This Chapter highlights the recent trends in the money market as a whole and analyses each of the money market instruments in terms of its evolution and and more importantly the policy implications in chronological order from 1985 to 2003. The Chapter also outlines the impact of the recent Credit and Monetary Policy of November 2003 on the Money Market.
4.1 INTRODUCTION

Indian Financial Market has been undergoing a rapid change as number of measures were undertaken by the government of India and Reserve Bank of India (RBI) during the last decade and halft. to widen, deepen and integrate the different segments of the financial markets, viz money markets, debt market (particularly Govt securities market) and foreign exchange market. Majority of these initiatives, form integral part of the financial sector reforms. An attempt has been made here to look into the various policy measures taken in the pre-reform period i.e. 1985-1991 and in the post-reform period i.e. 1991-1992 onwards, to develop and activate the money and Govt securities market and to evaluate the effect of these measures in bringing about the desired change in their operations.

4.2 THE MEASURES IN PRE-REFORM PERIOD (1985-91)

Until the economic reform process was initiated in 1991, the financial system in India has functioned in an environment of construction, driven primarily by fiscal compulsions. The financial system was mostly geared to provide significant credit support for Government expenditure and Monetary and Debt Management Policy was underlined by

The Researcher is benefited from the literature and records of RBI and DFHI for the period 1985-2003
excessive monetization of the central Government fiscal deficit. Consequently, the money and Government securities market did not display any vibrancy and had limited significant in the indirect conduct of monetary policy.

The dealings in Indian Money Market were initially confined to a few instruments such as call (overnight) and notice (up to 14 days) money, Treasury bills and bills rediscounting. The market had a narrow base and was limited to a few participants-commercial banks and All India Financial Institutions. Entry in the money market was tightly regulated. The rates of interest on such instruments were fully regulated. The Treasury Bills market, which was relatively free up to early 1960s, also came to be restricted by the trends in deficit financing. The bulk of the issues were by way of ad-hoc 91-day Treasury Bills. The 91-day Treasury Bills, which was earlier sold through auctions, was placed on tap since 1965 at fixed discount rate. Until 1994, the discount was periodically adjusted to changes in the Bank Rate, but subsequently this link was also dispensed with and the discount rate remained unchanged at a fixed rate of 4.6% although for such short-term instruments.

Apart from Treasury Bills, Government securities include term securities of different maturities issued by Central and State Governments. As noted earlier, for many years, the country had been following a policy under which the Government borrowings were done at rates which were far below market rates resulting in large monetisation and prescription of high reserve ratios. For example, for 30-year Government securities the interest rate was as low as 6.5% in 1977-78. Such a policy, in turn created distortions in the banking system with usually high lending rate on certain segments combined with relatively lower interest rates on deposits. The average maturity of securities remained
fairly long viz above 20 years reflecting more the preferences of the issuers rather than those of the investors.

4.3 INITIAL IMPETUS TO REFORM PROCESS

The initial impetus to reforms in the financial sector came with the submission of two reports. The committee to review the working of the monetary system (Chakravarty Committee) was the first to make several recommendations in 1985 for the development of money and Government security market. As a follow-up, RBI set up a working group on Money Market (Chairman, Shri N.Vaghul), which submitted its report in 1987. The Vaghul working group recommended a four pronged strategy, as under, to activate the money market.

- Attempt to be made to widen and deepen the market by a selective increase in the number of participants.

- An endeavor to be made to activate the existing instruments and to develop new instruments so as to have well diversified mix of instruments suited to different requirements of borrowers and lenders.

- A gradual shift from administered interest rates to market determined interest rates.

- To create an active secondary market for money and securities through a process of establishing new sets of institutions, which would impart sufficient liquidity into the system.
Based on the recommendations of the Chakravaty Committee and Vaghul Committee, RBI initiated number of measures, as under during the period 1985-91.

- With a view to encouraging secondary market activity, the maximum coupon rate, which was as low as 6.5 per cent in 1977-78 was raised in stages to 11.5 per cent in 1985-86. Along with it the maximum maturity period was reduced from 30 years to 20 years.

- RBI introduced in November 1986, for the first time issue of 182-day Treasury Bill on monthly auction basis.

- The Discount and Finance House of India Ltd (DFHI) was set up in April 1988 as a money market institution jointly by RBI, Public Sector Banks and All India Financial Institutions. The setting up of DFHI was a major step towards developing a secondary market for money market instruments and providing liquidity to these instruments.

- The interest rate ceiling on call money was freed in stages from October, 1988. First, operations of DFHI in the call/notice money market were excluded from the interest rate ceiling in 1988 and in May 1989 the interest rate ceiling was completely withdrawn for all operations in the call/notice money market and on inter-bank term money transaction and also on rediscounting of commercial bills.

- In May 1990 RBI allowed GIC, IDBI and NABARD to enter the call money market as lenders. 13 other institutions, which were already operating in the
bills rediscounting scheme, were granted entry into the call money market as lenders in October 1990.

- Certain other non-bank institutions were permitted in October 1991 to participate in the call money market through DFHI, as lenders only.

- In addition to 182-day Treasury bill on auction basis, a number of other instruments were developed to provide depth to the money market. Certificates of Deposits (CD), commercial paper (CP) and Inter-bank participation certificates (PC) all entered the scene in 1989-90, at the initiative of the RBI, which framed guidelines for issuance of these instruments.

4.4 REFORM MEASURES IN POST 1991 PERIOD

In the wake of the economy undergoing an acute balance of payment crisis in 1991, a comprehensive package of stabilization and structural reforms measures was initiated by GOI in mid 1991. In the financial sector, the recommendations of the committee on the financial system (the Narasimham Committee) provided the impetus for further initiatives, although the thrust provided by the Chakravarty and Vaghul committees formed the basis for the initial reform in Money and Government securities market. These are briefly discussed hereunder:

4.4.1 MONEY MARKET

Money market is a market for short-term assets that are close substitutes for money, usually with maturities up to one year. A well-functioning money market provides a relatively safe and steady income-yielding avenue, for the short-term investments of
funds both for banks and corporates and allows the investor institutions to optimize the yield on temporary surplus funds. Reserve Bank of India is a regular player in the money market and intervenes to regulate the liquidity and interest rates in the conduct of Monetary Policy to achieve the broad objectives of price stability, adequate availability of credit and orderly functioning of financial markets. The main segments of the money market are the Call/Notice Money, Repos, Term Money, Commercial Bills, Treasury Bills, Commercial Paper and Certificates of Deposit.

A. CALL/NOTICE MONEY MARKET

The most active segment of the money market has been the call money market where the imbalances in the fund position, mostly of banks are evened out. The call/notice money market has graduated into a broad and vibrant market from a restricted and narrow one, consequent on the steps initiated with the onset of the process of liberalization and deregulation. Presently, banks and Primary Dealers (PDs) are operating as both lenders and borrowers, with a large number of financial institutions and mutual funds operating only as lenders. Corporate entities having lendable surplus are permitted to lend through Primary Dealers.

Since the withdrawal of the ceiling on the call rate, the call money rate has shown a tendency to fluctuate significantly on occasions. The sharp imbalances that arise in the demand and supply of money due to combination of several factors have led to the volatile behavior of the call money rate. The most important of these has been bunching of banks' needs for short-term funds in order to meet the CRR compliance. Another factor has been withdrawal of substantial liquidity from the system at one time to take
acre of Government borrowing needs. The volatility in call money rates has also been the result of the asset/liability mismatches of some large banks and, their over reliance on call money market for liquidity management. There have been a variety of other reasons as well, like bunching of payment of tax at specific periods, slow off-take of credit etc.

