

# Funds Management – Context, Set-up and Funds Flow Tracking

**Kumudini Hajra**  
**Director, DICGC (India)**

**Investment Management for  
Deposit Insurance Agencies**

February 20-22, 2013  
MUMBAI, INDIA



**निक्षेप बीमा और प्रत्यय गारंटी निगम**

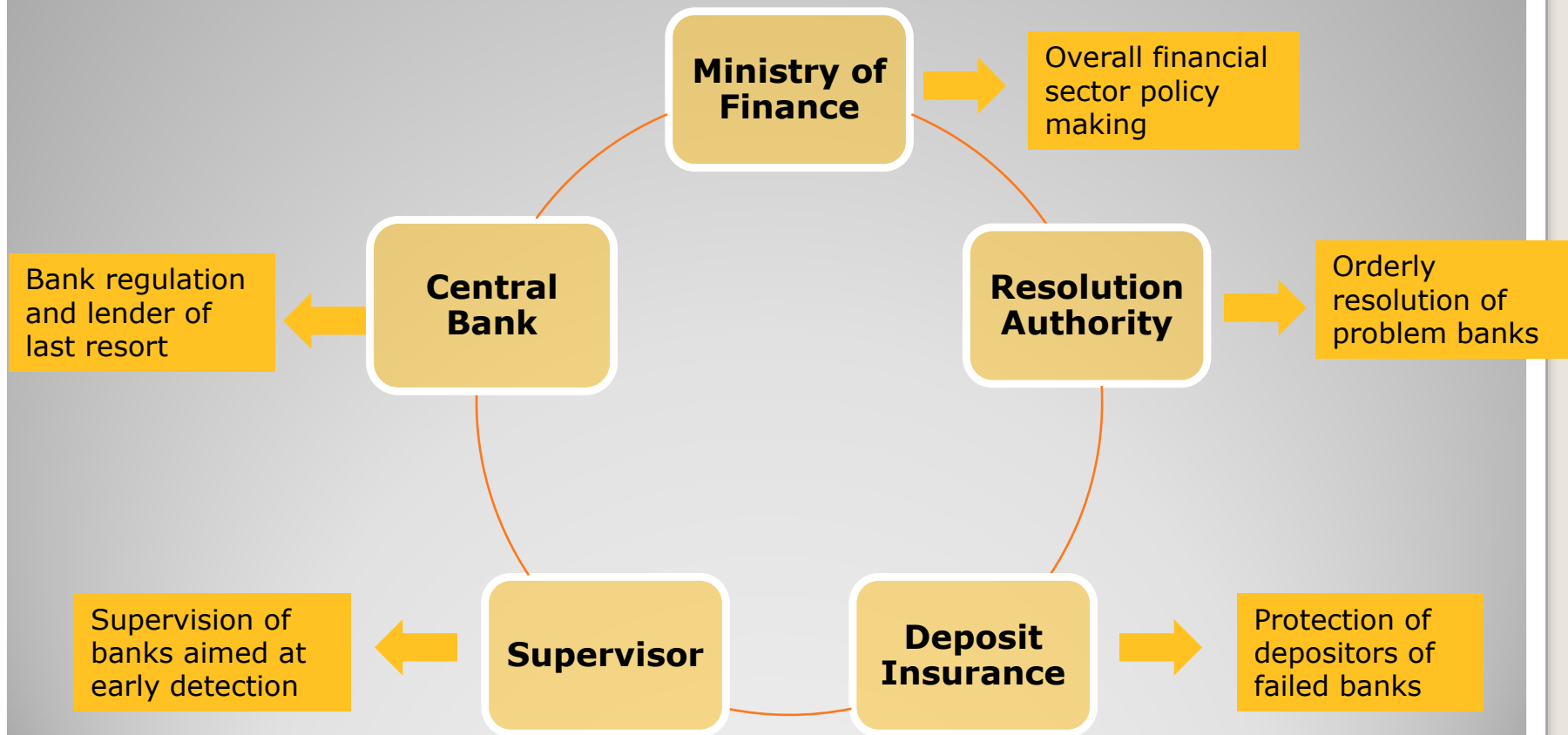
**DEPOSIT INSURANCE AND CREDIT GUARANTEE CORPORATION**

(भारतीय रिज़र्व बैंक की संपूर्ण स्वामित्ववाली सहयोगी Wholly owned subsidiary of the Reserve Bank of India)

