Important Rates and Definitions of RBI

Policy Rates of RBI

Repo Rate

Repo rate is the rate at which the central bank of a country (Reserve Bank of India in case of India) lends money to commercial banks in the event of any shortfall of funds. Repo rate is used by monetary authorities to control inflation.

In the event of inflation, ***central banks increase repo rate as this acts as a disincentive for banks to borrow from the central bank***. This ultimately reduces the money supply in the economy and thus helps in arresting inflation.

The central bank takes the contrary position in the event of a fall in inflationary pressures. Repo and reverse repo rates form a part of the liquidity adjustment facility.

Reverse Repo Rate (RRR)

Reverse repo rate is the rate at which the central bank of a country (Reserve Bank of India in case of India) borrows money from commercial banks within the country. It is a monetary policy instrument which can be used to **control the money supply in the country.**

An increase in the reverse repo rate will decrease the money supply and vice-versa, other things remaining constant. An increase in reverse repo rate means that commercial banks will get more incentives to park their funds with the RBI, thereby decreasing the supply of money in the market.

Bank Rate

It is defined in Sec 49 of RBI Act of 1934 as the 'standard rate at which RBI is prepared to buy or rediscount bills of exchange or other commercial papers eligible for purchase'. When banks want to borrow long term funds from RBI, **it is the interest rate which RBI charges to them.**

The bank rate is not used to control money supply these days. Although penal rates are linked to bank rate. **If a bank fails to keep SLR or CRR then RBI will impose penalty & it will be 300 basis points above bank rate.**

Marginal Standing Facility

Marginal standing facility (MSF) is a window for banks to borrow from the Reserve Bank of India in an emergency situation when inter-bank liquidity dries up completely.

Banks borrow from the central bank by pledging government securities at a rate higher than the repo rate under liquidity adjustment facility or LAF in short. ***The MSF rate is pegged 100 basis points or a percentage point above the repo rate***. Under MSF, banks can borrow funds up to one percentage of their net demand and time liabilities (NDTL).

This scheme was introduced in May 2011 and all the scheduled commercial bank can participate in this scheme.

Reserve Ratios of RBI

Statutory liquidity ratio (SLR)

Apart from the CRR, banks are required to maintain liquid assets in the form of gold, cash and approved securities. Higher liquidity ratio forces commercial banks to maintain a larger proportion of their resources in liquid form and thus reduces their capacity to grant loans and advances, thus it is an anti-inflationary impact.

A higher liquidity ratio diverts the bank funds from loans and advances to investment in government and approved securities.

The RBI is resorting more to open market operations in the more recent years. Generally, RBI uses

- Minimum margins for lending against specific securities.
- Ceiling on the amounts of credit for certain purposes.
- The discriminatory rate of interest charged on certain types of advances.

Direct credit controls in India are of three types:

- Part of the interest rate structure, i.e., on small savings and provident funds, are administratively set.
- Banks are mandatory required to keep **19.50% of their NDTL (Net Demand and Time Liabilities) in the form of liquid assets.**
- Banks are required to lend to the priority sectors **to the extent of 40% of their advances.**

Cash Reserve Ratio (CRR)

Cash Reserve Ratio (CRR) is a specified minimum fraction of the total deposits of customers, which commercial banks have to hold as reserves either in cash or as deposits with the central bank. **CRR is set according to the guidelines of the central bank of a country.**

In short, **CRR refers to the ratio of bank's cash reserve balances with RBI with reference to the bank's net demand & time liabilities to ensure the liquidity & solvency of the scheduled banks**.

The share of net demand and time liabilities that banks must maintain as cash with RBI. **The RBI has set CRR at 4%. 1% change in it today affects the economy with Rs. 1000000 crores.** An increase sucks this amount from the economy, while a decrease injects this amount into the economy. So, **if a bank has 200 Crore of NDTL then it has to keep Rs. 8 Crore in cash with RBI. RBI pays no interest on CRR.**

Lending/Deposit Rates of RBI

Base Rate

Base rate is the minimum rate set by the Reserve Bank of India below which banks are not allowed to lend to its customers.

The Base Rate system has replaced the erstwhile **Benchmark Prime Lending Rate system with effect from July 1, 2010.**

Marginal Cost of Funds-based Lending Rate (MCLR)

MCLR is the new benchmark lending rate at which banks will now lend to new borrowers. **Till 31 March 2016**, banks used the **base rate** as the benchmark rate to lend.

Commercial banks must use the MCLR to set their interest rates. This system replaced the base rate system with effect from 1 April 2016. Its main purpose is ensuring that banks pass on the benefit of rate cuts to borrowers.

The Reserve Bank of India (RBI) has asked **banks to set at least five MCLR rates—overnight, one month, three month, six month and one year.**

Savings Deposit Rate

The interest rate earned by an account holder for the amount maintained in their savings account is called savings deposit rate.

Term Deposit Rate

Term deposits are funds that are locked in for a specified time period, during which the bank invests in financial products with higher returns.

Exchange Rates of RBI

FBIL Reference Rate

FBIL announces the benchmark rates for Term MIBOR for three tenors of 14-day, 1-month and 3-month on a daily basis except Saturdays, Sundays and public holidays. The benchmark rates are determined through a polling-based submission by the participating banks and Primary Dealers [PDs] out of the FBIL's list of identified submitters.

MIBOR is the acronym for Mumbai Interbank Offer Rate.

The benchmark rate is calculated based on the **actual call money transactions data obtained from the NDS-call platform of Clearing Corporation of India Ltd (CCIL).**