FIEO Chief Takes Up Exporters' Issues Before RBI Credit Policy

On the eve of the announcement of the Reserve Bank of India's Monetary & Credit Policy, FIEO President Mr A. Sakthivel thanked the apex bank's Governor D. Subbarao for giving the Federation the opportunity to place its views/suggestions before this august body. The FIEO chief hoped the issues will merit the RBI's kind consideration. The following is the text of the recommendations submitted by FIEO to the RBI.

I. a) Export Credit as percentage on Net Banking Credit (NBC)

India has weathered the global economic crisis better than most countries and as per the Economist Intelligence Unit forecast India will be the ninth fastest growing economy in the world and the second fastest growing major economy this year. It states that India will overtake China as the fastest-growing major economy by 2018.

The Economic Intelligence Unit (EIU) predicts that India will sustain an average annual growth rate of 6.4% to 2030 and high savings rate (32.5% of GDP) and investment levels (34.9% of GDP) will spur India's economic acceleration but inflation would be a risk.

The present slowdown has seen a decline in the export credit vis-à-vis the net bank credit as given below:

The Economic survey in its analysis of India's export credit as a percentage of net banking credit has indicated a declining trend, in turn impacting the country's trade. As a result export credit as a percentage of net banking credit has fallen from 5.5 per cent as on March 28, 2008 to 4.6 per cent as on March 27, 2009 and further to 4.1 per cent as on January 15, 2010. The outstanding export credit as on March 28, 2008 was Rs 129,983 crore, a growth of 23.9 per cent over the previous year. The export credit as on March 27, 2009 was Rs 1,28,940 crore, a fall of 0.8 per cent from the previous year. On January 15, 2010, it was Rs 1,24,360 crore, a decline of 3.6 from the March 2009 figure. As per World Bank estimates the shortage in trade finance in the market would have accounted for 10-15 per cent of the decline in global trade.

The proposed Government Panel being set up to review the export credit related issues may do well in examining the cause and effect of this trend and how much of the decline in the export credit vis-à-vis net bank credit (NBC) can be attributed to the overall contraction in global demand and/or the fact that the cost of export credit per se makes export uncompetitive not to mention the innumerable transaction costs that have been discussed in the latter half of this Memorandum.

Export Credit

Outstanding as on	Export Credit (Rs. Crore)	Variations (percent)	Export Credit as percent on NBC	Export Credit as percent exports
March 24, 2000	39118	9.0	9.8	24.5
March 23, 2001	43321	10.7	9.3	21.3
March 22, 2002	42978	-0.8	8.0	20.6
March 21, 2003	49202	14.5	7.4	19.3
March 19, 2004	57687	17.2	7.6	19.7
March 18, 2005	69059	19.7	6.3	18.4
March 31, 2006	86207	24.8	5.7	18.9
March 30, 2007	104926	21.7	5.4	18.4
December 22, 2006	97763	13.4[b]	5.6	26.5
December 21, 2007[a]	117719	12.2	5.5	29.5

Source:* *Reserve Bank of India

a Over the corresponding figure as on March 30, 2007 (variation)

b Variation over March 31, 2006

Note: *1. Data up to March 2004 release to select banks accounting for 90% of bank credit.*

2. March 18, 2005, onwards, data pertain to all scheduled banks excluding RRBs availing export credit refinance from the RBI.

b) Priority Sector Lending for MSME Export Sector

As per the RBI Guidelines on Priority Sector Lending which earmark 40% of the funds for the priority sector, 18% of the net bank credit (NBC) has been allocated for agriculture and 10% for weaker sections including MSMEs. Only 15 out of 27 public banks and 17 out of 23 private banks have met their target (as per a study conducted in May, 2009).

It is suggested that the MSME Ministry, RBI and Finance Ministry have been considering a sub allocation under the priority sector of 15% which needs to be implemented at the earliest.

II. Export Credit related issues

a) Interest Subvention

As a measure to counter rupee appreciation and later due to recession the interest subvention facility was extended since July 2007 to various sectors including textiles and RMG which form a sizeable amount of our exports in the textile sector. However, in the RBI notification of 16th December 2008 while textiles were included garments did not find any mention. Further labour intensive sectors such as leather, gems and jewellery and marine sectors have been deprived the benefit of 2% interest subvention which has been extended for sectors such as handicrafts, handloom and SME sectors. Many of these sectors deprived of subvention would have negative growth in 2009-2010 and few of them may have shown a positive growth but that too on a very low base.

Since sectors such as Leather, gems and jewellery and marine sectors are highly employment intensive sectors with very high capital employment ratio Government should continue to provide them interest subvention both with a view to promote export as well as to encourage additional employment in these sectors.

