Commercial Banking in India

Commercial banks are the most important components of the whole banking system.

A commercial bank is a profit-based financial institution that grants loans, accepts deposits, and offers other financial services, such as overdraft facilities and electronic transfer of funds.

According to Culbertson,

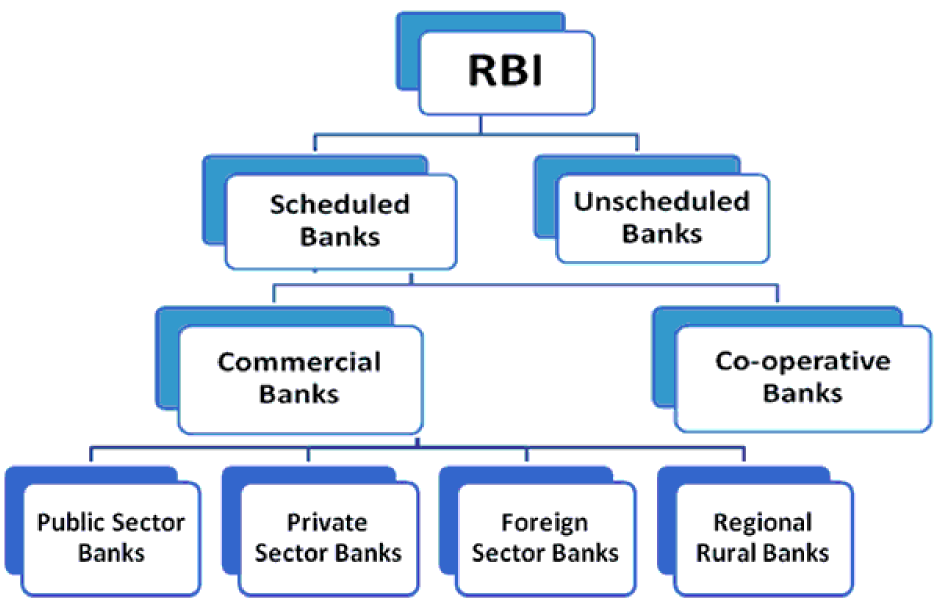
"Commercial Banks are the institutions that make short term loans to business and in the process create money."

In other words, commercial banks are financial institutions that accept demand deposits from the general public, transfer funds from the bank to another, and earn profit.

Commercial banks play a significant role in fulfilling the short-term and medium- term financial requirements of industries. They do not provide, long-term credit, so that liquidity of assets should be maintained. The funds of commercial banks belong to the general public and are withdrawn at a short notice; therefore, commercial banks prefers to provide credit for a short period of time backed by tangible and easily marketable securities. Commercial banks, while providing loans to businesses, consider various factors, such as nature and size of business, financial status and profitability of the business, and its ability to repay loans.

Classification of Commercial banks

Commercial banks are of three types, which are as follows:



- **Public Sector Banks**

Refer to a type of commercial banks that are nationalized by the government of a country. In public sector banks, the major stake is held by the government. In India, public sector banks operate under the guidelines of Reserve Bank of India (RBI), which is the central bank. Some of the Indian public sector banks are State Bank of India (SBI), Corporation Bank, Bank of Baroda, Dena Bank, and Punjab National Bank.

- **Private Sector Banks**

Refer to a kind of commercial banks in which major part of share capital is held by private businesses and individuals. These banks are registered as companies with limited liability. Some of the Indian private sector banks are Vysya Bank, Industrial Credit and Investment Corporation of India (ICICI) Bank, and Housing Development Finance Corporation (HDFC) Bank.

