Regional Rural Banks(RRBs)

What exactly are Regional Rural Banks?

- (RRBs) were established in 1975 following the Regional Rural Banks Act, 1976 and the Ordinance promulgated on September 26, 1975.

o RRBs are financial institutions that assure agriculture and other rural sectors can access adequate credit.

o RRBs combine the familiarity with rural issues of a cooperative with the professionalism and capacity to mobilize the financial resources of a commercial bank.

o Following the 1990s reforms, the government initiated a consolidation program in 2005-06, resulting in a decline in the number of RRBs from 196 in 2005 to 43 in FY21, with 30 of the 43 RRBs reporting net profits.

Responsibilities:

o The fundamental responsibilities of a bank are as follows:

- To provide security for customers' savings;
- To create credit and increase the money supply;
- To promote confidence in the financial system of the country;
- To mobilize the public's savings;
- To expand its network so as to reach every segment of society;
- To provide financial services to all customers, regardless of their income level;
- To promote social equity by providing financial services to every stratum of society.

What are the Concerns Regarding RRBs?

- <u>Rising expense:</u> The rising expense of operations of Regional Rural Banks (RRBs) in comparison to commercial banks with scheduled operations.

    o The government desires for them to increase their profits.

- <u>Limited Activities:</u> Many of these branches are incurring losses because they do not have sufficient business.

    o In rural areas, they offer primarily government programs such as Direct Benefit ransfer.

- Limited Internet Banking: Currently, only 19 RRBs offer Internet banking and 37 have mobile banking licenses.

- Existing regulations permit RRBs to offer internet banking only if they maintain a minimum statutory capital to risk-weighted assets ratio of at least 10%.

What are the Government's Suggestions?

- It has requested that RRBs progress toward digitization, including offering internet banking services to their customers and expanding their credit base through increased lending to the Micro, Small, and Medium-Sized Enterprises (MSME) sector.
  - In order for them to become financially viable
- It implored the sponsor banks to develop a clear, time-bound plan to further bolster the RRBs and support the post-pandemic economic recovery and
  - Additionally, it was suggested holding a workshop on RRBs and sharing the best practices.

In what ways is the government reforming RRBs?

- Various steps have been implemented by the government over the years to increase the contribution of citizens to the Indian financial system.
  - With the nationalization of all Indian banks in 1969, the Indian banking industry underwent a significant transformation. NABARD was founded in 1981.
    - The primary objective of establishing NABARD was to promote sustainable and unbiased agriculture and increase rural prosperity through effective credit support, institution support and other innovative initiatives.
- Consequently, the National Bank for Agriculture and Rural Development (Nabard) will lead the initiative to revitalize the RRBs.
  - Furthermore, the development bank is already working on a road map for 22 RRBs that will be implemented by the end of the year.
    - The plan also called for the merger of these RRBs' branches with sponsor banks once they reached a certain level of business.
- The government has contributed RS 4,084 crores towards RRB recapitalization in 2021-22, of which RS 3,197 crores has been released to 21 lenders.
  - The government established a commission comprised of members from NABARD and the RBI to make recommendations for strengthening regional lenders last year. focusing on financial inclusion through the use of technology

Going Forward

- There is a need for a common framework for RRBs, similar to the core banking solution (CBS), so that they can all offer online banking services to their consumers and expand their reach and profitability.
- There should be more such as internet banking etc.
- Additionally, they need to increase their efficiency and affect various other facets of banking, such as providing loans to merchants and MSME's, in order to boost their profitability.

Foreign Direct Investment (FDI)

Refers to any investment made by a foreign individual or business into a domestic economy.

• Foreign direct investment (FDI) generally occurs when a foreign entity acquires ownership or a controls stake in the shares of the company in one country or establishes enterprises there.

• It differs from foreign portfolio investment, in which a foreign entity simply purchases equity shares of a company.

• In FDI, the foreign investor has a say in the company's day-to-day operations.

