



maharashtra urban co operative banks federation
<admin@mucbf.com>

Shifting of G-sec portfolio as amortization of losses by transferring the portfolio to Held to Maturity

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federation <admin@mucbf.com>

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To: ssen@rbi.org.in
Cc: Anand <aamin@rbi.org.in>, rmukundan@rbi.org.in, dksajnani@rbi.org.in, "Nigam, Neeraj" <neerajnigam@rbi.org.in>, Mangaladevi Ashokkumar <mashokkumar@rbi.org.in>, anujranjan@rbi.org.in, nwrebello@rbi.org.in, bcsonawane@rbi.org.in, cgmdcbrco@rbi.org.in

To

Shri Sudarshan Sen
Executive Director,
Reserve Bank of India
Central Office Building
Shahid Bhagat Singh Road
Mumbai-400 001.

Respected sir,

Kindly refer our earlier letters dated March 9, 2017 & March 15, 2017 and as per discussion the delegation of Federation had with Shri Sudarshan Sen, Hon'ble Executive Director, RBI alongwith Shri Neeraj Nigam, Smt. M. Ashokkumar in the meeting held on March 21, 2017, please find enclosed herewith the required data collected from selected UCBs in Maharashtra for your kind information and further action.

Apart from required information received from UCBs as given above, we would like to highlight below some of our observations based on feedbacks from the UCBs.

1. During the Demonetization period, entire focus of every UCB was on cash management and practically no other banking activity took place like lending, NPA recovery etc.

2. Due to Demonetization, though there has been rise in CASA Deposits of UCBs, there was time lag of 1 to 2 months between receipt of SBN and the actual conversion of SBN by UCBs into usable funds in their accounts with banks/RBI. This time lag was due to the fact that the SBNs collected by UCBs were not readily accepted by RBI and other bank's currency chests or by their correspondent banks for immediate credit to depositing bank's account

3. Due to the delay in converting SBNs into Usable funds, the UCBs were put in to pecuniary loss, as the incidence of interest cost on deposits started from date of receiving SBNs and the income on the usable funds started very late only after they are put into some kind of investments after 31st Dec,2016.

4. Further many UCBs were maintaining 100% CRR as directed by RBI for a fortnight by literally borrowing funds from Money market (CBLO/REPO) if they had excess SLR by paying minimum 6.25% interest. In addition, during that period Electronic transactions were continued for the customers without any charges, hence there was outflow of funds which was arranged only through borrowing as there was no value of SBNs collected by UCBs for the reason mentioned above. Further some large Commercial banks' ATMs were available to public through which UCBs customers were withdrawing repeated small amounts and those banks were charging ATM transaction charge as applicable in NFS network (Rs.16/- per transaction), while UCBs were unable to start ATMs due to very less amount available in new notes with them to compensate such charges. Also, the branch expenditures of the UCBs had gone up due to uncompromising services rendered by them to their customers during demonetization period.

5. It may appear that UCBs got the benefit of CASA deposits but it is not the truth. The delay in converting SBNs into usable funds and the lack of commercial lending did not actually give benefit to UCBs for increasing Net Interest Income.

6. Generally, the usable funds generated from SBNs (with delay), had to be invested by UCBs in Investments in available liquid options like SLR securities, Debt Mutual funds, CDs etc.

7. If we look at the average yield on the investments in the range 6.20% to 6.30 % p.a. and the Interest cost of the banks @ 3.50 % p.a. on the incremental deposits during Demonetization period, the apparent theoretical NIM gain could have been in the range of 2.70% to 2.80 % p.a., under normal circumstances. However the circumstances were not normal for the reason mentioned above.

8. The entire gains in NIM which UCBs might have earned on the incremental funds invested post Demonetization period, the same were totally lost after the G-Sec yields rose sharply subsequent to the monetary policy stance change on 8th Feb 2017. The sharp depreciation in G-sec prices was more than 3 % to 5% across the yield curve compared to pre policy date.

9. Depreciation in G-sec prices by more than 3% put UCBs at heavy losses that will further put tremendous strain on the overall profitability of UCBs which are already struggling due to poor credit off take, rising NPAs and reduced standard loans during demonetization period.

Substantiating as above, we request RBI to consider our proposal favorably and permit all UCBs to shift their all G-Sec Portfolio as amortization of losses by transferring the portfolio to Held to Maturity and write off the loss over the period to maturity of the bond.

Thanking you

Yours faithfully

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(Sayali S. Bhoir)
Chief Executive & Secretary
The Maharashtra Urban Co-operative Banks' Federation Ltd
Wadala, Mumbai.