- **Foreign Banks**

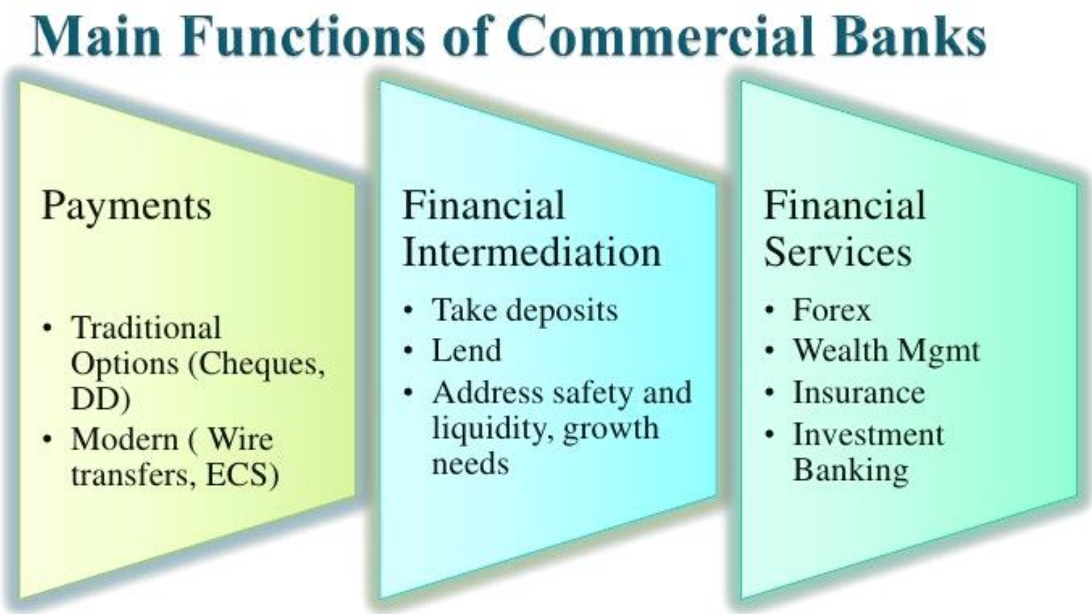
Refer to commercial banks that are headquartered in a foreign country, but operate branches in different countries. Some of the foreign banks operating in India are Hong Kong and Shanghai Banking Corporation (HSBC), Citibank, American Express Bank, Standard & Chartered Bank, and Grindlay's Bank. In India, since financial reforms of 1991, there is a rapid increase in the number of foreign banks. Commercial banks mark significant importance in the economic development of a country as well as serving the financial requirements of the general public.

Primary Functions of Commercial Banks:

- Accepting Deposits from the public in savings account, current account, fixed deposits, recurring deposits, deposits from NRIs.
- Lending money to the public for their various purposes like personal loans, housing loans, vehicular loans, etc.
- Providing overdraft facility to the credit card holders and under any schemes by the government like in Pradhan Mantri Jan Dhan Yojana Scheme.

Secondary Functions or Para banking Activities of the Commercial Banks:

- Issue debit, credit and prepaid cards.
- Issue Letter of Credit and Bank Guarantee.
- Collect amounts through cheques and other instruments.
- Sale and purchase of shares and debentures.
- Act as investment bank for Initial Public Offering (IPO) by a private company.
- Help in anti-money laundering through KYC process.
- Become an intermediary between its customers and other institutions, like payment of insurance premium, payment of various bills, direct benefit transfer (DBT) scheme of government, etc.
- Provide facilities such as Electronic Clearing Service, transfer of funds domestically and internationally, locker facilities, foreign exchange, etc.



With the advances in technology, the commercial banks are also making advancement and providing the citizens of India with the best facilities and they are also easing the lives of people by providing many good facilities.

2019 recent news:
In August, 2019 Jana Small Finance Bank Ltd, which commenced banking operations in March 2018, has got the status of a Scheduled Bank.

Functions of Commercial Banks

The two most distinctive features of a commercial bank are borrowing and lending, i.e. acceptance of deposits and lending of money to projects to earn Interest (profit). In short, banks borrow to lend. The rate of interest offered by the banks to depositors is called the borrowing rate while the rate at which banks lend out is called lending rate.

The difference between the rates is called 'spread' which is appropriated by the banks. Mind, all financial institutions are not commercial banks because only those which perform dual functions of (i) accepting deposits and (ii) giving loans are termed as commercial banks. For example, post offices are not bank because they do not give loans. Functions of commercial banks are classified in to two main categories: (A) Primary functions and (B) Secondary functions.

(A) PRIMARY FUNCTIONS:

- **It accepts deposits:**

A commercial bank accepts deposits in the form of current, savings and fixed deposits. It collects the surplus balances of the Individuals, firms and finances the temporary needs of commercial transactions. The first task is, therefore, the collection of the savings of the public. The bank does this by accepting deposits from its customers. Deposits are the lifeline of banks.

Deposits are of three types as under:

(i) Current account deposits:

Such deposits are payable on demand and are, therefore, called demand deposits. These can be withdrawn by the depositors any number of times depending upon the balance in the account. The bank does not pay any Interest on these deposits but provides cheque facilities. These accounts are generally maintained by businessmen and Industrialists who receive and make business payments of large amounts through cheques.

(ii) Fixed deposits (Time deposits):

Fixed deposits have a fixed period of maturity and are referred to as time deposits. These are deposits for a fixed term, i.e., period of time ranging from a few days to a few years. These are neither payable on demand nor they enjoy cheque facilities.

They can be withdrawn only after the maturity of the specified fixed period. They carry higher rate of interest. They are not treated as a part of money supply Recurring deposit in which a regular deposit of an agreed sum is made is also a variant of fixed deposits.

(iii) Savings account deposits:

These are deposits whose main objective is to save. Savings account is most suitable for individual households. They combine the features of both current account and fixed deposits. They are payable on demand and also withdraw able by cheque. But bank gives this facility with some restrictions, e.g., a bank may allow four or five cheques in a month. Interest paid on savings account deposits in lesser than that of fixed deposit.

