BANKING

The composition of the Indian Banking System:

The organized banking system in India can be broadly divided into three categories viz., the central bank of the country known as the Reserve Bank of India, the commercial banks and the co-operative banks. Another and more common classification of banks in India is between scheduled and non-scheduled banks. The Reserve Bank of India is the supreme monetary and banking authority in the country and has the responsibility to control the banking system in the country. It keeps the cash reserves of all scheduled banks and hence is known as the “Reserve Bank”.

Scheduled and Non-scheduled Bank

Under the reserve Bank of India Act, 1934, banks were classified as scheduled banks and non-scheduled banks.
The scheduled banks are those which are entered in the Seconds Schedule of RBI Act, 1934. Such banks are those which have a paid-up capital and reserves of an aggregate value of not less than Rs. 5 lakhs and which satisfy RBI that their affairs are carried out in the interests of their depositors. All commercial banks- Indian and foreign, regional rural banks and state co-operative banks-are scheduled banks.

Non-scheduled banks are those which have not been included in the second schedule of RBI Act, 1934. At present, there are only three non-scheduled banks in the country.

Scheduled banks are divided into commercial banks and co-operative banks. Commercial banks are based on profit, while co-operative banks are based on co-operative principle.

Commercial banks have been in existence for many decades. They mobilise savings in urban areas and make them available to large and small industrial and trading units mainly for working capital requirements. After 1969 commercial banks are broadly classified into nationalized or public sector banks and private sector banks. The State Bank of India and its associate banks along with another 20 banks are the public sector banks. The private sector banks include a small number of Indian scheduled banks which have not been nationalized and branched of foreign banks operating in India- commonly known as foreign exchange banks.

The Regional Rural Banks (RRBs) came into existence since the middle of 1970s with the specific objective of providing credit and deposit facilities particularly to the small and marginal farmers, agricultural labourers and artisans and small entrepreneurs. The Regional Rural Banks have the responsibility to develop agriculture, trade, commerce and industry in the rural areas. The RRBs are essentially commercial banks but their area of operation is generally limited to a district.

**THE RESERVE BANK OF INDIA AND MONETARY MANAGEMENT:**

The Reserve Bank of India was inaugurated in April 1935 with a share capital of Rs. 5crores, divided into shares of Rs.100 each fully paid up. The entire share capital was in the beginning, owned by private shareholders. But in view of the public nature of the Bank’s functions, the Reserve Bank of India, Act, 1934 provided for the appointment by the Central Government of the Governor and two
Deputy Governor (who were also directors of the central Board). The Reserve Bank was nationalized in 1949. Besides the central Board, there are four local Boards with headquarters at Bombay, Calcutta, Madras and New Delhi.

FUNCTIONS OF THE RESERVE BANK OF INDIA:

By the reserve Bank of India Act of 1934, all the important functions of a central bank have been entrusted to the Reserve Bank of India.

**Bank of Issue:** Under Section 22 of the Reserve Bank of India Act, the Bank has the sole right to issue bank notes of all denominations. The distribution of one rupee notes and coins and small coins all over the country is undertaken by the Reserve Bank as agent of the Government. The Reserve Bank has a separate Issue Department which is entrusted with the issue of currency notes. The assets and liabilities of the Issue Department are kept separate from those of the Banking Department. Since 1957, the Reserve Bank of India is required to maintain gold and foreign exchange reserves of Rs.200 crores, of which at least Rs.115 crores should be in gold. The system as it exists today is known as the minimum reserve system.

**Bankers to Government:** The second important function of the Reserve Bank of India is to act as Government banker, agent and adviser. The Reserve Bank is agent of central Government and of all state Government in India excepting that of Jammu and Kashmir. The Reserve Bank has the obligation to transact Government business, viz., to keep the cash balances as deposits free of interest, to receive and to make payments on behalf of the Government and to carry out their exchange remittances and other banking operations. The Reserve Bank of India helps the Government-both the Union and the States to float new loans and to manage public debt. The Banks makes ways and means advances to the Governments for 90 days. It makes loans and advances to the states and local authorities. It acts as adviser to the Government on all monetary and banking matters.

**Bankers’ Bank and Lender of the last resort:** The Reserve Bank of India acts as the bankers’ bank. According to the provisions of the Banking Companies Act of 1949, every scheduled bank was required to maintain with Reserve Bank a cash balance equivalent to 5 percent of its demand liabilities and 2 per cent of its time liabilities in India. By an amendment of 1962, the distinction between demand
and time liabilities was abolished and banks have been asked to keep cash reserves equal to 3 percent of their aggregate deposit liabilities. The minimum cash requirements can be changed by the Reserve Bank of India.

The scheduled banks can borrow from the Reserve Bank of India on the basis of eligible securities or get financial accommodation in times of need or stringency by re-discounting bills of exchange. Since commercial banks can always expect the Reserve Banks of India to come to their help in times of banking crisis, the Reserve Bank becomes not only the bankers’ bank but also the lender of the last resort.

