transform 1.5 lakh Primary Health Care Centers (PHC) to be transformed into Health & Wellness Centres (स्वास्थ्य और कल्याण केंद्र). Free drugs, checkup, mother-child care etc.
- National Health Protection Scheme (AB-NHPS) → Later renamed 'PM Jan Arogya Yojana (PMJAY)' giving ₹5 lakh health insurance per (poor family) per year.

#### 15.3.1 PM-JAY Funding pattern after removal of Art 370

	Category (श्रेणी)	Cost sharing (खर्च की साझेदारी)
A	"Special Category States" (विशेष श्रेणी के राज्य): - North-Eastern States, and - TWO Himalayan Hilly States: Himachal Pradesh and Uttarakhand <sup>#</sup>	Union contributes 90%: State contributes 10% of the cost for scheme implementation in the given State.
B	- <b>Other States:</b> who are not in above category (UP, Bihar, etc.) - <b>Union territory (UT) with legislature:</b> Delhi, Puducherry, Jammu & Kashmir.	60:40
C	- <b>UT without legislature</b> (बिना विधायिका के केंद्र शासित प्रदेश): <b>Ladakh</b> , Andaman Nicobar etc.	100%

- <sup>#</sup>Before the removal of Article 370, the State of J&K was previously in category, so it got 90:10 funding.
- But as a UT with legislature, J&K will get 60:40. So, 2019-Aug: Central Government considering creating a new category 'Hill Union Territory (पहाड़ी केंद्र शासित प्रदेश)' so J&K may continue to received 90:10 funding.

#### 15.3.2 Budget-2020: 5% Health CESS

- ✓ We'll setup more Ayushman BHARAT hospitals in aspirational (=backward) districts, for treatment of PM-JAY beneficiaries.
- ✓ Hospital construction Funding: Public private partnership (PPP) → Public side's funding will be provided using 5% health cess on customs duty on imported \_ \_ \_
- ✓ We'll use AI and Machine Learning to take preventive actions against the spread of diseases. Total ₹6400 cr allotted for PM-JAY.

**AB CD ? Which one of the following is not a feature of the Ayushman Bharat Scheme? (UPSC-CDS-i-2020)**

- There is no cap on family size and age.
- The scheme includes pre- and post-hospitalization expenses.
- A defined transport allowance per hospitalization will also be paid to the beneficiary.
- The scheme provides a benefit cover of Rs. 10 lakh per family.

**AB CD ? Centrally sponsored scheme Ayushman Bharat is a national health insurance system for: (UPSC-Geologist-2020)**

- women
- every citizen
- old age people
- poor and vulnerable.



## 15.4 🏠👤📊 PM FASAL BIMA YOJANA: NORMS CHANGED IN 2020

Before-2020	From 2020-Kharif
Premium (बीमा-किस्त) paid by farmers: - ⇒ Rabi winter crops (1.5%) ⇒ Kharif summer monsoon (2%) ⇒ Horticulture & Commercial crops other than oilseed & pulses 5% Remainder premium is paid by Union: State	Farmer's portion is unchanged. However, Union:state sharing changed:
Suppose a kharif crop insurance premium = ₹100. ⇒ Farmer paid ₹2 of the premium ⇒ Union paid ₹49 + State paid ₹49. In other words, Union and States shared their premium burden half-half (50:50).	Suppose a kharif crop insurance premium = ₹100. ⇒ Farmer pays ₹2 of the premium ⇒ Union pays only ₹25 to 30 based on whether it's irrigated or unirrigated respectively. ⇒ State may have to pay ₹68-73. So, states' burden increased. ⇒ However, the Union will bear _ _ _ _ of the burden in case of North Eastern States.
Compulsory (अनिवार्य) for farmer to buy this insurance policy, IF he wanted crop loans from bank	_ _ _ _ _ for farmers. But, critics fear this may result in higher premiums (e.g. ₹200) if less farmers are subscribing.
Multiple Perils (एकाधिक आपदाएं) covered such as flood, drought, hailstorm. But, farmers in Rajasthan had no fear of floods.	'Single-peril' (एकाकी आपदा) insurance can be taken e.g. "protection only against drought." This will help reduce premium amount.
Government allotted a district /area to an Insurance company for usually 1 year.	Minimum 3 years. And if company shows outstanding performance then even more years may be granted. This will encourage companies to invest more in the marketing & insurance agent network.
--	Updated the methodology for assessment of crop loss

