SYLLABUS

Class – B.Com I Years

Subject – Banking and Insurance

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UNIT I

Meaning and Definition of Bank:

A bank is an institution which deals with money and credit. It accepts deposits from the public, makes the funds available to those who need them, and helps in the remittance of money from one place to another. In fact, a modem bank performs such a variety of functions that it is difficult to give a precise and general definition of it. It is because of this reason that different economists give different definitions of the bank.

According to Crowther, a bank "collects money from those who have it to spare or who are saving it out of their incomes, and it lends this money to those who require it."

In the words of Kinley, "A bank is an establishment which makes to individuals such advances of money as may be required and safely made, and to which individuals entrust money when not required by them for use."

According to John Paget, "Nobody can be a banker who does not (i) take deposit accounts, (h) take current accounts, (iii) issue and pay cheques, and (iv) collects cheques-crossed and uncrossed-for its customers,"

Prof. Sayers defines the terms bank and banking distinctly. He defines a bank as "an institution whose debts (bank deposits) are widely accepted in settlement of other people's debts to each other."

Again, according to Sayers, "Ordinary banking business consists cash for bank deposits and bank deposits for cash; transferring bank deposits from one person or corporation to another; giving bank deposits in exchange for bills of exchange, government bonds, the secured promises of businessmen to repay and so forth".

As per Section 5(c) of the Banking Regulation Act, 1949 a "Banking Company" means any company which transacts the business of banking in India.

Explanation: Any company which is engaged in the manufacture of goods or carries on any trade and which accepts the deposits of money from public merely for the purpose of financing its business as such manufacturer or trader shall not be deemed to transact the business of banking within the meaning of this clause."

As per Section 5(b) of the Banking Regulation Act, 1949 , "banking" means the accepting, for the purpose of lending or investment, of deposits of money from the public, repayable on demand or otherwise, and withdrawable by cheque, draft, order or otherwise."

In short, the term bank in the modern times refers to an institution having the following features:

i. It deals with money; it accepts deposits and advances loans.
ii. It also deals with credit; it has the ability to create credit, i.e., the ability to expand its liabilities as a multiple of its reserves.
iii. It is commercial institution; it aims at earning profit.
iv. It is a unique financial institution that creates demand deposits which serve as a medium of exchange and, as a result, the banks manage the payment system of the country.

Creation of Money :

Banks accept deposits from the public for the purpose of lending it to those who need money to meet their personal or business needs.

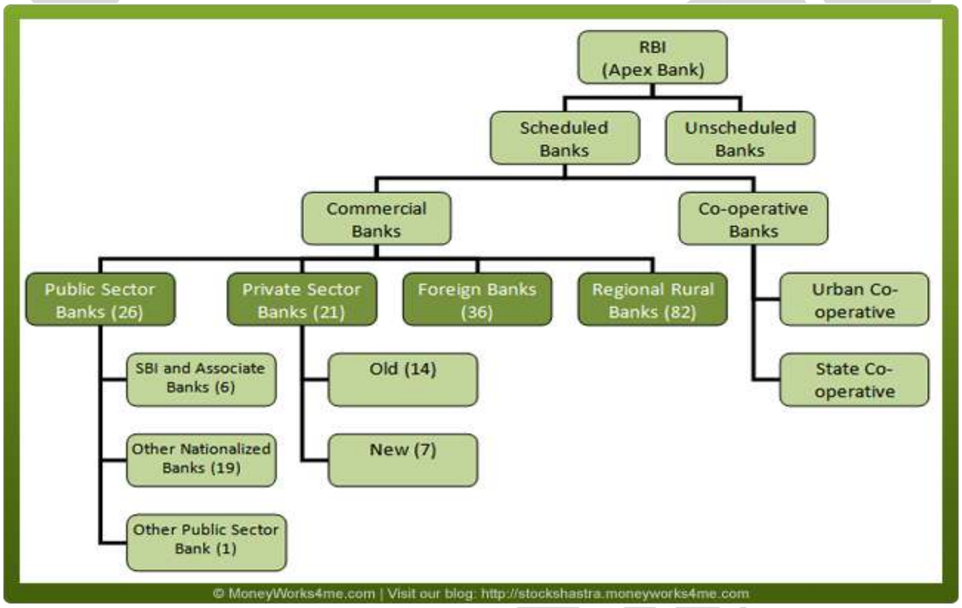
While granting loans to the borrowers, the bank does not handover the entire cash to him but credits the amount of the loan in his bank account. The borrower has a right to issue or draw cheques against it as and when he needs. According to Hartley Withers, "Every loan crates a deposit."

When a loan is granted to a borrower he acquires a right or claim against the bank to withdraw that amount. This right is similar to the right of a customer to withdraw his own deposit from his bank account.

In economics, money creation is the process by which the money supply of a country or a monetary region (such as the Eurozone) is increased. A central bank may introduce new money into the economy (termed 'expansionary monetary policy') by purchasing financial assets or lending money to financial institutions. Commercial bank lending then multiplies this base money through fractional reserve banking, which expands the total of broad money (cash plus demand deposits).

Structure of Commercial Banks In India:

Reserve Bank of India is the Central Bank of our country. It was established on 1st April 1935 under the RBI Act of 1934. It holds the apex position in the banking structure. RBI performs various developmental and promotional functions. As of now 26 public sector banks in India out of which 21 are Nationalised banks and 5 are State Bank of India and its associate banks. There are total 92 commercial banks in India. Public sector banks hold near about 75% of the total bank deposits in India.