**Controller of credit:** The Reserve Bank of India is the controller of credit, i.e., it has the power to influence the volume of credit created by banks in India. It can do so through changing the Bank rate or through open market operations. According to the Banking Regulation Act of 1949, the Reserve Bank of India can ask any particular bank or the whole banking system not to lend to particular groups or persons on the basis of certain types of securities. Since 1956, selective controls of credit are increasingly being used by the Reserve Bank.

The Reserve Bank of India is armed with many more powers to control the India money market. Every bank has to get a licence from the Reserve Bank of India to do banking business within India; the licence can be cancelled by the Reserve Bank if certain stipulated conditions are not fulfilled. Every bank will have to get the permission of the Reserve Bank it can open a new branch. Each scheduled bank must send a weekly return to the Reserve Bank showing, in detail, its assets and liabilities. This power of the Bank to call for information is also intended to give it effective control of the credit system. The Reserve Bank has also the power to inspect the accounts of any commercial bank.

As supreme banking authority in the country, the Reserve Bank of India, therefore, has the following powers:

- It holds the cash reserves of all the scheduled banks.
- It controls the credit operations of banks through quantitative and qualitative controls.
- It controls the banking system through the system of licensing, inspection and calling for information.
- It acts as the lender of the last resort by providing rediscount facilities to scheduled banks.
**Custodian of Foreign Exchange Reserves:** The Reserve Bank of India has the responsibility to maintain the official rate of exchange. According to the Reserve Bank of India Act of 1934, the Bank was required to buy and sell at fixed rates any amount of sterling in lots of not less than Rs. 10,000. The rate of exchange fixed was the exchange rate fixed at 1sh.6d. Though there were periods of extreme pressure in favour of or against the rupee. After India became a member of the International Monetary Fund in 1946, the Reserve Bank has the responsibility of maintaining fixed exchange rates with all other member countries of the I.M.F.

Besides maintaining the rate of exchange of the rupee, the Reserve Bank has to act as the custodian of India’s reserve of international currencies. The vast sterling balances were acquired and managed by the Bank. Further the RBI has the responsibility of administering the exchange controls of the country.

**Supervisory Functions:** In addition to its traditional central banking functions, the Reserve bank has certain non-monetary functions of the nature of supervision of banks and promotion of sound banking in India. The Reserve Banks Act, 1934, and the Banking Regulation Act, 1949 have given the RBI wide powers of supervision and control over commercial and co-operative banks, relating to licensing and establishments, branch expansion, liquidity of their assets, management and methods of working, amalgamation, reconstruction, and liquidation. The RBI is authorized to carryout periodical inspections of the banks and to call for return and necessary information from them. The nationalization of 14 major India scheduled banks in July 1969 has imposed new responsibilities on the RBI for directing the growth of banking and credit policies towards more rapid development of the economy and realization of certain desired objectives. The supervisory functions of the RBI have helped a great deal in improving the standard of banking in India to develop on sound lines and to improve the methods of their operation.

**Promotional Functions:** With economic growth assuming a new urgency since Independence, the range of the Reserve Bank’s functions has steadily widened. The Bank now performs a variety of developmental and promotional functions, which, at one time, were regarded as outside the normal scope of central banking. The Reserve Bank was asked to promote banking habit, extend banking facilities to rural and semi-urban areas, and establish and promote new specialized financing agencies. According, the Reserve bank has helped in the setting up of the IFCI and the SFC; it set up the Deposit Insurance Corporation in 1962, the Unit
Trust of India in 1964, the Industrial Development Bank of India in 1964, the Agricultural Refinance Corporation of India in 1963 and the Industrial Reconstruction Corporation of India in 1972. These institutions were set up directly or indirectly by the Reserve Bank to promote saving habit and to mobilise saving, and to provide industrial finance as well as agricultural finance. As far back as 1935, the Reserve Bank of India set up the Agricultural Credit Department to provide agricultural credit. But only since 1951 the Bank’s role in this field has become extremely important. The Bank has developed the co-operative credit movement to encourage saving, to eliminate money-lenders from the villages and to route its short term credit to agriculture. The RBI has set up the Agricultural Refinance and Development Corporation to provide long-term finance to farmers.

**CREDIT CONTROL:**

*General Credit Controls:* Since 1955-56 and particularly after 1973-74 the inflationary rise in price has been steadily mounting. Increased Government expenditure financed through deficit spending has the direct effect of pushing up the prices, wages and incomes. Shortfalls in production, and hoarding and speculation in essential commodities have contributed to this inflationary pressure. RBI has various weapons of control and, through using them; it hopes to achieve its monetary policy. These weapons of control are broadly two: Quantitative and qualitative controls. Quantitative controls are used to control the volume of credit and indirectly, to control the inflationary and deflationary pressures caused by expansion and contraction of credit. Quantitative controls are also known as generating credit controls and consist of bank rate policy, open market operations and cash reserve ratio.