- **It gives loans and advances:**

The second major function of a commercial bank is to give loans and advances particularly to businessmen and entrepreneurs and thereby earn interest. This is, in fact, the main source of income of the bank. A bank keeps a certain portion of the deposits with itself as reserve and gives (lends) the balance to the borrowers as loans and advances in the form of cash credit, demand loans, short-run loans, overdraft as explained under.

(i) Cash Credit:

An eligible borrower is first sanctioned a credit limit and within that limit he is allowed to withdraw a certain amount on a given security. The withdrawing power depends upon the borrower's current assets, the stock statement of which is submitted by him to the bank as the basis of security. Interest is charged by the bank on the drawn or utilised portion of credit (loan).

(ii) Demand Loans:

A loan which can be recalled on demand is called demand loan. There is no stated maturity. The entire loan amount is paid in lump sum by crediting it to the loan account of the borrower. Those like security brokers whose credit needs fluctuate generally, take such loans on personal security and financial assets.

(iii) Short-term Loans:

Short-term loans are given against some security as personal loans to finance working capital or as priority sector advances. The entire amount is repaid either in one instalment or in a number of instalments over the period of loan.

INVESTMENT:

Commercial banks invest their surplus fund in 3 types of securities:

(i) Government securities, (ii) Other approved securities and (iii) Other securities. Banks earn interest on these securities.

(B) SECONDARY FUNCTIONS:

Apart from the above-mentioned two primary (major) functions, commercial banks perform the following secondary functions also.

- **Discounting bills of exchange or bundles:** A bill of exchange represents a promise to pay a fixed amount of money at a specific point of time in future. It can also be encashed earlier through discounting process of a commercial bank. Alternatively, a bill of exchange is a document acknowledging an amount of money owed in consideration of goods received. It is a paper asset signed by the debtor and the creditor for a fixed amount payable on a fixed date. It works like this.

Suppose, A buys goods from B, he may not pay B immediately but instead give B a bill of exchange stating the amount of money owed and the time when A will settle the debt. Suppose, B wants the money immediately, he will present the bill of exchange (Hundi) to the bank for discounting. The bank will deduct the commission and pay to B the present value of the bill. When the bill matures after specified period, the bank will get payment from A.

- **Overdraft facility:**

An overdraft is an advance given by allowing a customer keeping current account to overdraw his current account up to an agreed limit. It is a facility to a depositor for overdrawing the amount than the balance amount in his account.

In other words, depositors of current account make arrangement with the banks that in case a cheque has been drawn by them which are not covered by the deposit, then the bank should grant overdraft and honour the cheque. The security for overdraft is generally financial assets like shares, debentures, life insurance policies of the account holder, etc.

- **Agency functions of the bank:**

The bank acts as an agent of its customers and gets commission for performing agency functions as under:

(i) Transfer of funds:

It provides facility for cheap and easy remittance of funds from place-to-place through demand drafts, mail transfers, telegraphic transfers, etc.

(ii) Collection of funds:

It collects funds through cheques, bills, bundles and demand drafts on behalf of its customers.

(iii) Payments of various items:

It makes payment of taxes. Insurance premium, bills, etc. as per the directions of its customers.

(iv) Purchase and sale of shares and securities:

It buys sells and keeps in safe custody securities and shares on behalf of its customers.

(v) Collection of dividends, interest on shares and debentures is made on behalf of its customers.

(iv) Acts as Trustee and Executor of property of its customers on advice of its customers.

(vii) Letters of References:

It gives information about economic position of its customers to traders and provides similar information about other traders to its customers.

- **Performing general utility services:**

The banks provide many general utility services, some of which are as under:

(i) Traveller's cheques .The banks issue traveler's cheques and gift cheques.

(ii) Locker facility. The customers can keep their ornaments and important documents in lockers for safe custody.

(iii) Underwriting securities issued by government, public or private bodies.

(iv) Purchase and sale of foreign exchange (currency).

Another important function of Commercial Banks is **CREDIT CREATION**. which is creation of monetory resource.

CREDIT CREATION

Some Concepts:

1. Bank as a business institution – Bank is a business institution which tries to

maximize profits through loans and advances from the deposits. 2. Bank Deposits – Bank deposits form the basis for credit creation and are of two types:

a) Primary Deposits – A bank accepts cash from the customer and opens a deposit in his name. This is a primary deposit. This does not mean credit creation. These deposits simply convert currency money into deposit money. However, these deposits form the basis for the creation of credit.

b) Secondary or Derivative Deposits – A bank grants loans and advances and instead of giving cash to the borrower, opens a deposit account in his name. This is the secondary or derivative deposit. Every loan crates a deposit. The creation of a derivative deposit means the creation of credit.