Indian Banks are classified into commercial banks and Co-operative banks. Commercial banks comprise: (1) Schedule Commercial Banks (SCBs) and non-scheduled commercial banks. SCBs are further classified into private, public, foreign banks and Regional Rural Banks (RRBs); and (2) Co-operative banks which include urban and rural Co-operative banks.

1. Central Bank or Apex Bank: The Reserve Bank of India

2. Commercial Banks:

(I) Public Sector Banks:

(a) State banks

(b) Nationalized Banks:

(II) Private Sector Banks:

(a)Indian Banks

(b)Foreign Banks

(III)Co-operative Banks:

(a)Central/ District Co- operative Banks

(b) Primary Credit Society

(IV)Regional Rural Banks

(V)National Bank for Agriculture and Rural Development (NABARD)

(VI)Development Bank

Principles of Management In Banks:

Recruitment:

Recruitment is a process to discover the sources of manpower to meet the requirement of the staffing schedule and to employ effective measures for attracting that manpower in adequate numbers to facilitate effective selection of efficient personnel.

Recruiting is an ongoing project for any organization. From the moment an employment application is submitted, recruitment software should be there to rank it, match the applicant to job if necessary and place the information in a database that can share the information across different software applications or applicant tracking tasks, including scheduling interviews and sending out letters for every stage of the recruitment process.

Definitions:

It is the process of finding and attracting capable applicants of employment. The process begins when new recruits are sought and ends when their applications are submitted. The result is pool of applicant from which new employees are selected.

- K. ASWATHAPPA.

Significance:

The general purpose of recruitment is to provide a pool of potentially qualified job candidates. Specifically, the purpose is to:

1. Determine the present and future requirements of the organization in conjunction with its personal planning and job-analysis activities.
2. Increase the pool of job candidates at minimum cost.
3. Help to increase the success rate of the selection process by reducing the number of visibly under qualified or over qualified job applicants.
4. Help to reduce the probability that job applicants, once recruited and selected, will leave the organization only after a short period of time.
5. Meet the organization's legal and social obligations regarding the composition of its workforce.
6. Begin identifying and preparing potential job applicants who will be appropriate candidates.
7. Increase organizational and individual effectiveness in the short term and long term.
8. Evaluate the effectiveness of various recruiting techniques and sources for all types of job applicants.

Objectives of recruitment:

1. To attract people with multi dimensional skills and experiences that suits the present and future organizational strategies.
2. To induct the outsiders with a new perspective to lead the company
3. To infuse fresh blood at all levels of the organization.
4. To develop an organizational culture that attracts competent people to the company.
5. To devise methodologies for assessing psychological traits.
6. To seek out non-conventional grounds of talent.
7. To design entry pay that competes on quality but not on quantum.
8. To anticipate and find people for positions that does not exist.

Recruitment policy:

The recruitment policy of any organization is derived from the personnel policy of the same organization. It includes:

- Government policies
- Personnel policies of other competing organizations
- Organization's personnel policies
- Recruitment sources
- Recruitment needs
- Recruitment cost
- Selection criteria and preference etc

Sources of recruitment:

The sources of recruitment are broadly divided into internal and external sources.

Sources of Recruitment

Internal
(i) Transfers
(ii) Promotions
(iii) Present employees

External
(i) Advertisement
(ii) Employment Exchanges
(iii) Educational Institutions
(iv) Recommendation of Existing Employees
(v) Factory Gates
(vi) Casual Callers
(vii) Central Application File (Data Banks)
(viii) Labour Unions
(ix) Labour Contractors
(x) Former Employees

Internal Sources:

- Present permanent employees
- Present temporary or casual employees
- Retrenched or retired employees
- Dependents of deceased, disabled, present and retired employees.

Why do organizations prefer internal sources?

- It can be used as a technique for motivation.
- Morale of the employees can be improved.
- Suitability of the internal candidates can be judged better than the external candidates as "known devils are better than unknown angels".
- Cost of selection can be minimized.
- Trade unions can be satisfied.
- Stability of the employees can be ensured.

External Sources:

a) **Campus recruitment**:
Different types of organizations like industries, business firms, service organizations ,social organizations can get inexperienced candidates of different types from various educational institutions like colleges and universities. Many companies realize that campus recruitment is one of the best techniques for recruiting new blood. These include

- Short listing the institutes based on the quality of the students intake, faculty facilities and past track record.
- Offering the smart pay rather than high pay package.
- Presenting a clear image of the company and the corporate culture.
- Getting in early. Make an early bird offer.
- Include young line managers and business school and engineering school alumni in the recruiting team.

b) **Private employee agencies**:
Consultants in India perform the recruitment functions on behalf of a client company by charging fee. Line managers are relieved from recruitment functions so that they can concentrate on operational activities. Hence these agencies work effectively in the recruitment of executives.

c) **Public employee exchanges**:
The government set up public employment exchanges in the country to provide information about vacancies to the candidates and to help the organization in finding out suitable candidates.

d) **Professional Organizations:**
These organizations maintain complete bio-data of their members and provide the same to various organizations on requisition. They also act as an exchange between their members and recruiting firms in exchanging information, clarifying doubts etc.

e) **Data banks**:
The management can collect the bio-data of the candidates from different sources like employee exchange, educational training institutes, candidates etc and feed them in the computer. it will become another source and the company can get the particulars as and when it needs to recruit.

f) **Casual applicants**:
Depending upon the image of the organization, its prompt response, participation of the organization in the local activities, level of unemployment. Candidates apply casually for jobs through mail or handover the applications in the personnel department.

g) **Similar organizations**:
Generally experienced candidates are available in organizations producing similar products or are engaged in similar business. The management can get most suitable candidates from this source.

h) **Trade unions**:
Generally unemployed or underemployed persons or employees seeking change in employment put a word to the trade union leaders with a view to getting suitable employment due to latter's intimacy with management. In view of this fact and in order to satisfy the trade union leaders, management enquires trade unions for suitable candidates.