*Bank Rate:* The bank rate or the central banks’ rediscount rate is an important monetary instrument in modern economies. Its most useful role is to signal and/or clarify the central banks’ monetary and interest rate stance to all participants in the financial sector and particularly to banks. If monetary policy is effective and credible, a change in the bank rate will result in a change in prime lending rate of banks and thus act as an independent instrument of monetary control. However, the role of the bank rate as an instrument of monetary policy has been very limited in India because of these basic factors:

- The structure of interest rates is administered by RBI- they are not automatically linked to the bank rate;
Commercial banks enjoy specific refinance facilities, and not necessarily rediscount their eligible securities with RBI at bank rate; and
The bill marked is under-developed and the different sub-markets of the money market are not influenced by the bank rate.

In other words, the bank rate in India is not the “pace setter” to the other market rates of interest and the money market rates do not automatically adjust themselves to changes in the bank rate. At the sometime, the deposit rates and lending rates of banks (and of development finance instaurations) are not related to the bank rate. The Government of India and RBI are reviewing the rules and procedures for general access to RBI rediscount facilities so as to make bank rate an active instrument of monetary policy as in other modern economies.

Since the later part of 1995, India passed through a severe liquidity crunch and as a result the prime lending rates were ruling high. Industrial production was affected adversely. One step which RBI took was to reduce the bank rate from 12 to 11 percent in April 1997, and gradually to 6.5 percent. The reduction of the bank rate was to help in the reduction of other interest rates and thus stimulate borrowing from banks.

**Cash Reserve Requirements (CRR):** Another weapon available to RBI for credit control is the use of variable cash reserve requirements. Under the RBI Act, 1934, very commercial bank has to keep certain minimum cash reserve with RBI initially; it was 5 percent against demand deposits and 2 per cent against time deposits - these are known as the statutory cash reserve requirement between 3 per cent and 15 percent of the total demand and time deposits.

The purpose of reducing CRR is to leave large cash reserves with banks so as to enable them to expand bank credit. It may be mentioned that the Indian economy has been reeling under serious economic recession for many years and reduction of CRR and expansion of bank credit to industry and trade is one method to stimulate the Indian economy. RBI has been pursuing its medium term objective of reducing CRR to the statutory minimum of 3 percent.

**Statutory Liquidity Requirements (SLR):** Apart from cash reserve requirement which commercial banks have to keep with RBI (under RBI Act, 1934), all commercial banks have to maintain liquid assets in the form of cash, gold
and unencumbered approved securities equal to not less than 25 percent of their total demand and time deposit liabilities. This is known as the statutory liquidity requirement; this is in addition to statutory cash reserve requirements.

Maintenance of adequate liquid assets is a basic principle of sound banking. Hence commercial banks in India have been required by the Banking Regulation Act, 1949, to maintain minimum ratio of liquidity ratio. Accordingly, it raised the liquidity ratio from 25 percent gradually and finally to 38.5 percent. RBI has stepped up the liquidity ratio for two reasons:

- Higher liquidity ratio forces commercial banks to maintain a larger proportion of their resources in liquid form and thus reduces their capacity to grant loans and advances to business and industry - thus it is anti-inflationary in impact, and

- A higher liquidity ratio diverts banks from loans and advances to investment in government and other approved securities. In other words, a higher SLR was used to divert bank funds to finance Government expenditure.

It may be mentioned here that stepping up statutory liquidity requirements (SLR) and the cash reserve ratio (CRR) have the same effects, viz., they reduce the capacity of commercial banks to expand credit to business and industry and thus are anti-inflationary.

After accepting Narasimham Committee (1991) recommendation, RBI reduced the SLR by successive steps to 25 per cent in October 1997. There is now a demand to abolish SLR altogether.

**Open Market Operations of RBI:**

In economies with well-developed money markets, central banks use open market operation - i.e. buying and selling eligible securities by the central bank in the money market - to influence the volume of cash reserves with commercial banks and thus influence the volume of loans and advances they can make to the industrial and loans and advances they can make to the industrial and commercial sectors. RBI had not used this weapon for many years.

Since 1991, the enormous inflow of foreign funds into India created the problem of excess liquidity with the banking Sector and RBI undertook large
scale open market operations. When RBI sells Government securities in the commercial banks and thereby, reduces the ability of banks to lend to the industrial and commercial sectors. At any given time, the banks’ capacity to create credit – i.e., to give fresh loans- depends upon their surplus cash that is the amount of cash reserves in excess of their statutory CRR. Once the surplus cash is eliminated and even part of the statutory CRR is reduced, the banks have to contract their credit supply so as to generate some cash reserves to meet their statutory CRR. As a result, the supply of bank credit which involves the creation of demand deposits, falls and money supply contracts.

**PLR (Prime Lending Rate)** is that rate of interest at which bank gives loans to its prime borrowers or to blue chip, high profile borrowers like corporate. Money are call on short note means inter bank loans on a day to day basis that is loans given by one bank to another on a day to day basis Rate of interest that prevails in market on day to day basis call money rate depends on demands and supply on day to day basis it is nothing to do with RBI.