3. Cash Reserve Ratio (CRR) – Banks know that all depositors will not withdraw all deposits at the same time. Therefore, they keep a fraction of the total deposits for meeting the cash demand of the depositors and lend the remaining excess deposits. CRR is the percentage of total deposits which the banks must hold in cash reserves for meeting the depositors' demand for cash.

4. Excess Reserves – The reserves over and above the cash reserves are the excess reserves. These reserves are used for loans and credit creation.

5. Credit Multiplier – Given a certain amount of cash, a bank can create multiple times credit. In the process of multiple credit creation, the total amount of derivative deposits that a bank creates is a multiple of the initial cash reserves.

Q. What is Credit Creation?

Credit creation is the expansion of deposits. And, banks can expand their demand deposits as a multiple of their cash reserves because demand deposits serve as the principal medium of exchange. Credit creation separates a bank from other financial institutions.

Demand deposits are an important constituent of money supply and the expansion of demand deposits means the expansion of money supply. The entire structure of banking is based on credit. Credit basically means getting the purchasing power now and promising to pay at some time in the future. Bank credit means bank loans and advances. A bank keeps a certain part of its deposits as a minimum reserve to meet the demands of its depositors and lends out the remaining to earn income. The loan is credited to the account of the borrower. Every bank loan creates an equivalent deposit in the bank. Therefore, credit creation means expansion of bank deposits.

The two most important aspects of credit creation are:

1. Liquidity – The bank must pay cash to its depositors when they exercise their right to demand cash against their deposits.

2. Profitability – Banks are profit-driven enterprises. Therefore, a bank must grant loans in a manner which earns higher interest than what it pays on its deposits.

Q. How do banks create credit?

Credit creation is the expansion of deposits .The bank's credit creation process is based on the assumption that during any time interval, only a fraction of its customers genuinely need cash. Also, the bank assumes that all its customers would not turn up demanding cash against their deposits at one point in time. There are two ways of analyzing the credit creation process:

a) Credit creation by a single bank

b) Credit creation by the banking system as a whole

Credit creation by a single bank :-

In a single bank system, one bank operates all the cash deposits and claques. The process of creating credit is explained with the hypothetical example below

Table 1: Credit Creation by Single Bank

Rounds	Primary Deposits	Cash Reserves (r = 20%)	Credit Creation or Derivative Deposits (ΔD)
1. (Person A)	Rs. 1000 (Initial primary deposits)	Rs. 200	Rs. 800 (Initial excess reserves ΔR)
2. (Person B)	800	160	640
3. (Person C)	640	128	512
4. (Person D)	512	102	410
-	-	-	-
-	-	-	-
Total	5000	1000	4000

In a single bank system, one bank operates all the cash deposits and claques. The process of creating credit is explained with the hypothetical example below:

Let's assume that the bank requires to maintain a CRR of 20 percent.

- If a person (person A) deposits 1,000 rupees with the bank, then the bank keeps only 200 rupees in the cash reserve and lends the remaining 800 to another person (person B). They open a credit account in the borrower's name for the same.
- Similarly, the bank keeps 20 percent of Rs. 800 (i.e. Rs. 160) and advances the remaining Rs. 640 to person C.
- Further, the bank keeps 20 percent of Rs. 640 (i.e. Rs. 128) and advances the remaining Rs. 512 to person D.

This process continues until the initial primary deposit of Rs. 1,000 and the initial additional reserves of Rs. 800 lead to additional or derivative deposits of Rs. 4,000 (800+640+512+….).
Adding the initial deposits, we get total deposits of Rs. 5,000. In this case, the credit multiplier is 5 (reciprocal of the CRR) and the credit creation is five times the initial excess reserves of Rs. 800.

Multiple Credit Creation by the Banking System:-

The banking system has many banks in it and it cannot grant loans in excess of the cash it creates. When a bank creates a derivative deposit, it loses cash to other banks. The loss of deposit of one bank is the gain of deposit for some other bank. This transfer of cash within the banking system creates primary deposits and increases the possibility for further creation of derivative deposits. Here is an illustration to explain this process better:

Table 2 : Multiple Credit Creation by Banking System

Banks	Primary Deposits	Cash Reserves (r = 20%)	Credit Creation or Derivative Deposits (ΔD)
A	Rs. 1000 (Initial primary deposits)	Rs. 200	Rs. 800 (Initial excess reserves ΔR)
B	800	160	640
C	640	128	512
D	512	102	410
-	-	-	-
-	-	-	-
Total	5000	1000	4000

As explained above, the initial deposit of Rs. 1,000 with bank A leads to a creation of total deposits of Rs. 5,000.

Q. How is credit created when there are more than one bank?

Ans: Credit creation is the expansion of deposits .The bank's credit creation process is based on the assumption that during any time interval, only a fraction of its customers genuinely need cash. Also, the bank assumes that all its customers would not turn up demanding cash against their deposits at one point in time.

There are two ways of analyzing the credit creation process:

- Credit creation by a single bank
- Credit creation by the banking system as a whole

Let's assume that the banks require to maintain a CRR of 20 percent.

- If a Bank (Bank A) deposits 1,000 rupees with the bank, then the bank keeps only 200 rupees in the cash reserve and lends the remaining 800 to another Bank(Bank B). They open a credit account in the borrower's name for the same.
- Similarly, the bank B keeps 20 percent of Rs. 800 (i.e. Rs. 160) and advances the remaining Rs. 640 to Bank C.

- Further, the bank keeps 20 percent of Rs. 640 (i.e. Rs. 128) and advances the remaining Rs. 512 to Bank D.
  This process continues until the initial primary deposit of Rs. 1,000 and the initial additional reserves of Rs. 800 lead to additional or derivative deposits of Rs. 4,000 (800+640+512+….).

Adding the initial deposits, we get total deposits of Rs. 5,000. In this case, the credit multiplier is 5 (reciprocal of the CRR) and the credit creation is five times the initial excess reserves of Rs. 800.

Q. What are the limitations of Credit Creation?

Ans: Credit creation is the expansion of deposits . There are specific limitations on the power to create deposits. While banks would prefer an unlimited capacity for creating credit to increase profits, there are many limitations. These limitations make the process of creating credit non-profitable. Therefore, a bank continues to create additional credit as long as:

- There is a negligible chance of the loans turning into bad debts
- The interest rate that banks charge on loans and advances is greater than the interest that the bank gives to depositors for the money deposited in the bank.

Various draw backs are:

- **Cash Reserve Ratio:** The credit creation power of banks depends upon the amount of cash they possess.The larger the cash, the larger the amount of credit that can be created by banks.

Thus, the bank's power of creating credit is limited by the cash it possesses.

- **Availability of Adequate and Proper Securities**: If proper securities are not available with the public, a bank cannot create credit. As Crowther has written—"the bank does not create money out of thin air, it transmutes other forms of wealth into money."
- **Keeping of Reserve with the Central Bank**: Every affiliated and attached bank has to keep certain reserves with the Central Bank of the country. The Central Bank keeps on

changing the percentages of these reserves from time to time. When the Central Bank increases the percentages of these reserves, then the power of the commercial banks to create credit is reduced in the same proportion.

- Banking Habits of the People:The banking habits of the people are an important factor which governs the power of credit creation on the part of banks. If people are not in the habit of using cheques, the grant of loans will lead to the withdrawal of cash from the credit creation stream of the banking system. This reduces the power of banks to create credit to the desired level.
- Volume of Currency in Circulation: Volume of currency in circulation is an important factor of creation of credit. If the primary deposits are large, then the derivative deposits created on their basis will also be large. But the volume of primary deposits is closely connected with the actual volume of currency in circulation.
- If heavy with-drawl of Cash by the Borrowers: If the borrowers will withdraw money in cash, then the balance of deposits will be disturbed. With the withdrawal of cash, the excess reserves of the banks are automatically reduced. This reduces the power of credit creation.
- **Existence of Cash Transactions in the Economy**: This system of doing transaction sets another limitation on the power of the banks to create credit. In under-developed area most of the transactions have to be effected in cash. This puts a question as to what extent banks power to create credit is reduced.
- **Economic Conditions of Trade and Business**: Banks cannot continue to create credit limitlessly. Their power to create credit depends upon the economic climate present in the country. If there are boom times, there is a greater scope of profitable investment and thus greater demand for bank loans on the part of businessmen.
- **If Good Collateral Securities are not Available**: We are aware that every loan made by the bank must be backed by some valuable security like stocks, shares, bills and bonds etc. If these collateral securities are not available in sufficient number the banks cannot expand their lending activities and consequently cannot expand credit in the economy.
- **It is Essential to Maintain Statutory Liquidity Ratio**: The Commercial Banks under law are required to maintain a second line of defence in the form of the liquid assets. In India it has become essential to keep 34% of the assets in liquid forms. The liquid assets have been considered as government bonds and securities, treasury bills and other approved securities which can be en-cashed quite easily in emergency.

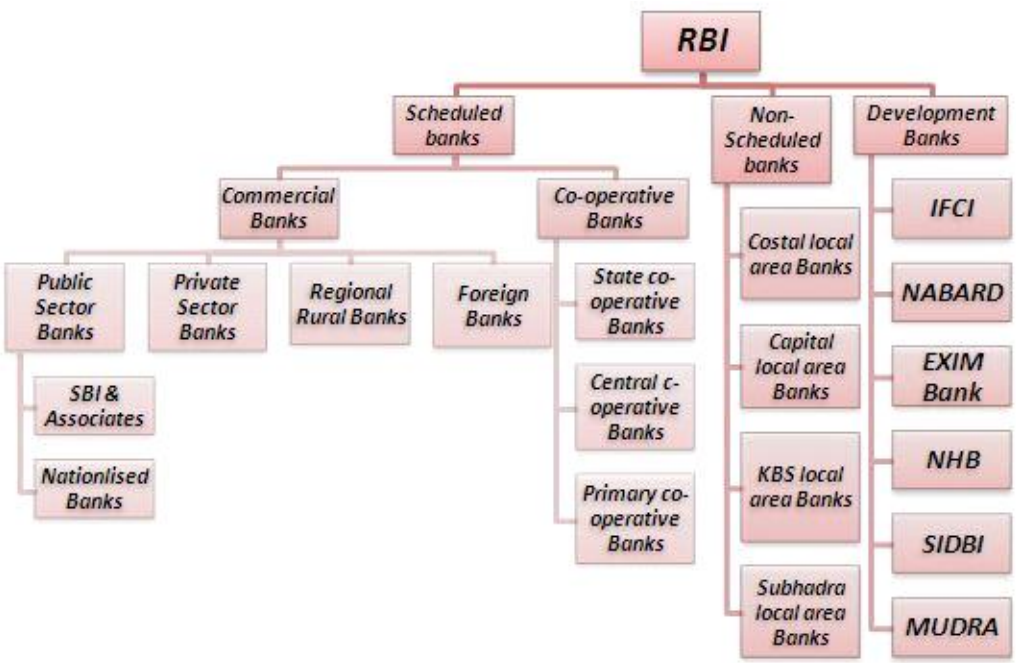
Such restrictions reduce the lendable resources with the banks and curtail their power to create credit to that extent.

- **If the Behaviour of Other Banks is Not Co-operative**: If some of the banks do not advance loans to the extent required of the banking system, the chain of credit expansion will be broken. The effect will be that the banking system will not operate properly.

Q. How CRR affects credit creation?

If the Cash Reserve Ratio (CRR) is increased by the RBI, its impact on the expansion of credit creation will be to decrease it. In short, credit creation is the reciprocal of the CRR.

BANKING SYSTEM IN INDIA



The Banking system of a country is an important pillar holding up the financial system of the country's economy. The major role of banks in a financial system is the mobilization of deposits and disbursement of credit to various sectors of the economy. The existing, elaborate banking structure of India has evolved over several decades.

STRUCTURE OF THE INDIAN BANKING SYSTEM

RESERVE BANK OF INDIA is the central bank of the country and regulates the banking system of India. The structure of the banking system of India can be broadly divided into scheduled banks, non-scheduled banks and development banks.

SCHEDULED BANKS Bank's that are included in the second schedule of the Reserve Bank of India Act, 1934 are considered to be scheduled banks.

All scheduled banks enjoy the following facilities:

- Such a bank becomes eligible for debts/loans on bank rate from the RBI
- Such a bank automatically acquires the membership of a clearing house.

NON SCHEDULED BANKS All the banks which are not included in the second schedule of the Reserve Bank of India Act, 1934. They are not eligible to borrow from the RBI for normal banking purposes except for emergencies.

Scheduled banks are further divided into commercial and cooperative banks.

Scheduled, Non-Scheduled Banks and Development Banks

COMMERCIAL BANKS

The institutions that accept deposits from the general public and advance loans with the purpose of earning profits are known as Commercial Banks.

Commercial banks can be broadly divided into public sector, private sector, foreign banks and RRBs.

- **Public Sector Banks** The majority stake is held by the government. After the recent amalgamation of smaller banks with larger banks, there are **12 public sector banks** in India as of now. **Largest Public Sector Bank is State Bank of India with headquarters in Mumbai.**

List of Nationalized Banks *(Government Shareholding%,as of 30 June 2021)*

- State Bank of India (57.6%)
- Bank of Baroda (63.97%)
- Canara Bank (62.93%)
- Punjab National Bank (73.15%)
- Indian Bank (79.86%)
- Union Bank of India (83.49%)
- Bank of India (81.41%)
- Central Bank of India (93.08%)
- Bank of Maharashtra (90.97%)
- UCO Bank (95.39%)
- Indian Overseas Bank (96.38%)
- Punjab and Sind Bank (97.07%)

- **Private Sector Banks** are banks where the major stakes in the equity are owned by private stakeholders or business houses. At present there are **21 private sector banks**

in India.A few major private sector banks in India are HDFC Bank, Kotak Mahindra Bank, ICICI Bank etc. **Largest private sector bank in terms of assets is HDFC with headquarters in Mumbai.**
List of PVT Sector banks :- https://moneymint.com/list-of-private-banks-in-india/

- **Foreign Bank** is a bank that has its headquarters outside the country but runs its offices as a private entity at any other location outside the country. Such banks are under an obligation to operate under the regulations provided by the central bank of the country as well as the rule prescribed by the parent organization located outside India. **Largest foreign bank in India is Standard Chartered Bank with headquarters in London.**
  Other Foreign Banks Operating in India are :- Citi Bank, Bank of America, Barclays Bank, HSBC India, Deutsche Bank, and Royal Bank of Scotland.

- **Regional Rural Banks** were established under the Regional Rural Banks Ordinance, 1975 with the aim of ensuring sufficient institutional credit for agriculture and other rural sectors. The area of operation of RRBs is limited to the area notified by the Government. RRBs are owned jointly by the Government of India, the State Government and Sponsor Banks. An example of RRB in India is Arunachal Pradesh Rural Bank.
  Kerala Grameen Bank is the biggest RRB in india by business. It was formed in 2013 by the merging of North Malabar Bank and South Malabar Bank, headquartered at Malappuram in Kerala, India. The bank is jointly owned by Central and State Governments & sponsored by Canara Bank.

  List of RRBs Functioning in the Country:- https://financialservices.gov.in/list-rrbs-functioning-country

COOPERATIVE BANKS

A **Cooperative Bank** is a financial entity that belongs to its members, who are also the owners as well as the customers of their bank. They provide their members with numerous banking and financial services. Cooperative banks are the primary supporters of agricultural activities, some small-scale industries and self-employed workers. An example of a Cooperative Bank in India is Mehsana Urban Co-operative Bank.

At the ground level, individuals come together to form a Credit Co-operative Society. The individuals in the society include an association of borrowers and non-borrowers residing in a particular locality and taking interest in the business affairs of one another. As membership is practically open to all inhabitants of a locality, people of different status are brought together into the common organization. All the societies in an area come together to form a Central Co-operative Banks.

- ## Central Co-operative Banks:

These banks are organized and operated at the district level and can be of two types:

- Co-operative Banking Union
- Mixed control Co-operative Bank

In the first, the members of the bank are the co-operative societies only. However, in the second, the members can be co-operative societies as well as individuals. The central co-operative banks lend money mainly to the affiliated primary societies with typical loan tenure lending between 1 to 3 years.

Here's a look at the 10 best performing co-operative banks in India.

- Saraswat Co-operative Bank.
- Cosmos Co-operative Bank.
- Shamrao Vithal Co-operative Bank (SVC Bank)
- Abhyudaya Co-operative Bank Ltd.
- Bharat Co-operative Bank.
- TJSB Co-operative Bank.
- Janata Co-operative Bank.
- Kalupur Commercial Co-operative Bank.
- NKGSB Co-operative Bank.
- The Ahmedabad Mercantile Co-operative Bank.

SOURCE : https://www.nelito.com/blog/the-top-10-cooperative-banks-in-india-2022.html

2. State Co-operative Banks:

These banks are organized and operated at the district level and rest at the top of the hierarchy in the co-operative credit structure.
With the help of State Co-operative Banks (SCBs), the RBI funds the co-operative institutions. These banks also get loans at an interest rate of 1% to 2% lower than the standard bank rate.

- The Andaman and Nicobar State Co-operative Bank Ltd. ...
- The Andhra Pradesh State Co-operative Bank Ltd. ...
- The Arunachal Pradesh State co-operative Apex Bank Ltd. ...
- The Assam Co-operative Apex Bank Ltd. ...
- The Bihar State Co-operative Bank Ltd. ...
- The Chandigarh State Co-operative Bank Ltd.

3. Primary Co-operative Banks:

These offer credit services in the urban and semi-urban regions. Thus, they are not considered agricultural credit societies.
Primary Co-Operative Banks receive concessional refinance services from RBI and IDBI from time to time for them to offer housing loans and other types of loans that can be used by small businesses.

Cooperative banks are further divided into two categories - **urban and rural.**

- **Rural cooperative Banks are either short-term or long-term.**
- Short-term cooperative banks can be subdivided into State Co-operative Banks, District Central Co-operative Banks, Primary Agricultural Credit Societies.

- Long-term banks are either State Cooperative Agriculture and Rural Development Banks (SCARDBs) or Primary Cooperative Agriculture and Rural Development Banks (PCARDBs).
- **Urban Co-operative Banks (UCBs) refer to primary cooperative banks located in urban and semi-urban areas.**

DEVELOPMENT BANKS

Financial institutions that provide long-term credit in order to support capital-intensive investments spread over a long period and yielding low rates of return with considerable social benefits are known as **Development Banks**. The major development banks in India are; Industrial Finance Corporation of India (IFCI Ltd), 1948, Industrial Development Bank of India' (IDBI) 1964, Export-Import Banks of India (EXIM) 1982, Small Industries Development Bank Of India (SIDBI) 1989, National Bank for Agriculture and Rural Development (NABARD) 1982.