Reasons for external sources:
- Candidates can be selected without any pre-conceived notion or reservations.
- HR mix can be balanced with different background, experience and skill etc.
- Latest knowledge skill, innovative or creative talent can also be flowed in to the organization.
- Long run benefit to the organization in the sense that qualitative human resources can be brought.

Recruitment Techniques:
These are the techniques by which the management contracts prospective employees or provides necessary information or exchanges ideas or stimulates them to apply for jobs. Management uses different types of techniques to stimulate internal and external candidates. Techniques useful to stimulate internal candidates are promotion and transfer.

Modern sources and techniques of recruitment:

A number of modern recruitment sources and techniques are being used by the corporate sector in addition to traditional sources and techniques. These techniques include.
a) Walk-in:
The busy organizations and the rapid changing companies do not find time to perform various functions of recruitment. Therefore, they advise the potential candidates to attend for an interview directly and without a prior application on a specified date, time and at a specified place.
b) Consult-in:
The busy and dynamic companies encourage the potential job seekers to approach them personally and consult them regarding the jobs; the companies select the suitable candidates from among such candidates through the selection process.
c) Head Hunting (search consultants):

In this the professional organizations search for the most suitable candidates and advise the company regarding the filling up of the positions.

d) Body Shopping:

The prospective employees contact these organizations to recruit the candidates. These professional and training institutions are called body shoppers and these activities are known as body shopping.

e) Business Alliances:

Business alliances like acquisition, mergers and takeovers help in getting human resources. In addition, the companies do also have alliances in sharing their human resources on ad-hoc basis.

f) Tele-recruitment:

Organizations advertise the job vacancies through the World Wide Web (internet). The job seekers send their applications through e-mail or internet.

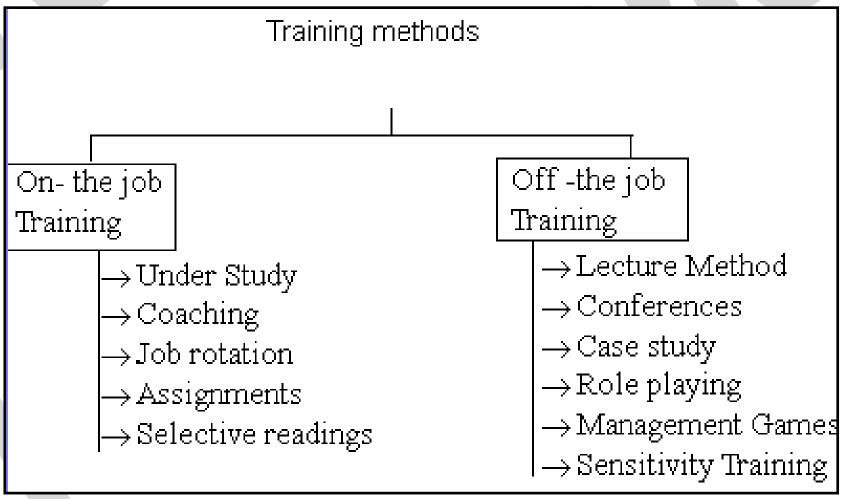
TRAINING:

Training is the acquisition of knowledge, skills, and competencies as a result of the teaching of vocational or practical skills and knowledge that relate to specific useful competencies. Training has specific goals of improving one's capability, capacity, productivity and performance.

Importance of Training:

1. Increased executive management skills.
2. Development in each executive of a broad background and appreciation of the company's overall operations and objectives.
3. Greater delegation of authority because executives down the like are better qualified and better able to assure increased responsibilities.
4. Creation of a reserve of qualified personnel to replace present incumanets and staff new positions.
5. Improved selection for promotion. .
6. Minimum delay in staffing new positions and minimum a distribution of operations during replacement in incumbents.
7. Provision for the best combination of youth, vigour and experience in top management and increased span of productive life in high level position.
8. Improved executive morale.
9. Attractive t6 the company of ambitious men who wish to move ahead as rapidly as their abilities permit.
10. Increased effectiveness and reduced costs, resulting in greater assurance of continued profitability.

Methods of Training:



A. On- the job training Methods: This type of training is also known as job instruction training. Under on - the job training method, the individual is placed on a regular job and taught the skills necessary to perform that job. The trainee learns under the supervision and guidance of a qualified worker or instructor.

On-the - job training methods include the following:
(i) Under Study :This method makes the trainee an assistant to the current job holder. The trainee learns by experience, observation and imitation. It is a kind of mentoring that to help the employee to learn the skills of superior position.

(ii) Coaching : This method involves training by a superior about the knowledge and skills of a job to the junior or subordinate. The superior points out the mistakes committed by the trainee and make suggestions to improve upon.