GRAPH 4.1
RATE TRENDS - CALL MONEY, REPO, REVERSE REPO
JUNE 2000 - OCTOBER 2003

Source: Report of the Internal Group on Liquidity Adjustment Facility, RBI, Dec '03

With the deregulation of the interest rate and the widening of the market through large number of participants, the call money market has been playing an increasing important role in equilibrating the banking systems demand and supply of short-term funds. However, despite widening of the call money market and DFHI's attempts to smoothen liquidity needs as mentioned earlier, there had been relatively high degree of volatility in the call money market in the post 1991 period. In order to reduce the instability in the call
market, RBI has taken several steps in the past few years. Since December 1992, initially it had injected liquidity through DFHI and STCI. In subsequent years, RBI has been moderating liquidity and volatilities in the call money market through continuous use of repos and refinances operations and changes in the procedure for maintenance of CRR requirements.

**GRAPH 4.2**

*Chart 3: Spread between Call Rate and Repo Rate and Turnover in Call and Repo Market*

*Source: Report of the Internal Group on Liquidity Adjustment Facility. RBI, Dec '03*
B. TREASURY BILLS

Treasury Bills are short-term (up to one year) borrowing instruments of Government of India. They are issued at discount to face value and on maturity, the face value is paid to the holder. The rate of discount and the corresponding issue price are determined at each auction. 364-day Treasury Bills on an auction basis were introduced in April 1992; this replaced the previous 182-day Treasury Bills. Subsequently, in January 1993, a 91-day Treasury Bill was introduced (in addition to the then-existing 91-day tap bill). The parallel existence of 91-day tap and adhoc Treasury Bill continued till the end of March 1997. Further, a 14-day intermediate Treasury Bill was introduced in April 1997 to enable State Govt. and some foreign Central Banks to invest their surplus funds. This intermediate Treasury Bill was not issued through auction, nor was it transferable as a negotiable instrument. During the subsequent period, it was felt that Treasury Bills of various maturities are essential to activate the market and to facilitate the cash management requirements of various market players. Accordingly, regular 14 day Treasury Bill was introduced in June 1997 and recently 182 Treasury Bill has been brought into use from May 1999. Now all Treasury Bills are issued with fixed notified amounts and non-competitive bids are kept outside the notified amounts. A uniform price auction for 91-day Treasury Bill has also been introduced on an experimental basis as against the discriminatory price auction for the other types of Treasury Bills.

Thus, with the availability of various maturities of treasury Bills in the market, this segment should obviously be the most preferred portfolio by the market participants who have short-term investible surplus funds. Being risk-free instruments and with the auction rates more aligned to market expectations, their yields have been serving as benchmarks
for short-term money and help in the pricing of various floating rate products in the market.

C. OTHER MONEY MARKET INSTRUMENTS

As noted earlier, new money market instruments such as Certificates of Deposit (CDs) and commercial papers (CPs) were introduced in 1989-90 to give greater flexibility to investors in the deployment of their short-term surplus funds. Also CPs enable highly rated corporate borrowers to diversify their sources of short-term borrowings and raise a part of their requirement at competitive rates from the market. In order to broad base the primary market and also to widen the scope for the secondary market, RBI has been liberating and relaxing gradually the guidelines governing the issues of CDs/CPs particularly relating to maturity and size. However, the lack of an active secondary market in CDs/CPs has greatly limited the usefulness of these two instruments. Further, CDs are resorted to when the deposit growth is sluggish and credit demand is high and a tightening trend in call rate is evident. Thus, CDs are generally considered to be high cost liabilities and banks have recourse to them only under tight liquidity conditions.

Another important money market instrument is Bills Rediscounting. Although the entry of participants in the bills rediscounting market still continues to be regulated, RBI has significantly widened the market by selectively allowing, besides banks and PDs, the entry of co-op banks, Mutual Funds, Financial institutions, etc. with a view to eliminating movement of papers and facilitating rediscounting. RBI introduced an innovative instrument known as “Derivative Usance Promissory Notes (DUPN)” backed by eligible usance (up to 90-days) commercial bills for the required amounts. Government has also
exempted stamp duty on DUPN. This has indeed simplified and streamlined the bill rediscourting by institutions and made commercial bill an active facility of rediscourting for even such short period as one day merely as a substitute for call money, RBI has since restricted such rediscourting for a minimum period of 15 days.

D. MONEY MARKET MUTUAL FUNDS (MMMFs)

Money Market Mutual Funds were introduced in April 1992 to provide an additional short-term avenue to investors and to bring money market instruments within the reach of individual investors. Despite several relaxations and modifications in the scheme, growth in MMMFs has not been on the expected lines. So far, only a few MMMFs have been set up. The total size of the funds is also not substantial. With the introduction of the policy of restricting call money to banks and PDs, MMMFs will be able to participate in the Repo transaction and also actively engage themselves in dealing in other money market instruments. The regulation of Money Market Mutual Funds is under the scope of Securities and Exchange Board of India (SEBI) since March 2000. However, banks and financial institutions desirous of setting up MMMFs will have to seek necessary clearance from Reserve Bank of India before approaching SEBI for registration.

E. READY FORWARD CONTRACTS (REPOS)

Ready forward or Repo is a transaction in which two parties agree to sell and buyback the same security at an agreed price at future date. It is a combination of security trading (purchase/sale) and money market (lending/borrowing) operation. In a way, it is a collateralized lending, and the 'repo rate' will represent the borrowing/lending rate, for the use of the money in the intervening period. Internationally, Repos are versatile
instruments and used extensively in money market operations. While inter-bank Repos were being allowed prior to 1992 subject to certain regulations, there were large scale violation of laid down guidelines leading to the ‘securities scam’ in 1992; this led Government and RBI to clamp down severe restrictions on the usage of this facility by the different market participants. With the plugging of the loophole in the operation, the conditions have been relaxed gradually and currently all dated Government securities are eligible for Repo. Along with banks, Primary Dealers are allowed to participate in both repo and reverse repo transactions. Certain non-bank entities, having current and SGL A/Cs with RBI, Mumbai have also been allowed to participate in reverse repo for lending money to other eligible participants. Also PSU bonds and private debt instruments have also been allowed as eligible repo instruments provided they are in dematerialized form in a depository and the transactions are put through recognized exchanges. This has not taken off yet, owing to certain operational problems. However, with the removal of stamp duty on transactions in debt instruments in demat form, a major hurdle has been cleared.

Repos can be for any period. While earlier there was a minimum period of 3 days, this has since been withdrawn.

Apart from inter-bank repos RBI has been using this instrument effectively for its liquidity management, both for absorbing liquidity and also for injecting funds into the system. The repo rate for absorption of liquidity, has become a benchmark rate- acting as a floor for the call money, while the Bank Rate at which liquidity is injected into the system by way of refinance acts as the ceiling for the money market rate, under normal circumstances.
There is a technical Advisory Committee on Government securities market and RBI had appointed a sub-group of the technical advisory committee to go into various aspects for expanding the repo market. The committee has since submitted its report and implementation of the various recommendations of the committee is under the active consideration of RBI.

4.5 INTER-LINKAGES IN THE MARKETS

Financial sector reforms initiated since 1985-86 and particularly after 1991-92, appear to have strengthened the market forces and have substantially activated the process of integration amongst various segments of the market. The inter-linkages between money and forex markets have come into sharper focus since then. These two markets influence each other to a significant extent as both the markets involve trading in funds and also due to the fact that banks are the major players in both these markets. Subject to the leeway available in the current guidelines, banks may use their forex funds to lend in the call money market by swapping their foreign currency and cover the exposure through forward purchase at a premium. Similarly, if the call money rates are quite low, banks may tend to buy spot dollars, lend in the forex market and cover their position with a forward contract. And an easy availability of money at low rate led to speculative activities in the forex market and contributed to the rupee showing signs of depreciation against U.S dollar, RBI had to take several measures in the past such as variation in CRR, increase in repo rates, hike in bank rates, changes in refinance facilities, etc to bring about the required stability in the forex market.
4.6 GOVERNMENT SECURITIES MARKET

Since the onset of financial sector reforms, Government of India and RBI have initiated various policies and other measures to develop a vibrant Govt. securities market. Governments (both Central and States) raise resources through issues of market loans. As these are liabilities of Govt. of India and State Governments, and because of the fact that repayments are made through Reserve Bank of India, investments in such securities are considered safe and risk free. These securities are also eligible as SLR investments. Since the date of maturity is specified in the securities, they are known as dated Government securities. This market has two segments: (a) Primary Market and (b) Secondary Market. The primary market consists of issuers of securities viz Central and state governments. The secondary market includes banks, financial institutions, insurance companies, provident funds, trusts, individuals, primary dealers, satellite dealers and RBI.

