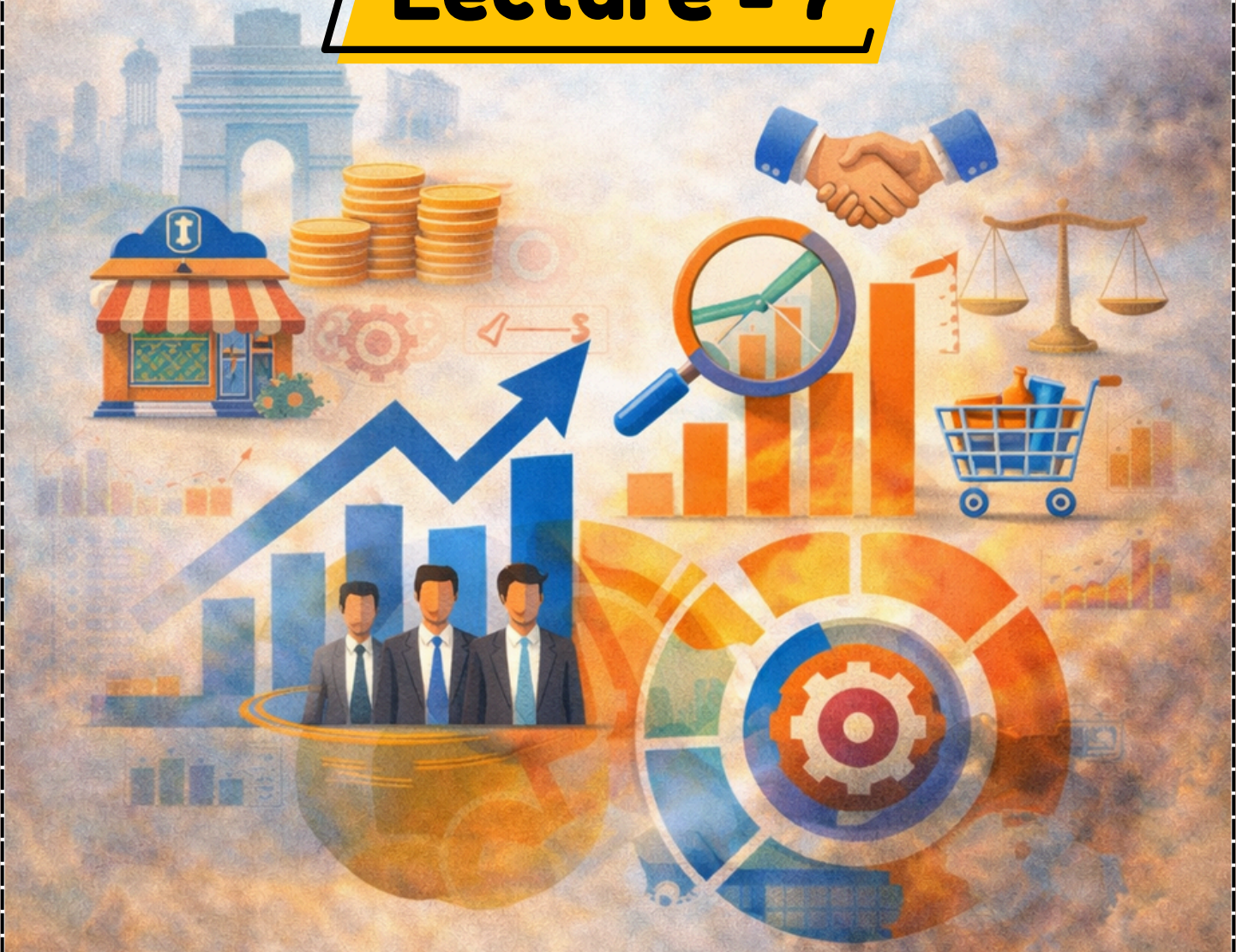
PARMAR SSC

BANKING SYSTEM

(PART - 1)

Lecture - 7



BY PARMAR SIR

INTRODUCTION & THE RESERVE BANK OF INDIA (RBI)

What is Banking?

- **Definition:** Banking is a financial activity that involves managing money and providing financial services to individuals, businesses, and governments.
- **Core Activities:** Banks primarily accept deposits, lend money, and facilitate transactions.