(iii) Job rotation : This method involves movement of employees to different types of jobs to gain knowledge and functioning of various jobs within the organisation. Banks and insurance companies follow this approach. This method is also known as position rotation or cross training

(iv) Committee Assignment : In this method a committee consisting of a group of emplyees are given a problem and invited solutions. The employees solve the problem and submit the solution. The object of this method is to develop a team work among the employees.

(v) Selective readings: Selective reading may include professional journals and books. Some business organisations maintain libraries for their executives. This is a good method for assimilating knowledge.

B) Of -the job training Method: In off- the -job training, a trainee has to leave his place of working and devote his entire time for training purpose. During this period, the trainee does not contribute anything to the organization. These methods can be followed either in the organization itself or the trainee may be sent away for training courses organized by specialized institutions.

In our country, there are many organizations which have their own training institutes.
Prominent among them in the private sector are TISCO, Larsen & Tubro, ITC, Hindustan Unilever Ltd etc. And Steel Authority of India Ltd (SAIL), State Trading Corporation (STC), Life Insurance corporation, Coal India etc. in the public sector. Besides, there are special training institutes like Administrative Staff College of India, National Productivity Council, All India Management Association, India Institute of Management etc.

Various methods of off-the job training are as follows:
(i) Lecture Method : Special courses and lectures are knowledge based training methods. These courses are organised for a short period. Lectures are supplemented by demonstrations. It also known as class room training.

(ii) Conferences: In order to overcome the limitations of lecture method many organisations have adopted guided-discussion type of conferences in their training programmes. In this method, the participants pool their ideas and experiences and draw conclusions.

(iii) Case Study: Case Study method of training has been developed by Harvard Business School of USA. Cases are widely used in a variety of programmes. This method increases the trainees power of observation. Case studies are generally used for teaching law, marketing, personnel management etc.

(iv) Role Playing: This method of training is used for improving human relations and development of leadership qualities. Role playing technique is used in group where various individuals are given roles of different managers. Dialogue spontaneously grows out of the situation. This method helps the trainee to develop insight into his behaviour and deal with others accordingly.

(v) Management Games: Management games are used to stimulate the thinking of people to run an organisation or its department. A game involves the participation of two or more teams depending on the situation. All the teams have to make decisions regarding the operation of their companies in the given situation. Strength and weakness of decisions are analysed in the light of the results.

(vi) Sensitivity Training: Sensitivity training was first used by National Training Laboratories at Bethel, USA. The training group called itself as T- group. Therefore, it is also called as T-Group training. It is a laboratory training method. The trainees can develop tolerance for others views, become less prejudiced, develop understanding for group process and listening skills.

After imparting training to the employees it becomes necessary to evaluate the training programme because organizations spend a sizeable amount on it. It is, therefore, necessary to examine what value is added to the performance by the training so that in future such training programmes may be arranged or abandoned if they fail to pay some benefit.

The effectiveness of the training Programme can by judged on the basis of the following criteria:
(a) Need: After training, the performance is evaluated .If there is positive demonstration from the workers the need is fulfilled. It is to ascertain whether the training has helped in achieving the results
(b) Change in behavior: The training should bring about change in the behavior of the employee as regards his performance of job. He should use the knowledge acquired by him during training for job performance.
(c) Value addition: Value addition is another criterion for assessment of training. It can be visualized through overall performance, change in trainees' personality, socialization, development etc.

PROMOTION:
A **promotion** is the advancement of an employee's rank or position in an organizational hierarchy system. Promotion may be an employee's reward for good performance, i.e., positive appraisal. Before a company promotes an employee to a particular position it ensures that the person is able to handle the added responsibilities by screening the employee with interviews and tests and giving them training or on-the-job experience. A promotion can involve advancement in terms of designation, salary and benefits, and in some organizations the type of job activities may change a great deal. The opposite of a promotion is a demotion.

Advantages of Promotion:

i. It is an important source of internal recruitment.
ii. It motivates employees.
iii. It increases job satisfaction.
iv. It increases morale.
v. It increases loyalty.
vi. It promotes self development of employees.

vii. Reduced training cost.
viii. Better industrial relations.
ix. No induction delay.

Disadvantages of Promotion:

i. Lack of new blood.
ii. Breeds Corruption
iii. Lack of capable or suitable employees.
iv. Not suitable for posts requiring innovative thinking.

Bases of Promotion:

Promotion is given on the basis of seniority or merit or a combination of both. Let us discuss each one as a basis of promotion.

Seniority as a basis: It implies relative length of service in the same organization. The advantages of this are: relatively easy to measure, simple to understand and operate, reduces labour turnover and provides sense of satisfaction to senior employees. It has also certain disadvantages: beyond a certain age a person may not learn, performance and potential of an employee is not recognized, it kills ambition and zeal to improve performance.

Merit as a basis: Merit implies the knowledge, skills and performance record of an employee. The advantages are: motivates competent employees to work hard, helps to maintain efficiency by recognizing talent and performance. It also suffers from certain disadvantages like: difficulty in judging merit, merit indicates past achievement, may not denote future potential and old employees feel insecure.

Seniority-cum-Merit as basis: As both seniority and merit as basis suffer from certain limitations, therefore, a sound promotion policy should be based on a combination of both seniority and merit. A proper balance between the two can be maintained by different ways: minimum length of service may be prescribed, relative weightage may be assigned to seniority and merit and employees with a minimum performance record and qualifications are treated eligible for promotion, seniority is used to choose from the eligible candidates.

