Bimal Jalan Committee

June 23, 2020
The Reserve Bank of India (RBI), in consultation with the central government, had constituted a Committee(Chair: Dr Bimal Jalan) to review the current economic capital framework, in November 2018.

Why was it set up?

To review the current economic capital framework

What is ECF?

- The economic capital framework provides a methodology for determining the appropriate level of risk provisions and profit distribution to be made under Section 47 of the RBI Act, 1934.

What are its recommendations?

- **International practices**: The Committee observed that there is no internationally laid down risk capital framework for central banks.
- It noted that the RBI's central banking economic capital, at 26.8% of its balance sheet, is the fifth largest amongst central banks.
- (Economic capital = its capital + reserves + risk provisions + Revaluation balances.

→ Revaluation balances are unrealized gains, net losses resulting from movement of the exchange rate, gold price or interest rate.

→ Note that revaluation balances are the major component of RBI's economic capital (73%).

- **Risk assessment**: The central bank is exposed to different types of risks. These include (i) market risk arising out of currency, gold or interest rate fluctuations, (ii) credit risk, (iii) operational risks arising from managing multi-currency portfolios across multiple legal jurisdictions, and (iv) contingent risks (monetary and financial stability risks).

- **Surplus distribution policy**:
- The current surplus distribution policy targets only total economic capital.
- ***Target should also include realized equity.***
- The size of the realized equity, in the form of **CRB,** must be **maintained** between **5% to 6.5%** of the RBI's balance sheet (current target: 3% to 4%).
- The total economic capital should be maintained between 20.8% to 25.4% of the balance sheet (current target: 28.1% to 29.1%).
- As of June 30, 2018, the CRB and total economic capital for the central bank were 7.2% and 26.8% of the balance sheet, respectively.
- If the realized equity is above the required levels, the entire net income of RBI will be transferred to the government.
- If it is lower, risk provisioning will be made to the necessary extent and only the residual net income will be transferred.
- This framework may be reviewed every five years.