• FDI is not only a transfer of money, but also of technology, knowledge, skills, and expertise/know-how. It is a significant supply of non-debt financial resources for a country's economic development.

• FDI typically occurs in economies with the potential for growth and a skilled labour force. In recent decades, FDI has emerged as a significant form of international capital transfer.

• The benefits of FDI are not distributed equally. It depends on the procedures and infrastructure of the host nation.

• The factors that determine FDI in host nations are:

o Policy framework

o Entry and operations/functioning rules (mergers/acquisitions and competition)

o Political, economic and social stability

o Standards for the treatment of foreign subsidiaries

o International agreements

o International trade policy (tariff and non-tariff barriers)

o Privatization policy

Foreign Direct Investment (FDI) in India – Most recent information

1. From April to August of 2020, a total of USD 35.73 billion in Foreign Direct Investment was received. It is unprecedented for the first five months of a fiscal year. FDI inflow has increased despite a 23.9% contraction in GDP growth in the first quarter of 2020 (April-June).

2. The amount of FDI received in the first five months of 2020-21 (USD 35.73 billion) is 13% greater than the amount received in the first five months of 2019-2020 (USD 31.60 billion).

FDI in India

Since 1991, when the government opened the economy and initiated LPG strategies, the investment climate in India has improved significantly.

• Commonly, this improvement is attributed to the relaxation of FDI regulations.

• Since the country's economic liberalization, many sectors have been partially or entirely opened to foreign investment.

• India currently ranks among the top 100 countries in terms of business-friendliness.

• According to a UN report, India was among the top ten recipients of FDI in 2019, with total inflows of $49 billion. This represents a 16% increase over 2018.

• In February of 2020, the DPIIT will announce a policy that permits 100 percent FDI in insurance intermediaries.

• In April 2020, the DPIIT issued a new rule stating that any entity or company that shares a land border with India or whose beneficial proprietor resides in or is a citizen of such a country may only invest via the Government route. In other words, these entities can only invest after receiving sanction from the Indian government.

• Beginning in 2020, the government decided to sell a 100 percent stake in Air India, the national airline.

Foreign Direct Investment (FDI) Routes in India

There are three channels through which FDI enters India. They are described in the table below:

Category 1

100% FDI allowed via Automatic Route

Category 2

Up to 100 percent FDI allowed via Government Route

Category 3

Up to 100 percent FDI permitted through Automatic + Government Routes

Automatic route FDI

In automatic route, the foreign entity does not require government or RBI approval beforehand.

Examples:

• Medical devices: up to 100%

• Thermal energy: up to 100 percent

• Services categorized under Civil Aviation Services, including Maintenance & Repair Organizations

• Insurance: as high as 49%

• Infrastructure company on the stock market: up to 49 percent

• Ports and transport

• Infrastructure railways • Pension: up to 49%

• Exchanges of power: up to 49%

• Petroleum Refining (By Government Agencies): up to 49%

Government Facilitated FDI

Under the government route, the foreign entity is required to obtain government approval. It must submit a request via the Foreign Investment Facilitation Portal, which facilitates single-window clearance. This application is then transmitted to the respective ministry or department, which, after consultation with the DPIIT, approves or rejects the application.

Examples:

• Services for Broadcasting Content: 49%

• Banking & Government: 20%

• Food Products Retailing: 100 Percent

• 100% Core Investment Company

• Multi-Brand Retail Sales: 51 Percent

• Mining & Minerals titanium-bearing mineral and ore separations: one hundred percent

• Media that is printed and distributed physically, such as scientific and technical periodicals, magazines, and books; foreign newspaper facsimiles): 100 percent

• Satellite (installation and operations): 100 percent

• Print Media (publishing of newspapers, periodicals, and Indian editions of foreign news and current affairs magazines): 26%

Sectors where foreign direct investment (FDI) is prohibited

There are certain industries where FDI is strictly prohibited. The following are:

• Agricultural or Plantation Activities

• Nuclear Energy Production

• Nidhi Company

• Online, private, and government lotteries

• Investment in Chit Funds

• Trading in TDRs • Gambling and betting enterprises • Cigars, cigarettes, and all tobacco-related industries • Housing and real estate (except for townships and commercial projects, etc.)