Merit Vs Seniority

MERIT	**SENIORITY**
Advantages:	
Motivates Employees	It is objective
Adds to job satisfaction.	Simple
Increases loyalty	Favoured by Union
	Increases Loyalty
	Reduces Turnover
Disadvantages	
It is subjective	Promotes Inefficiency
Complicated	Reduces motivation
Scope for Favoritism	Kills initiative and Innovative Thinking
Opposition by Union	Lowers morale of employees
Promotes Industrial Unrest	

CONTROL OF STAFF:

The setting up of a good control system should be guided by certain important principles.

1. Principle of Reflection of Plans:
The more clear and complete the plans of the organisation and the more controls are designed to reflect these plans, the more effectively will controls serve its needs.

2. Principle of Prevention:
The truth of the saying 'Prevention is better than cure' is well-established. In control more attention should be directed to prevention of shortfalls than, remedying them after they occur. Peed forward control is very helpful in this respect.

3. Principle of Responsibility:
Responsibility for control particular measurement of deviations taking corrective action should be given to specific individuals at each stage of the operation.

4. Exception Principle:
The managers should concern themselves with exceptional cases i.e., those where the deviations from standards are very significant. Deviations of a minor mature may be left to subordinates for necessary action.

5. Principle of Critical Points:
All operations have got' certain vulnerable or critical points. It is these which cause most of the troubles - give rise to major deviations. The managers should pay more attention to the guarding of these points.

6. Principle of Pyramid:
Feedback data should first be communicated to the bottom of the pyramid i.e., those supervisors and even operating staff who is at the lowest levels. This will give the employees opportunity to control their own situations, apart from quickening remedial action.

The important provisions:
i. Punctuality
ii. Leave Rules
iii. Trade Union Activities

SALIENT FEATURES OF INDIAN BANKING SYSTEM

1. Establishment **:** Most of the commercial banks in India have been registered as joint stock companies under the Companies Act, 1956. Reserve Bank was established under the Reserve Bank of India Act, 1934. The State Bank of India and its subsidiaries were established under their respective statutes. Cooperative banks were established under the Central or State Co-operative Acts. Nationalised banks have been re-established under the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970 Foreign banks operating in India have been established under the respective laws of the country of their origin.
2. Ownership : Ownership of these banks differ depending upon how these have been established. Commercial banks are owned by the public. State Banks and its subsidiaries as well as the major commercial banks are owned by the Government. Co-operative banks are owned by respective co-operative societies.
3. Capital Rquirements : Minimum paid up capital of each schedule bank shall not be less than 5 lacs. A nationalised bank must have authorised capital of 1,500 crore which can be increased upto 3,000 crore. A new private sector bank must have a minimum paid up capital of crore.
4. Capital Adequacy Norms : An Indian bank having foreign branches and a foreign bank operating in India must have capital adequacy norms of 8% (the proportion of its capital and reserve in relation to risk weight: asset).
Other banks have capital adequacy norms of 4%.

5. Mixed Banking : Commercial banks in India are practising mixed banking. Originally these banks were lending for short-term requirements. Recently, the banks have also started term lending.
6. Increased Credit to Private Sector : In accordance with the recommendations of the Narsimham Committee Report banks have increased credit to the priority sector viz., agriculture, small scale industry and export etc.
7. Control over the banks : Reserve Bank of India is empowered to regulate and control the banking sector. Banks have to comply with the provisions of the Reserve Bank of India Act, 1934 and the Banking Regulation Act, 1949 and the rules made thereunder.
8. Maintenance of Cash Reserve Ratio (CRR) : Every bank is under an obligation to maintain a cash reserve ratio of 5% of its demand and time Liabilities. It can be raised upto 20%.
9. Maintenance of Statutory Liquidity Ratio (SLR) : Likewise every bank -Las to maintain SLR equal to 25% of its demand and time liabilities. It can raised upto 40%.
10. Reserve Bank's Monopoly of Note Issue : Reserve Bank of India has been given the monopoly of issuing currency notes of Rs. 2 denomination and above. The Central Government has the monopoly of issuing notes of Rs. 1.
11. Uniform Accounting Policy : Banks are under an obligation to follow uniform accounting policy. It relates to income recognition, provisioning for k an losses and classification and valuation of assets.
12. Technology Changes : Technology changes are taking place very rapidly. Banks have fully computerised their branches. Most of the major public sector banks and new private sector banks have introduced Core Banking Service (CBS). This has enabled a bank's customer to avail banking -ices 'any time anywhere'. A customer in Delhi can operate his account any other CBS branch anywhere in India. Shift to payment system from o cashless (Debit Cards) and mobile banking.
13. Internet Banking : It is a corollary of the above feature. Internet king means transacting Banking business on-line with the help of internet. This helps in facilitating banking transactions on-line, banking and Automatic Teller Machine (A.T.M.) operations throughout country 24 x 7.
14. Branch Banking : Indian banking system is dominated by branch banking system due to the huge size, topography and economic system of country.
15. Diversification of Banking Operations : Gone are the days when were doing business of deposit acceptance and money lending. Now are embarking upon number of new businesses. However, banks can diversify their business only with the prior approval of the Reserve Bank h is subject to certain conditions being fulfilled.

Different types of bank categorized by functions, ownership and domicile:
Banks can be classified into various types on the basis of their functions, ownership, domicile, etc. The following are the various types of banks:

1. Commercial Banks:

The banks, which perform all kinds of banking business and generally finance trade and commerce, are called commercial banks. Since their deposits are for a short period, these banks normally advance short-term loans to the businessmen and traders and avoid medium-term and long-term lending.