As part of reform process in the post July 1991 period, the debt management underwent significant changes. It was recognized that the principle objectives of debt management were: (a) to smoothen the maturity structure of debt, (b) to enable debt to be raised at close-to-market rates and (c) to improve the liquidity of Government securities by developing an active secondary market. It was recognized that the Govt securities market needed to be made specially vibrant, broad based and efficient in view of its role in setting a benchmark for the development of the financial market as a whole and bringing about an effective and reliable transmission channel for the use of indirect instruments and monetary control. Keeping the aforesaid objectives in view, the major planks of the initial stage of reforms in Govt securities market was focused on the Primary Market. Following were the measures initiated:
• Auction system of issuing securities has been introduced both in case of treasury Bills and term securities since the year 1992-93. This initiative is of great significance as it paved the way for market related rates of interest for the government paper.

• Base for Treasury Bill market was widened with auctioning of different types of treasury bills viz introduction of 364-day Treasury Bill in April 1992 and 91-day Treasury Bill in January 1993, and reintroduction of 182-day Treasury Bill in May 1999.

• Funding of auctioned Treasury Bills into term securities at the option of holders as part of debt management.

• New instruments such as Zero coupon bonds, Tap stock, Partly Paid stock, Floating Rate Bonds were introduced.

• Bringing down the maximum maturity of Govt securities from 30 years which was so in early eighties.

• Development of the instrument of repurchase agreements (repos) between Reserve Bank of India and commercial banks resumed from November 1996. The period of repo was varied between 3 to 4 days. This was changed into fixed rate repo in the November 1997. Reserve Bank of India discontinued the fixed rate repo on 5th June 2000, with the introduction of Liquidity Adjustment facility under which daily repos are conducted for absorption of liquidity and the interest rate is determined through auction procedure under uniform price method.
Since April 1997, a new approach was followed by Reserve Bank of India in its Open Market Operations – ie sale/purchase operations in Govt securities. In setting its price, Reserve Bank of India responded to market expectations. It was also prepared to purchase certain securities in cash.

Thus, through the reform measures in Primary Market, a groundwork was created to expand the investor base gradually towards non-traditional investors. Auction system contributed to a new treasury culture and a progressive development of bidding and portfolio management skills. The yield curve became flexible showing shifts according to market conditions and expectations. The move to market related rates of interest has given a powerful impetus to the primary market and to some extent open market acquiring depth, the focus now being shifted to building up of the institutional structure and development of the secondary market in government securities. These measures included:

- A phased in SLR requirements from an effective 37.4 per cent in March 1992 to a little over 28 per cent in March 1996 and to the statutory minimum level of 25 per cent in October, 1997.

- DFHI was authorized to deal in Government securities since 1992-93.

- The Securities Trading Corporation of India (STCI) was set up in 1994 by the Reserve Bank of India jointly with public sector banks and All-India Financial Institutions with the main objective of fostering the development of Government securities market (it commenced operations in Sept 1994).
In March 1995 Reserve Bank of India announced guidelines for setting up Primary Dealers (PD) with the objectives of:

(a) Strengthening the infrastructure in the Govt securities market in order to make it vibrant, liquid and broad based.

(b) Ensuring development of underwriting and market making capabilities for Govt securities outside the Reserve Bank of India.

(c) Improving secondary market trading system which could contribute to price discovery, enhance liquidity and turnover and encourage voluntary holdings of Govt securities amongst wider investor base; and

(d) Making PDs an effective conduit for conducting open market operations.

Two institutions viz DFHI and STCI were accredited as PDs in March 1996 and subsequently in June 1996 four more PDs viz SBI gilts, PNB gilts, Gilts securities Trading Corporation and ICICI securities became operational in June 1996. More licenses have since been issued and currently there are 16 Primary Dealers. With a view to providing incentive to PDs to develop secondary markets in Govt securities, Reserve Bank of India decided in June 1996 to pay some remuneration for their primary purchases by way of commission. In May 1997, this scheme was replaced by a new scheme for payment of under-writing fees to PDs. In terms of the revised procedure, a minimum of 25% of the notified amount (subsequently raised to 50% and now for the full amount) of each issues of dated Govt securities and T.Bills were
offered for underwriting and underwriting fees and amounts to be allowed to each PDs were to be decided on the basis of auction amongst PDs prior to auction of each security. The scheme was changed recently in the case of T.Bills where PDs are required to give minimum bidding commitments and fixed underwriting fee/commission for T.Bills has since been fully withdrawn. Reserve Bank of India was earlier providing liquidity support to PDs to support the reverse through the reverse repo route. This procedure was also subsequently dispensed with and Reserve Bank of India began giving liquidity support to PDs through their holdings in SGL A/C. however, later when new PDs entered the market they were permitted with liquidity support through reverse repo. The liquidity support is presently given to the Primary Dealers for a fixed quantum and at the Bank Rate based on their bidding commitment and also on their past performance. For any additional liquidity requirements Primary Dealers are allowed to participate in the reverse repo auction under the Liquidity Adjustment Facility along with banks, introduced by RBI in June 2000. These measures are expected to provide operational flexibility to PDs.

- Great market transparency was achieved through regular publications of details of SGL transactions in Govt securities put through at Bombay PDO since Sept 1994. Additionally, National Stock exchange, became operational in Jun 1994, providing secondary market trading facilities through its wholesale debt market segment since 1994-95. Further a system of Delivery versus payment (DVP) in Govt securities was introduced in Mumbai in June1995 to ensure that the
transactions in Govt securities has resulted in encouraging trading in securities and thereby imparting depth to the market.

- Repo market has been activated by allowing repos/reverse repos transactions in all Central Govt dated securities beside Treasury bills of all maturities. State Government securities and other debt instruments in demat form and dealt through the exchanges are also made eligible who are holders of SGL A/C with Reserve Bank of India Mumbai, have been allowed to have repo transactions with banks/PDs.

- In terms of notification issued under section 16 of the securities contracts (Regulation) Act, 1956 and under the amended Section 29A of the Act, Government of India has delegated regulatory powers to RBI to regulate dealings in Government securities, money market securities, gold securities and securities derived from these securities as also ready forward contracts in debt securities, vide notification dated March 1,2000.

- With a view to encourage Mutual Funds to set up Gilt Funds (in government securities) which will widen the investor base for Govt securities, Reserve Bank of India announced liquidity support facility to Mutual funds dedicated exclusively to Govt securities either by way of outright purchases or reverse repo to the extent of 20% of their outstanding investments.

- Guidelines for Satellite Dealers in Govt securities market were announced in Dec 1996 and in April 1997 and Reserve Bank of India granted approval to 16 entities
for registration as Satellite Dealers in Govt securities. The institution of Satellite Dealers was expected to activate retailing of Govt securities.

All the measures referred to above considerably helped development of the secondary market in Govt securities. It is however, vital for the emergence of a market with adequate depth and liquidity that players with different perceptions and liquidity requirements should also emerge; this is also essential in order to avoid unidirectional movements in the market. It is towards this objective that further steps are being taken by Reserve Bank of India. Now the presence of sixteen PDs in Govt securities market during last three years has brought about an element of dynamism both in primary and secondary segments. They have built-up a significant share in the primary market and the turnover in the secondary market has gone up substantially; furthermore reliable market related quotes are now available.

