Regional Rural Bank

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In news

Reserve Bank of India (RBI) will permit Scheduled Regional Rural Banks to access the liquidity adjustment facility, the marginal standing facility, and the call money market.

Regional Rural Banks

- The n**ationalization of the banks in 1969** boosted the confidence of the public in the Banking system of the country.
- However, **in the early 1970s**, there was a feeling that even after nationalization, there were cultural issues which made it difficult for commercial banks, even under government ownership, to lend to farmers.
- This issue was taken up by the government and it set up the **Narasimham Working Grou**p in **1975**.
- On the **basis of this committee's recommendations, a** Regional Rural Banks Ordinance was promulgated in September 1975, which was replaced by the **Regional Rural Banks Act 1976.**
- Regional Rural Banks **came into existence on Gandhi Jayanti in 1975 with the formation of a Prathama Grameen Bank.**
- The RRBs were owned by three entities with their r**espective shares as follows:**
  - Central Government – 50%
  - State government – 15%
  - Sponsor bank – 35%

Regulation of RRBs

Regional Rural Banks are **regulated by RBI** and **supervised by National Bank for Agriculture and Rural Development (NABARD).**

Liquidity Adjustment Facility (LAF)

• Primary instrument of Reserve Bank of India for modulating liquidity and transmitting interest rate signals to the market.

• t refers to the difference between the two key rates viz. repo rate and reverse repo rate.

• Informally, Liquidity Adjustment Facility is also known as Liquidity Corridor.

Liquidity Adjustment Facility works?

• **Under Repo,** the banks borrow money from RBI to meet short term needs by putting government securities (G-secs) as collateral. **Under Reverse Repo,** RBI borrows money from banks by lending securities.

• While repo injects liquidity into the system, the Reverse repo absorbs the liquidity from the system.

• **RBI only announces Repo Rate**. The Reverse Repo Rate is linked to Repo Rate and is 100 basis points (1%) below repo rate.

Marginal standing facility (MSF)

• Window for banks to borrow from the Reserve Bank of India in an emergency when interbank liquidity dries up completely.

• The Marginal standing facility is a scheme launched by RBI while reforming the monetary policy in 2011-12.

• It is a penal rate at which banks can borrow money from RBI when they are completely exhausted of all borrowing assistance.

• The Marginal Standing facility allows banks to borrow money with an interest rate above the repo rate and can be termed as the Marginal standing facility rate.

MSF Description

• Banks borrow from the RBI by pledging government securities at a rate greater than the repo rate under LAF (liquidity adjustment facility).

• 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 percent of their net demand and time liabilities (NDTL).

• The minimum amount for which RBI receives application is Rs.1 Crore, and afterward in multiples of Rs.1 Crore.

Call Money Market

• The call money market part of the Indian Money Market, where the day-to-day surplus funds are traded. The money market is a market for short-term financial assets that are close substitutes of money. Important feature of a money market instrument is that it is liquid and can be turned into money quickly at low cost .

• The loans short-term duration from 1 to 14 days, and are traded in the call money market. The money that is lent for one day in this market is known as **“Call Money”**, and if it exceeds one day (but less than 15 days) it is referred to as **“Notice Money”.** Term Money refers to Money lent for 15 days or more in the **InterBank Market.**