# PRESENTATION OUTLINE

- **Safety net framework**
- **Fund management**
  - **Conceptual framework**
  - **Indian context**
- **Investment management**
  - **Conceptual framework**
  - **Indian context**

# FINANCIAL SAFETY NET FRAMEWORK



# FINANCIAL CRISIS – EVOLUTION OF REGULATORY FRAMEWORK

- Review of deposit insurance systems and resolution frameworks
- Role of DIA in systemic crisis management (not only protecting depositors of failed individual banks but also stabilising the overall financial system)
- Increased role of DIS as resolution authority
- Crisis arrangements – enhanced interaction among Central Bank, Supervisor, Ministry of Finance and DIA

# DI SYSTEM– DIFFERENT MANDATES

- Roles of DIAs differ:
  - Paybox
  - Paybox plus
  - Loss minimizer
  - Risk Minimizer
- For the deposit insurer agency to perform its role, it has to be backed by adequate fund.

## CORE PRINCIPLE 11 ON FUNDING:

A deposit insurance system should have available all funding mechanisms necessary to ensure the prompt reimbursement of depositors' claims including a means of obtaining supplementary back-up funding for liquidity purposes when required. Primary responsibility for paying the cost of deposit insurance should be borne by banks since they and their clients directly benefit from having an effective deposit insurance system.

# FUND MANAGEMENT

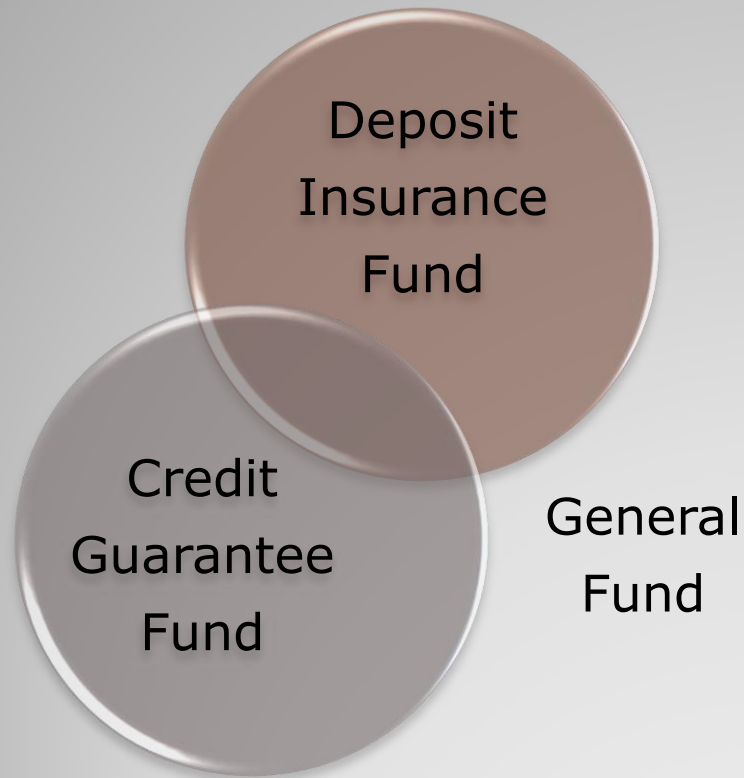
- **Type of Funds** – Ex-ante, Ex-post and Hybrid
- **Sources of Funds** –
  - Capital (initial contribution)
  - Premium from member institutions
  - Investment income
  - Share in recoveries
  - Lines of credit (from CB/MoF)
  - Borrowings
- **Use of Funds** –
  - Payouts
  - Resolution Funding
  - Operational Expenditure
  - Other (Taxes?)

# A SNAPSHOT OF DICGC

- Founded in 1962
- Paybox mandate (credit guarantee mandate added in 1978 but has remained non-operational since 2003)
- Provides funding for mergers of banks
- Maintains three distinct funds
- Insurance limit of INR 0.1 mn fully protects 93% of accounts and covers 35% of deposit value
- Insures 2174 banks, including 2011 co-operative banks
- Claims largely originate from co-operative banks



# FUND MANAGEMENT BY DICGC



- DICGC maintains three balance sheets
- DIF – Largest Fund
- CGF – Small fund; no schemes at present
- GF – Used for operational expenses
- Transfer between funds is permitted
- Limited explicit back-up funding