THE RESERVE BANK OF INDIA (RBI)

- The RBI is the central bank of the country, often referred to as the "Father of all Banks" because it manages, controls, and regulates the entire banking system.

History and Establishment

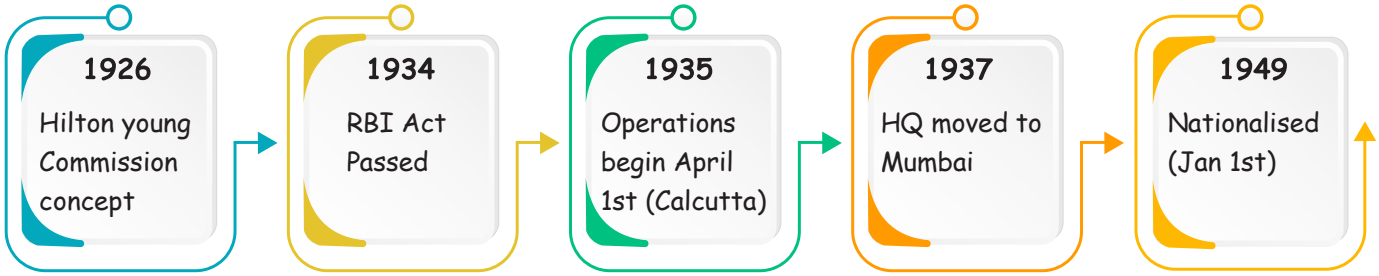
- **Recommendation:** The RBI was established based on the recommendations of the Hilton Young Commission in 1926.
- **Act:** It was officially established under the Reserve Bank of India Act, 1934.
- **Operational Start:** Operations commenced on 1st April 1935 in Calcutta.
- **Headquarters Shift:** The headquarters was permanently moved from Calcutta to Mumbai in 1937.

Nationalization

- **Date:** RBI was nationalized on 1st January 1949 the specific Act used was the Reserve Bank of India (Transfer to Public Ownership) Act, 1948.
- **Meaning:** Nationalization means the government acquired full shareholding/ownership from private players.
- **The Act:** The nationalization was executed through the Transfer of Public Ownership Act, 1948.

Key Leadership & Symbols

- **First Governor:** Sir Osborne Smith.
- **First Indian Governor:** Sir C.D. Deshmukh.
- **Current Governor:** Sanjay Malhotra
- **Logo:** Features a Tiger and a Palm Tree.



FUNCTIONS OF RBI

- The RBI performs several critical functions to maintain economic stability.

1. Regulator of Banks ("Bank of Banks")

- **Authority:** The RBI regulates the country's banking system primarily under the Banking Regulation Act of 1949.
- **Responsibilities:**
  - Grants licenses to banking companies.
  - Regulates CRR (Cash Reserve Ratio) and SLR (Statutory Liquidity Ratio).
  - Acts as the "Bank of Banks" by ensuring banks meet specific criteria before operating.

2. Monetary Authority

- **Role:** Formulates and implements monetary policy to control inflation, manage money supply, and ensure credit flow to various sectors.
- **Tools:** Uses instruments like the Repo Rate (the rate at which banks borrow from RBI) to influence interest rates in the economy.

3. Currency Printing & Management

- **Responsibility:** RBI prints and manages currency in India, including banknotes.
- **Exception:** The ₹1 note and all coins are issued by the Ministry of Finance (Government of India).



Printing Press Locations (Notes):
- ➤ Nasik (Maharashtra)
- ➤ Dewas (Madhya Pradesh)
- ➤ Mysore (Karnataka)
- ➤ Salboni (West Bengal)



Minting Locations (Coins):
- ➤ Mumbai
- ➤ Hyderabad
- ➤ Calcutta
- ➤ Noida.

How to Identify Where a Coin Was Minted?
- Check the small mark below the year on the coin:
- Diamond (💎): Minted in Mumbai.
- Star (★): Minted in Hyderabad.
- No Mark: Minted in Calcutta (Kolkata).
- Dot (•): Minted in Noida.