While a crore base has already established, it is important further widen and broaden the money and Govt securities markets with the objective of achieving the required depth in terms of both volume and liquidity. We also need to bring about reforms in legislation (Public Debt Act 1944 is being amended to Government Security Act) without which it may not be possible for the new products such as strips, interest rate swaps, forwards futures etc. to take off in full measure. Further the term money market also to take roots which is possible once the asset/liability management of Banks and FIs acquire the required sophistication and the Risk Management policies are implemented with full vigor. It is also essential to accelerate the use of information technology in the various markets so that geographical distance may not remain a handicap. A more transparent dealing system
is also necessary for an efficient market. Efforts on the part of PDs will also be required in coming years to develop a dealer distribution network, enabling portfolio adjustments by market agents, particularly banks. A diversification of investor base in Govt securities would not only improve the liquidity in the system but also create a class of investors with different requirements and perception of investment pattern. Indeed considerable work needs to be done both from policy and systems angle to make the Governments securities market more vibrant and highly liquid, and the current environment appears to be quite appropriate for initiating the required efforts in this regard.
4.7 CHRONOLOGY OF DEVELOPMENTS/POLICY MEASURES IN MONEY AND GOVT. SECURITIES MARKETS FROM 1985 TO 2003

Apr 1985

Important recommendations of the committee to the review the working of the monetary system (Sukhomoy Chakravarty Committee). Main recommendations:

- To develop Treasury Bills as a monetary instrument so that open market operations would gradually become the dominant instrument of monetary policy.

- To revise upward, the yield structure of Government securities so as to create a demand for public debt outside the RBI and hence limit the degree of monetisation of the debt and

- To adopt monetary targeting as monetary tool with price stability being the ultimate objective of monetary policy

Sept 1986

In pursuance of the recommendations of the Chakravarty Committee RBI appointed on Sept 86 a Working Group under the chairmanship of Shri.N.Vaghul to examine the possibilities of enlarging the scope of the money market and to recommend specific measures for evolving money market instruments.

Nov 1986

RBI introduced for the first time an issue of 182 day Treasury Bills on Auction basis.
The Vaghul Committee submitted its report to RBI. The working Group recommended the following:

- A premier house should be established to develop the bill culture.

- The call money rates (including the inter-bank term money arte) should be left to be determined by the market forces.

- The maximum discount rate on bills should not exceed an effective interest rate of 16 per cent.

- The procedure for re-discounting of bills should be simplified and rediscounting by the institution should be freely permitted.

- Commercial paper should be introduced in a restricted way and the interest rate of commercial paper should be freely determined by market considerations.

- It would be necessary for larger no. of participants to bid regularly in the auction and to build a portfolio of varying maturities to develop an active secondary market in Treasury Bills.

- A Treasury Bill refinance should be introduced.

- Interbank participation certificate should be reintroduced.
Apr 1988  The Discount and Finance house of India Limited (DFHI) was set up by RBI jointly with public sector banks and All India Financial institutions, as a major step towards developing a secondary market for money market instruments in order to provide liquidity to these instruments. DFHI commenced its operations on April 1998.

Apr 1989  Interest rate ceiling of 10 per cent in inter bank call money, 10.5% to 11.50% on inter bank term money and 12.50% on re-discounting of commercial bills was removed by RBI.

Jun 1989  Certificate of Deposit introduced by RBI as a money market instrument.

Minimum size of issues was Rs1 crore, in multiples of Rs25 lacs; maturity period 3 months to 1 year; total issue not to exceed 1% of aggregate deposits.

Jan 1990  Commercial Paper was introduced by RBI as money market instrument. Maturity period was fixed at 3 to 6 months, highest rating requirement (P1+), minimum size of the issue to be Rs1 crore and in multiples of Rs25 lacs.

May 1990  RBI allowed GIC, IDBI, and NABARD to enter the call/notice market as lenders only.
Oct 1990

RBI allowed other institutions which were already operating in bills rediscounhng scheme to access call money market as lenders only.

Bank wise limit on issues of CDs rose from 1 to 2% of aggregate deposits of the previous year. This limit was further raised to 3%. Minimum denomination of CD lowered from Rs1 crore to Rs50 lacs. Minimum issues size reduced.

Apr 1991

Guidelines for CPS relaxed. Tangible networth requirements reduced from Rs10 crore to Rs5 crore. Minimum rating requirement from P1+ to P1. Minimum denomination and issue size reduced from Rs25 lacs to Rs10 lacs and Rs10 crore to Rs50 lacs respectively.

Jan 1992

The corporate entities having lendable resources of minimum of Rs20 crore were permitted to lend in call money market through DFHI, provided they do not have any term borrowing from a bank.

Bank wise limits on issuance of CDs rose from 3% to 5% of average deposits.

Money Market Mutual Funds (MMMF) allowed to be set up by scheduled commercial banks and public financial institutions and debt market intermediaries.
Apr 1992  RBI discovered wide spread irregularities in securities operations of certain commercial banks and some prominent institutions and debt market intermediaries. New guidelines were issued to curb speculative activities. Ban on repurchase agreement and ready forward deals enforced. Such transactions allowed only between banks and in specified securities.

364-day Treasury Bill auction commenced on a fortnightly basis by RBI at market determined yields. Auction of 182-day Treasury Bill discontinued

May 1992  Banks allowed to issue CDs to the extent of 7% of fortnightly average outstanding deposits. Limit was further raised to 10% in Nov 92.

June 1992  RBI commenced auction of Central Government securities at market determined yields for the first time.

Dec 1992.  RBI commenced auction of Repurchase Agreements (Repos) in Central Government securities.

Jan 1993  91-Day Treasury Bill offered through auctions at market determined yield on weekly basis by RBI. Guidelines for issuance of CPs by corporates relaxed to allow other companies to access the market. Corporates, rated at least P2/A2 by CRISIL/ICRA allowed to issue CPs. Corporates with maximum permissible bank
finance limits of Rs50 crore allowed to issue CPs. (Reduced from
Rs100 crore fixed earlier). Six all India Financial Institutions
allowed to issue CDs with a minimum maturity period of one year
and a maximum maturity period of three years.

Apr 1993

RBI indicated intention to form Securities Trading Corporation of
India (STCI) to promote and develop secondary markets in
Government securities and PSU Bonds.

Oct 1993

Limit on issuance of CDs by scheduled commercial banks was
removed completely. Guidelines for issue of CPs by corporates
relaxed further. Minimum working capital limit also reduced form
Rs5 core to Rs4 crore, tangible networth limit also reduced from
Rs5 crore to Rs4 crore.

Maximum maturity of CP raised from 3 months to one year.
Corporates allowed to issue CPs to the extent of 75% of their
aggregate borrowings from the banking sector.

Term lending financial institutions allowed to access and develop
term market by borrowing for periods ranging from 3 to 6 months
within the stipulated limit.

Jan 1994

Government issued a zero coupon bond for the first time.
Securities Trading Corporation of India Ltd (STCI) commenced
operations.
<table>
<thead>
<tr>
<th>Date</th>
<th>Event</th>
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<tbody>
<tr>
<td>Jul 1994</td>
<td>GOI for the first time issued securities on a tap basis.</td>
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<tr>
<td>Aug 1994</td>
<td>State Governments and non Government PFs were allowed to participate in 91-day Treasury Bill auctions on a non-competitive basis.</td>
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<td></td>
<td>A historic agreement was signed between RBI and Government of India on the net issue of ad-hoc Treasury Bills.</td>
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<tr>
<td>Sep 1994</td>
<td>Particulars of transactions in Government securities and Treasury Bills put through SGL accounts at PDO, Mumbai were released to the press, daily, beginning Sep 1, 1994.</td>
</tr>
<tr>
<td>Oct 1994</td>
<td>Facility of standby arrangement for repayment of CPs was abolished.</td>
</tr>
<tr>
<td>Nov 1994</td>
<td>GOI issued first time Govt stock for which payment was received in installments.</td>
</tr>
<tr>
<td></td>
<td>Reverse Repo facility with RBI in dated Government securities was extended to DFHI and STCI to provide liquidity support to their operations.</td>
</tr>
<tr>
<td>Mar 1995</td>
<td>To strengthen Govt securities market, guidelines and procedures for enlistment of Primary Dealers were issued.</td>
</tr>
<tr>
<td>Apr 1995</td>
<td>Private sector mutual funds approved by SEBI allowed by RBI to operate only as lenders in the call/notice money market.</td>
</tr>
</tbody>
</table>
An auction system for conversion of Treasury Bills into dated Government securities was introduced.