New FDI Policy

New Foreign Direct Investment (FDI) policy states that

from a country that shares a land border with India or where the beneficial proprietor of an investment in India resides in or is a citizen of such a country may only invest via the Government route.

The government must also approve any transfer of ownership in an FDI transaction that benefits a country that shares a border with India.

Need only notify the RBI following a transaction, as opposed to obtaining permission from the relevant government agency beforehand.

Previously, only Bangladesh and Pakistan were permitted to receive FDI via the government route in all sectors. The revised rule now applies the government route restriction to Chinese companies.

Advantages of FDI

FDI offers numerous benefits to the country. Several of them are discussed in the following section.

1. Brings in financial resources to support economic growth.

2. Introduces new technologies, abilities, and/or knowledge, etc.

3. Creates additional employment opportunities for the populace.

4. Makes the country's commercial environment more competitive.

5. Enhances the quality of goods and services within sectors.

Disadvantages of FDI

However, foreign direct investment is also associated with some disadvantages.

- It can have a negative impact on domestic investment and domestic companies.

- Small businesses in a country may not be able to withstand the assault of multinational corporations in their industry. As a consequence of increased FDI, there is a risk that many domestic companies will close.
- FDI may also negatively impact a country's exchange rates.

Government Measures to Increase Foreign Direct Investment (FDI) in India

1.Government programs, such as the production-linked incentive (PLI) scheme for electronics manufacturing in 2020, have been announced in an effort to attract foreign investments.

2.In 2019, the government's amendment of FDI Policy 2017 to permit 100 percent FDI via the automatic route in coal mining activities increased FDI inflow.

3.FDI in manufacturing was already permitted via the 100% automatic approach; however, the government confirmed in 2019 that investments in Indian businesses involved in contract manufacturing are also permitted under the 100% automatic route, so long as they are carried out under a valid contract.

4.In addition, the government authorized 26% FDI in digital sectors. The sector has notably high return potential in India due to the country's favorable demographics, substantial mobile and internet penetration, massive consumption, and technology adoption, all of which present an excellent market opportunity for foreign investors.

5.Foreign Investment Facilitation Portal (FIFP) is the Government of India's online interface with investors to facilitate FDI. It is administered by the Ministry of Commerce and Industry's Department for Promotion of Industry and Internal Trade.

6.Foreign direct investment (FDI) inflows are anticipated to increase further,

  - as foreign investors have expressed interest in the government's steps to allow private train operations and auction off airports.
  - Valuable industries such as defense manufacturing, where the government increased the FDI limit under automatic route from 49% to 74%, are also anticipated to attract substantial investment in the future.

Framework for FDI Regulation in India

There are numerous laws in India that regulate FDI inflows. The following are:

• SEBI Act, 1992 and SEBI Regulations • Companies Act

• Foreign Exchange Management Act

• The Indian Contract Act of 1872, the Arbitration and Conciliation Act of 1996, and the Competition Act of 2002.

• Revenue Tax Act of 1961

• Policy on Foreign Direct Investment (FDI Policy)

Important Indian Government Authorities Regarding FDI

• Ministry of Corporate Affairs, Government of India

• Foreign Investment Promotion Board

• Department for Promotion of Industry and Internal Trade

• (RBI) • Directorate of Foreign Trade (DGFT)

• (SEBI) • Income Tax Department

• Numerous Ministries of the Government of India, including Power, Information & Communication, Energy, etc.

The Way Forward for FDI

1. FDI is a primary driver of economic growth and a significant source of non-debt financing for India's economic development. Consequently, a robust and readily accessible FDI regime must be ensured.

2. Economic growth in the post-pandemic period and India's large market will continue to attract market-oriented investments to the nation.