Further, the benefit of interest subvention may be extended to merchant exporters also who may be classified as SME based on the investment in equipment. Further, RBI notification at present only covers manufacturers with a ceiling of Rs.10 crores on investment in plant and machinery which needs to be upgraded to Rs.25 crores.

b) Liberal debt to equity ratio for export credit

Export credit should be kept outside the purview of the Tandon and/or Chore and Kannan Committee norms where a equity to debt ratio of 1:2 was suggested. Debt/equity ratio for export credit may be kept at higher levels, for example, such as 9:1.

c) Non-availability of dollar loans for export finance

MSME export sector has drawn our attention to the fact that post the announcement of the reduction in Foreign Currency Loans to LIBOR + 2% vide RBI Circular No. DBOD.DIR.(Exp). No. 76/04.02.001/2009-10 dated February 19, 2010, banks are refusing PCFC Loans. Prior to the reductions PCFC Loans were being extended at interest cost totalling 3.90% but with the refusal of the banks to provide dollar loans at the said rates, the credit costs (in rupee loans) have increased to twice the earlier rates.

d) Flexibility in Packing Credit Limits

Increase the Packing Credit (PC) Limit to 1/3rd of the Turnover instead of the present 1/5th. Currently, the Packing Credit has to be rotated five times in a year, which is contrary to the company needs because the cycle for imported raw material/other inputs from LC establishment to complete utilization of a container is between 4 to 8 months or more. Hence, rotating PC 3 times in a given financial year or increasing PC limit to 1/3rd of the turnover is requested.

e) Penal Rate of Interest

Banks charge interest 3% to 4% p.a for payments received beyond due date. This problem has become more acute because of delay in export realizations from foreign buyers. The penal interest should not exceed 1% over and above the normal rate of interest being extended to MSME export sector. (Although RBI permits 360 days but if there is a clause in the L/C stating DA 120 days then in such cases, if the export realization comes on the 130th day then banks charge additional interest of 3% to 4% over and above the existing rate from the date of shipment).

III. Relaxation in Working Capital / Term Loans / Restructuring package

a) Working Capital

Inadequacy of Working Capital has been a problem with most MSMEs and banks insist on additional collaterals before providing an enhancement. The process of giving Working Capital Limits (WCL) at the branch level is not transparent. It is suggested that adhoc demand loans up to 20% may be sanctioned on priority basis for those MSME's requiring the same.

b) Term loans

As inflationary pressure build up there is a general apprehension that short term interest rates may increase, further constricting credit offtake. It is, therefore, suggested that some flexibility be introduced in term loans, restructuring package etc. to support the MSME sector in the existing slow-down.

The present interest rate on term loans/working capital term loans is also high i.e in the range of 14% to 16%. Therefore, there is a need to reduce the interest rates on the Term Loans/working capital term loans, so that the MSME can avail the much needed financial assistance at affordable interest rates.

Interest on term loans/working capital term loans including the existing loans be reduced to about 5% to 6%.

Moratorium of one year is needed for affected MSMEs.

c) Restructuring package

The present restructuring package available is found to be of little use to the industry, as the exporters end up paying a very high interest rate of 16% even on restructured loans. Restructured loans and also on the Working Capital Term Loan for export be brought down at least to the level of the present normal interest rates of 8% to 10%.

d) Delinquency / NPA norms

Amendment of delinquency/NPA norms on restructuring of loans from current 90 to 360 days has been allowed by the RBI. However, buyers abroad are declaring insolvency under Chapter XI and in such cases where buyer is insolvent or exporter has sought help of debt collection agencies extension beyond 360 days may be considered.

IV Transaction Costs in Banking Channel adding to the overheads

a) Processing charges for annual renewal of limits

Banks are charging processing charges of Rs 400 per lac subject to a maximum of Rs 20 lacs on renewal of limits. If an exporter goes for renewal of a limit of Rs 50 crore, he has to pay Rs 20 lacs as processing charges. You will appreciate that while renewing the limit of exporters, banks heavily rely on his past track record in approving or disapproving such limits. Therefore, there is no reason to impose such high charges and they may be reduced to Rs 100 per lac subject to a ceiling of Rs 5 lacs. Moreover, these charges should only be levied on grant of a new limit and not on its renewal.

b) Cross Currency Booking

Banks are presently levying their own mark up on the margins between the spot and forward rate for quoting forward quotation. As a result, a bank earns 4 bips (0.0004) on each transaction of a dollar be it buying or selling which adds on to 8 bips [1 Euro = 1.3600 USD +/- 0.004 while buying/selling in a Euro / USD transaction]. It is suggested that 1 bip per transaction may be charged by banks in order to cut down the transaction cost in case of cross currency transactions.

c) Negotiation Charges

Banks are levying 0.15% as the negotiation charges while negotiating the documents which need to be reduced to 0.05%.

d) Booking Charges

Banks are levying Rs 750 as booking charges and Rs 750 as cancellation charges against every booking of FOREX with them. These charges need to be lowered to Rs 250 from Rs 750.

e) Pre-shipment credit in foreign currency

PCFC being levied in contravention of the recent RBI circular DBOD.DIR.(Exp).No. 76/04.02.001/2009-10 dated February 19, 2010 wherein credit in foreign currency is available at LIBOR plus 2%. Some banks are adding other costs such as Rs. 0.25 per US$ whereas circular clearly specifies "subject to the express condition that the banks will not levy any other charges viz. service charge, management charge etc., except for recovery towards out of pocket expenses incurred. Similar changes may be effected in interest rates in cases where EURO LIBOR/EURIBOR has been used as the benchmark".