# SOURCE AND USE OF FUNDS IN DIF

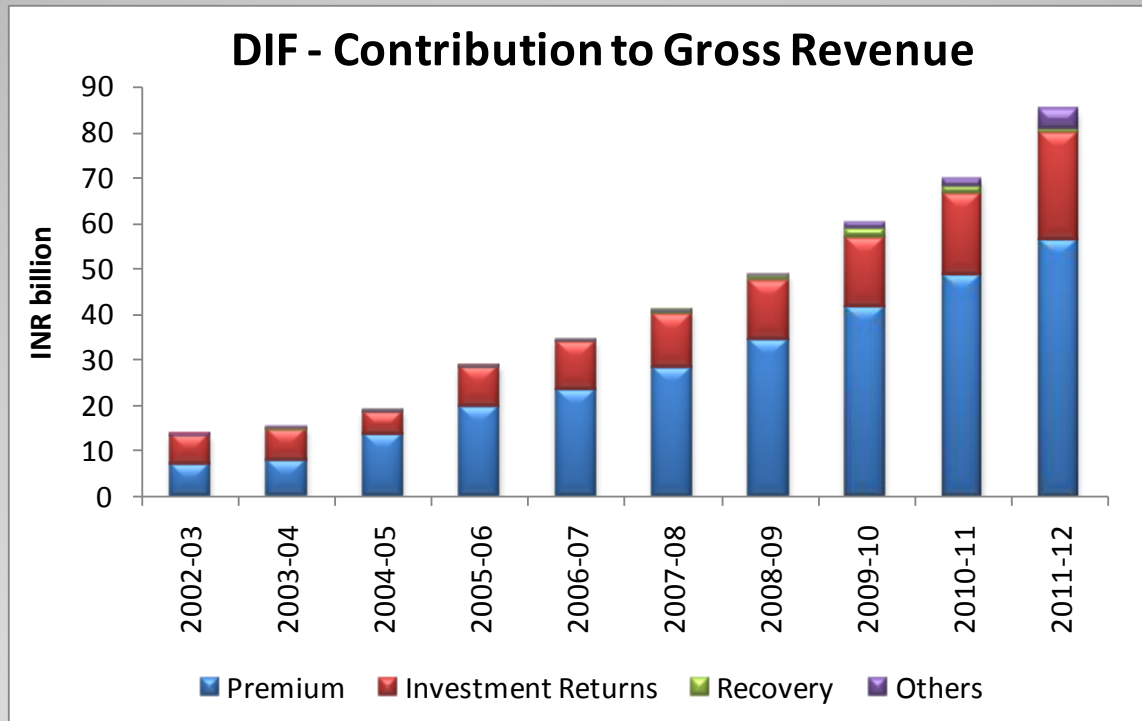
## SOURCE OF FUNDS

- Premium from insured banks
- Recoveries
- Coupon (Interest) received from existing investments
- Income from Reverse Repo transactions
- Any capital gains from rebalancing activity