**Money market** – market for short term funds up to 1 year.

Major players in money markets are banks

RBI contributes credit generation to commercial banks through some measurements. They are of two types:

**RBI credit control measures**

- Quantitative
- Qualitative (Selective measures) qualitative measures popularly called detective measures)

**Quantitative measures**

- Bank rate
- CRR
- Open market operation
- SLR (Statutory Liquidity Rate)

**Qualitative measures**

- Rationing of credit
- Variation of margin requirements
- Regulation of consumer credit
- Priority and moral analysis
- Direct action

**Quantitative Measures:** These methods are called traditional methods because they have been in use for decades. Through these methods, the credit creation is controlled by changing the cash reserves of commercial banks. They are designed to affect the lendable resources of commercial banks either directly affecting their reserve base or by making the cost of funds cheaper or dearer to them. The important methods of this nature are explained herein below:

- **Bank Rate**

  **What is Bank rate?** Bank Rate is the rate at which central bank of the country (in India it is RBI) allows finance to commercial banks. Bank Rate is a tool, which central bank uses for short-term purposes. Any upward revision in Bank Rate by central bank is an indication that banks should also increase deposit rates as well as Prime Lending Rate. This any revision in the Bank rate indicates could mean more or less interest on your deposits and also an increase or decrease in your EMI.

  **What is Bank Rate? (For Non Bankers):** This is the rate at which central bank (RBI) lends money to other banks or financial institutions. If the bank rate goes up, long-term interest rates also tend to move up, and vice-versa. Thus, it can said that in case bank rate is hiked, in all likelihood banks will hikes their own lending rates to ensure and they continue to make a profit.

  Monetary policy or credit policy in announced by RBI twice in a year. These periods are called

  - Lean season. Sowing (May to September)
  - Busy season (October to April Harvesting)

- **CRR (Cash Reserve Ratio)**

  CRR is also known as Variable Reserve Ratio. CRR is that ratio of the total deposits of bank which it has to keep with the central bank of country (or RBI).

  - It may be lowered when recession
  - It may be raised when inflation
What is CRR? RBI uses CRR either to drain excess liquidity or to release funds needed for the economy from time to time. Increase in CRR means that banks have less funds available and money is sucked out of circulation. Thus we can say that this serves dual purposes i.e. it not only ensures that a portion of bank deposits is totally risk-free, but also enables RBI to control liquidity in the system, and thereby, inflation by tying the hands of the banks in lending money.

What is CRR (For Non Bankers): CRR means Cash Reserve Ratio. Banks in India are required to hold a certain proportion of their deposits in the form of cash. However, actually Banks don’t hold these as cash with themselves, but deposit such case with Reserve Bank of India (RBI) / currency chests, which is considered as equivalent to holding cash with themselves. This minimum ratio (that is the part of the total deposits to be held as cash) is stipulated by the RBI and is known as the CRR or Cash Reserve Ratio. Thus, When a bank’s deposits increase by Rs100, and if the cash reserve ratio is 9%, the banks will have to hold additional Rs 9 with RBI and Bank will be able to use only Rs 91 for investments and lending / credit purpose. Therefore, higher the ratio (i.e. CRR), the lower is the amount that banks will be able to use for lending and investment. This power of RBI to reduce the lendable amount by increasing the CRR, makes it an instrument in the hands of a central bank through which it can control the amount that banks lend. Thus, it is a tool used by RBI to control liquidity in the banking system.

SLR (Statutory Liquidity Ratio): -
It is that ratio of the total deposits of a bank which it has to maintain with itself in the form of liquid funds like government securities and cash in hand at any given conditions and point of time.

SLR is exclusive to India. No other country has SLR. Then why SLR?
- It helps the government to borrow from banking system.
- To stop or reduce union bank.
- Run on the bank- When heavy load

What is SLR? Every bank is required to maintain at the close of business every day, a minimum proportion of their Net Demand and Time Liabilities as liquid assets in the form of cash, gold and un-encumbered approved securities. The
ratio of liquid assets to demand and time liabilities is known as Statutory Liquidity Ratio (SLR). RBI is empowered to increase this ratio up to 40%. An increase in SLR also restrict the bank’s leverage position to pump more money into the economy.

**What is SLR? (For Non Bankers):** SLR stands for Statutory Liquidity Ratio. This term is used by bankers and indicates the minimum percentage of deposits that the bank has to maintain in form of gold, cash or other approved securities. Thus, we can say that it is ratio of cash and some other approved to liabilities (deposits) It regulates the credit growth in India.

- **Open Market Operations:**
  These are the operations carried by the central bank (RBI) who conducts buying & selling operations in terms of first class securities predominately Government securities buying & selling to banks & financial institutions. These are day to day basis Government securities.
  A government piece of paper promising to repay the amount written on it (interest).