### 15.4.1 🏠👤📊 Insurance to Banks on Exporters' NPA → NIRVIC Scheme (2019)

Boss? \_ \_ \_ \_ \_ Ministry → Export Credit Guarantee Corporation (ECGC)

- ✓ NIRVIK (Niryat Rin Vikas Yojana) is an Export Credit Insurance Scheme (ECIS).
- ✓ Exporter takes a loan from a bank. But if he defaults then ECGC will cover upto \_ \_ of his principal + interest losses to the bank. (Before NIRVIC scheme, it was only 60%)
- ✓ Exporters pay 'premium (बीमा-किस्त)' to the bank → bank pays it to ECGC.
- ✓ Premium rates depend on sector e.g. gems jewellery sector has higher premium because risk/losses are more than other sectors.



#### 15.4.2 📄🏠📑 Title Insurance (जमीन / इमारत का टाइटल बीमा)

- 'Title' (अधिकार-विलेख) means a legal document showing ownership of a property. 'Title dispute': usually happens when multiple persons are claiming ownership of the same land / building.
- 'Title Insurance' protects the new buyer in case of such legal disputes (by refunding the money he had spent in buying land, construction, legal expenses etc).
- Real Estate Regulation and Development Act 2016 (RERA) requires the builders to buy this type of insurance. More on RERA in pillar#5.

#### 15.4.3 🛖🌪️ (Proposed) Catastrophe Insurance (आपदा बीमा)

- ⇒ Protects the client from natural and manmade disasters.
- ⇒ Presently, farmers' crops are protected from natural disasters through PM-Fasal Bima Yojana. But, if his own home was destroyed in floods, it's not covered → Union & State Governments forced to use taxpayers' money for paying compensation to victims of floods, cyclones etc.
- ⇒ 2019: IRDAI planning to allow catastrophe insurance (or CAT cover) for poor people.  
<update when done>

#### 15.4.4 Insurance progress indicators (बीमा प्रगति संकेतक)

As per 📊📅 ES20	Insurance penetration (%: बीमा प्रवेश) =Premium divided by _ _ _	Insurance Density (\$:बीमा घनत्व) =Premium divided by _ _ _
Life (2011-18)	📉 Declining in zigzag fashion. (2.74% in 2018).	📈 Improving in zigzag fashion. (\$55 in 2018)
Non-Life (2011-18)	📈 Improving zigzag fashion. (0.94% in 2018)	📈 Improving steadily (\$19 in 2018)

For India, these indicators are low compared to many developing countries due to aforementioned challenges.

#### 15.4.5 FDI in Insurance Sector changed by 📁 Full Budget-2029

(Full) Budget-2019: FDI limits increased from 49% to 100% in insurance intermediaries i.e.

- Agents & brokers.
  - Surveyor/ Loss Assessor.
  - Third Party Administrators (e.g. Hospital where treatment is given)
- Benefit?** Foreign companies can enter this space, increased competition, better services.





## 16 → (₹ 31) PENSION (पेंशन)

### 16.1 EPF COMMUTATION (2020)


- ⇒ EPFO: Employees' Pension Scheme (EPS: कर्मचारियों की पेंशन योजना) = worker gets pension after retirement age (58 years).
- ⇒ EPF Pension commutation (रूपांतरण) = Worker can partially withdraw his pension in advance (before reaching retirement age). But, then EPFO will pay him less pension afterwards when he actually reaches retirement age.
- ⇒ 2020: some technical reforms made to help workers here. What/How? NOTIMP

### 16.2 OLD PENSION SCHEME (OPS) WILL NOT BE RE-INTRODUCED

- **Before-2004:** Government was entirely responsible for arranging the pension money for its employees.
- **But after 2004's NPS:** Govt Employee's salary is partially deducted and invested in financial securities, his pension is thus "NOT FIXED nor fully paid by Government" but it's dynamically linked with dividend & interest generated by those financial securities.
- Thus, in NPS, Govt employee himself is 'contributing money' towards his pension.
- So, some government employee organizations oppose NPS because it does not provide a fixed pension amount but depends on uncertainty in financial market. They keep demanding re-introduction of the old pension scheme (OPS: पुरानी पेंशन योजना).
- 2019-July: Govt clarified in Lok Sabha, "We have no plans of reverting to OPS. Because in OPS, Government has to arrange entire pension money = less funds available for poor people's welfare schemes. So, we're going to keep NPS for Government employees."

