

## **Base Rate System in Indian Banks: An Analysis\***

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*This paper analyses the Base rate structure which is followed by commercial banks in India from July 2010 as per the directions of RBI. It makes a comparison of the Benchmark Prime Lending Rate (BPLR) regime and the new Base rate regime and the related pros and cons of both the bases of lending rate mechanisms. As the BPLR system fell short of its original objective of bringing transparency in lending rates, RBI introduced the Base rate system. The latter is aimed at enhancing transparency in lending rates of banks and proper transmission of monetary policy. The study computes the Base rates for a sample of 68 banks as per the formula given by RBI and compares them with Base rates declared by the respective banks. The study reveals that banks are setting their Base rates below their Break-Even Base rate to attract high value business to counter stiff competition in the banking industry.*

### **I Introduction**

The Reserve Bank of India (RBI) released its final guidelines on implementation of the Base rate System on April 9, 2010. Flexibility and transparency were the key themes of these guidelines. They came into effect from July 1, 2010. While a glance at them gives an impression that they are another version of the Benchmark Prime Lending Rate (BPLR), a close scrutiny enables us to identify the differences between the two concepts. The Base rate system is proposed to ensure transparency and consistency in the dissemination of rates and the non-discriminatory application of lending rates to all borrowers, both existing and new.

With the objective of making credit available to the productive sectors of the economy, RBI regulated the sectoral credit allocation and bank lending rates till late 1980s. Borrowers were discriminated and charged different rates for the same loan amount, based on their socio-economic background and bargaining capacity. Furthermore, the terms and conditions of credit were sector-specific, programme-specific and purpose-specific. With the initiation of financial sector reforms in early 1990s, various steps were taken by RBI to deregulate the

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