However, recently, the commercial banks have also extended their areas of operation to medium-term and long-term finance. Majority of the commercial banks are in the public sector. However, there are certain private sector banks operating as joint stock companies. Hence, the commercial banks are also called joint stock banks.

2. Industrial Banks:

Industrial banks, also known as investment banks, mainly meet the medium-term and long-term financial needs of the industries. Such long-term needs cannot be met by the commercial banks, which generally deal with short-term lending.

The main functions of the industrial banks are:
(a) They accept long-term deposits.
(b) They grant long-term loans to the industrialists to enable them to purchase land, construct factory building, purchase heavy machinery, etc.
(c) They help selling or even underwrite the debentures and shares of industrial firms,
(d) They can also provide information regarding the general economic position of the economy. In India, industrial hanks, like Industrial Development Bank of India, Industrial Finance Corporation of India, Slate Finance Corporations, are playing significant role in the industrial development of the country.

3. Agricultural Banks:

Agricultural credit needs are different from those of industry and trade. Industrial and commercial banks normally do not deal with agricultural finance. The agriculturists require:

(a) short-term credit to buy seeds, fertilizers and other inputs, and
(b) long-term credit to purchase land, to make permanent improvements on land, to purchase agricultural machinery and equipment, etc. In India, agricultural finance is generally provided by co-operative institutions. Agricultural co-operatives provide short-term loans and Land Development Banks provide the long-term credit to the agriculturists.

4. Exchange Banks:

Exchange banks deal in foreign exchange and specialise in financing foreign trade. They facilitate international payments through the sale, purchase of bills of exchange, and thus play an important role in promoting foreign trade.

5. Saving Banks:

The main purpose of saving banks is to promote saving habits among the general public and mobilise their small savings. In India, postal saving banks do this job. They open accounts and issue postal cash certificates.

6. Central Bank:

Central bank is the apex institution, which controls, regulates and supervises the monetary and credit system of the country. Important functions of the central bank are:
(a) It has the monopoly of note issue;
(b) It acts as the banker, agent and financial adviser to the state;
(c) It is the custodian of member banks reserves;
(d) It is the custodian of nation's reserves of international currency;
(e) It serves as the lender of the last resort;
(f) It functions as the bank of central clearance, settlement and transfer; and
(g) It acts as the controller of credit. Besides these functions, India's central bank, i.e., the Reserve Bank of India, also performs many developmental functions to promote economic development in the country.

7. Classification on the Basis of Ownership:

On the basis of ownership, banks can be classified into three categories:
(a) Public Sector Banks:

These arc owned and controlled by the government. In India, the nationalized banks and the regional rural banks come under these categories,

(b) Private Sector Banks:

These banks are owned by the private individuals or corporations and not by the government or co-operative societies,

(c) Cooperative Banks:

Cooperative banks are operated on the cooperative lines. In India, cooperative credit institutions are organised under the cooperative societies law and play an important role in meeting financial needs in the rural areas.

8. Classification on the Basis of Domicile:

On the basis of domicile, the banks are divided into two categories:

(a) Domestic Banks:

These are registered and incorporated within the country,

(b) Foreign Banks:

These are foreign in origin and have their head offices in the country of origin.

9. Scheduled and Non-Scheduled Banks:

In India, banks have been broadly classified into scheduled and non-scheduled banks. A Scheduled Bank is that which has been included in the Second Schedule of the Reserve Bank of India Act, 1934 and fulfills the three conditions

(a) it has paid-up capital and reserves of at least Rs. 5 lakhs. It ensures the Reserve Bank that its operations are not detrimental to the interest of the depositors;

(b) It is a corporation or a cooperative society and not a partnership or a single owner firm. The banks which are not included in the Second Schedule of the Reserve Bank of India Act are non-scheduled banks.

RESERVE BANK OF INDIA:

The **Reserve Bank of India** (**RBI**) is India's central banking institution, which controls the monetary policy of the Indian rupee. It was established on 1 April 1935 during the British Raj in accordance with the provisions of the Reserve Bank of India Act, 1934. The share capital was divided into shares of 100 each fully paid, which was entirely owned by private shareholders in the beginning. Following India's independence in 1947, the RBI was nationalized in the year 1949.

The RBI plays an important part in the development strategy of the Government of India. It is a member bank of the Asian Clearing Union. The general superintendence and direction of the RBI is entrusted with the 21-member- Central Board of Directors—the Governor, four Deputy Governors, two Finance Ministry representative, ten government-nominated directors to represent important elements from India's economy, and four directors to represent local boards headquartered at Mumbai, Kolkata, Chennai and New Delhi. Each of these local boards consists of five members who represent regional interests, as well as the interests of co-operative and indigenous banks.

The bank is also active in promoting financial inclusion policy and is a leading member of the Alliance for Financial Inclusion (AFI).

Powers/ Functions of RBI:

The Reserve Bank of India performs various traditional central banking functions as well as undertakes different promotional and developmental measures to meet the dynamic requirements of the country. The broad objectives of the Reserve Bank are:

a) Regulating the issue of currency in India;
b) keeping the foreign exchange reserves of the country;
c) establishing the monetary stability in the country; and
d) Developing the financial structure of the country on sound lines consistent with the national socio-economic objectives and policies.