Jul 1995

For the first time, GOI converted maturity of two year dated Government security into another dated Government security of the same maturity.

A system of Delivery Versus Payment (DVP) in Govt securities introduced in Mumbai to synchronize the transfer of securities with cash payment thereby reducing the settlement risk in the securities transactions and also preventing diversions of funds in case of transactions put through SGL a/c.

Sept 1995

A new instrument of Floating rate bond was introduced.

The minimum period for Repos in Treasury Bills and dated Government security was stipulated as three days.

Nov 1995

The private sector was allowed to set up Money Market Mutual Fund (MMMF). The size of MMMF and limits on instruments was deregulated.

Feb/Mar 1996

DFHI and STCI started functioning as a Primary Dealer in Government securities Market.

Apr 1996

RBI announced provision of liquidity support to MMMFs dedicated exclusively to investments in Government securities up
to 20 per cent of their outstanding investment either by way of outright purchase or reverse repos in Central Government securities.

In addition to DFHI and STCI four more PDs viz SBI Gilts, Gilt Securities trading Corporation and ICICI securities and Finance Co. become operational.

Four new PDs were permitted to participate in call/notice/term money market and bill rediscounting scheme both as lenders and borrowers.

RBI issued guidelines to banks for retailing of Government securities with non-bank clients.

With a view to providing incentive to PDs for developing the secondary market in Government securities, RBI introduced a scheme for payment of commission to PDs on all securities acquired by them in all auctions (including through devolvement route). The rate of commission for Rs100 face value was 25 paise (subsequently reduced to 12.50 paise), 50 paise and Re1 for 91-day Treasury Bill, 364-day treasury Bill and dated Government security respectively.
PDs were permitted by RBI to issue commercial paper and raise inter-corporate deposits subject to certain conditions to enable them to augment their resources.

With the object of mopping up the excess liquidity in the system RBI resumed conduct of Repo auctions.

Guidelines for satellite dealers in Government securities market announced.

RBI constituted Technical Advisory Committee on Government securities market to advice on on-going basis on policy issues aimed at development of a healthy and vibrant Govt securities market and on issues relating to open market operations.

A supplementary agreement was entered between Government of India and RBI to discontinue the system of automatic monetisation through ad-hoc Treasury Bills, effective April 1, 1997. The issue of 91-day Treasury Bills was also discontinued.

A scheme of Ways and Means Advances (WMA) to Central Government was introduced, effective April 1, 1997.

To further develop the money market, a Standing Advisory Committee on money market, (Chairman Dr.Y.V.Reddy) was set up on April 23, 1997 to advise the RBI.
The facility of routing call money transactions of non-bank entities (corporates) was extended to all primary dealers as against only through the DFHI, permitted earlier. 14-day Treasury Bill which was not transferable (and not through auction) was introduced.

The minimum size of issue of CDs to a single investor reduced from Rs25 lacs to Rs10 lacs; additional amount to be in multiple of Rs5 lacs.

The maturity period of CP was brought down from 3 months to 30 days.

Banks and PDs decided to form an autonomous self-regulating body called Fixed Income Money Market and Derivative Association (FIMMDA) for the money and securities market.

RBI granted approval to 17 entities for registration as Satellite Dealers (SDs) in Government securities market.

The rate of interest for liquidity support to PDs was linked to bank rate.

In order to activate the repo market, repo/reverse repo transactions were extended in all DGS and non-bank holders of SGL account with the RBI allowed entry into reverse repo transactions with banks/PDs in all Treasury Bills/all Central Government Securities.
Exemption was granted to banks from maintenance of CRR/SLR liabilities of the banking system (including Primary dealers) subject to compliance with minimum statutory requirements. This relaxation was intended to facilitate development of a more realistic yield curve and term money market.

Entities able to provide evidence to RBI of bulk lendable resources were permitted to operate in call/notice money market as lenders only through all PDs. The minimum size of operation per transaction was reduced from Rs20 crore to Rs10 crore.

RBI decided to introduce the practice of notifying amounts of all Treasury Bills auctions and to keep the 'non competitive bidders' outside the notified amount.

May 1997

A scheme for payment of underwriting fees to PDs was announced by RBI.

Jun 1997

Tax deducted at source was abolished on Government Securities by exempting interest payable on any security of central or state Government from the Provisions of Sec 193 of Income Tax Act. Consequently, the voucher system prevalent in the gilts market which was impending the growth of the secondary market ceased to exist.

14- Day Treasury Bill introduced by RBI.
Jul 1997  
FIs were permitted to invest in dated Government securities.

Oct 1997  
The minimum size of the issue of CDs to a single investor was reduced from Rs10 lacs to Rs5 lacs. CDs above Rs5 lacs to be issued in multiples of Rs1 lac.

The requirement of minimum current ratio of 1.33:1 as part of the eligibility norms for issue of CPs was dispensed with.

With a view to eliminating the problem of winners curse and broaden the market participation in respect of 91-day Treasury Bill “Uniform Price Method” auction was introduced in 91-day Treasury Bill auctions.

The size of the transactions for lending by the entities which route their transactions through PDs in call/notice money market was further reduced from Rs10 crore to Rs5 crore.

Ready forward transactions were permitted in PSU Bonds and private corporate debt securities which are held in dematerialized form.

Non competitive bids would be kept outside the notified amount in respect of day and 91-day Treasury Bill auctions.

Nov 1997  
SDs to be provided liquidity support from RBI through reverse repo in dated Government security and Treasury Bills.
RBI decided to register nine companies as satellite dealers (out of 17 entities announced in April 97).

RBI announced a fixed rate repo scheme. Repo rate was fixed at 4.50%.

Dec 1997

GOI announced for the first time Capital Indexed Bonds. The repayment of the principal amount would be on the basis of monthly average of the wholesale Price Index.

The Primary Dealers’ Association of India was formed as Self-Regulatory Organisation (SRO) under section 25 of the Companies Act, 1956 on December 22, 1997.

Jan 1998

Liquidity support to Primary Dealers in G-Sec given on discretionary basis.

Mar 1998

Satellite Dealers were extended the facility of ready forward transactions.

Apr 1998

Notified amounts for 364 and 14-day Treasury Bills introduced.

Credit policy for the first half announced the following measures:

1. To introduce one day repo,

2. To provide liquidity support to PDs against the holdings of securities in SGL a/c instead by way of reverse repo.
Minimum size per call money transactions of corporate reduced from Rs5 crore to Rs3 crore.

The minimum lock in period for CDs and units of MMMFs was reduced from 30 days to 15 days.

Jun 1998
SDs were allowed to issue CPs under certain conditions.

Aug 1998
5 non-banking entities allowed to do reverse repo.

Sep 1998
RBI issued draft guidelines on Asset-Liability Management.

Oct 1998
Credit Policy Measures:

- Capital Adequacy Ratio for Banks/FI's was increased to 9% from 8% since March 31, 2000.

- 2.50% Risk weight to be provided on DGS from March 31, 2000.

Jan 1999
Subscription to State Government loans through auction allowed.

Apr 1999
Four new Primary Dealers added to the existing six PDs.

Cheque writing facility given to the investors of MMMFs.

Non- bank entities permitted to lend in call money till December 31, 1999.
Non-banking entities allowed borrowing money through repos on par with banks and PDs.

RBI decided to issue dated Government securities on price basis instead of yield basis.

Calendar of issue for Treasury Bills introduced.

System of fixed underwriting commission on Treasury Bills introduced.

May 1999

Three more new primary dealers added.

Price based auction of dated Government securities commenced.

Jun 1999

182-Day Treasury Bill was re-introduced.

Jul 1999

35 non-banking entities were allowed to undertake repos.

Guidelines on FRA and IRS issued.

