

325-BANKING MANAGEMENT

UNIT-1

INTRODUCTION TO BANKING

Banking is an industry that handles cash, credit, and other financial transactions. Banks provide a Safe place to Store extra cash and credit. They offer savings accounts, Certificates of Deposit, and checking accounts. Banks use these deposits to make loans. These loans include home mortgages, business loans, and car loans.

A Bank is a financial institution licensed to receive deposits and make loans. Two of the most common types of banks are commercial/retail and investment banks. Depending on type, a bank may also provide various financial services ranging from providing safe deposit boxes and currency exchange to retirement and wealth management.

Definition

Banking is defined as “Accepting of deposits of money from public for the purpose of Lending or Investment, repayable on demand or otherwise and withdrawable by cheque, draft, or otherwise”

Structure of 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.

Banks 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:

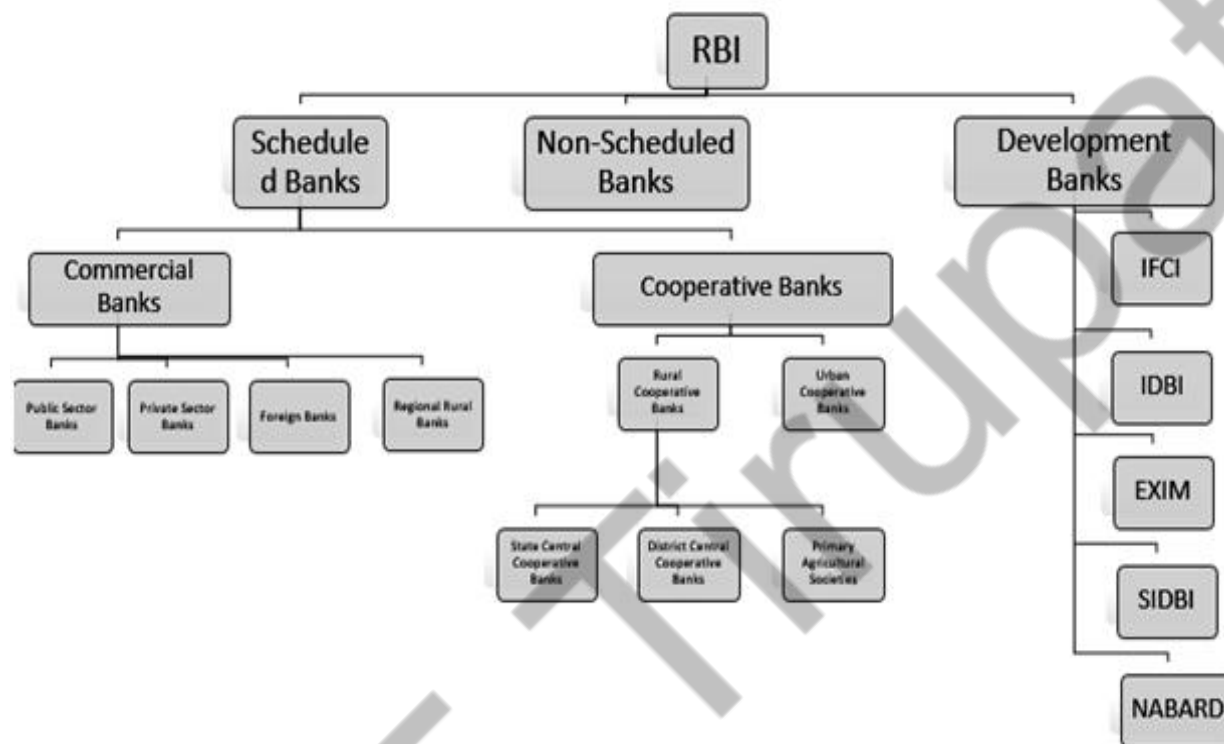
- Such a bank becomes eligible for debts/loans on bank rate from the RBI
- Such a bank automatically acquires the membership of a clearing house.

All banks which are not included in the second section of the Reserve Bank of India Act, 1934 are **Non-scheduled Banks**. 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.

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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.

- In **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. An example of Public Sector Bank is State Bank of India.
- **Private Sector Banks** are banks where the major stakes in the equity are owned by private stakeholders or business houses. A few major private sector banks in India are HDFC Bank, Kotak Mahindra Bank, ICICI Bank etc.
- A **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. An example of Foreign Bank in India is Citi Bank.

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- **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.

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.

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.

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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.

Scheduled Commercial Banks

The scheduled commercial banks are those banks which are included in the second schedule of RBI Act 1934 and which carry out the normal business of banking such as accepting deposits, giving out loans and other banking services. The major difference between Scheduled Commercial Banks and Scheduled Cooperative Banks is their holding pattern, since cooperatives are registered under the Cooperative Societies Act as cooperative credit institutions.

Scheduled Commercial Banks can be further divided into four groups:

- Public Sector Banks: This includes:
 - SBI & Associates
 - Nationalized Banks
 - Other Public Sector Banks
- Private Banks
- Foreign Banks
- Regional Rural Banks

Scheduled Commercial Banks (Public Sector)

At present, there are 27 Public Sector Banks in India including SBI (plus its 5 associates) and 19 nationalized banks. Further, there are two banks which have been categorized by RBI as "Other Public Sector Banks". IDBI and Bhartiya Mahila Bank come under this category.

Scheduled Commercial Banks (Private Banks)

In private sector banks, most of the capital is in private hands. There are two types of private sector banks in India viz. Old Private Sector Banks and New Private Sector Banks.

Foreign Banks

As of December 2014, there are 43 foreign banks from 26 countries operating as branches in India and 46 banks from 22 countries operating as representative offices in India. Most of the foreign banks in India are niche players. RBI policy towards presence of foreign banks in India is based upon two cardinal principles viz. reciprocity and single mode of presence. more details about regulation of Foreign Banks by RBI, click [here](#)

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Regional Rural Banks

Regional Rural Banks were started in 1970s due to the fact that even after nationalization, there were cultural issues which made it difficult for commercial banks, even under government ownership, to lend to farmers. **Each RRB is** owned by three entities with their respective shares as follows:

- Central Government → 50%
- State government → 15%
- Sponsor bank → 35%

They are regulated by NABARD.

Foreign Banks

A foreign bank branch is a type of foreign bank that is obligated to follow the regulations of both the home and host countries. Because the foreign bank branch has loan limits based on the total bank capital, they can provide more loans than subsidiary banks. That is because the foreign bank branch, while possibly small in one market, is technically part of a larger bank. Hence, it enjoys the capital base of the larger entity.

Understanding Foreign Bank Branches

Banks often open a foreign branch to provide more services to their multinational corporate clients. However, operating a foreign bank branch may be considerably more complicated because of the dual banking regulations that the foreign branch needs to follow.

For example, suppose that Bank of America opens a foreign bank branch in Canada. The branch would be legally obligated to follow both Canadian and American banking regulations in many cases. In actual practice, foreign bank branches are sometimes exempted from specific rules in one country or the other.

With globalization and capital markets maturing, the administrative burden of multiple regulatory standards might be offset by other operational economies of scale. These may include global branding, marketing, and product offerings best served by a single entity with numerous local branches.

Advantages of Foreign Bank Branches

Foreign bank branches tend to be more effective in countries with high taxes and nations where it is easy for international firms to enter the market.

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According to an article in the Journal of Banking and Finance, banks are more likely to organize themselves as branches in nations that have higher corporate taxes. Depending on the country, a branch of a foreign bank may be able to avoid some of the high taxes faced by domestic firms.

Foreign bank branches are also more likely to operate where they face lower regulatory barriers to entry. When it is easy to enter the market, a bank does not need to spend money setting up a subsidiary in the country.

Disadvantages of Foreign Bank Branches

Foreign bank branches may face special difficulties during an economic or political crisis. Since they operate in that foreign country during a crisis, they will be negatively impacted by events there. At the very least, foreign bank branches stand to lose money. At worst, they might have to deal with a run on the bank branch with little support from the foreign government.

A government in crisis is more likely to use its limited resources to support domestic banks. Foreign banks might be left to bail out their own branches. This situation is different from a subsidiary bank, which is technically a domestic company in the foreign country. Subsidiary banks are also sometimes joint ventures with domestic banks, further increasing the chances that the local government will support them.

Commercial Banks

Commercial Bank

As per the commercial bank definition, it is a financial institution whose purpose is to accept deposits from people and provide loans and other facilities. Commercial banks provide basic services of banking to their customers and small to medium-sized businesses.

What is Commercial bank?

A commercial bank is a financial institution that provides services like loans, certificates of deposits, savings bank accounts bank overdrafts, etc. to its customers. These institutions make money by lending loans to individuals and earning interest on loans. Various types of loans given by a commercial bank are business loans, car loans, house loans, personal loans, and education loans.

They give out these loans from the money deposited by their customers in different types of accounts. They use the deposits as capital for providing loans. Commercial banks are essential for the economy of a country because they help in creating capital, credit as well as liquidity in

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the market. These banks are generally physically located in cities but these days there are online banks are growing in numbers.

How commercial bank works?

Commercial banks offer basic services of banking to the public including individual customers as well as small and medium-sized businesses. Money is made by banks by charging for services and fees. The fees depend on the products given such as overdraft fees, fees for safe deposit boxes, late fees, etc. Various loans also consist of fees other than interest on loans.

Banks earn money by giving out loans and for that purpose they use funds from customer deposits. They charge higher interest rates on loans they give out and comparatively less rate of interest on the amount they get as deposits from their customers. For e.g., a bank may provide a 0.30 per cent rate of interest on savings account to its customers but charges a 4.8 per cent rate of interest annually for home loans.

Generally, commercial banks are situated in buildings where their customers come for using ATM machines and other banker window facilities. As internet technology has risen in recent years, most banks allow customers to do most services online. People can now make money transfers, deposits or make payments for bills online.

Importance of commercial banks

Commercial banks are essential for the economy because they create liquidity in the market and create capital besides providing their customers with essential services. Banks make sure liquidity in the market by lending out loans from the deposits of their customers.

What is commercial bank?

According to the commercial bank definition, it is a financial institution whose purpose is to accept deposits from customers and lend out loans.

What is commercial bank types?

Public sector banks, private sector banks, and regional rural banks are the types of commercial banks.

What is commercial bank functions?

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The basic functions are accepting deposits, lending out loans, transfer of money, and discounting bills of exchange.

Why are commercial banks important?

Commercial banks are important because they help in creating liquidity in the market.

Payment Bank

Definition: A payments bank is like any other bank, but operating on a smaller scale without involving any credit risk. In simple words, it can carry out most banking operations but can't advance loans or issue credit cards. It can accept demand deposits (up to Rs 1 lakh), offer remittance services, mobile payments/transfers/purchases and other banking services like ATM/debit cards, net banking and third party fund transfers.

Description: In September 2013, the Reserve Bank of India constituted a committee headed by Dr Nachiket Mor to study 'Comprehensive financial services for small businesses and low income households'. The objective of the committee was to propose measures for achieving financial inclusion and increased access to financial services.

The committee submitted its report to RBI in January 2014. One of the key suggestions of the committee was to introduce specialised banks or 'payments bank' to cater to the lower income groups and small businesses so that by January 1, 2016 each Indian resident can have a global bank account.

Why payments banks? The main objective of payments bank is to widen the spread of payment and financial services to small business, low-income households, migrant labour workforce in secured technology-driven environment.

With payments banks, RBI seeks to increase the penetration level of financial services to the remote areas of the country.

Existing prepaid payment instruments (PPI model) like Airtel Money does not give pay any interest on deposits.

Small Finance Banks

Small finance banks are those banks that operate in rural sections or sections of society that are excluded from the urban section. To help farmers, small business owners the small finance banks help Like all other banking organisations these types of banks i.e small finance banks also perform major tasks such as deposits and withdrawals.

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Small finance banks are registered under public limited companies under the Companies Act 2013. The main significance of small finance banks is to provide inclusion to underdeveloped areas. These banks provide provisions for saving vehicles to underserved or unserved sections of society.

These banks provide financing to the small business units in rural sections.

Who is Allowed to set up Small Finance Banks?

The functioning of small finance banks depends on if the resident individual has more than 10 years of banking experience. The companies registered, owned and controlled by residents will be eligible for setting up small finance banks. Small finance banks have the potential to make better opportunities unlike major banks because they solely focus on underserved people.

The promoters of small finance banks need to be eligible to be considered a part of small finance banks. RBI is usually the intelligent body behind reviewing the organisations, companies whole apply for being promoters of small finance banks.

Promoters' initial offering to the small finance banks should be at least 40% and gradually brought down throughout the years. The RBI needs to approve all the plans regarding the expansion of the small finance banks in the initial 5 years stage.

What is the Importance of Small Finance Banks?

Small finance banks have accepted deposits and lending money as their primary task. These banks can undertake activities like acting as distributors of various types of mutual funds and pension funds.

Importance of Small Finance Banks:

The small finance banks being an important part of the banking system have various important features that are mentioned below:

- The small finance banks have no restrictions on where they can operate
- They have open permission to operate in any desired location given they fall under proper proximity
- Small Finance Banks are just like any other commercial bank when it comes to risk management
- The company has to submit CRR and SLR like commercial banks
- The small finance banks should mainly focus on the important sectors like agriculture and small business
- The small business bank needs to have at least half of its loan portfolio as loans and advances to microfinance business
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List of Small Finance Banks

There are a total of 11 small finance banks that are recognised under RBI namely:

1. Au Small Finance Bank Limited
2. