CONTENTS

RBI AND ITS ROLE

The Banking system in India is regulated by the Reserve Bank of India (RBI) which was created by an Act in 1935. RBI plays the role of monetary Authority as well as supervisor of banks in India.

Since Banking and Financial services deal with public money, it is necessary to have control and regulation relating to these so as to generate, maintain and promote confidence in financial/banking institutions. At the same time, it is necessary to protect depositors/investors interest. It is also necessary to ensure that banks are fair and efficient and also observe the rules and regulations of the industry.

The main objectives of establishing RBI were as follows :-

- **To maintain monetary stability** so that welfare measures can be delivered to the needy segment of the population.
- **To maintain financial stability** and ensure soundness of financial institutions.
- **To maintain stable, secure and efficient payment and settlemen[redacted]ystems.**
- **To ensure that credit extended by the financial system broadly conforms to the national priorities set by the Government.**
- **To regulate the money supply and credit allocation** in the economy so as to ensure price stability.
- **To promote the development of financial markets and systems** to enable efficient functioning.

Main functions of RBI are as follows :-

- **Issuance of Currency Notes :** RBI is the sole authority to issue currency notes in India.
- **Banker to the Government :** RBI provides banking services to Central and State Governments including collection and transfer of funds, management of public debt.
- **Bankers' Bank :** RBI acts as a Central Bank for all bankers in the country. Commercial and co-operative banks are required to fulfil the obligations of maintaining statutory reserves as well as reporting. The reserves include Cash Reserve Ratio (CRR) as well as Statutory Liquidity Ratio (SLR) which is to be kept at the rates prescribed from time to time as a percentage of Net Demand and Time Liabilities. All banks, whether they are Scheduled or Non-Scheduled, have to maintain the reserves at these rates.
- **Supervision of Banks :** Banking supervision functions have now been delegated to the Board of Financial Supervision under the aegis of RBI. The supervisory powers of RBI include – issuing licences for new banks and for starting new branches, prescribing minimum capital and reserves, maintaining CRR and other reserves, inspect the working of banks operating in India, conduct investigations into complaints, irregularities, frauds relating to banks and their customers, control and approve appointments, re-appointments, termination of Chairmen and MD & CEOs of private banks.
- **Developing the financial system :** This is one of the important functions of RBI and over the years, RBI has created specialized financial institutions such as the NABARD (National Bank for Agriculture and Rural Development), Export Import Bank of India, Deposit Insurance and Credit Guarantee Corporation of India (DICGC). RBI has also initiated several activities such as Bill Market Scheme, Lead Bank Scheme, Inventory norms for Bank credit, Credit Authorisation Scheme, Consortium Financing, Priority Sector Credit scheme etc.
- **Exchange Control :** RBI has been given the task of maintaining the external value of rupee vis-à-vis foreign currencies by regulating the foreign exchange market operating in India. Presently, RBI derives its powers from the Foreign Exchange Management Act (FEMA) on account of which it is responsible for exchange controls, management of rupee exchange rate against foreign currencies as well as foreign exchange reserves.

- **Monetary regulator :** RBI controls the money supply in the economy through various instruments such as Repo Rate, Bank rate, CRR, SLR, Open Market Operations and Credit control measures.