Oct 1999

Guidelines for Risk Management Systems Banks issued.

Credit Policy Measures:

Non-bank entities permitted to lend in call money till June, 2000.

MMMF brought under SEBI Regulations.

Cheque writing facility to Gilt funds.
Mutual funds also permitted to undertake Interest Rate Swap/Forward Rate Agreement.

Working group on retailing of government securities constituted.

Self imposed leverage ratio should be set by each Primary Dealer.

Special liquidity support announced for banks during Dec 99 to Jan 2000.

Dec 1999  Constitution of working group on Discounting of Bills by banks.

New guidelines on securities transactions for Primary Dealers issued.

Jan 2000  Shut period in Government securities reduced from 7 days to 3 days.

Mar 2000  In terms of notification issues under Section 16 of the Securities Contracts (Regulations) Act, 1956 and under the amended section 29A of the Act, Government of India has delegated regulatory powers to RBI to regulate dealings in Government securities, money market securities, gold related securities and securities derived from these as also ready forward contracts in debt securities, vide notification dated March 1, 2000.
The Reserve Bank reduced the bank rate by 1.0 percentage point to 7.0 per cent, effective from the close of the business on April 1, 2000.

The Reserve Bank reduced the fixed repo rate by 1.0 percentage point from 6.0 per cent to 5.0 per cent, effective April 1, 2000.

CRR was reduced by 1.0 percentage point to 8.0 per cent in two stages of 0.5 percentage point each, from the fortnights beginning April 8 and April 22, 2000, respectively.

In order to facilitate the movement of short-term money market rate within a corridor, impart greater stability and facilitate the emergence of a short-term rupee yield curve, it was announced that a full-fledged Liquidity Adjustment Facility (LAF) operated through repos and reverse repos would be progressively introduced with effect from June 5, 2000. In the first stage, it was proposed that the Additional Collateralized Lending Facility (ACLF) would be replaced by variable rate repo auctions with same day settlement; in the second stage, the Collateralized Lending Facility (CLF) and Level-I liquidity support would be replaced by variable rate repo auctions (some minimum support to PDs would be continued but at interest rate linked to variable rate in the daily repos auctions as determined by the Reserve Bank), and in the third stage, with full computerization of Public Debt Office and
introduction of Real Time Gross Settlement System (RTGS), repo 
operations through electronic transfers would be introduced and in 
the final stage I.AF would possibly be operated at different timings 
of the same day.

In order to impart greater flexibility in the pricing of rupee interest 
rate derivatives and facilitate integration between money and forex 
markets, interest rates implied in the foreign exchange forward 
market could be used as a benchmark for FRA/IRS in addition to 
the existing domestic money and debt market rates.

The minimum maturity of CDs was reduced from 3 months to 15 
days in order to bring it at par with other instruments like CPs and 
term deposits.

It was decided that the facility to non-bank entities for routing 
transactions through Primary Dealers (PDs) would be extended 
from end-June 2000 to end-December 2000 and simultaneously 
steps will be initiated to extend repo facility to such entities 
through Subsidiary General Ledger (SGL) II accounts.

In order to facilitate operational flexibility to existing lenders to 
adjust their asset liability structure by widening the repo market 
and improve the participation of the non-bank entities, a time 
bound programme of withdrawing permission to non-bank entities
for lending in call/notice money market coinciding with the development of the repo market was announced.

Special facility for securities settlement was proposed to be introduced for banks and PDs having SGL accounts for providing smooth securities settlement.

May 2000

With a view to providing further flexibility to banks and enabling them to choose an optimum strategy of holding reserves depending upon their intra-period cash flows, the requirements of minimum 85 per cent of the CRR balances on the first 13 days to be maintained on a daily basis was reduced to 65 per cent from the fortnight beginning May 6, 2000.

Jul 2000

The Reserve Bank issued draft guidelines for the issue of commercial paper (CP). It was proposed to permit all-India financial institutions to issue CPs, to allow issue of CPs in maturities ranging from 15 days to one year in denominations of Rs.5 lakh or its multiples, to facilitate corporates route, to permit FIIs to invest in CPs within their 30 per cent limit of debt instruments, to have discretion on the validity period of the rating and to assign clear roles for issuer, financing banking company, issuing and paying agent and CRA.

After a review of the recent developments in the international and domestic financial markets, including the foreign exchange market,
the Reserve Bank raised the Bank rate by 1 percentage point to 8.0 per cent with effect from the close of business on July 21, 2000. Further it was announced that the CRR would be hiked by .5 percentage point to 8.5 per cent in two stages of .25 percentage point each, effective from the fortnights beginning July 29 and August 12, 2000, respectively, and all refinance limits available to banks (including those for CLF), as a temporary measure, would be reduced by 25.0 per cent each in two stages of the eligible limits as per the existing formula.

Aug 2000

PDs were allowed “switch facility” to swap their long-dated government securities with 364-day Treasury Bills available in the list of open market operations. Reserve Bank offered to purchase from August 24 three dated Government of India securities against sale for an equal amount in face value of 364-day Treasury Bills.

Sept 2000

The Reserve Bank announced, with effect from October 3, 2000, an introduction of a special fund facility for banks and PDs to provide intra-day funds to facilitate the settlement of securities transactions in case of a gridlock occurring on account of shortage of funds on a gross basis in the current account of one or more SGL account holders especially when transactions are linked. Banks and PDs who are eligible for CLF/liquidity support facility at the Bank Rate would be made eligible. Credit was made available on a collateralized basis against un-drawn CLF/primary
deals liquidity support (PDLS) at Bank Rate with equal interest cost sharing by all the beneficiary participants.

Following the recommendations of Narasimham Committee II, the Reserve Bank widened the repo market by permitting the non-bank participants current and SGL accounts with the Reserve Bank to undertake both repos and reverse repos, reducing the minimum maturity of repo transactions to 1 day, making state government securities eligible for repos and opening of its purchase window to impart liquidity to government securities whenever situation warrants. As suggested by the committee, it is necessary to move towards a pure inter-bank call money market as early as possible. However, as the repo market was not yet broad-based and deep, the permission granted to select corporates for routing call money transactions through PDs was further extended from December 2000 to June 2001.

In order to make necessary transactional provisions in respect of non-bank institutions including FIs and MFs, before the call money market is confined to only banks/PDs, it was decided to constitute a group to suggest smooth phasing out by a planned reduction in their access to call/notice money market.

New guidelines were released on issue of CPs, accounting for the suggestions on draft revised guidelines circulated in July 2000, for
providing flexibility, depth and vibrancy in the CP market while retaining the prudential safeguards and transparency. In particular, the guidelines were to enable companies in the services sector to more easily meet their short-term working capital needs. CP is not allowed to be issued as a ‘stand alone’ product. Banks and FIs would have the flexibility to fix working capital limits duly taking into account resource pattern of companies’ financing, including CPs.

With a view to providing flexibility and depth to the secondary market, it was decided to withdraw the restriction on transferability period for CDs issued by both banks and financial institutions.

A scheme was introduced for automatic invocation by the SGL Account holder of undrawn refinance/liquidity support from the Reserve Bank for facilitating smooth securities settlement to banks and PDs only.

The notified amount in respect of auctions of 364-day Treasury Bills was enhanced from Rs.500 crore to Rs.750 crore.

New capital adequacy guidelines were issued for PDs taking into account credit and market risks faced by them. PDs were asked to submit capital adequacy returns on a quarterly basis with effect from September 30, 2000. For meeting the market risk capital charges, Tier-II capital was specifically introduced in accordance
with the international norms. PDs were asked to calculate their market risk charges with help of the higher of the capital charges obtained from standardized method and the value at Risk method.

**Feb 2001**

The Reserve Bank reduced the Bank rate by 50 basis points to 7.5 per cent effective close of business on February 16, 2001 and lowered the CRR by 50 basis points to 8.0 per cent in two stages of .25 percentage point each, effective from fortnights beginning February 24 and March 10, 2001, respectively.