## APPLICATION OF FUNDS

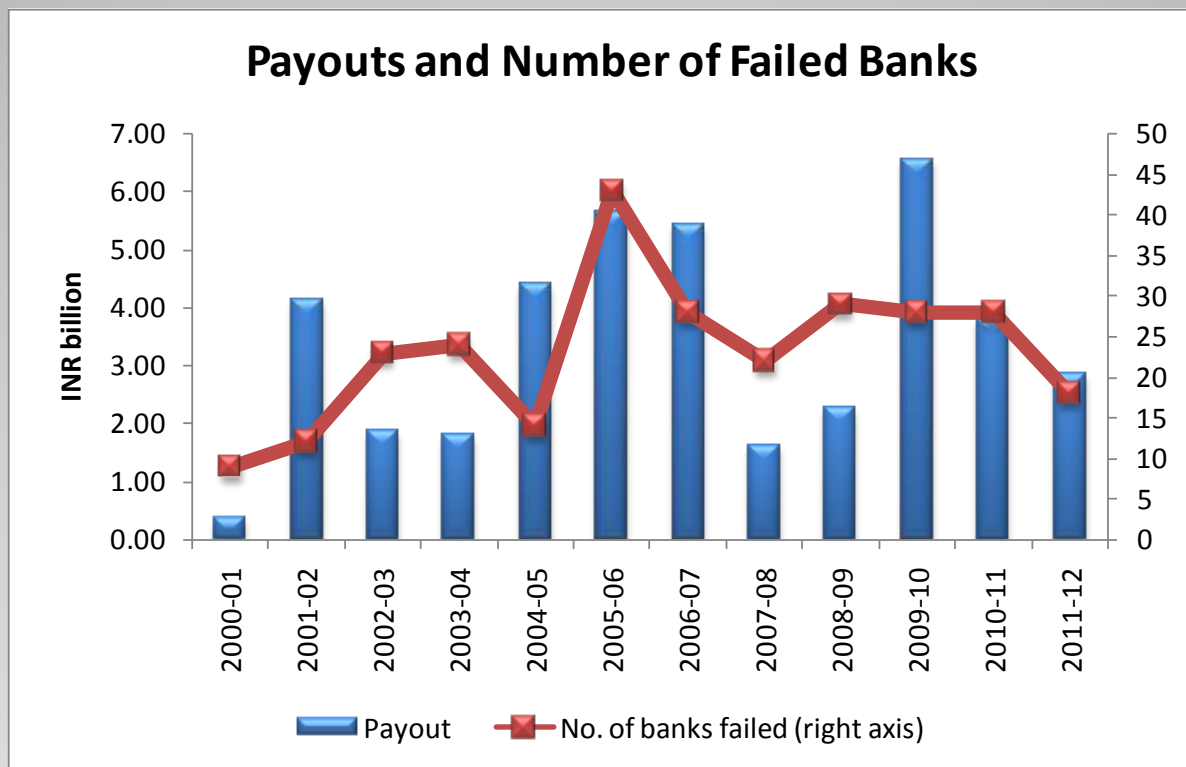
- Settlement of Claims
- Tax Payments:
  - Income Tax
  - Service Tax
- Operational expenses
- Any capital losses from rebalancing activity