4. Publication of Reports

Financial Stability Report (FSR):

- The RBI publishes this biannual report (twice a year in June and December).
- **Purpose:** To assess the risks to the financial system.

Handbook of Statistics on the Indian Economy:

- This is published annually by the RBI.
- **Purpose:** To provide comprehensive data and statistics on the Indian economy.

5. Lender of Last Resort

- **Definition:** RBI acts as the final source of funding for commercial banks when they are unable to secure loans from other sources during financial crises.

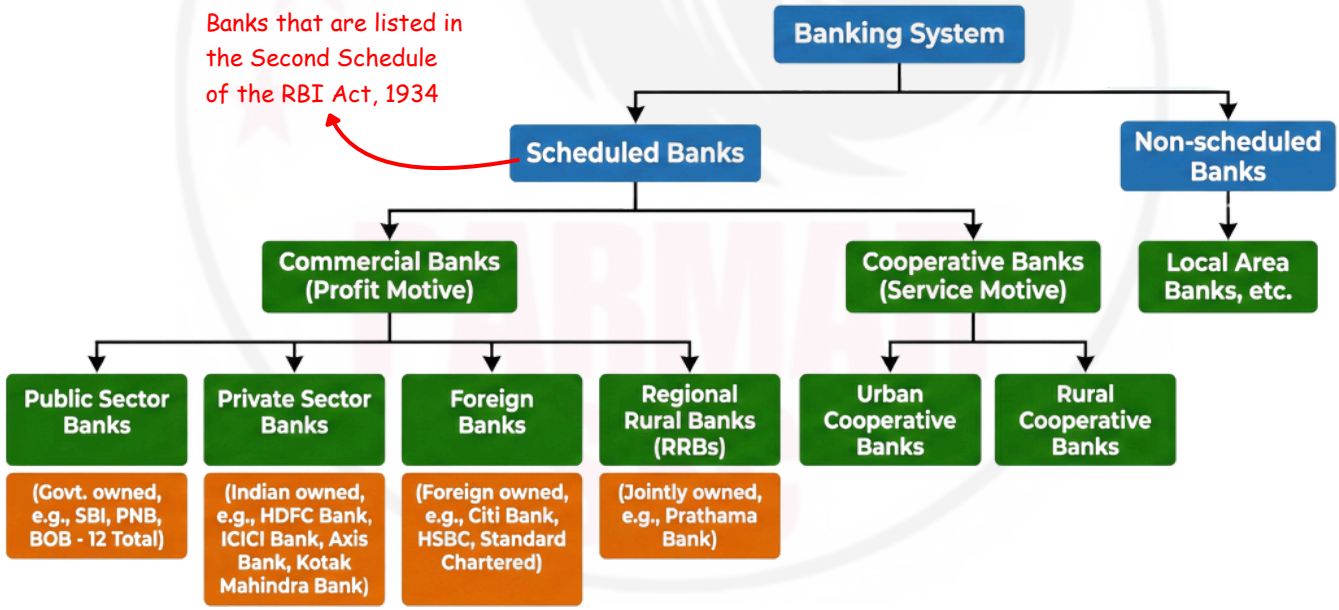
> The general public (individuals) cannot directly open accounts with or borrow money from the RBI. We deal with banks; banks deal with the RBI.

CLEAN NOTE POLICY

- **Introduction:** The RBI introduced the Clean Note Policy in 1999.
- **Objective:** The policy directs banks not to pass on soiled, torn, or scribbled notes to customers. Instead, these notes must be deposited back to the RBI.
- **Legal Basis:** This policy was introduced under Section 35A of the Banking Regulation Act, 1949.

Classification of Banking System in India

(According to RBI Act, 1934)



EVOLUTION & HISTORY OF INDIAN BANKING

- The history of banking in India is a journey from colonial-era institutions to modern nationalized banks, driven by the need to shift from "Class Banking" to "Mass Banking".