- **REPO AND REVERSE REPO:**
  **Repo (Repurchase) rate** is the rate at which the RBI lends short-term money to the banks. When the repo rate increases borrowing from RBI becomes more expensive. Therefore, we can say that in case, RBI wants to make it more expensive for the banks to borrow money, it increases the repo rate; similarly, if it wants to make it cheaper for banks to borrow money, it reduces the repo rate.

  **Reverse Repo** rate is the rate at which banks park their short-term excess liquidity with the RBI. The RBI uses this tool when it feels there is too much money floating in the banking system. An increase in the reverse repo rate means that the RBI will borrow money from the banks at a higher rate of interest. As a result, banks would prefer to keep their money with the RBI.

  *Thus, we can conclude that Repo Rate signifies the rate at which liquidity is injected in the banking system by RBI, whereas Reverse repo rate signifies the rate at which the central bank absorbs liquidity from the banks.*

  *Liquidity → overall availability of fund/cash*
**Qualitative measures:** The selective or qualitative credit control is intended to ensure an adequate credit flow to the desired sectors and preventing excessive credit for less essential economic activities. The RBI issues directives under Section 21 of the Banking Regulation Act 1949, to regulate the flow of banks' credit against the security of selected commodities. It is usually applied to control the credit provided by the banks against certain essential commodities which may otherwise lead to traders using the credit facilities for hoarding and black marketing and thereby permitting spiraling prices of these commodities. The selective credit control measures by RBI are resorted to commodities like, wheat, sugar, oilseeds, etc.

- **Rationing of credit**
  This method is used to control the scheduled banks borrowings from the RBI. The RBI shows differential treatment in giving financial help to its member banks according to the purpose for which the credit is used.

- **Variation of Margin Requirement**
  Here the term "margin "refers to a portion of the loan amount which cannot be borrowed from bank. In other words, the margin money is required to be brought in by the borrower from his own sources. This much percentage of money will not be lent by banks. The RBI lowers the margin to expand the credit and raises margin to contract or control the credit for stock market operations. The changes in the minimum margin requirements were effected mainly to discourage speculative hoarding tendencies and to check the rising prices of agricultural commodities.

- **Regulation for consumer credits**

  The credit facilities provided by the banks to purchase durable consumer goods like cars, refrigerators, T.V. furniture, etc. is called as consumer credit. If consumer credit is expanded, it leads to the increase in production of consumer goods in the country.

  Such increased sale of consumer goods will affect savings of people and capital formation in the economy. Hence, RBI may control the consumer credit extended by the commercial banks. These days RBI does not use such credit control measure as increased consumption lead to more economic activity.
■ Publicity and moral suasion
RBI outlays guidelines to banks of banks countries to disobey the guideline. It may increase Bank rate or cancel licensing. Moral suasion is a means of strengthening mutual confidence and understanding between the monetary authority and the banks as well as financial institute and, therefore, is an essential instrument of monetary regulation.

■ Direct action
When the moral suasion proves ineffective the RBI may have to use direct action on banks. The RBI is empowered to take certain penal actions against banks which do not follow the line of policy dictated by it. This method is essentially a corrective measure which may bring about some psycho-logical pressure on the commercial banks to follow the RBI instructions.

COMMERCIAL BANKS

*Scheduled Commercial Bank:* is a bank listed in the second schedule of the RBI Act, 1934 which lies down that such a bank must have a paid up capital of 5 lakhs and above. It must be working in the interest of the depository.

Commercial banks are an organisation which normally performs certain financial transactions. It performs the twin task of accepting deposits from members of public and make advances to needy and worthy people form the society. When banks accept deposits its liabilities increase and it becomes a debtor, but when it makes advances its assets increases and it becomes a creditor. Banking transactions are socially and legally approved. It is responsible in maintaining the deposits of its account holders.
Before the steps of nationalisation of Indian banks, only State Bank of India (SBI) was nationalised. It took place in July 1955 under the SBI Act of 1955. Nationalisation of Seven State Banks of India (formed subsidiary) took place on 19th July, 1960 due to following reasons:

- To prevent concentration of economic power
- To direct banking activities to more and more to the agricultural sector & rural sector.
- To mobilize saving of small people
- To convert banking from else banking to mass banking
- To direct the banking industry to sub serve social interest.
- To direct banking to serve product line purpose rather than consumption or commercial purposes.
- To develop a pool of professional banks and managers.

- 1955 : Nationalisation of State Bank of India.
- 1959 : Nationalisation of SBI subsidiaries.
- 1980 : Nationalisation of seven banks with deposits over 200 crores.

1969-91 was a period of total nationalization

1991 onwards banking reforms came in picture. Why?
July 1969- Lead Bank Scheme introduced
Under this banks were allotted districts and given the lead responsibilities to bring about development of these districts.

Identifying needs, problems of district then prepare plans and give RBI so that this can be aligned with policies. This scheme is based on area approach.

1972 DIRS (Differentiated Interest Rate Scheme)

Scheme under which banks give loans at near 4% rate of interest to people below the poverty line. RBI gave instruction that the target amount is 1% of previous deposits of the banks.