#### 16.2.1 → : Pension: Three Maan Dhan Yojanas

18-40 Age; ₹ 55-200 fees; Pension @60=3000 → family pension ₹ 1500	LIC Fund manager + This Ministry co-contributes	Who?
1) Pradhan Mantri Shram-Yogi Maan-dhan (Feb'19)	Labour	unorganized sector workers with monthly income upto ₹15k
2) Pradhan Mantri Laghu Vyapari Maan-dhan Yojana (Jul'19)#	-- --	Small trader / shopkeepers whose annual turnover does not exceed Rs 1.5 crore, based on self-declaration.
3) Pradhan Mantri KISAN Maan-dhan Yojana (Aug'19)	-- --	small / marginal farmers with upto 2ht land.

- 1 person can join only 1 type of above scheme.
- Income Taxpayers & those who joined EPFO/ESIC are not eligible for any of these schemes.
-  **(Full) Budget-2019:** announced to launch "Pradhan Mantri Karam Yogi Maandhan Yojana" for Small traders / shopkeepers. But, when they actually notified it, the title was changed to "Pradhan Mantri Laghu Vyapari Maan dhan Yojana" technically called,





“National Pension Scheme for Traders and Self Employed Persons Yojana” or in shorter form “NPS-traders”.

- **Budget-2020:** we'll launch a **Universal Pension Coverage** with auto enrolment for workers. It'll cover workers even when they change jobs. <update when actually done>

### 16.2.2 Separation of PFRDA and NPS Trust

- 2008: PFRDA setup a body NPS Trust. NPS Trust manages the National Pension System (NPS) and Atal Pension Yojana funds.
- **(Full) Budget-2019:** PFRDA is the pension sector regulator, so it should separate itself from NPS-trust which is doing pension business activity. We'll initiate technical steps for this. *(Recall that Government took over NHB from RBI. Similar pattern visible here- the financial regulators themselves should not be involved in running financial products, so that they can work in a dispassionate and impartial manner.)*

Sidenote: [pensionsanchay.org.in](http://pensionsanchay.org.in) = PFRDA webportal for creating financial awareness

## 16.3 SOCIAL SECURITY FOR OVERSEAS INDIANS (PENSION / INSURANCE)

Following schemes' boss? Ministry of External Affairs (विदेश मंत्रालय)

### 16.3.1 Mahatma Gandhi Pravasi Suraksha Yojana, 2012 to 2017

- ✓ It was a voluntary “insurance+pension” policy for Indian workers in foreign countries.
- ✓ but very few people subscribed so ultimately closed in 2017.

### 16.3.2 Pravasi Bharatiya Bima Yojana, 2017

Some nations do not have strict laws regulating the entry, employment or safety of foreign workers. So, the Indian Government classifies them under Emigration Check Required (ECR: उत्प्रवास जांच की आवश्यकता) countries. e.g. Saudi, Qatar, UAE, Libya, Malaysia, etc.

- ✓ It's compulsory for Indian workers going ECR nations to join Pravasi Bharatiya Bima Yojana from the empanelled insurance companies.
- ✓ Insurance cover of Rs. 10 lakhs if accidental death/permanent disability while abroad,
- ✓ Maternity expenses (प्रसूति खर्च) cover for women worker, Family Hospitalization etc.
- ✓ Premium: ₹275-375 depending on tenure of policy (पॉलिसी की अवधि के हिसाब से).

## 16.4 GIG WORKERS' SOCIAL SECURITY CODE (गिग कर्मी की सामाजिक सुरक्षा संहिता)

- ⇒ **Informal workers** (अयथाविधि कर्मी)= doesn't have formal job contracts with employers. E.g. Domestic Maids, Brick Kiln Workers, Construction Labourers, Gurkha Chowkidar, Dhaabaa cooks/waiters etc.
- ⇒ **Gig workers** (गिग कर्मी)= Uber Taxi Drivers, Amazon/Zomato Delivery boys, Urbanclap's beauticians/ plumbers/ AC repairman, Unacademy Educators etc. They are freelancers / independent contractors (स्वतंत्र ठेकेदारों) hired by startup or digital companies for short-term engagements. While they may have some written contract to deliver services to the company, but the contract is worded in such manner they are not “regular employees” of a company = not eligible for EPFO, ESIC etc.
- ⇒ 2019-Sept: Labour Ministry drafting a “social security code for all informal & gig workers”. It aims to provide insurance on death/disability/sickness, maternity benefit, pension, scholarship for their children etc.