Main functions of the Reserve Bank are described below:

1. Note Issue:

The Reserve Bank has the monopoly of note issue in the country. It has the sole right to issue currency notes of all denominations except one-rupee notes. One-rupee notes are issued by the Ministry of Finance of the Government of India. The Reserve Bank acts as the only source of legal tender because even the one-rupee notes are circulated through it. The Reserve Bank has a separate Issue Department, which is entrusted with the job of issuing currency notes. The Reserve Bank has adopted minimum reserve system of note issue. Since 1957, it maintains gold and foreign exchange reserves of Rs. 200 crore, of which at least Rs. 115 crore should be in gold.

2. Banker to Government:

The Reserve Bank acts as the banker, agent and adviser to Government of India:

i. It maintains and operates government deposits,
ii. It collects and makes payments on behalf of the government,
iii. It helps the government to float new loans and manages the public debt,
iv. It sells for the Central Government treasury bills of 91 days duration,
v. It makes 'Ways and Means' advances to the Central and State Governments for periods not exceeding three months,
vi. It provides development finance to the government for carrying out five year plans,
vii. It undertakes foreign exchange transactions on behalf of the Central Government,
viii. It acts as the agent of the Government of India in the latter's dealings with the International Monetary Fund (IMF), the World Bank, and other international financial institutions, (i) It advises the government on all financial matters such as loan operations, investments, agricultural and industrial finance, banking, planning, economic development, etc.

3. Banker's Bank:

The Reserve Bank acts as the banker's bank in the following respects:

(a) Every Bank is under the statutory obligation to keep a certain minimum of cash reserves with the Reserve Bank. The purpose of these reserves is to enable the Reserve Bank to extend financial assistance to the scheduled banks in times of emergency and thus to act as the lender of the last resort. According to the Banking Regulation Act, 1949, all scheduled banks are required to maintain with the Reserve Bank minimum cash reserves of 5% of their demand liabilities and 2% of their time liabilities. The Reserve Bank (Amendment) Act, 1956 empowered the Reserve Bank to raise the cash reserve ratio to 20% in the case of demand deposits and to 8% in case of time deposits. Due to the difficulty of classifying deposits into demand and time categories, the amendment to the Banking Regulation Act in September 1972 changed the provision of reserves to 3% of aggregate deposit liabilities, which can be raised to 15% if the Reserve Bank considers it necessary,

(b) The Reserve Bank provide financial assistance to the scheduled banks by discounting their eligible bilk and through loans and advances against approved securities,

(c) Under the Banking Regulation Act,1949 and its various amendments, the Reserve Bank has been given extensive powers of supervision and control over the banking system. These regulatory powers relate to the licensing of banks and their branch expansion; liquidity of assets of the banks; management and methods of working of the banks; amalgamation, reconstruction and liquidation of banks; inspection of banks; etc.

4. Custodian of Exchange Reserves:

The Reserve Bank is the custodian of India's foreign exchange reserves. It maintains and stabilises the external value of the rupee, administers exchange controls and other restrictions imposed by the government, and manages the foreign exchange reserves. Initially, the stability of exchange rate was maintained through selling and purchasing sterling at fixed rates. But after India became a member of the international Monetary Fund (IMF) in 1947, the rupee was delinked with sterling and became a multilaterally convertible currency. Therefore the Reserve Bank now sells and buys foreign currencies, and not sterling alone, in order to achieve the objective of exchange stability. The Reserve Bank fixes the selling and buying rates of foreign currencies. All Indian remittances to foreign countries and foreign remittances to India are made through the Reserve Bank.

5. Controller of Credit:

As the central bank of the country, the Reserve Bank undertakes the responsibility of controlling credit in order to ensure internal price stability and promote economic growth. Through this function, the Reserve Bank attempts to achieve price stability in the country and avoids inflationary and deflationary tendencies in the country. Price stability is essential for economic development. The Reserve Bank regulates the money supply in accordance with the changing requirements of the economy. The Reserve Bank makes extensive use of various quantitative and qualitative techniques to effectively control and regulate credit in the country.

6. Ordinary Banking Functions:

The Reserve Bank also performs various ordinary banking functions:

a) It accepts deposits from the central government, state governments and even private individuals without interest,
b) It buys, sells and rediscounts the bills of exchange and promissory notes of the scheduled banks without restrictions,
c) It grants loans and advances to the central government, state governments, local authorities, scheduled banks and state cooperative banks, repayable within 90 days,

d) It buys and sells securities of the Government of India and foreign securities,
e) It buys from and sells to the scheduled banks foreign exchange for a minimum amount of Rs. 1 lakh,
f) It can borrow from any scheduled bank in India or from any foreign bank,
g) It can open an account in the World Bank or in some foreign central bank.
i. It accepts valuables, securities, etc., for keeping them in safe custody.
ii. It buys and sells gold and silver.

7. Miscellaneous Functions:

In addition to central banking and ordinary banking functions, the Reserve Bank performs the following miscellaneous functions:

(a) Banker's Training College has been set up to extend training facilities to supervisory staff of commercial banks. Arrangements have been made to impart training lo the cooperative personnel,
(b) The Reserve Bank collects and publishes statistical information relating to banking, finance, credit, currency, agricultural and industrial production, etc. It also publishes the results of various studies and review of economic situation of the country in its monthly bulletins and periodicals.

8. Forbidden Business:

Being the central bank of the country, the Reserve Bank:

(a) Should not compete with member banks and
(b) should keep its assets in liquid form to meet any situation of economic crisis.