The banking system of a country has the capability to heavily influence the development of a country's economy. It is also instrumental in the development of rural and suburban regions of a country as it provides capital for small businesses and helps them to grow their business. The organized financial system comprises Commercial Banks, Regional Rural Banks (RRBs), Urban Co-operative Banks (UCBs), Primary Agricultural Credit Societies (PACS) etc. caters to the financial service requirement of the people. The initiatives taken by the Reserve Bank and the Government of India in order to promote financial inclusion have considerably improved the access to the formal financial institutions. Thus, the banking system of a country is very significant not only for economic growth but also for promoting economic equality.

What is the role of Reserve Bank of India (RBI) in Indian Economy?

From time to time, we read and watch news about the Reserve Bank of India (RBI) implementing some policies, increasing or decreasing some complex sounding rates, the RBI Governor talking about how inflation is rising, etc. Occasionally we might also hear a friend from finance background talk about how the latest act of RBI is going to make a difference in our daily lives and all we do is stand there nodding our heads in oblivion.

For an average Indian, all of these news articles seem to be coming straight out of the complex world of finance and economics. But have you ever wondered what does the RBI actually do and what role does it play in the Indian economy? Well, that's a natural question to ask and you're probably not alone wondering about it. So let's understand what does the RBI do.

Who is the RBI?

RBI is India's Central Bank. Every country has its own Central Bank. The US has Federal Reserve Bank (FED) and England has Bank of England (BOE) while the whole of Europe has European Central Bank (ECB). Simply put the role of a Central Bank is to monitor a country's economy and stabilize it by using its various policies. A Central Bank acts like an adviser to the Government on issues related to the economy. As opposed to popular belief, the RBI is NOT controlled by the Government but instead it works as an independent institution.

Structure of the RBI

The RBI was founded in 1935 to tackle the economic difficulties arising in British ruled India after the First World War. Since then it has undergone a lot of changes in its organizational structure. Currently, the RBI consists of a central board of directors that overlooks its functioning.

The board of directors is formed of 21 members:

Governor – appointed by the Government for a 4 year term.

Deputy Governors – up to 4.

Executive Directors – nominated from various fields and regions and also 2 directors nominated by the Government from the Ministry of Finance.

Role of RBI

RBI has 7 primary functions. Each function has an objective of managing a particular part of the economy.

1. Issuer of Currency

The RBI has the sole right to issue new currency notes and coins, exchanges or destroy currency not fit for circulation.

Objective: To give the public adequate quantity of supplies of currency notes and coins and in good quality.

2. Monetary Authority

RBI formulates, implements and monitors the monetary policy. This policy is the most important tool that the RBI has. Using this policy RBI manages the interest rates offered by banks on loans and deposits and which affects the inflation and deflation in the country. In simple words, lower rates give rise to higher inflation and vice versa.

Objective: To maintain price stability while keeping in mind the objective of growth.

3. Manager of Foreign Exchange

RBI also manages the flow of foreign currency in Indian economy by enforcing the Foreign Exchange Management Act, 1999. As part of this function, the RBI makes sure that the exchange rate value of Indian National Rupee is maintained in the international markets.

Objective: To facilitate external trade and payment and promote orderly development and maintenance of foreign exchange market in India.

4. Regulator and Supervisor of the Financial System

RBI prescribes broad parameters of banking operations within which the country's banking and financial system functions. It makes sure that the banks are following the issued guidelines by overlooking their financial operations and in cases of banking failures, RBI comes ahead to safeguard the depositors' money by bailing out the distressed bank.

Objective: To maintain public confidence in the system, protect depositors' interest and provide cost-effective banking services to the public.

5. Regulator and Supervisor of Payment and Settlement Systems

RBI introduces and upgrades safe and efficient modes of payment systems in the country to meet the requirements of the public at large. This includes implementing various advanced technologies like the NEFT, RTGS or the latest Unified Payment Interface (UPI) or overlooking the operations of National Financial Switch (NFS) which is necessary for ATMs.

Objective: To maintain public confidence in payment and settlement system

6. Related Functions

Banker to the Government: performs merchant banking function for the central and the state governments; also acts as their banker. This includes dealing with financial securities issued by the Government like treasury bills, infrastructure bonds, etc.

Banker to the banks: To maintains banking accounts of all scheduled banks. This includes managing the minimum reserve capital balance required to be held by the banks with the RBI.

7. Developmental Role

Performs a wide range of promotional functions to support national objectives. This includes work like providing timely credit to the productive sectors of the economy, creating institutions to build financial infrastructure like UPI, NEFT, etc., expanding access to affordable financial services and working on financial inclusion of all classes of the society.