# DIF – CONTRIBUTION TO REVENUE



**Investment Management for Deposit Insurance Agencies**  
February 20-22, 2013, Mumbai, India

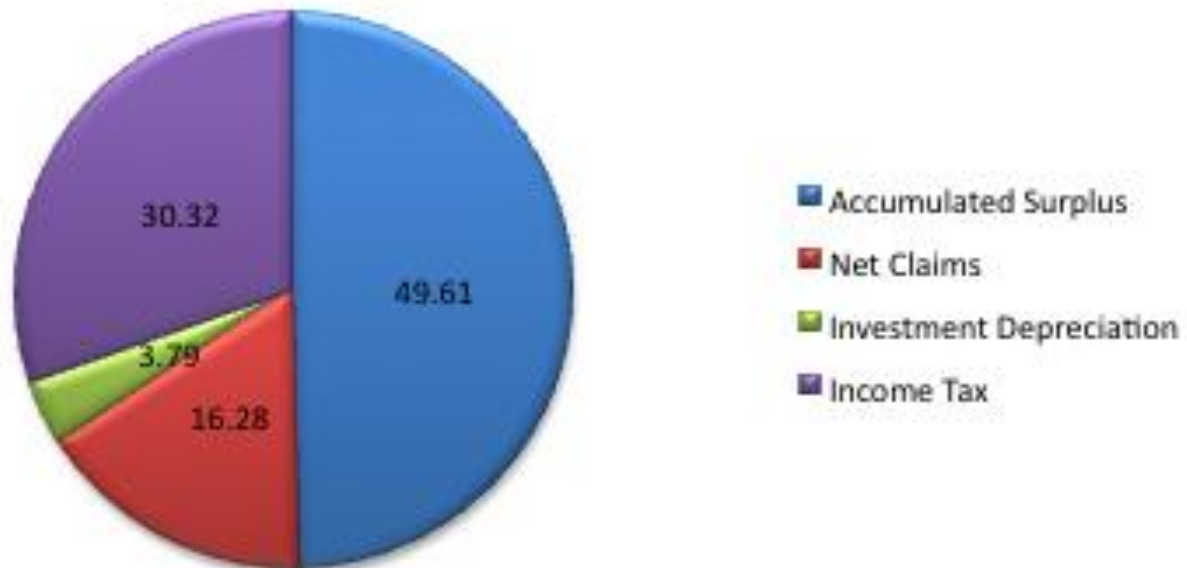
# TREND IN CLAIMS



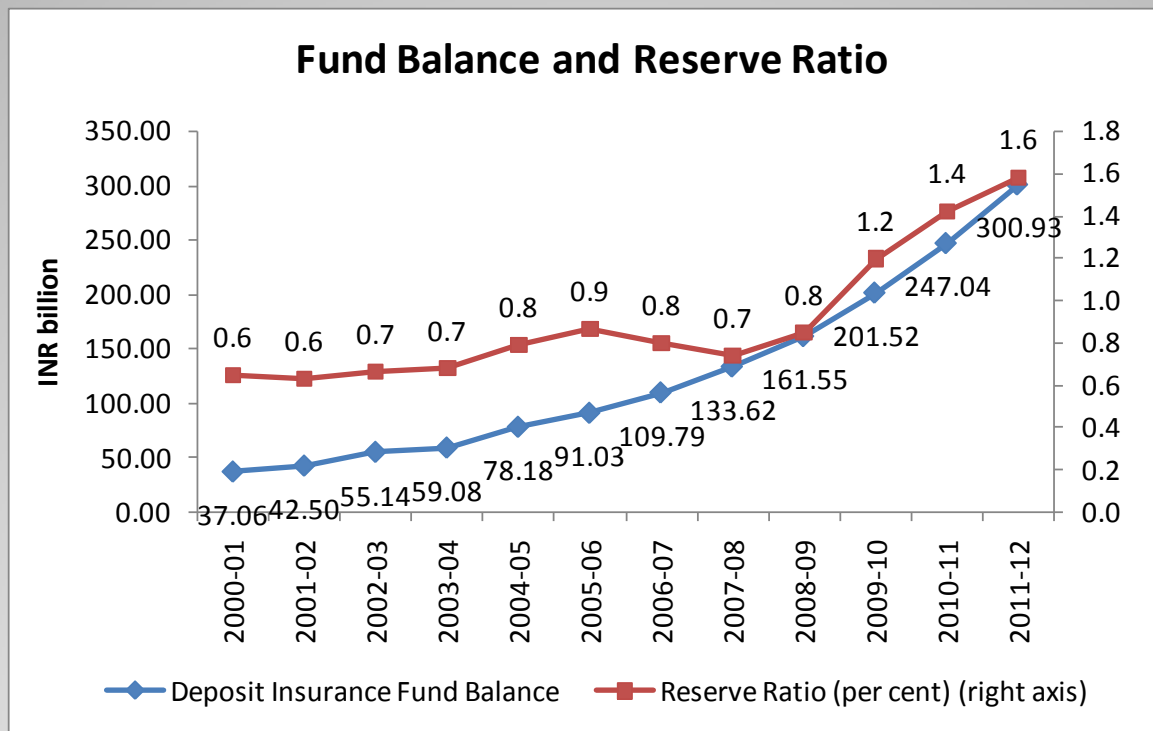
**Investment Management for Deposit Insurance Agencies**  
**February 20-22, 2013, Mumbai, India**

# DIF – DISPOSAL OF REVENUE

DIF - Disposal of Gross Revenue (%)



# DIF – FUND ADEQUACY



Investment Management for Deposit Insurance Agencies  
February 20-22, 2013, Mumbai, India

# OPTIMAL SIZE OF FUND / TARGET RESERVE LEVEL

- Normal situations
  - Establish how large a reserve is appropriate
  - Target level should be adequate to at least cover the potential losses of the insurer under normal circumstances
  - Should factor in:
    - Composition of member banks (number, size, complexity of banks)
    - Liabilities of members and exposure of insurer to them
    - Probabilities of failures
- Crisis situation
  - Over-reliance on back-up funding from government (essential for maintaining depositor confidence) – budgetary limits?
  - Issue of bonds (backed by government guarantee?)

# OBJECTIVES OF INVESTMENT MANAGEMENT BY DICGC

To invest the Corporation's Funds in manner which will provide for:

- ❑ Maximum security; while meeting
- ❑ Cash flow demands of the institution; with
- ❑ High returns on investment

In accordance with

- ❑ provisions of the DICGC Act/Regulations
- ❑ Sound and acceptable business practices



# MARKET AND INSTRUMENTS

- **Market:**

Overnight Funds

- **Instruments:**

Reverse Repo

- Done on an anonymous, electronic dealing system provided by CCIL
- Telephonic deals, reported via PDO-NDS, an RBI package