1989 Service Area Approach scheme was introduced as part of lead bank scheme under which banks have to adopt certain service area consisting of rural & semi-urban area, for bringing about their intensive development.

What lead to Reforms?

- Uneconomic & and discriminatory branch expansion.
- Directed investments that is banks directed by RBI to keep a very high SLR & very high CRR (SLR-38.5%, CRR-15% in 1991). Thus blocking a major part of the bank funds- 53.5% of their deposits blocked. Under the SLR it was mandatory to keep a predominant portion in the form of government securities which were low yielding thereby affecting the probability of bank. Other portion is in the form of ideal case which further affected probability.
- Directed Credit Program i.e. mandatory lending of 40% to the priority sector thus implying that over 90% of bank funds were blocked. This also meant that throughout this period. The focus was purpose oriented lending rather than security oriented lending.
- Over staffing & over manning in the banking industry leading to escalation of cost.
- Rampant political interference in the day to day forcing of banks. Even forcing on many occasion to meet 40% target of priority sector. Lending without regard to prudential banking norms.
- Poor recovery of loans, precipitated by day to day political interference due to which political bosses would some time even announce loan waives. So much
so on man occasions in order to meet priority sector lending by end of the Banks would even reason to contacting loan useless for disbursement of loans without any sound criteria to people.
- *Fast declining consumer services* further effecting the overall image and profile of banking
- Total disregard of transparency of maintaining balance sheets
- Total disregard of provisioning norms and capital adequacy norms as well as total disregard of classifying had loans in to various categories.

As a result profitability became the biggest casualty for the banking industry and there is no motivation for banking industry to improve itself on the face of political interference. So the recovery rate was becoming poorer and poorer with result that losses were mounting expenditures were rising, profitability was decline so that in 1991 as many as 14 out of 20 nationalized banks were reported sick. This prompted to the Government to carry out sweeping reforms of the Banking Industry as part of economic reforms party launched in 1991. Hence the **Narsimham committee on Financial Sector reforms** was set up in 1991 whose major recommendation most of which were implemented were as follows:

- There should be a 3 tier banking structure in the country viz. 3 to 4 banks should be of international character, 8 to 10 Banks of national character and the rest meeting local & regional requirements.
- There should be no further branch expansion and bands should enjoy the freedom to open or close a branch other than closing the branch in the Rural Area.
- There should be no further nationalization banking sector.
- More and more of private sector & foreign banks should be encouraged to be set up so as to infuse competition in banking sector.
- Public Sector banks should be permitted to float shares in the market and rural capital to boost their capital funds.
- SLR & CRR should be brought down in a phased manner 20 as to give flexibility to bank funds.
- Debt Recovery Tribunal should be set up to recover bad debts money of banks in an expeditions manner.
NPA

Technically a NPA according to RBI is a debt for which repayment has not been made for ever today. NPAs are further classified into substandard, doubtful, Loss.

Capital Adequacy Ratio

It is a ratio of the total unimpaired capital funds of a bank to its risk weighted assets. It is also known as CRAR that is capital to Risk weighted Ratio. This ratio strengthens the countries’ stability of a banks/financial institution. Banks in India are required to attain CAR of 10% by 2002. But till date they have attained only 9%.

Securitization, Reconstruction of financial Assets and Enforcement of security interests Act, 2002

The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, (SARFAESI Act) was born out of the Narasimham Committee-II recommendations after some modifications. Asset reconstruction companies are set up, and registered with the Reserve bank of India (RBI) as a securitisation company (SC) and reconstruction company (RC) to acquire distressed secured financial assets (both moveable and immovables).

The underlying idea of bringing into fruition ARCs under SARFAESI Act is to enable banks to clean up their balance sheets, pass on the burden of recovery to an agency which could give full-time attention to realize a higher amount than what the borrower is willing to offer and thus generally help faster resolution of NPA.

MONEY SUPPLY

When RBI calculates money supply in country on the basis of narrow money & broad money for Narrow money it uses symbol like;

M1 which means, currency & coins in inclusion + demand deposits of banks + other deposits with the RBI government IDBI etc.

M2 = M1 + post office saving deposits
M3 is called broad money = M1 + timed deposits of banks

M4 = M3 + total post office deposits

Reserve money is money created by the central bank of the country also called HF-powered money which is actually the base of monetary expansion in country. Currency and coins in circulation + cash in hands with banks + cash reserves in hand of RBI + other deposits with RBI.

CAMELS is an acronym used for banking Regulation

C: Capital adequacy
A: Asset quality
M: Management
E: Earning
L: Liquidity
S: Systems control

All banks have to be conformed of CAMELS at any time.

CDs (Certification of Deposits) are a financial Institution issued by a Bank to raise short term loans form it corporate clients. A CD is issued at a discount to the face value and it can be issued subject to a certain minimum amount and a certain minimum to maximum period. The maximum being one year and it can’t be less than 15 days and 5 lack minimum.