## 17(👤👤:💰)→🏠 FINANCIAL INCLUSION (वित्तीय समोवेशन)

### 17.1 RBI'S LEAD BANK SCHEME (1969)

- RBI Selects a public or private sector bank which has significant presence in a rural area of a given district. Such bank is designated as "Lead Bank".
- Lead bank prepares credit plan with 'Service Area Approach', and coordinate with the efforts of Government, banks and NBFCs.

(Pre19-SetA) Q61. Service Area Approach was implemented under the purview of

- (a) Integrated Rural Development Programme
- (b) Lead Bank Scheme
- (c) Mahatma Gandhi National Rural Employment Guarantee Scheme
- (d) National Skill Development Mission

### 17.2 📁(FULL) BUDGET-2019: JANDHAN OVERDRAFTS TO WOMEN IN SHG

- Rural Development Ministry → National Rural Livelihoods Mission (NRLM) → Self Help groups (SHG) are formed.
- Every verified woman SHG member with a PM Jan Dhan account eligible for overdraft of ₹ 5,000. One woman in every SHG will also be eligible for upto ₹ 1 lakh MUDRA loan.

### 17.3 📱 JAN DHAN DARSHAK APP (2018)

Jointly developed by Department of Financial Services (DFS) & National Informatics Centre (NIC). It helps people find the nearby financial touch points such as Bank branches, ATMs, Post Offices etc.

### 17.4 (👤👤:💰)→📄 CHIT FUNDS AND PRIZE CHITS

Chit Funds (चिट फंड/कोष)	Prize Chits (इनामी चिट्स)
Scheme runs for a definite period of e.g. 12 months from Jan to Dec-2020.	Scheme is illegal and vaguely designed. It runs until idiot investors keep coming, then it collapses.
⇒ Every month each subscriber deposits equal ₹, as stipulated in the scheme document ⇒ Every month Foreman draws 'chit' → whichever subscribers' name comes he may get loan / prize. (in next month, previous winners' names may not be added to the lottery pool). This way, everyone has an equal chance of winning.	⇒ There are no official documents or account books. ⇒ Scamster will accept whatever small / large amount is offered by the poor person who falls prey. ⇒ Investor doesn't know with surety how much is contributed by other investors?
Even if you won in Feb-2020, still you'll have to compulsorily pay monthly deposits until Dec-2020 when the scheme is officially over.	Not compulsory to pay the monthly deposits after you've won the prize. (Therefore the scheme will collapse eventually, when new subscribers stop coming).



This is legal, under Chit Funds Act	This is illegal under Prize Chits and Money Circulation Schemes Banning Act, 1978
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~~Beyond that, — How does that work? How's that different from NIDHI companies (regulated by Ministry of Corporate Affairs) — B.com thing not. Imp. For UPSC.~~

#### 17.4.1 (👤👤💰) → 📄 Chit Funds (Amendment) Act, 2019

- ⇒ To amend 1982's Chit Funds Act.
- ⇒ Will regulate: 'Chit Funds', 'Kuri', 'fraternity fund', 'rotating savings and credit institution (ROSCA)'. (they're basically synonyms)
- ⇒ Chit must be drawn in the presence of at least two subscribers. Video-conferencing is allowed.
- ⇒ Chit Fund's fund manager is called 'Foreman'. New act increases his commission%
- ⇒ New Act also increases the maximum amount of investment the foreman can accept from subscribers.
- ⇒ Further powers with State Governments.

### 17.5 BANNING OF UNREGULATED DEPOSIT SCHEMES ACT, 2019

- अनियमित जमा योजनाओं पर प्रतिबंध कानून
- If an entity is soliciting public to deposit /invest money, then it could be regulated by RBI (Bank, NBFC-D), NHB RBI (Home loan NBFCs), SEBI (MF, ReITs, InvITs etc), IRDAI & PFRDA, Corporate Affairs ministry (NIDHI), State Governments (chit fund), EPFO, Multi state cooperative societies Register under Agriculture Ministry.
- A deposit-taking scheme is defined as 'unregulated' if person is asking people to deposit/invest money but he has not registered with any of the above organizations. E.g. builders, jewellers, etc. Act prohibits advertisement & money collection in it.
- Penalty upto ₹50 crores and jailtime upto 10 years + attaching the assets to refund depositors within prescribed timelines.
- Union to setup an online central database of deposit-taking activities in the country.

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