- **Rationale:**

Temporary surplus funds are invested for overnight tenor, since the G-Sec market follows a T+1 settlement cycle, while in the overnight market, settlement is on T+0 basis

- **Market:**

G-Sec

- **Instruments:**

- Dated securities from GoI
- Treasury Bills from GoI
- Special securities from GoI such as Oil Bonds, Fertiliser Bonds
- Cash Management Bills from GoI
- Done on electronic platform

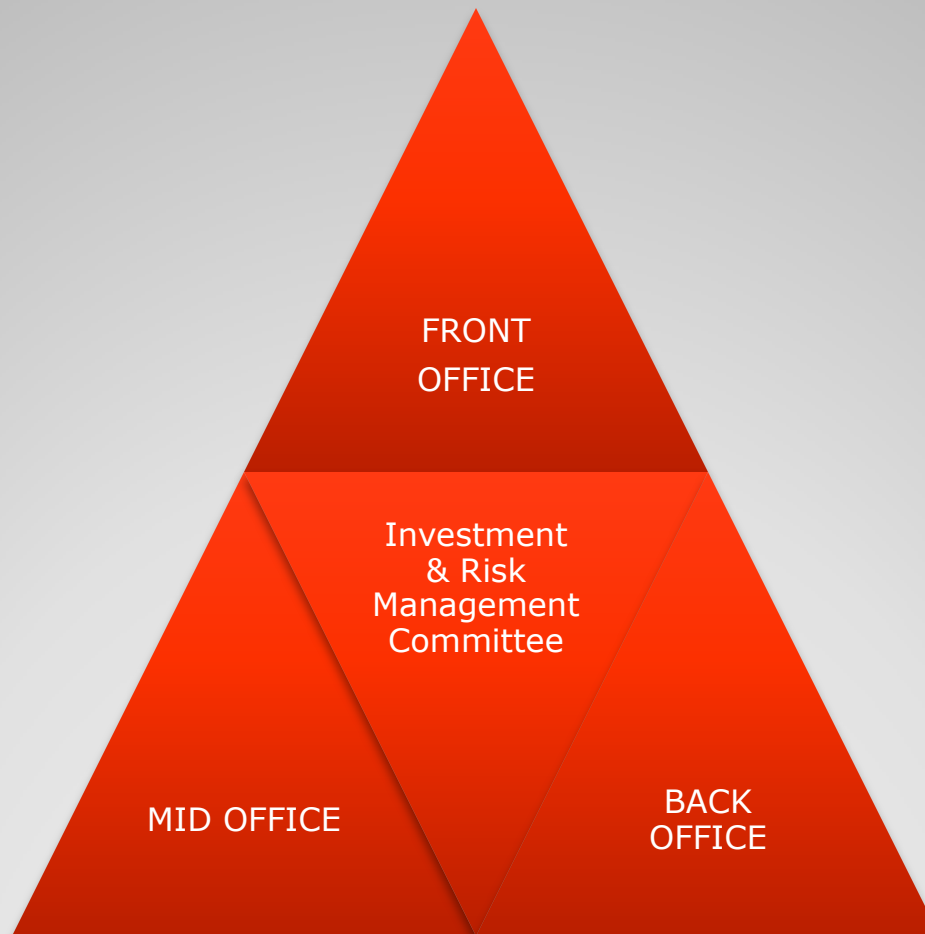
- **Rationale:**

In accordance with Sec. 25 of the DICGC Act

# **INVESTMENT MANAGEMENT GUIDELINES & RISK MANAGEMENT FRAMEWORK**

- Approved by the Board every year
- Provide overall guidance to treasury operations and clarify concepts
- Lays down the policy for investing corporation's funds
- Identification and measurement of risk, risk mitigation strategy, continuous tracking