Further, availability of PCFC continues to be difficult. The RBI may issue directives to banks to provide PCFC loans to MSME export sector without fail and on priority basis.

f) Collateral and Guarantees

While the RBI does not insist on collateral in case of irrevocable L/C but banks demand collateral security from the borrower from 50% to 75% of the advance required.

g) Factoring / Forfeiting / Bill Discounting

The banks keep a cap on discounting of Direct Bills at around 50%. In the diamond industry all sales are through the Direct Bill route, and the cap creates difficulties. We suggest that banks be persuaded to remove the cap.

h) Review of system of Collaterals and Guarantees

Banks insist on abnormally higher collateral of 15% to 20% by way of cash or immovable property. Increases in valuations by bank approved valuers are not taken into account and where taken valuations by valuers are further discounted by 15% for computational purposes.

i) Guarantee Charges collected by banks

The exporters are allowed to import capital goods at lower rate of import duty by under taking to export goods equivalent to eight times the import duty saved in the next eight years to come. For this purpose the JDGFT issues licence after obtaining the Bank Guarantee.

The bank issued this bank guarantee at 3% p.a for an amount not over 75% of the "Guarantee Amount" the balance of 25% is to be arranged by the exporter by way of pledging Fixed Deposit Receipts with the bank. Now if the exporter takes say 6 years to complete this turnover target, he has to spend 18% of the money so saved by importing the capital goods.

The bank continues to collect guarantee charges year after year until it is cleared by the exporter, of course, after meeting the export obligation. The banks may be advised to collect guarantee charges of say 3% or less only once and not every year.

j) Rupee fluctuation to be kept within a band

Following the sub-prime crises in December 2007 and the fall of

Lehman Brothers a year later and with other major banks and financial institution collapsing, the impact on the markets has been unprecedented.

The rupee for e.g. has seen fluctuations ranging from Rs 39 against the US$ in April 2008 to Rs 51 in March 2009 and to Rs 47 in May 2009.

The fluctuations in the rupee have thrown all hedging methods out of gear and are causing sever losses to the MSME export sector.

The rupee has undergone constant fluctuations during 2009-10 around the range of Rs 45. On account of this fluctuation, the exporters have suffered huge financial losses. As the MSME sector is already operating on very thin profit margins, such fluctuations have affected not only the small companies but also well established companies, thereby severely affecting their financial stability.

Hence, the intervention of the RBI/Government is required in this matter to ensure stability of the rupee within a band, to enable the exporters to fix/negotiate their prices accordingly. Alternately, a foreign exchange fluctuation allowance may be considered for the exporters, depending on their value of exports so as to reduce the losses.

k) Credit Rating

The RBI is committed to the adoption of Basel II by the Banks and had earlier indicated March 31, 2007 as the intended date for adoption by all commercial banks.

All scheduled commercial banks are encouraged to adhere to standardized approach for credit risk under Basel II w.e.f from March 31, 2009. As a result credit ratings system (which vary from Bank to Bank) is mandatory for borrowers with turnovers exceeding Rs 50 crores annually.

Suggestion

Credit Rating Agencies such as CRISIL, FITCH, CARE levy very high charges. They must be replaced by agencies like SMERA which are under SIDBI and cost effective for the MSME export sector.

l) Waiver of ECGC Premia on Post Shipment Guarantee

ECGC premium has also gone up significantly and works out to anything between 0.36% and 1.32% of the borrowings. As a result the already struggling exporter is burdened with an additional cost, besides the high cost of credit.

As per practice, at the time of release of Working Capital Limits (WCL), banks are normally taking the following securities:

- Stock and Book Debts
- Collateral Security
- Personal Guarantees of the Directors/Promoters & in the case of companies, corporate guarantees from the Group/ Associated Companies.

Suggestion

It is recommended that since the banks are already taking the above mentioned securities from the exporters and levying service charges on various transactions (such as L/C advising charges, renewal cum enhancement of limit charges, stock audits, processing fee on non-funded limits, etc) the RBI may issue directives to the banks that the premia for both pre and post shipment be borne by them and not be passed on to the exporter. ■

Priority Sector Lending: Advances to Micro and Small Enterprises engaged in exports

RBI Circular No. RPCD.CO.Plan.BC.64 /04.09.01/2009 dated 10 April 9, 2010

Please refer to our Master Circular dated July 1, 2009 on Lending to Priority Sector, in terms of which finance granted by banks to micro and small enterprises as defined under the Micro, Small and Medium Enterprises Development (MSMED) Act, 2006, is eligible for classification under priority sector.

Some commercial banks have sought clarification in respect of classification of loans granted to micro and small enterprises engaged in exports, under priority sector. The issue has been examined and it is clarified that loans granted by commercial banks to micro and small enterprises (MSE) (manufacturing and services) are eligible for classification under priority sector, provided such enterprises satisfy the definition of MSE sector as contained in MSMED Act, 2006, irrespective of whether the borrowing entity is engaged in export or otherwise.

The export credit granted to MSEs may be reported separately under heading “Export credit to micro and small enterprises sector”.