NATIONAL JUDICIAL ACADEMY

धर्मेण धार्यते लोक

Heartiest welcome

to all Delegates
for this training programme

Reserve Bank of India & Banks

Monitor, Mentor & Regulator

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Brief background of RBI

- Chamberlin Commission (1914) recommended amalgamation of three Presidency Banks in Imperial Bank of India.
- In 1926, the Royal Commission on Indian Currency and Finance (Hilton Young Commission) recommended establishment of a Central Bank to be called as Reserve Bank of India.
- The Reserve Bank of India (RBI) is India's central banking institution.
- It was established on 1 April 1935 during the British Raj in accordance with the provisions of the Reserve Bank of India Act, 1934
- The Reserve Bank of India was nationalized in 1949 under the Reserve Bank (Transfer of Public Ownership)Act, 1948.

Brief background of RBI

- The headquarters of the Reserve Bank of India are located in Mumbai. RBI has 19 regional offices most of them in state capitals and 9 sub-offices.
- The Reserve Bank's affairs are governed by a Central Board of Directors. The board is appointed by the Government of India in keeping with the Reserve Bank of India Act.
- Consequently, a special legislation called the Banking Companies Act was passed in March 1949 which was renamed as Banking Regulation Act in March 1966.

Preamble of RBI Act 1934

- **The preamble of the Reserve Bank of India Act, 1934 states that the objectives of the RBI are "*to <u>regulate the issue of bank notes</u> and the <u>keeping of reserves</u> with a view to <u>securing monetary stability</u> in India and generally to <u>operate the currency and credit</u> system of the country to its advantage.*"**

Organizational Structure

- Central Board of Directors consist of 21 members.
- It is constituted as follows

  a) One Governor- Dr. Urjit Patel

  b) Four Deputy Governors – B.P. Kanungo, Dr. Viral Acharya, N.S.Vishwanathan, S.S. Mundhra

  c) Fifteen Directors
- Local Boards: One each for the four regions of the country in Mumbai, Calcutta, Chennai and New Delhi consist of five members each & appointed by the Central Government for a term of four years.

Functions of RBI

Issue Dept.

- ❖ Issue Currency
- ❖ Exchange of notes
- ❖ Destruction of soiled

  and fake notes
- ❖ Currency Chests
- ❖ Cash Txn Report
- ❖ Suspicious Txn Report
- ❖ Cross Border Txn
- ❖ NPO Report

D.B.O.D.

- ❖ Licensing
- ❖ Capital Adequacy
- ❖ IRAC status
- ❖ Audit of Banks
- ❖ ALM
- ❖ Mgt. of FEMA
- ❖ Fraud Mgt.
- ❖ Rehab of poor functioning banks
- ❖ Mgt. Control
- ❖ Credit Control
- ❖ Payment & Settlement

Main functions of RBI

- Monetary authority
- Issuer of currency
- Banker, Agent and Financial Advisor to the Govt.
- Banker to the Banks
- Regulation and supervision of the banking and financial system
- Management of Foreign Exchange
- Regulation and Supervision of the Payment and Settlement

Monetary authority

- The main objectives of monetary policy are:
- Maintaining price stability
- Ensuring adequate flow of credit to the productive sectors of the economy to support economic growth
- Financial stability
- RBI formulates, implements and monitors the monetary policy

Issue of currency

- **The Reserve Bank is the nation’s sole note issuing authority.**
- **Along with the Government of India, RBI is responsible for the design and production and overall management of the nation’s currency, with the goal of ensuring an adequate supply of clean and genuine notes.**
- **The Reserve Bank also makes sure there is an adequate supply of coins, produced by the government and also destroys currency and coins not fit for circulation.**
- **It brings uniformity to note issue and keeps the public faith in the paper currency alive.**

Issue of currency

- Issue Dept. replenishes the stock of currency against equivalent transfer of eligible assets. Those eligible assets are:
- Gold coins & bullion
- Foreign Securities
- Rupee coins
- Govt. of India securities
- Bills of Exchange & Promissory Notes
- There were 4075 Currency Chests and 3746 Small coins Depot as on 31st March 2016.

Banker, Agent and Financial Advisor to the Govt.

- It keeps the banking accounts of the government.
- It advances short-term loans to the government and raises loans from the public. It manages public debt.
- It purchases and sells through bills and currencies on behalf to the government.
- It receives and makes payment on behalf of the government.
- It advises the government on economic matters like deficit financing price stability, management of public debt etc.

Banker to the Banks

- Enabling smooth, swift clearing and settlement of interbank obligations.
- Providing an efficient means of funds transfer for banks.
- Enabling banks to maintain their accounts with RBI for purpose of statutory reserve requirements and maintain transaction balances.
- Acting as lender of the last resort.