Pre-Independence History (Early Beginnings)

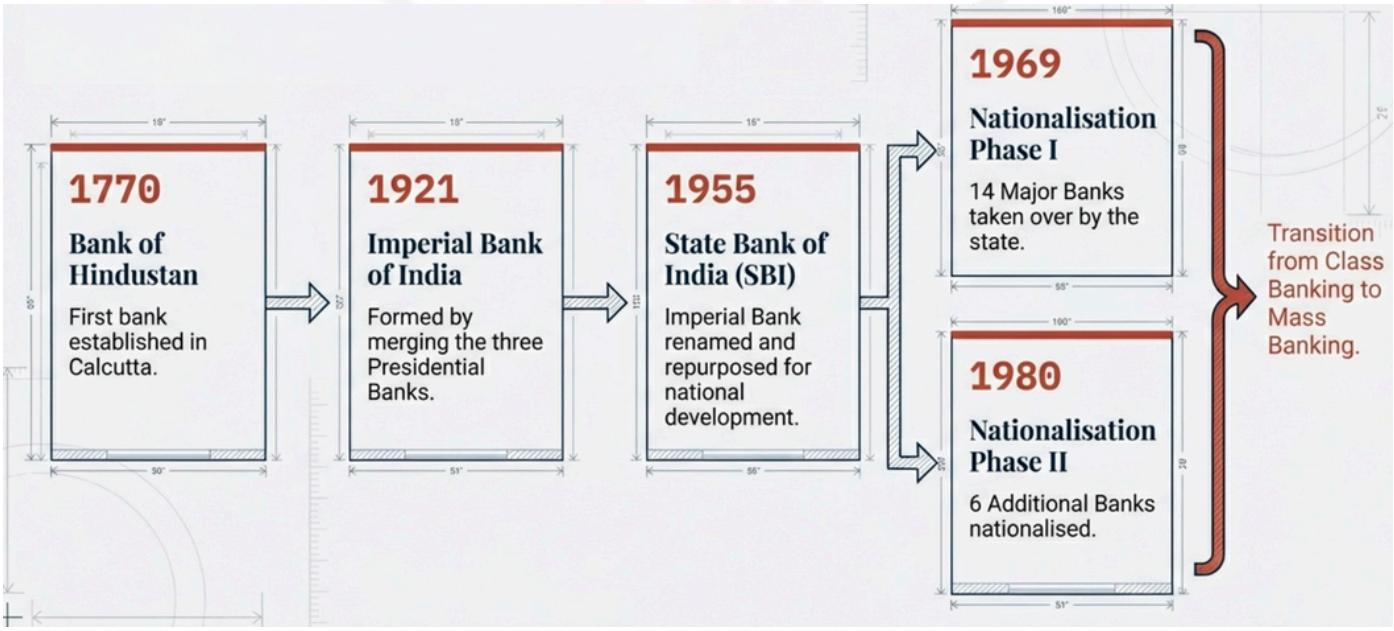
- **First Bank:** The Bank of Hindustan was the first bank to be established in India in 1770 in Calcutta.
- **First Indian-Owned Bank:** The Allahabad Bank, established in 1865, was the first bank owned by Indians.

The Story of the State Bank of India (SBI)

- The SBI's lineage traces back to the three "Presidency Banks" established by the British Rule.

Timeline of Consolidation:

Year	Event	Details
1806	Bank of Calcutta	Established as the first Presidency Bank.
1840	Bank of Bombay	Second Presidency Bank.
1843	Bank of Madras	Third Presidency Bank.
1921	Imperial Bank of India	The three Presidency Banks were merged into a single entity called the Imperial Bank of India.
1955	State Bank of India (SBI)	The Imperial Bank was nationalized and renamed as State Bank of India to foster national development.



NATIONALIZATION OF BANKS

- To ensure banking services reached rural areas and were not limited to the wealthy ("Class Banking"), the Government of India initiated nationalization drives to take ownership of private banks.

Nationalization Phase I

- **Year:** 1969.
- **Prime Minister:** Indira Gandhi.
- **Action:** 14 Major Banks were nationalized.
- **Criteria:** Banks with deposits greater than ₹50 Crore were taken over.
- **Legislation:** Banking Companies (Acquisition and Transfer of Undertakings) Act, 1969.

Nationalization Phase II

- **Year:** 1980.
- **Prime Minister:** Indira Gandhi.
- **Action:** 6 Additional Banks were nationalized.
- **Criteria:** Banks with deposits greater than ₹200 Crore were taken over.