LIBOR- London Inter Bank Offered Rate

It is the Rate of Interest that prevails in the London Inter Bank Money Market. That is the rate at which loans are given on inter bank basis in the London money market.
1. What does S & P 500 relate to?
   a. Supercomputer
   b. A new technique in e-business
   c. A new technique in bridge building
   d. **An index of stocks of large companies**

2. Basel II relates to which one of the following?
   a. International standards for safety in civil aviation
   b. Measures against cyber crimes
   c. Measures against drug abuse by sportspersons
   d. **International standards for measuring the adequacy of a bank’s capital**

3. Consider the following statements
   1. The repo rate is the at which other banks borrow from the Reserve Bank of India.
   2. A value of 1 for Gini coefficient in a country implies that there is perfectly equal income for everyone in its population.
   3. Which one of the statements given above is/are correct?
      a) 1 only       b) 2 only       c) Both 1 and 2       d) **Neither 1 nor 2**

4. The National Housing Bank was set up in India as a wholly-owned subsidiary of which one of the following?
   a. State Bank of India
   b. **Reserve Bank of India**
   c. ICICI Bank
   d. Life Insurance Corporation of India

5. Consider the following statements;
   1. Life Insurance Corporation of India is the oldest insurance company in India.
2. National Insurance company Limited was nationalized in the year 1972 and made a subsidiary of General Insurance corporation of India.

3. Head Quarters of United India Insurance Limited are Located at Chennai

Which one of the statements given above is/are correct?

a) 1, 2 and 3  
b) 2 and 3 only  
c) **1 and 2 only**  
d) 1 and 3 only

6. What is Indo next which was launched in January, 2005?

a) A new scheme to promote Indian Tourism
b) A new scheme to promote export of Indian Handicrafts

c) An association of the non resident Indians to organize Pravasi Bhartiya Divas every year in India.

d) **An alternative trading Platform being promoted by the Bombay Stock Exchange and Regional Stock Exchange.**

7. Consider the following statements;

1. Sensex is based on 50 of the most important stocks available on the Bombay Stock Exchange (BSE)

2. For calculating the sensex, all the sensex stocks are assigned proportional weightage.

3. New York stock Exchange is the oldest stock Exchange in the world.

Which one of the statements given above is/are correct?

a) **2 only**  
b) 2 and 3  
c) 1 and 3  
d) None

8. Consider the following statements;

1. The National Housing Bank, the Apex institution of housing finance in India, was set up as a wholly owned subsidiary of the Reserve bank of India.

2. The small Industries Development Bank of India was established as wholly-owned subsidiary of the Industrial Development Bank of India.

Which one of the statements given above is/are correct?

a) **1 only**  
b) 2 only  
c) **both 1 and 2**  
d) Neither 1 nor 2

9. In India, the first of limited liability managed by Indians and founded in 1881 was

a) Hindustan Commercial Bank

b) **Oudh Commercial Bank**
10. Debenture holders of a company are its
   a) Shareholders  b) Creditors  c) Debtors  d) Directors

11. Which one of the following statements is correct with reference to FEMA in India?
   a) The foreign Exchange Regulation Act (FERA) was replaced by Foreign Exchange Management Act (FEMA) in the year 2001.
   b) FERA was given a sunset clause of one year till 31st May, 2002 to enable Enforcement Directorate to complete the investigation of pending issues.
   c) Under FEMA, violation of foreign exchange rules has ceased to be a criminal offence.
   d) As per the new dispensation, Enforcement Directorate can arrest and prosecute the people for the people for the violation of foreign exchange rules.

12. Consider the following statements;
   1. Currency with the public
   2. Demand deposits with banks
   3. Time deposits with banks
   a) 1 and 2  b) 1 and 3  c) 2 and 3  d) 1, 2 and 3

13. Among the following major stock exchanges of India, the exchange which recorded highest turnover during the year 2000-01
   a) Bombay stock Exchange
   b) Calcutta Stock Exchange
   c) Delhi Stock Exchange
   d) National Stock Exchange

14. Consider the following financial institutions of India;
   1. Industrial Finance corporation of India (IFCI)
   2. Industrial Credit and Investment Corporation of India (ICICI)
   3. Industrial Development Bank of India (IDBI)
   4. National Bank for Agriculture and rural Development (NABARD)
The correct chronological sequence of the establishment of these institutions
   a) 1, 2, 3, 4    b) 3, 4, 1, 2    c) 2, 3, 4, 1    d) 4, 1, 2, 3

15. Consider the following statements:
   Full convertibility of the rupee may mean-
   1. Its free float with other international currencies.
   2. Its direct exchange with any other international currency at any prescribed place inside and outside the country.
   3. It acts just like any other international currency.
   Which of these statements are correct?
   a) 1 and 2    b) 1 and 3    c) 2 and 3    d) 1, 2 and 3

16. With reference to the Wholesale Price Index (WPI). Consider the following statements:
   2. In the new WPI series, the weight for primary articles has gone down by 10 percentage points.
   3. The weight for electricity has increased in the new WPI series.
   Which of these statements are correct?
   a) 1, 2 and 3    b) 2 and 3    c) 1 and 3    d) 1 and 2

