In a move to instil discipline among large borrowers with working capital facility, the Reserve Bank of India has mooted a proposal that at least 40 per cent of the sanctioned limit should be a term loan component.

For borrowers with an aggregate fund-based working capital limit of Rs 1.5 billion and above from the banking system, a minimum level of 'loan component' of 40 per cent shall be effective from October 1, 2018, the RBI said in draft norms placed on its website. It has sought feedback from banks and stakeholders till June 26, 2018.

The 40 per cent loan component will be revised to 60 per cent with effect from April 1, 2019.

For large borrowers, the outstanding 'loan component' must be equal to at least 40 per cent of the sanctioned fund-based working capital limit, including ad hoc credit facilities.

Drawings in excess of the minimum 'loan component' may be in the form of a cash credit facility, the RBI said.

Public sector bank executives said the move was expected to provide predictability over cash flow for lenders.

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Banks provide working capital finance by way of cash credit/overdraft, working capital demand loan, purchase/discount of bills, bank guarantee, letter of credit and factoring.

Cash credit (CC) is by far the most popular mode of working capital financing. While CC has its benefits, it also poses several regulatory challenges such as perpetual roll-overs, transmission of liquidity management from borrowers to banks/RBI and hampering of smooth transmission of monetary policy, according to bankers.

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The draft states the amount and tenor of the working capital demand loan (WCDL) may be fixed by banks in consultation with the borrower. The tenor of loan should not be less than seven days. Banks may decide to split the loan component with different maturity periods according to the needs of borrowers.

The ground rules for sharing of cash credit and loan components may be laid down by the consortium subject to guidelines on bifurcation (term loan and cash credit).

All lenders in the consortium shall be individually and severally responsible to make sure that, at the aggregate level, the 'loan component' meets the above mentioned requirements. Under Multiple Banking Arrangements (MBAs), each bank will have to adhere to these guidelines at the individual bank level.

About repayment and rollover of the loan component, the RBI said banks, consortiums and syndicates would have the discretion to stipulate repayment of the 'loan component' in instalments or by way of a "bullet" repayment. This would be subject to prudential norms for components like income recognition and asset quality.

The RBI said effective April 1, 2019, the undrawn portion of cash credit/overdraft limits sanctioned to large borrowers would attract a credit conversion factor of 20 per cent.

Loan Component

- At least 40% term loan component prescribed from October
- Public sector bank executives said the move was expected to provide predictability over cash flow for lenders
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- The draft states the amount and tenor of the working capital demand loan may be fixed by banks