# ORGANISATION OF TREASURY



**Investment Management for Deposit Insurance Agencies  
February 20-22, 2013, Mumbai, India**

# RISK PARAMETERS

Duration of long-term portfolio

- Tracks CCIL CASBI Index

Modified duration

- Measure of interest rate sensitivity

Concentration risk

- Concentration in top 4 securities not to exceed 20% of entire portfolio

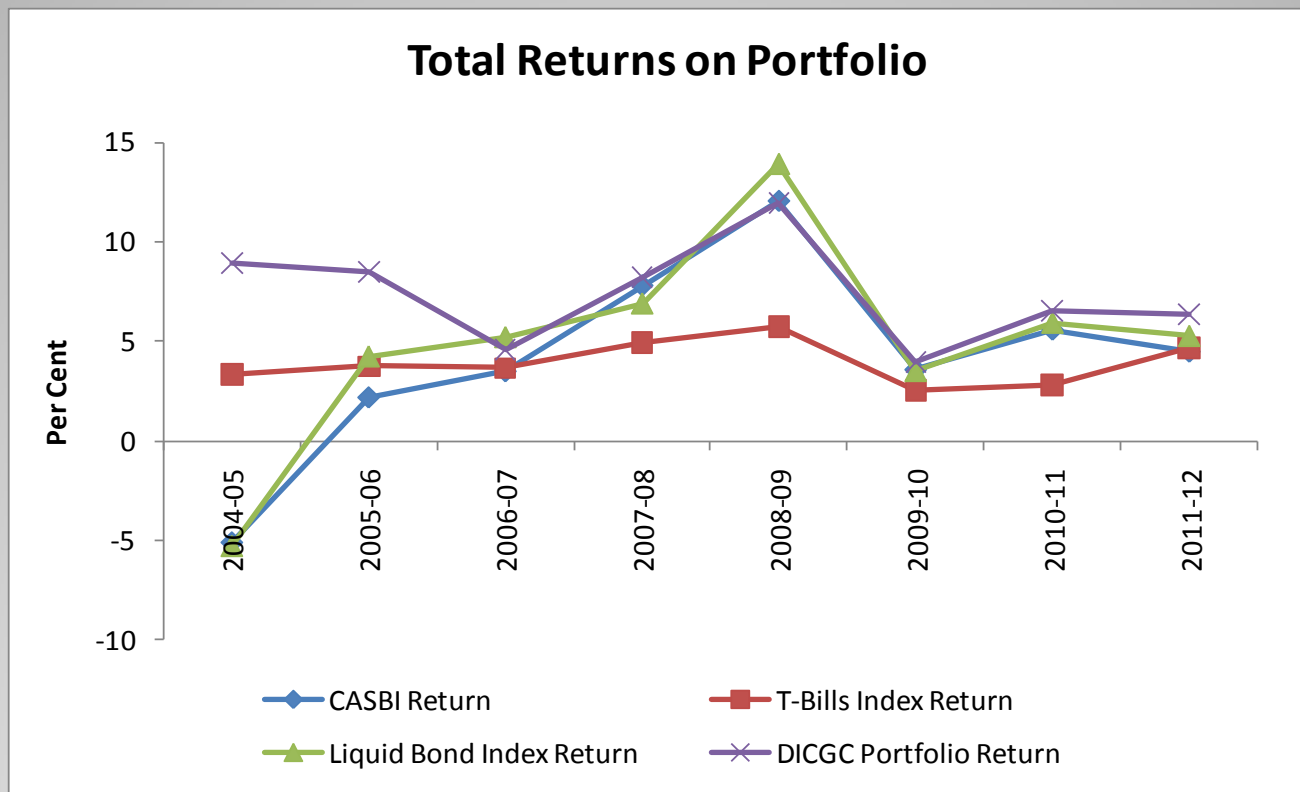
Market risk  
(VaR/Standardised  
duration method)