17. The new series of Wholesale Price Index (WPI) released by the Government of India is with reference to the base prices of
   a) 1981-82    b) 199-91    c) 1993-94    d) 1994-95

18. The average rate of domestic savings (gross) for the Indian economy is currently estimated to be in the range of
   a) 15 to 20 per cent    b) 20 to 25 per cent
   c) 15 to 30 per cent    d) 30 to 35 per cent

19. Consider the following statements:
   The Indian Rupee is fully convertible-
   1. In respect of Current Account of Balance of Payment
   2. In respect of Capital Account of Balance of Payment
   3. Into gold
Which of these statements is/are correct?

a) 1 alone  b) 3 alone  c) 1 and 2  d) 1, 2 and 3

20. Gilt-edged market means
   a) bullion market
   b) market of Government securities
   c) market of guns
   d) market of pure metals

21. Resurgent India Bonds were issued in US dollar, Pound Sterling and
   a) Japanese Yen  b) Deutsche Mark
   c) Euro  d) French Franc

22. A rise in ‘SENSEX’ means
   a) A rise in prices of shares of all companies registered with Bombay Stock Exchange
   b) A rise in prices of shares of all companies registered with National Stock Exchange
   c) An overall rise in prices of shares of group of companies registered with Bombay Stock Exchange
   d) A rise in prices of shares of all companies belonging to a group of companies registered with Bombay Stock Exchange

23. From the balance sheet of a company, it is possible to
   a) Judge the extent of profitability of the company
   b) Assess the profitability and size of the company
   c) Determine the size and composition of the assets and liabilities of the company
   d) Determine the market share, debts and assets of the company

24. The current price index (base 1960) is nearly 330. This means that
   a) All items cost 3-3 times more than what they did in 1960
   b) The prices of certain selected items have gone up to 3-3 times
   c) Weighted mean of prices of certain items has increased 3-3 times
   d) Gold price has gone up 3-3 times
25. The banks are required to maintain a certain ratio between their cash in hand and total assets. This is called
   a) SBR (Statutory Bank Ratio)   b) SLR (Statutory Liquid Ratio)
   c) CBR (Central Bank Reserve)   d) CLR (Central Liquid Reserve)

26. The accounting year of the Reserve Bank of India is
   a) April–March       b) July–June
   c) October–September d) January–December

27. Capital Account Convertibility of the Indian Rupee implies
   a) that the Indian Rupee can be exchanged by the authorized dealer for travel
   b) that the India Rupee can be exchanged for any major currency for the purpose of trade in goods and services
   c) that the Indian Rupee can be exchanged for any major currency for the purpose of trading financial assets
   d) none of the above

28. Economic Survey in India is published officially, every year by the
   a) Reserve Bank of India
   b) Planning Commission of India
   c) Ministry of Finance, Government of India
   d) Ministry of Industries, Government of India

29. In India, the interest rate on savings accounts in all the nationalized commercial banks is fixed by
   a) Union Ministry of Finance       b) Union Finance Commission
   c) Indian Banks Association       d) None of the above

30. With reference to the institution of Banking Ombudsman in India, Which one of the statements is not correct?
   a) The Banking Ombudsman is appointed by the Reserve Bank of India
   b) The Banking Ombudsman can consider complaints from Non–Resident Indians having accounts in India
   c) The orders passed by the Banking Ombudsman are final and binding on the parties concerned
   d) The service provided by the Banking Ombudsman is free of any fee
31. With reference to India, consider the following:
   1. Nationalization or Banks
   2. Formation of Regional Rural Banks
   3. Adoption of villages by Bank Branches
Which of the above can be considered as steps taken to achieve the “financial inclusion” in India?
   a) 1 and 2 only   b) 2 and 3 Only   c) 3 Only   d) 1, 2 and 3

32. Consider the following statements:
   The Functions of commercial banks in India include-
   1. Purchase and sale of shares and securities on behalf of customers.
   2. Acting as executive and trustees of wills.
Which of the statements given above is/are correct?
   a) 1 Only   b) 2 Only   c) Both 1 and 2   d) Neither 1 nor 2

33. Which of the following terms indicates a mechanism used by commercial banks for providing credit to the government?
   a) Cash Credit Ratio   b) Debt Service Obligation   c) Liquidity Adjustment Facility   d) Statutory Liquidity Ratio

34. With reference to the Non-banking Financial Companies (NBFCs) in India consider the following statements:
   1. They cannot engage in the acquisition of securities issued by the government.
   2. They cannot accept demand deposits like savings Account.
Which of the statements given above is/are correct?
   a) 1 only   b) 2 only   c) Both 1 and 2   d) Neither 1 nor 2

35. When the Reserve Bank of India announces an increase of the Cash Reserve Ratio, what does it mean?
   a) The commercial banks will have less money to lend
   b) The Reserve Bank of India will have less money to lend
   c) The Union Government will have less money to lend
   d) The commercial banks will have more money to lend.