Regulation of the Banking & financial System

- **As the regulator and supervisor of the banking system, the Reserve Bank protects the interests of depositors, ensures a framework for orderly development and conduct of banking operations.**
- **RBI's objectives are to maintain public confidence in the system, protect depositors' interest and provide cost-effective banking services to the public.**
- **RBI prescribes broad parameters of banking operations within which the country's banking and financial system functions**

Relationship between RBI & Commercial Banks

- **As a Supervisory and controlling authority:**

a) Licensing of Banking Companies- Sec. 22

b) Permission to open new branches or change in location of existing branch- Sec. 23

c) Power to inspect Banks- Sec. 35

d) Powers to issue directions- Sec. 35-A & 36

e) Control over top management, appointment or termination of Chairman, MD- Sec. 36AA

Relationship between RBI & Commercial Banks

- **As a Controller of Credit:**
- **By changing statutory requirement of reserves i.e. CRR (Sec. 42) & SLR (Sec. 24)**
- **By issuing directives regarding purpose of advances, margins to be maintained and maximum amount to be advanced, rate of interest etc.**
- **By changing the Bank Rate**
- **By purchasing and rediscounting of bills**
- **Collection and furnishing of credit information: CRILC, Central Fraud Registry**

Relationship between RBI & Commercial Banks

- **As a Controller of Credit: There are two methods of credit control.**

a) **General or quantitative method**

b) **Selective or qualitative method**

Bank Rate policy, variable reserve requirements Statutory liquidity requirement and open market operations falls in category of General method.

The various directives issued by the RBI restricting the quantum and other terms of granting credit against certain specified commodities constitute the Selective Credit Control. Advances against i) Foodgrains ii) Pulses iii) Oilseeds iv) Vegetable Oils v) Cotton and vi) Sugar have been covered by SCC.

Relationship between RBI & Commercial Banks

- The main difference between the general and selective credit control methods is that the former influence the cost and overall volume of credit granted by the Banks. They affect the credit granted to the whole economy whereas selective controls affect the flow of credit to only specified sector of the economy, wherein speculative tendency and rising trend of prices, due to excessive bank credit is noticed.

- Regulation of credit by RBI means regulations of the quantum of cash reserves of commercial banks. The cash reserves increases through i) a rise in bank deposits ii) borrowings from RBI or iii) sale of investments

Management of Foreign Exchange

- RBI regulates transactions related to the external sector and facilitates the development of the foreign exchange market.
- RBI buys and sells foreign currency to maintain the exchange rate of Indian Rupee v/s foreign currencies like dollar, euro etc.
- The RBI is the custodian of the country's foreign exchange reserves, i.e., it is vested with the responsibility of managing the investment and utilization of the reserves in the most advantageous manner.
- Managing the foreign currency assets and gold reserves of the country.

Regulator and Supervisor of Payment and Settlement Systems

- The Payment and Settlement Systems Act of 2007 (PSS Act) gives the Reserve Bank oversight authority, including regulation and supervision, for the payment and settlement systems in the country.
- In this role Reserve Bank focuses on the development and functioning of safe, secure and efficient payment and settlement mechanism.

Credit control function

- In modern times credit control is considered as the most crucial and important functional of a Reserve Bank.
- The Reserve Bank regulates and controls the volume and direction of credit by using quantitative and qualitative controls.
- Quantitative controls include the bank rate policy, the open market operations, and the variable reserve ratio.
- Qualitative or selective credit control, on the other hand includes rationing of credit, margin requirements, direct action, moral suasion publicity, etc

NPA Management

- **Special Mention Accounts**
- **IRAC Norms & Provisioning**
- **Asset Quality Review**
- **Restructuring- Flexible, SDR, S4A**
- **Insolvency & Bankruptcy Code**

Developmental Role of RBI

- Lastly, the RBI also has a developmental role in that it performs a variety of promotional functions directed at supporting national objectives.
- In pursuance of this function, the RBI has taken several promotional measures such as the establishment of financial corporations to ensure credit availability for the agricultural and industrial sector, the promotion of the establishment of Regional Rural Banks so that banking facilities may be available in the rural areas as well, the establishment of the Export-Import bank in India to finance exports and so on.

Developmental Role

- This role includes the development of the quality of banking system in India and ensuring that credit is available to the productive sectors of the economy.
- RBI performs a wide range of promotional functions to support national objectives.
- It also includes establishing institutions designed to build the country's financial infrastructure. E.g.: NABARD, SIDBI, IDBI Exim Bank etc.
- Expanding access to affordable financial services and promoting financial education & literacy.

Supervisory Functions of RBI

- **Granting license to banks & controlling the opening of new branches.**
- **Bank Inspection**
- **Control over Non-Bank Financial Institutions: The Non Bank Financial Institutions are not influenced by the working of a monitory policy. RBI has a right to issue directives to the NBFIs from time to time regarding their functioning.**
- **Implementation of the Deposit Insurance Scheme: In order to protect the deposits of small depositors, RBI work to implement the Deposit Insurance Scheme in case of a bank failure. (For bank deposits Rs. 1.00 lakh)**

Role of RBI in economic development

- Development of banking system
- Development of financial institutions
- Development of backward areas
- Economic stability
- Economic growth
- Proper interest rate structure
- Miscellaneous