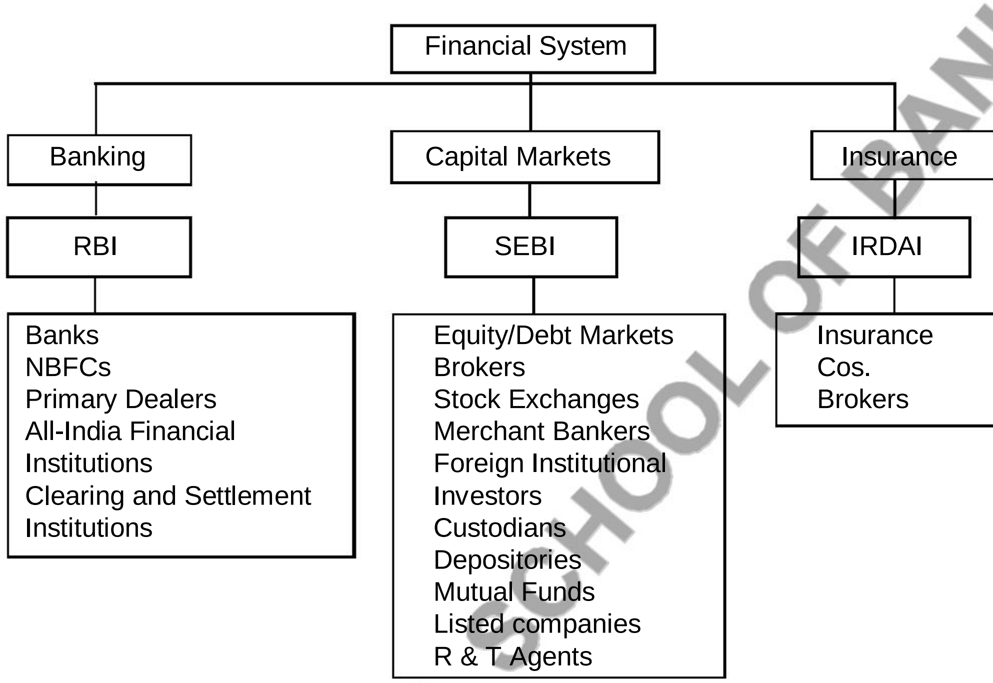
  With the establishment of the Monetary Policy Committee (MPC) in the year 2017, the monetary role of the RBI has undergone some change in that the exclusive right to decide benchmark rates now rests with the MPC where outside members, who are eminent persons in their respective fields, also participate in this process. Besides, inflation monitoring is now the main focus of the RBI. Growth depends on a number of policies/ initiatives taken by the Government.

MARKET STRUCTURE AND BANKS

The Indian Financial System is broadly a structure created to mobilize capital from various segments of the economy and distribute the same to various sectors that stand in need of them.

This process is assisted by various players called financial intermediaries with various products and services. Banks, Insurance Companies, Mutual funds are some of the examples in this regard.

The following diagram briefly explains the structure -



In India, Banks can be classified as Commercial Banks, Co-operative Banks, Development Banks, Regional Rural Banks, Payment Banks, Small Finance Banks and Local Area Banks. Commercial Banks include Public sector, Private sector and Foreign Banks (operating in India). All these banks require licence for opening and operating branches in India from RBI. Once they commence their operations, all banks have to comply with RBI regulations on a continuous basis.

Banks operating in India can be further classified as **Scheduled Banks and Non-scheduled Banks.** A scheduled bank is one which is included in the 2nd schedule of the RBI Act and is required to follow certain prescribed norms of maintaining reserves such as Cash Reserve Ratio (CRR) and Statutory Liquidity Ratio (SLR) in relation to their Net Demand and Time Liabilities (NDTL) i.e. deposits, submission of specified periodical returns, maintenance of specified books of account etc. They are also entitled to borrow from RBI under specified circumstances.

Co-operative Banks can be broadly classified into Urban Co-operative Banks and others. Urban Co-operative Banks are regulated by the respective State Government as well as RBI. Other Co-operative Banks are supervised by NABARD on behalf of RBI as well as the respective State Government. However, in case of Multi-state Co-operative Banks, they come under the jurisdiction of Central Government as well as RBI.

Development Banks are created by the Government of India under separate Acts. SIDBI, IIFCL, Mudra, NABARD, EXIM, IFCI, Tourism Finance Corporation of India etc. These institutions are involved in providing long-term funds to industry, exports, agriculture, tourism, infrastructure etc. All these institutions are also supervised by RBI.

Payment Banks and Small Finance Banks are new categories of banks started recently. While payment Banks are not permitted to grant loans, they can accept deposits upto Rs. one lakh. Their main function is collection and settlement.

Small Finance Banks are a type of niche banks. Small Finance Bank can provide basic banking services of acceptance of deposits and lending. They are required to cater to the banking needs of the population, who had no access to banking till now. They must have capital of Rs.100 crore.

Primary Dealers (PDs) are involved in the buying and selling of Government securities in primary and secondary markets. In terms of RBI regulations, all banks have to invest in Government securities to maintain the required level of SLR. Thus, the PDs are associated with the banking system.

Clearing and settlement system in India is yet another sphere of the financial market under the supervision and administration of RBI. Some of the functions under clearing and settlement are handled by the Clearing Corporation of India set up by RBI.

Non-Banking Financial Companies (NBFCs) are regulated by RBI and are allowed to raise money from the public by way of deposit and are also allowed to lend under leasing, hire purchase, discounting of bills etc.