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All about LOU and Nirav Modi Fraud with PNB



FRAUD



A satisfied customer is bank's ambassador. Indian banking sector grew at 8% in the last fiscal, whereas Karnataka Bank registered an annual growth rate of 17.82%.

Mahabaleshwara MS
MD and CEO, Karnataka Bank



Post GST and demonetization implementation, India can now propel itself into a higher growth trajectory.

Arvind Subramanian
Chief Economic Adviser



The Union Cabinet's decision to allow the government to contribute the entire 12% towards employees' provident fund (EPF) of new employees will cost about Rs 4,500 crore.

Santosh Kumar
Minister of State (MoS) for Finance

ALL ABOUT LOU AND NIRAV MODI FRAUD WITH PNB

On the morning of St. Valentine's Day when many young Indians were preparing to exchange roses and presents, a horror was unfolding at Punjab National Bank (PNB), the nation's second largest lender. On 14 February, 2018, PNB informed the stock exchanges that it had detected a fraud of ₹1.8 billion (around Rs11,400 crore), shaking the financial community and the nation at large. In 2011, it began with a much smaller amount with a single letter of undertaking (LOU) worth around Rs.800 crore.

Modus operandi

PNB fraud surfaced after one of the key accused bank officials retired. When Nirav Modi's executives came calling

for a letter of undertaking, or LOU for renewing a foreign currency loan, the new official in charge demanded the mandatory collateral. He told them that no record of approval of issuance of any LOU was available at the branch. Modi's executives insisted they had never given collateral before. This raised a red flag at the bank.

All about LOU

A customer of an Indian bank imports goods. He has to make payment in Foreign Currency. He may raise a loan in Indian Rupees at high rate of interest (12-15% p.a) and convert this amount to foreign currency to pay for import. He prefers to raise a short-term foreign currency loan in a foreign country to pay for imports at much cheaper rate of interest (2 - 5% p. a). He approaches the foreign exchange department of his bank and asks for issue of a Letter of Undertaking (also known as Letter of Comfort) in favor of a foreign bank, normally a branch of an Indian bank overseas who agrees to lend him based on LOU (a commitment like a bank guarantee).

In return, the bank would ask him for a collateral in the form

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