Quantitative Measures of Credit Control under Monetary Policy

- **Bank Rate : Rate at which RBI discounts bills of commercial banks. (Present Bank Rate- 6.25%)**
- **Repo Rate : (Present Repo Rate – 6%) It is also known as the benchmark interest rate at which the RBI lends money to the banks for a short-term (max. 90 days). Generally, repo rates are cut down whenever the country needs to progress in banking and economy.**
- **Reverse Repo Rate : (Present RR Rate- 5.75%) Reverse Repo rate is the short term borrowing rate at which RBI borrows money from banks.**
- **Repo Rate signifies the rate at which liquidity is injected into the banking system by RBI, whereas Reverse Repo rate signifies the rate at which the central bank absorbs liquidity from the banks.**

Interest rates		
What is bank rate?	The rate at which a bank can borrow from the RBI	Any hike in the bank, repo and reverse repo rates will lead to a rise in interest rates in the economy and vice versa.
What is repo rate?	The rate at which RBI lends short-term money to banks against deposits.	
What is reverse repo rate?	The rate at which a bank can park excess short-term funds with the RBI.	

Quantitative Measures of Credit Control under Monetary Policy

- **Cash Reserve Ratio (CRR) : Portion of Deposit which commercial banks have to keep with RBI in the form of Cash Reserves. (Present CRR- 4%)**
- **Statutory Liquidity Rate (SLR): Portion of Total Deposit which commercial banks have to keep with RBI in the form of Liquid Assets viz – Gold, Cash or Approved Government securities. (Present SLR- 19.5%)**
- **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, thus it is an anti-inflationary impact.**

Quantitative Measures of Credit Control under Monetary Policy

- **Marginal Standing Facility Rate:** Banks can borrow up to 2.5% of their respective Net Demand and Time LiabilitiesThe important difference with repo rate is that bank can pledge government securities from SLR quota (up to 1%). Current MSF rate is 6.25%
- **Marginal Cost of FB Lending Rate (MCLR):** This rate is based on marginal cost of funds, tenor premium and negative carry on CRR. Present MCLR ranges from 7.70% to 8.05%. It is 5 maturities i.e. Overnight, One month, Three months, Six months & One year

Recent initiatives of RBI

- The Indian banking system consists of 27 public sector banks, 26 private sector banks, 46 foreign banks, 56 regional rural banks, 1,574 urban cooperative banks and 93,913 rural cooperative banks, in addition to cooperative credit institutions. Public-sector banks control more than 70 per cent of the banking system assets, thereby leaving a comparatively smaller share for its private peers.
- ICRA estimates that credit growth in India's banking sector would be at 7-8 per cent in FY 2017-18.

Latest Developments

- IndiaPost has received the final license from RBI to start its payment bank operations, thus becoming the third entity in India after Bharti Airtel and Paytm to receive payment bank license from RBI.
- The Government of India has announced demonetization of high denomination bank notes of Rs 1000 and Rs 500, with effect from November 08, 2016, in order to eliminate black money and the growing menace of fake Indian currency notes, thereby creating opportunities for improvement in economic growth.

Latest Developments

- The RBI has cut its key repo rate by 25 basis points to 6.25 per cent, in order to boost growth as according to RBI, the inflation momentum has moderated because of a normal monsoon.
- The RBI has allowed banks in India to raise funds through issuance of rupee-denominated bonds overseas, also called masala bonds, within the current limit of Rs 2,44,323 crore (US$ 36.6 billion) set for foreign investment in corporate bonds.

Developmental role of RBI

- For accelerating industrial investment, various term lending industrial finance institutions were established. E.g. IFCI, IDBI, SFCs, ICICI etc.
- The traditional concern for agriculture credit continued and Agriculture Finance Corporation was established in 1963 which was subsequently transformed in NABARD in 1982.
- UTI was established in 1964 to mobilize the resources from wider public and to provide an opportunity for retail investors to invest in capital market.
- Similarly, NHB (1980), IDFC (1990), DFHI (1988), CCIL (2001) were established.

Educative Role of RBI

- **RBI has two training colleges for its officers, viz. Reserve Bank Staff College, Chennai and College of Agricultural Banking, Pune.**
- **There are three autonomous institutions run by RBI namely National Institute of Bank Management (NIBM), Indira Gandhi Institute of Development Research (IGIDR), Institute for Development and Research in Banking Technology (IDRBT).**
- **There are also four Zonal Training Centres at Mumbai, Chennai, Kolkata and New Delhi.**

Moral Suasion (Mentor)

- Besides various credit control measures, RBI also resorts to the informal methods of persuasion. It arranges meetings and discussions with Chief Executives of the banks.
- Governor of RBI reviews credit trends at regular intervals and suggest corrective steps to suit prevailing situation.
- Social responsibility by way of Agri Debt Waiver
- BCSBI Code
- Financial inclusion
- The *Banking Ombudsman Scheme* has been formulated by the Reserve Bank of India (RBI) for effective addressing of complaints by bank customers.

Moral Suasion (Mentor)

- **Credit Guarantee Schemes for small industries especially MSME sector.**
- **Deposit Insurance (DICGC)**


ThAnK yOu