1. Andhra Bank
2. Corporation Bank
3. New Bank of India - Later merged with PNB in 1993.
4. Oriental Bank of Commerce (OBC)
5. Punjab & Sind Bank
6. Vijaya Bank

Nationalization vs. Consolidation

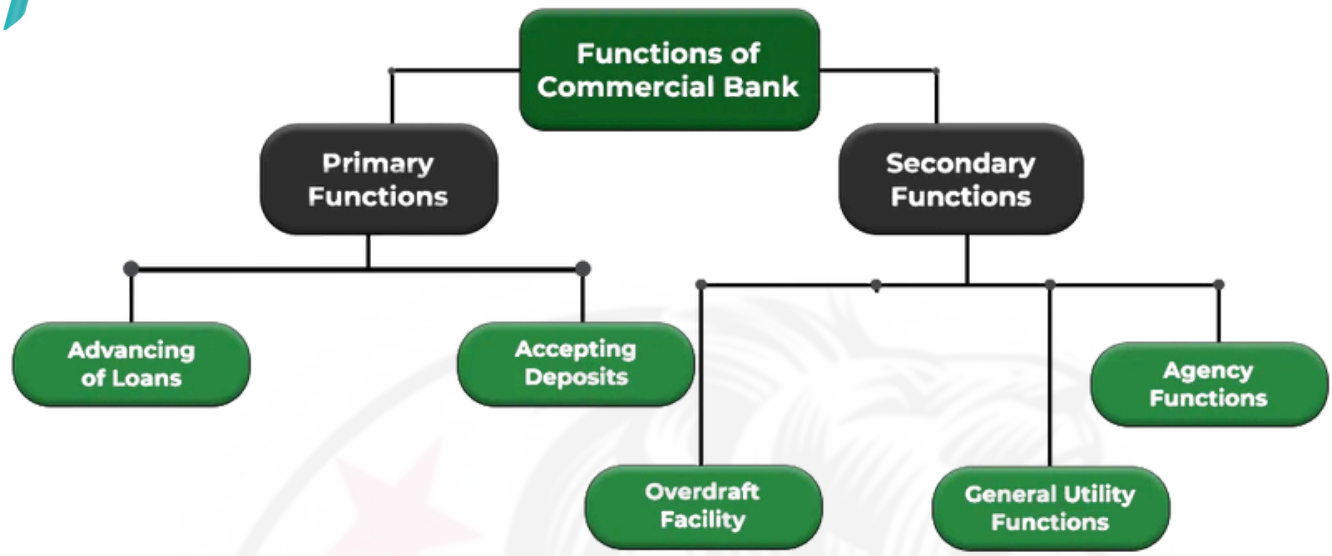
- **Nationalization:** The government taking over ownership of private banks (e.g., 1969, 1980).
- **Consolidation (Merger):** Merging multiple banks into fewer, larger entities to create stronger financial institutions capable of global recognition.

Consolidation & The Narasimham Committee

- **Objective:** To strengthen the banking sector, the government has pursued consolidation (mergers) to create large, globally competitive banks.
- **Narasimham Committee (1998):**
  - This committee is crucial for banking reforms.
  - **Recommendation:** It specifically recommended the merger (consolidation) of strong banks to create "Global Sized Banks".

Note: An earlier Narasimham Committee (1991) had recommended lowering CRR/SLR and removing mandatory government investment requirements.

FUNCTIONS OF COMMERCIAL BANKS & REGIONAL RURAL BANKS (RRBS)



A. Primary Functions

- The core business of a bank involves dealing with debts and credits.

I. Accepting Deposits (Liabilities):

- Deposits are considered the Liability of the bank because the bank owes this money back to the customer.
- **Demand Deposits:** Money that can be withdrawn anytime (e.g., Savings Account, Current Account).
- **Time/Term Deposits:** Money locked for a fixed period (e.g., Fixed Deposit, Recurring Deposit).

II. Advancing of Loans (Assets):

- Loans are the Asset of the bank because they generate income (interest) for the bank.

B. Secondary Functions

- These are additional services provided by banks.

I. Overdraft Facility:

- Allows a customer to withdraw more money than what is currently in their account.
- It is essentially a short-term loan based on the customer's credit score and history.

II. Agency Functions:

- The bank acts as an agent for the customer.
- Fund Transfer: Moving money from one account to another.
- Tax Collection: Collecting Income Tax on behalf of the government.

III. General Utility Functions:

- **Locker Facility:** Safe storage for jewelry and documents.
- **Note:** If items in a locker are stolen/lost, the bank is liable to compensate (up to a limit).
- **Other Services:** Providing information, financial management, and issuing guarantees.

REGIONAL RURAL BANKS (RRBs)

A. Purpose and Need

- Commercial banks were primarily located in cities and trade hubs (like Gujarat/Maharashtra) due to profitability.
- RRBs were established to provide credit and banking facilities to rural areas, farmers, and the weaker sections who were ignored by commercial banks.

B. Establishment Facts

- **First RRB:** Pratham Grameen Bank.
  - Established on 2nd October 1975 (Gandhi Jayanti).
  - **Location:** Moradabad, Uttar Pradesh.
- **Act:** They were formalized under the RRB Act, 1976.
- **Kelkar Committee Recommendation:** Later, the Kelkar Committee suggested stopping the opening of new RRBs to focus on viability.

C. Ownership Structure (Shareholding)

- The ownership of an RRB is divided among three entities:

Stakeholder	Ownership %	Role
Central Government	50%	Largest stakeholder.
Sponsor Bank	35%	A Commercial Bank (e.g., SBI, HDFC) that provides technical & financial support.
State Government	15%	The state where the RRB operates.

D. Regulation vs. Supervision

- **Regulator:** RBI (Reserve Bank of India).
- **Supervisor:** NABARD (National Bank for Agriculture and Rural Development).

Note: NABARD inspects and oversees the functioning of RRBs, but the regulatory guidelines come from the RBI.

IMPORTANT FINANCIAL INSTITUTIONS (IFIs)

- This section covers the specialized financial bodies established to support specific sectors like agriculture, housing, industries, and capital markets.

1. NABARD (National Bank for Agriculture and Rural Development)

Establishment:

- **Date:** Established on 12 July 1982.
- **Committee:** Formed on the recommendation of the B. Sivaraman Committee (1979).
- **Act:** Established under the NABARD Act, 1981.
- **Headquarters:** Mumbai.

Key Functions:

- **Rural Credit:** Offers loans and financial assistance to promote agriculture and rural development.
- **Supervision:** It oversees and regulates the working of Cooperative Banks and Regional Rural Banks (RRBs) to ensure their financial stability.
- **Refinancing:** It provides funding to banks (like RRBs) rather than directly to the public.
- **Direct Interaction:** Unlike commercial banks, NABARD does not provide loans or banking services directly to individuals.

Schemes & Initiatives:

- **Rural Financing:** Facilitates schemes like PMAY (Pradhan Mantri Awas Yojana), KCC (Kisan Credit Cards), and RuPay Kisan Cards.
- **E-Shakti & LEDP:** Launched in 2015 for digitization of SHGs and Livelihood and Enterprise Development Programs.
- **SHG-Bank Linkage Program (1992):** Launched by NABARD to link Self Help Groups (SHGs) with banks to increase their financial access.

2. Regulatory & Development Bodies

Institution	Establishment Year	Headquarters	Chairman/ Head - 2026	Main Objective
SEBI (Securities and Exchange Board of India)	Established on April 12, 1988, and given statutory status through the SEBI Act, 1992.	Mumbai	Tuhin Kanta Pandey	To protect the interests of investors in the securities market.
SIDBI (Small Industries Development Bank of India)	2 April 1990.	Lucknow	Manoj Mittal	To provide financial and developmental assistance to MSMEs.

Institution	Establishment Year	Headquarters	Chairman/ Head - 2026	Main Objective
NHB (National Housing Bank)	Established in 1988 through the Act of 1987.	New Delhi	Sanjay Shukla	To regulate and promote the housing finance sector.
IRDAI (Insurance Regulatory and Development Authority of India)	Established as a statutory body in April 2000 through the IRDAI Act, 1999.	Hyderabad	Ajay Seth	Regulation of the insurance sector and protection of policyholders.
IDBI (Industrial Development Bank of India)	Established in 1964 by the Govt. of India as a subsidiary of RBI. Later, LIC acquired a 51% stake in the bank.	Mumbai	T. N. Manoharan (Chairman)	Loans and financial facilities for the development of industries.
NAFED (National Agricultural Cooperative Marketing Federation of India)	October 2, 1958.	New Delhi	Jethabhai Ahir	It is an apex organization of marketing cooperative societies for agricultural produce.