**Mar 2001**

On a further review, the Bank rate was reduced from 7.5 per cent to 7.0 per cent effective close of business on March 1, 2001.

The Technical Group report on phasing out of non-banks from call/notice money market was submitted. It recommended three-staged reductions in call money lendings by non-bank participants (including mutual funds and insurance companies). In the first stage, the recommendation was to permit lending up to 70 per cent of their average daily lendings during 2000-01 for a period of three months after which the lending limit was reduced to 40 per cent in the second stage. In the third stage, by which time Clearing Corporation is expected to be operationalised, their lendings may be reduced to 10 per cent for a period of three months to enable them to be familiar with the operations of the Clearing Corporation.
In-principle approval to become PDs in Government securities market was given to four more entities viz, Bank of America Securities (India) Pvt. Ltd., Subsidiary of Bank of Baroda, HSBC Primary Dealership (India) Pvt. Ltd and Standard Chartered-UTI securities India Pvt. Ltd. this was in addition to the 15 PDs already working in the Government securities market.

Inter-bank term liabilities with original maturity of 15 days to one year exempted from the prescription of minimum Cash Reserve Ratio (CRR) requirement of 3.0 per cent, effective fortnight beginning August 11, 2001.

LAF operating procedures changed as follows (effective May 8, 2001): (a) minimum bid size reduced to Rs.5 crore from the existing Rs.10 crore; (b) option to switch over to fixed rate repos on overnight basis as and when felt necessary; (c) discretion to introduce longer-term repos up to 14 days; (d) LAF auction timing advanced by 30 minutes and result by 12 noon; (e) data on SCBs aggregate cumulative cash balances during the fortnight to be disseminated with a lag of two days; and (f) multiple price auctions (in place of existing uniform price auctions) to be introduced on an experimental basis during May 2001.

Gradual phasing out of non-bank participation in call money market in four stages. In stage 1, effective May 5, 2001, lending in
call/notice money market during the reporting fortnight by any non-bank entity not to exceed, on an average, 85 percent of its daily average lending during the year 2000-01.

The repo rate was cut by 25 basis points from 7.00 per cent to 6.75 per cent.

The Reserve Bank granted final approval to HSBC Primary Dealership India Private Limited to operate as a PD in the government securities market thereby increasing the number of PDs to sixteen.

A national level Clearing Corporation with the name “The Clearing Corporation of India Ltd.,” (CCIL) was registered as a limited liability company under the Companies Act, 1956 at the initiative of the Reserve Bank with the SBI as chief promoter for facilitating smooth clearing and settlement of transactions in foreign exchange, Government securities and money markets.

May 2001

CRR reduced by 0.50 percentage point from 8.0 per cent effective fortnight beginning May 19, 2001, augmenting the lendable resources of banks by about Rs.4,500 crore.

The repo rate cut by 25 basis points to 6.50 per cent.

14-day and 182-day Treasury Bills discontinued with effect from May 14, 2001.
Notified amount in the auctions of 91-day Treasury Bills enhanced from Rs.100 crore to Rs.250 crore.

Auctions of 91-day Treasury Bills conducted every Wednesday with payment on the following Friday and the auctions of 364-day Treasury Bills on the Wednesday preceding the reporting Friday with payment on the following Friday.

Jun 2001

Multiple price Auctions for LAF to continue till further announcement.

Sept 2001

Authorization of Ceat Financial Services Limited as PD was not renewed. Hence the company ceased to be a PD with effect from this date.

The Technical Advisory Committee on Money and Government Securities markets reconstituted for a further term of two years from the day of its first meeting.

Oct 2001

Bank Rate reduced by .50 percentage point from 7.00 per cent to 6.50 per cent with effect from the close of business on October 22, 2001.

CRR rationalized through (a) reduction by 200 basis points from 7.50 per cent to 5.50 per cent and (b) withdrawal of exemptions on all liabilities, except inter-bank, for the computation of net demand.
and time liabilities (NDTL) for the purpose of maintenance of CRR, with effect from the fortnight beginning November 3, 2001.

**Nov 2001**

The Reserve Bank granted final approval to Banc of America Securities (India) Pvt. Ltd. and Standard Chartered- UTI Securities India Pvt. Ltd. to operate as PDs in the Government Securities market taking number of PDs to 17.

Fortnightly repo auction introduced with auctions conducted on every Monday following reporting Friday.

**Jan 2002**

Asset Liability Management (ALM) guidelines for NBFCs were made applicable to PDs with some modifications.

Guidelines on Inter-Corporate Deposits (ICDs) for PDs were issued: (i) PDs prohibited from placing ICD with other counterparts; (ii) acceptance of ICDs restricted to 50 per cent of Net Owned Funds; and (iii) PDs to evolve a policy for acceptance of ICDs.

**Feb 2002**

The Negotiated Dealing System (NDS) (phase 1) was operationalised.

The CCIIL, who's operationalised, was linked to the NDS, also commenced operations.
Mar 2002

The Reserve Bank granted final approval to BOB Capital Markets Ltd. To operate as PD in the Government Securities market taking number of PDs to 18.

Apr 2002

Cash reserve ratio (CRR) to be reduced from 5.5 per cent to 5.0 per cent effective from fortnight beginning June 15, 2002.

A reduction in Bank Rate by 50 basis points to be considered by the Reserve Bank as and when necessary.

The daily borrowings of State co-operative Banks and District Central Co-operative Banks in the call/notice money market not to exceed 2.0 per cent of their aggregate deposits as at the end of March of the previous financial year.

The limit on banks to borrow and invest from/in overseas market increased from 15 per cent to 25 per cent of their unimpaired Tier I capital within the banks' open position Limit and maturity mismatch limits (Gap Limits).

Notified amount of 364-day Treasury Bills raised from Rs.750 crore to Rs.1000 crore in the auctions effective April 3, 2002.

May 2002

The CRR reduction by .5 percentage point from the then existing level of 5.5 per cent, initially proposed to be effective fortnight beginning June 15, 2002, advanced to reporting fortnight beginning June 1, 2002.
The repo rate was cut by 25 basis points to 5.75 per cent from 6.00 per cent.

Prudential limit stipulated on the exposure of scheduled commercial banks (SCBs) in call money market in two stages:

(i) In the first stage, effective October 5, 2002, SCBs daily lending in the call/notice money market, on a fortnightly average basis, not to exceed 50 per cent of their owned funds as at the end of March of the previous financial year; their fortnightly average borrowing not to exceed 150 per cent of their owned funds or 2.0 per cent of aggregate deposits as at the end of March of the previous financial year, whichever is higher. However, they will be allowed to lend and borrow a maximum of 100 per cent and 250 per cent, respectively, of their owned funds on any day during a fortnight.

(ii) In the second stage, effective fortnight beginning December 14, 2002, SCBs fortnightly average lending in the call/notice money market not to exceed 25 per cent of their owned funds; fortnightly average borrowings not to exceed 100 per cent of their owned funds or 2.0 per cent of aggregate deposits as at the end of March of the previous financial year, which ever is higher. They will be allowed
to lend and borrow a maximum of 50 per cent and 125 per cent, respectively, of their owned funds on any day during a fortnight.

(iii) An increased access may be allowed for a temporary period in case of mismatches in liquidity position. If the bank has a fully functional Asset Liability Management (ALM) system to the satisfaction of the Reserve Bank, an increased access over the stipulated norm may be permitted for a longer period.

PDs brought under the purview of Board for Financial Supervision (BFS).

Jul 2002

Following the recommendations of the Working Group constituted to suggest the criteria for fixing limits for transactions of primary dealers (PDs) in call/notice money markets as also to suggest a roadmap for phasing them out from call/notice money markets, it was decided:

(i) With effect from October 5, 2002, PDs will be permitted to lend in call/notice money market up to 25 per cent of their net owned funds (NOF).