Therefore, the Reserve Bank has been forbidden to do certain types of business:

(a) It can neither participate in, nor directly provide financial assistance to any business, trade or industry,
(b) It can neither buy its own shares not those of other banks or commercial and industrial undertakings,
(c) It cannot grant unsecured loans and advances,
(d) It cannot give loans against mortgage security,
(e) It cannot give interest on deposits.
(f) It cannot draw or accept bills not payable on demand,
(g) It cannot purchase immovable property except for its own offices.

9. Promotional and Developmental Functions:

Besides the traditional central banking functions, the Reserve Bank also performs a variety of promotional and developmental functions:

(a) By encouraging the commercial banks to expand their branches in the semi-urban and rural areas, the Reserve Bank helps (i) to reduce the dependence of the people in these areas on the defective unorganised sector of indigenous bankers and money lenders, and (ii) to develop the banking habits of the people
(b) By establishing the Deposit Insurance Corporation, the Reserve Bank helps to develop the banking system of the country, instills confidence of the depositors and avoids bank failures,
(c) Through the institutions like Unit Trust of India, the (Reserve Bank helps to mobilise savings in the country,
(d) Since its inception, the Reserve Bank has been mating efforts to promote institutional agricultural credit by developing cooperative credit institutions.
(e) The Reserve Bank also helps to promote the process of industrialisation in the country by setting up specialised institutions for industrial finance,
(f) it also undertakes measures for developing bill market in the country.

CONTROL OF CREDIT BY RBI:

What is Credit Control: Credit Control is an important tool used by the Reserve Bank of India, a major weapon of the monetary policy used to control the demand and supply of money (liquidity) in the economy.

Why Credit Control is required: The basic and important needs of Credit Control in the economy are:

- To encourage the overall growth of the "priority sector" i.e. those sectors of the economy which is recognized by the government as "prioritized
- To keep a check over the channelization of credit so that credit is not delivered for undesirable purposes.
- To achieve the objective of controlling "Inflation" as well as "Deflation".
- To boost the economy by facilitating the flow of adequate volume of bank credit to different sectors.

What are the methods of Credit Control?

There are two methods that the RBI uses to control the money supply in the economy-

(1) Qualitative Method: By qualitative methods means the control or management of the uses of bank credit or manner of channelizing of cash and credit in the economy. Tools used under this method are:

(a) **Marginal Requirement:** Marginal Requirement of loan can be increased or decreased to control the flow of credit for e.g. – a person mortgages his property worth Rs. 1,00,000 against loan. The bank will give loan of Rs. 80,000 only. The marginal requirement here is 20%. In case the flow of credit has to be increased, the marginal requirement will be lowered.

(b) **Rationing of credit:** Under this method there is a maximum limit to loans and advances that can be made, which the commercial banks cannot exceed.

(c) **Publicity:** RBI uses media for the publicity of its views on the current market condition and its directions that will be required to be implemented by the commercial banks to control the unrest.

(d) **Direct Action:** Under the banking regulation Act, the central bank has the authority to take strict action against any of the commercial banks that refuses to obey the directions given by Reserve Bank of India.

(e) **Moral Suasion:** This method is also known as "Moral Persuasion" as the method that the Reserve Bank of India, being the apex bank uses here, is that of persuading the commercial banks to follow its directions/orders on the flow of credit.

(2) Quantitative Method: By Quantitative Credit Control we mean the control of the total quantity of credit. Different tools used under this method are:

(a) **Bank Rate:** Bank Rate also known as the Discount Rate is the official minimum rate at which the Central Bank of the country is ready to rediscount approved bills of exchange or lend on approved securities. When the commercial bank for instance, has lent or invested all its available funds and has little or no cash over and above the prescribed minimum, it may ask the central bank for funds. It may either re-discount some of its bills with the central bank or it may borrow from the central bank against the collateral of its own promissory notes. In either case, the central bank accommodates the commercial bank and increases the latter's cash reserves. This Rate is increased during the times of inflation when the money supply in the economy has to be controlled.

(b) **Open Market Operations:** Open Market Operations indicate the buying/selling of government securities in the open market to balance the money supply in the economy. During inflation, RBI sells the government securities to the commercial banks and other financial institution. This reduces their cash lending and credit creation capacities. Thus, Inflation can be controlled. During recessions, RBI purchases government securities from commercial banks and other financial institution. This leaves them with more cash balances for lending and increases their credit creation capacities. Thus, recession can be overcome.

(c) **Repo Rates and Reverse Repo Rates:** Repo is a swap deal involving immediate sale of securities and a simultaneous re purchase of those securities at a future date at a predetermined price. Commercial banks and financial institution also park their funds with RBI at a certain rate, this rate is called the Reverse Repo Rate. Repo rates and Reverse repo rate used by RBI to make liquidity adjustments in the market.

(d) **Cash Reserve Ratio:** The money supply in the economy is influenced by the cash reserve ratio. It is the ratio of a bank's time and demand liabilities to be kept in reserve with the RBI. A high CRR reduces the flow of money in the economy and is used to control inflation. A low CRR increases the flow of money and is used to overcome recession.

(e) **Statutory Liquidity Ratio:** Under SLR, banks have to invest a certain percentage of its time and demand liabilities in Government approved securities. The reduction in SLR enhances the liquidity of commercial banks.

(f) **Deployment of Credit:** The RBI has taken various measures to deploy credit in different of the economy. The certain percentage of bank credit has been fixed for various sectors like agriculture, export, etc.