- Quantification of market risk is set at higher of that arrived by 2 methods

Investment fluctuation  
reserve

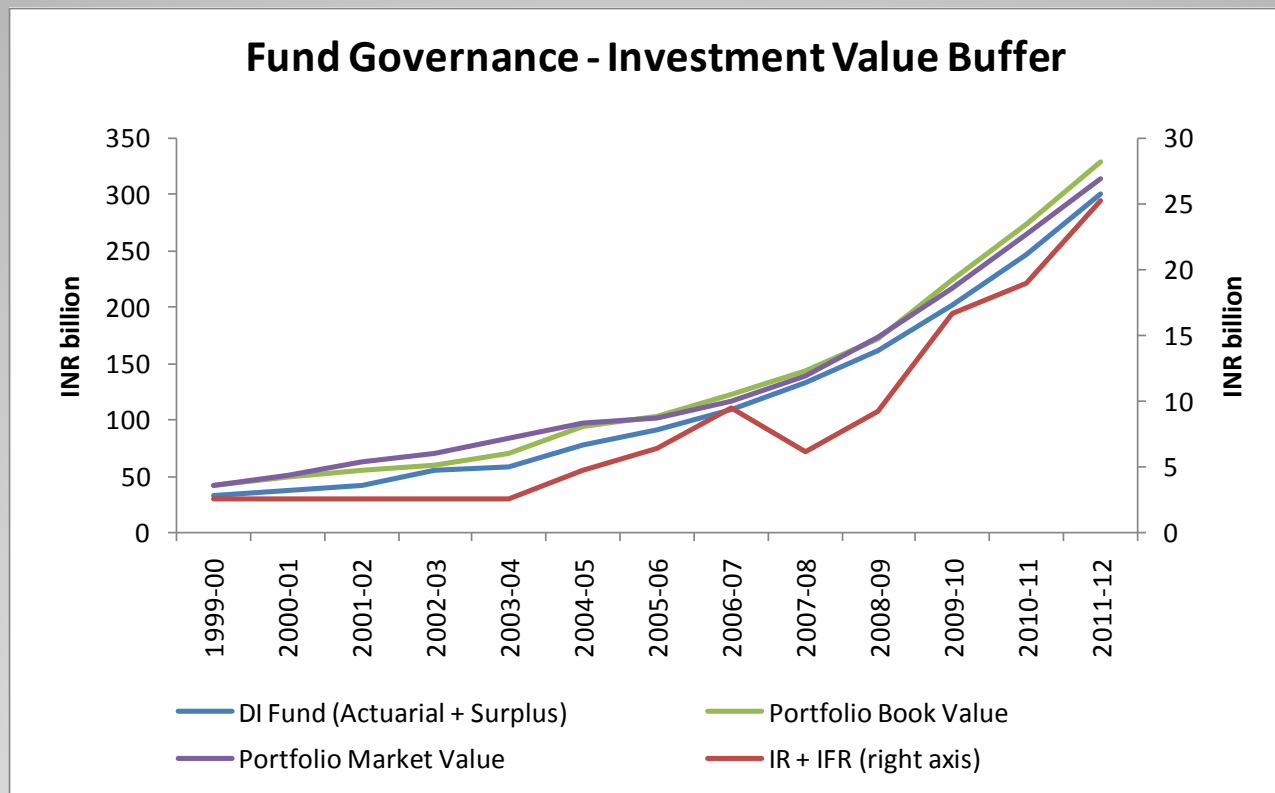
- IFR cushion maintained against market risk

# INVESTMENT VALUE BUFFER



Investment Management for Deposit Insurance Agencies  
February 20-22, 2013, Mumbai, India

# INVESTMENT VALUE BUFFER



IR: Investment Reserve

IFR: Investment Fluctuation Reserve

**Investment Management for Deposit Insurance Agencies**  
February 20-22, 2013, Mumbai, India

# ACCOUNTABILITY AND GOVERNANCE

- Precluded from taking speculative position
- Day-to-day audit of treasury transactions
- Checks and balances at various levels
  - Head of treasury
  - CEO level – Treasury dashboard (part of MIS)
  - Investment Committee – Monthly review
  - Board and Audit Committee – Quarterly review
  - Statutory audit - Annual

# **LIMITATIONS OF INVESTMENT MANAGEMENT FRAMEWORK**

- Conservative stance – limits earnings potential
- Narrow pool of instruments
- Illiquidity in G-sec market
- Low maneuverability (directive to work on fully-invested basis)



# ONGOING CHALLENGES FOR DICGC

## SHORT-TERM

- Implementation of risk-based premiums
- Faster settlement of claims – IT solutions (unique customer view?)
- Information sharing with central bank – MoU
- Estimation of actuarial liabilities / target fund size
- Enhanced public awareness

## MEDIUM TERM

- Broader reforms in deposit insurance (Working Group, Financial sector legislative reforms commission)
- Focus on 3 things – (i) Efficiency in payouts, (ii) Financial strength of DICGC, (iii) Broader mandate (incl. resolution)

# CHALLENGES FOR FUND MANAGEMENT – SUMMARY OF POINTS

- Develop and sustain fund raising capabilities
  - Especially in the case of systemic crises
  - Quick access to large amount of money
- Fund management in normal times
  - Appropriate target size of reserve fund
  - Feasible differential premium scheme
- Investment management framework
  - Balance between liquidity and profitability
  - Portfolio management within tolerable risk parameters
  - Accountability for performance

**THANK YOU**  
**QUESTIONS?**