(ii) Access of PDs to borrow in call/notice money market would be gradually reduced in two stages: in stage 1, PDs
would be allowed to borrow up to 200 per cent of their NOF as at end-March of the preceding financial year. In Stage 11, PDs would be allowed to borrow up to 100 per cent of their NOF. The limits under both the stages would not be applicable for the days on which Government dated securities are issued to the market. The date of implementation of the Stage 1, to be notified later, would be operational upon the finalization of uniform accounting and documentation procedures for repos, allowing rollover of repos, introduction of tripartite repos or collateralized borrowing and lending obligations and permitting repos out of 'available for sale' category. Stage 11 will commence one month after permitting sale of repoed securities.

Oct 2002

Repo rate under the LAF was reduced by 25 basis points to 5.50 per cent.

CRR to be reduced by 25 basis points to 4.75 per cent, effective fortnight beginning November 16, 2002.

Anonymous screen based order driven trading in Government securities on the stock exchanges to be introduced in consultation with SEBI.

To move in the direction of categorization and valuation of banks' investments in consonance with best international practices, the
Reserve Bank issued guidelines for uniform accounting norms for repo and reverse repo transactions in consultation with market participants.

For deepening and making the repo market more liquid, the Reserve Bank proposed (i) extension of repo to all regulated entities with gilt/CSGL accounts as long as all transactions are mandatorily reported and settled through the Delivery Versus Payment (DvP) system and (ii) to allow rollover of repo contracts using the same securities between the same counter parties.

For improving the pricing of bonds in the secondary market and enhanced their liquidity (i) fresh issues of floating rate bonds (FRBs) will provide for annual reset of base rate instead of existing practice of semi-annual reset, and (ii) the base rate will be determined on the basis of the average cut-off yields of 364-day Treasury Bills in the preceding three auctions as against preceding six auctions as applicable for existing FRBs.

Buying and selling of Government securities through the stock exchanges commenced in NSE, BSE and OTCCEI.

Collateralized borrowing and lending obligation (CBLO) was operationalised as a money market instrument through the CCIL.
Feb 2003  The interest rate on savings account offered by bank was reduced to 3.5 per cent per annum from 4.0 per cent per annum with effect from March 1, 2003.

Guidelines were issued to extend eligibility for ready forward (repo) contracts to select categories of gilt account holders, with adequate safeguards to ensure DvP and transparency. The guidelines came into effect from March 3, 2003.

Mar 2003  Guidelines were issued for uniform accounting of repo transactions.

Apr 2003  Bank Rate was reduced by 0.25 percentage point from 6.25 per cent to 6.0 per cent with effect from close of business on April 29, 2003 with a policy bias to keep it stable until the Mid-term of October 2003.

CRR to be reduced by 0.25 percentage point from 4.75 percent to 4.50 percent with effect from fortnight beginning June 14, 2003.

The multiplicity of rates at which liquidity is absorbed/injected under back-stop facility rationalized as under: (i) the back-stop interest rate will be at the reverse repo cut-off rate at the regular LAF auctions on that day; (ii) in case of no reverse repo in the LAF auctions, back-stop will be 2.0 percentage point above the repo cut-off rate; and (iii) on days when no repo/reverse repo bids
are received/accepted, back-stop rate will be decided by the Reserve Bank on an ad-hoc basis.

Stage 11 of the transaction to a pure inter-bank call/notice market would be effective from the fortnight beginning June 14, 2003, wherein non-bank participants would be allowed to lend, on average in a reporting fortnight, up to 75 per cent of their average daily lending in call/notice money market during 2000-01.

With effect from fortnight beginning May 3, 2003, reporting of all call/notice money market deals on Negotiated Dealing System (NDS) would be mandatory for all NDS members. Deals done outside also be reported within 15 minutes on NDS, irrespective of the size of the deal or whether the counter party is a member of the NDS or not. Full compliance with the reporting requirement to NDS will be reviewed in September 2003. In case there is repeated non-reporting of deals by an NDS member, it will be considered whether non-reported deals by that member should be treated as invalid with effect from a future date.

Operational guidelines were issued to CCIL for operationalisation of Government securities lending scheme. The CCIL was permitted to enter into an arrangement with any of its members for borrowing Government securities for the purpose of handling securities shortage in the settlement of transactions.
Operational guidelines were issued to PDs for Portfolio Management Services (PMS). PDs, with prior approval of the Reserve Bank and registration with SEBI, were permitted to offer PMS services only to entities not regulated by the Reserve Bank.

with a view to enabling PDs to manage their exposure to interest rate risk, they were allowed to deal in exchange traded Interest Rate Derivatives (IRDs) in a phased manner. In the first phase, such entities were permitted to transact only in interest rate futures on notional bonds and Treasury Bills for limited purpose of hedging the risk in their underlying investment portfolio subject to prudential guidelines and appropriate disclosures.
4.8 REVIEW OF MONETARY AND CREDIT POLICY 2003-04

RELATING TO MONEY MARKET

4.8.1 MOVING TOWARDS PURE INTER-BANK CALL/NOTICE MONEY MARKET

Following the recommendations of Narasimhan Committee II, in the annual policy statement of April’01, the intention to move towards a pure inter-bank call/notice money market by gradually phasing out the non-bank participation was announced. In the annual policy statement of April’03, daily lending of non-bank participants in call/notice money market was reduced from 85% to 75%. In view of further market developments as also to move towards a pure inter-bank call/notice money market, it is proposed that;

With effect from the fortnight beginning December 27, 2003, non-bank participants would be allowed to lend, on average in a reporting fortnight, up to 60% of their average lending in call/notice money market during 2000-01. The time table for further phasing out of non-bank participation will be announced in consultation with market participants. If a particular non-bank institution has genuine difficulty in developing proper alternative avenues for development of excess liquidity because of its size, RBI may consider providing temporary permission to lend a higher amount in call/notice money market for a specific period on a case-to-case basis.

4.8.2 RATIONALIZATION OF STANDING FACILITIES

Banks are eligible for standing facility (export credit eligible for refinance) and PDs are eligible for collateralized liquidity support from RBI subject to certain limits. These
limits are split into “normal” facility and “back-stop” facility. With the emergence to
Liquidity Adjustment Facility as an effective instrument in modulating system liquidity,
in the mid-term review of October’02, the appointment between “normal” and “back-
stop” facilities was changed to one-half each. In view of current liquidity conditions, the
utilization of these facilities by banks and PDs has been negligible. In order to move
further towards phasing out sector-specific standing facilities as also to rationalize the
rates at which liquidity is injected into the system, it is proposed that;

The “normal” and “back-stop” standing facilities will be available in a ratio of
one-third to two-thirds (33:67) from the fortnight beginning December 27, 2003.

4.8.3 PRIMARY DEALERS’ ACCESS TO CALL/NOTICE MONEY MARKET

Following the annual policy statement of April’02, it was announced in July’02 that
access of PDs to borrow in call/notice money market would be gradually reduced in two
stages subject to certain market developments. With a view to develop Repo market
further as also to ensure a balanced development of various segments of money market, it
is proposed that;

With effect from February 07, 2004 PDs will be allowed to borrow, on average
basis in a reporting fortnight, up to 200% of their net owned funds as at end
march of preceding financial year. Any Pd which has genuine difficulties in
adhering to above schedule may approach RBI for appropriate reasonable
dispensation with full justification for extension of period of compliance sought.
4.8.4 REPORTING OF CALL/NOTICE MONEY MARKET TRANSACTIONS ON NDS PLATFORM

As indicated in the annual policy statement of April'03, it is mandatory for all NDS members to report all their call/notice money market deals on NDS. Deal done outside NDS should also be reported within 15 minutes of the deal irrespective of the size of the deal or whether the counterparty is a member of the NDS or not. In order to facilitate the NDS members to report their deals among the NDS members and with non-NDS members, RBI has amended the software incorporating the necessary changes and distributed it amongst NDS members in July'03. As a result of this, there has been significant increase in the reporting of deals. Complete dissemination of trade information relating to money, government securities and foreign exchange markets will improve transparency and strengthen efficiency in the market. In this direction, all NDS members should report their deals as soon as the deals are concluded.