MICROFINANCE INSTITUTIONS (MFIs)

- **Services**: MFIs provide micro-loans and other financial services such as credit, savings, insurance, and remittances to the low-income population.
- **Eligibility and Collateral**: MFIs provide micro-finance loans without any collateral (without keeping anything as a guarantee) to households with an annual income of up to ₹3 lakh.

Important Facts and History

- **Father of Micro-finance System**: Muhammad Yunus (In 2006, he won the Nobel Peace Prize for establishing the Bangladesh Grameen Bank).
- **First Micro-finance Institution**: Self Employed Women's Association (SEWA) Bank, which was established in 1974 in Ahmedabad.

Business Model of Micro Finance Banks

- The business model of Microfinance Banks revolves around providing small loans and financial services to low-income individuals, primarily in rural area through various schemes and groups.

Self Help Groups (SHG)

- **Structure of the Group**: It is a group of 10-20 people living below the poverty line (BPL) who come together in rural areas to find ways to improve their living conditions.
- **Loans and Interest Rates**: SHGs provide loans to their members without collateral (without keeping anything as a guarantee) at lower interest rates compared to the informal sector (such as moneylenders).
- **Social and Economic Impact**: SHGs also help women and other marginalized groups become more self-reliant.

Joint Liability Groups (JLG)

- **Structure of the Group**: It involves a group of 4-10 people who come together to apply for a bank loan.
- **Collateral-free Loan**: By forming a JLG, individuals can obtain collateral-free loans (without keeping anything as a guarantee) and expand their businesses without worrying about security or margins.
- **Target Beneficiaries**: This loan is provided to individuals, sharecroppers, tenant farmers, and small and marginal farmers.

Non-Banking Financial Companies (NBFCs)

- **Definition**: Non-Banking Financial Institutions (NBFIs) provide various banking services but do not possess a banking license.
- **Registration and Regulation**: These are registered under the Companies Act, 1956, and are regulated by the Reserve Bank of India (RBI) under the RBI Act, 1934.
- **Deposit and Cheque Limitations**: These cannot accept demand deposits (such as savings/current accounts) and cannot issue cheques.
- **Gold Loan**: NBFCs provide loans against gold.
- **Lack of Deposit Protection**: Deposits in an NBFC are not guaranteed. If an NBFC fails, depositors may lose their money because there is no government protection (DICGC insurance).
- **Reserve Funds**: Unlike banks, it is not mandatory for them to maintain CRR (Cash Reserve Ratio) and SLR (Statutory Liquidity Ratio).

Capital Requirements for NBFCs

- For NBFC-MFIs (Microfinance Institutions), the minimum Net Owned Fund (NOF) requirement is tiered based on geography:
  - **General (All over India)**: Must have a minimum NOF of ₹5 crore.
  - **North-East Region**: Requires a lower minimum NOF of ₹2 crore to encourage financial inclusion in that specific area.

- **Examples of NBFCs**
  - Non-Banking Financial Companies vary by their specialization:
  - **Gold Loans**: Muthoot Finance, Manappuram Finance.
  - **Asset/Vehicle Finance**: Shriram Finance, Mahindra Finance.
  - **Consumer/Personal Finance**: Bajaj Finance, Tata Capital.
  - **Infrastructure Finance**: Power Finance Corporation (PFC), REC Limited.

Payment and Settlement Systems

- NBFC Limitation: NBFCs are not part of the Payment and Settlement System.

Entity Type	Min. Capital Requirement	Key Regulatory Fact
Scheduled Commercial Bank	₹500 Crore	Part of Payment & Settlement System
Payments Bank	₹100 Crore	Cannot issue loans or credit cards

Payment and Settlement Systems Act, 2007

- **Regulation (PSS Act, 2007)**: All payment systems in India (like UPI, NEFT, RTGS, and Credit Cards) are regulated by the RBI under the Payment and Settlement Systems Act, 2007.
- **Function**: This Act gives RBI the legal authority to supervise and oversee any system that enables payments between a player and a beneficiary.

Non-Banking Financial Company-Micro Finance Institution (NBFC-MFI)

- **Registration and Regulation:** These are registered under the RBI and are regulated by the RBI.
- **Goals and Services**: They provide micro-loans/micro-financial services to low-income individuals, especially in rural areas, who do not have access to formal banking services.
- **Basis of Establishment**: NBFC-MFIs were established based on the recommendations of the Malegam Committee (2010), which also investigated the issues concerning MFIs.
- **Eligibility for License**: To be eligible for an NBFC-MFI license, they are required to hold 60% (excluding intangible assets) in qualifying microfinance loans. Previously, this requirement was 75% (following a 2022 revision from 85%).

Priority Sector Lending (PSL)

- The RBI mandates that banks allocate a specific portion of their lending to sectors that impact large segments of the population.
  - Commercial Banks (Domestic & Foreign with >20 branches): Must allocate 40% of ANBC (Adjusted Net Bank Credit) to PSL.
  - Foreign Banks (<20 branches): Target is 40% of ANBC.
  - Regional Rural Banks (RRBs) & Small Finance Banks (SFBs): Have a higher target of 75% of ANBC.
- NBFCs: Generally, NBFCs do not have specific PSL targets like commercial banks.

Specific Sub-targets:

- Agriculture: 18%.
- Weaker Sections (SC, ST & Women's): 12%.
- Non-Achievement: If banks fail to meet these targets, the shortfall is deposited into the Rural Infrastructure Development Fund (RIDF), managed by NABARD.

Urban Cooperative Banks (UCBs)

- **Dual Regulation**: UCBs operate under two regulatory bodies:
  a. **RBI**: Manages banking functions, prudential norms, and monetary policy.
  b. **Registrar of Cooperative Societies (RCS)**: Manages incorporation, management, elections, and audit.

Pradhan Mantri Mudra Yojana (PMMY) Scheme

- This is a government scheme that promotes financial inclusion by providing micro-credit or loans to small businesses. The loans are categorised into
  - **Shishu**: Covering loans upto ₹50,000
  - **Kishor**: Covering loans above ₹50,000-₹5 lakh.
  - **Tarun**: Covering loans above ₹5 lakh-₹10 lakh.
  - **Tarun Plus**: Covering loans above ₹10 lakh-₹20 lakh.

MUDRA (Micro Units Development & Refinance Agency Ltd.)

- **Year**: This scheme was launched on 8 April 2015.
- **Funding**: It receives 100% funding from SIDBI (Small Industries Development Bank of India).



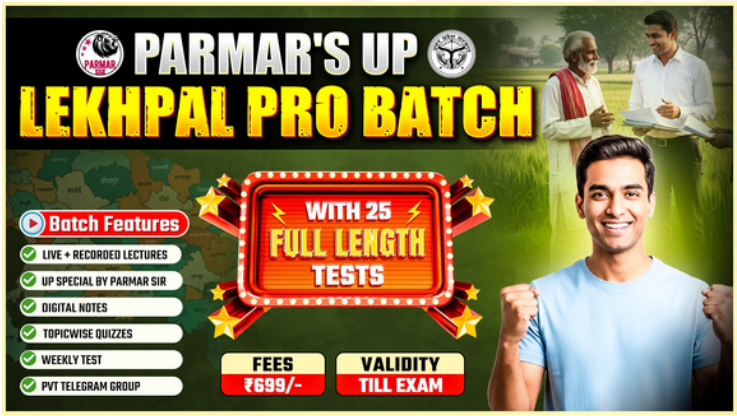


Join Now – Start Your Smart Preparation Today!

CLICK HERE

Join Now – Start Your Smart Preparation Today!

CLICK HERE





Join Now – Start Your Smart Preparation Today!

CLICK HERE

Join Now – Start Your Smart Preparation Today!

CLICK HERE



Join Now – Start Your Smart Preparation Today!

CLICK HERE

