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## Liquidity Measures Extended for Banks

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Recently, the **Reserve Bank of India (RBI)** has extended the relaxation relating to **Marginal Standing Facility (MSF) scheme** till 30<sup>th</sup> September 2020.

- It has also extended the relaxation relating to maintenance of **Cash Reserve Ratio (CRR)** up to 25<sup>th</sup> September 2020.
- This was done in view of the hardships being faced by banks in terms of social distancing at work and consequent strain on reporting requirements.

### Key Points

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- **Marginal Standing Facility:**

- The RBI, as a temporary measure, had increased the borrowing limit of scheduled banks under the MSF scheme from 2% to 3% of their deposits with effect from 27<sup>th</sup> March 2020.

Earlier, the above relaxation was granted till 30<sup>th</sup> June 2020.

- **MSF is a window for scheduled banks to borrow overnight** from the RBI in an emergency situation when interbank liquidity dries up completely.  
Under interbank lending, banks lend funds to one another for a specified term.
- Banks borrow from the RBI by pledging government securities at a rate higher than the **repo rate** under **Liquidity Adjustment Facility (LAF)**.
  - Repo rate is the rate at which the **RBI lends money to commercial banks** against the securities in the event of any shortfall of funds.
  - Loans provided at repo rate are provided for a specified period with an obligation that the bank will repurchase the securities back at a predetermined rate.
- **Differences between Repo Rate and MSF**
  - Repo rate is the rate at which RBI lends money to **commercial banks**, while MSF is a rate at which RBI lends money to **scheduled banks**.
  - The repo rate is given to banks that are looking to meet their short-term financial needs. While, the MSF is meant for lending **overnight to banks**.
  - Lending at repo rates involves a **repurchase agreement** of securities. While it is not so in MSF.
  - Under MSF, banks are also allowed to use the securities that come under **Statutory Liquidity Ratio (SLR)** in the process of availing loans from RBI.

Under SLR, commercial **banks are mandated by RBI to maintain a stipulated proportion of their deposits in the form of liquid assets** like cash, gold and unencumbered (free from debt) securities.

- **Cash Reserve Ratio:**

- On 27<sup>th</sup> March, 2020 the minimum daily maintenance of the CRR was reduced from 90% of the prescribed CRR to 80%.

The above facility was available till 26th June 2020.

- CRR is the amount of **liquid cash that banks have to maintain with the RBI**, as a percentage of their total deposits.

## Key Terms

- **Scheduled Banks:** Any bank which is listed in the **2<sup>nd</sup> schedule of the RBI Act, 1934** is considered a scheduled bank.

The banks included in this category should fulfil two conditions:

- The paid up capital and collected fund of the bank should not be less than Rs. 5 lakh.
  - Any activity of the bank shall not adversely affect the interests of the depositors.
- **Commercial Banks:** It refers to both scheduled and non-scheduled commercial banks which are regulated under the **Banking Regulation Act, 1949.**
  - **Liquidity Adjustment Facility (LAF)** is a tool used in monetary policy by the RBI, that allows banks to borrow money through repurchase agreements (repos) or for banks to make loans to the RBI through reverse repo agreements.

**Reverse repo rate** is the rate at which the RBI borrows money from commercial banks within the country.

**Source: FE**