Glossary of Terms for the Parameters used in the 'Report of the Committee on Differential Premium System for Banks in India'

The precise clarification on various parameters (used by the Committee) is given below for a ready reference, which shall facilitate a better understanding of the report by all the stakeholders. However, for further details on these parameters, kindly see the relevant RBI Circulars on https://www.rbi.org.in/.

1. Solvency

1.1 Tier I Capital

It consists mainly of share capital and disclosed reserves (minus goodwill, if any). Tier I items are deemed to be of the highest quality because they are fully available to cover losses Hence it is also termed as core capital.

1.2 Tier II Capital (%)

It is also known as supplementary capital, which consists of certain reserves and certain types of subordinated debt. Tier II items qualify as regulatory capital to the extent that they can be used to absorb losses arising from a bank's activities. Tier II's capital loss absorption capacity is lower than that of Tier I capital.

1.3 Capital to Risk-weighted Asset Ratio (CRAR) (%)

Capital to risk weighted assets ratio is arrived at by dividing the capital of the bank with aggregated risk weighted assets for credit risk, market risk and operational risk. The higher the CRAR of a bank the better capitalized it is.

CRAR = (Tier I capital + Tier II capital) / Risk weighted assets * 100

Here, Risk Weighted Assets (RWA) refers the value of each asset after assigning corresponding risk weights (as per instructions from RBI).

1. Asset Quality

2.1 Gross NPA Ratio = [Gross NPA/ Gross Advances] X 100

Here, Gross NPA is the amount which is outstanding in the books, regardless of any interest recorded and debited.

2.2 Net NPA Ratio = [Net NPA/ Net Advances] X 100

Here, Net NPA = Gross NPA – (Balance in Interest Suspense account + DICGC/ECGC claims received and held pending adjustment + part payment received and kept in suspense account + Total provisions held).

2.3 Substandard Assets/ Gross NPA (%)

A substandard asset would be one, which has remained NPA for a period less than or equal to 12 months. Such an asset will have well defined credit weaknesses that jeopardize the liquidation of the debt and are characterised by the distinct possibility that the banks will sustain some loss, if deficiencies are not corrected.

2. Liquidity

3.1 Liquid Assets to Deposits and Borrowings (%) Or Liquidity ratio

Liquid Assets consist of cash in hand, balance with RBI, balances with banks, monies placed with counterparties (interbank) and maturing within one month i.e. money at call & short notice, market value of government securities held (in India). It also includes cash reserves in excess of required CRR and G-secs in excess of the minimum SLR requirement. Further, the Liquid assets needs to be divided by the total of deposits & borrowings to find out the liquidity ratio.

3.2 Term Deposit to Total Deposit

Term Deposit shall mean a deposit received by the bank for a fixed period and which is withdrawable only after the expiry of the said fixed period and shall also include deposits such as Recurring/Cumulative/ Annuity/Reinvestment deposits, Cash Certificates etc.

4. Profitability

4.1 Return on assets (ROA)

Return on Assets (ROA) is a profitability ratio which indicates the net income (profits) generated by the bank on its total assets (including fixed assets). The higher the proportion of average earnings assets, the better would be the resulting returns on total assets.

ROA = Net profits (Profit after tax) / Avg. total assets (in %)

4.2 Cost / Income (%) or (Efficiency Ratio)

The cost income ratio reflects the extent to which non-interest expenses of a bank make a charge on the net total income (total income - interest expense). The lower the ratio, the more efficient is the bank.

Formula: **Non interest expenditure / Net Total Income * 100.**

4.3 Net Interest Margin (NIM)

Net interest margin is the net interest income divided by average interest earning assets and it is calculated as:

$$\textbf{Net Interest Margin} = \frac{\textbf{Interest income – Interest Expenses}}{\textbf{Average earning assets (during the year)}}$$

4.4 <u>For further clarification please refer to:</u>

A) https://rbi.org.in/Scripts/Glossary.aspx

B) UCB, DCCB & StCB:

Master Circular- Prudential Norms on Capital Adequacy – UCBs of July 01, 2015:

https://www.rbi.org.in/scripts/BS_ViewMasCirculardetails.aspx?id=9816

C) SCB, LAB, RRB

- Master Circular -Basel III Capital Regulations of July 01, 2015*
https://rbidocs.rbi.org.in/rdocs/notification/PDFs/58BS09C403D06BC14726AB61783180628D39.PDF

- Master Circular - Prudential Guidelines on Capital Adequacy and Market Discipline-New Capital Adequacy Framework (NCAF) of July 01, 2015*
https://rbidocs.rbi.org.in/rdocs/notification/PDFs/85BL4697A788DAB5485B826CFA24D35EA1BE.PDF

- Master Circular - Prudential norms on Income Recognition, Asset Classification and provisioning pertaining to Advances of July 01, 2015*
https://rbidocs.rbi.org.in/rdocs/notification/PDFs/101MC16B68A0EDCA9434CBC239741F5267329.PDF

*(The above circulars are subject to updation time to time)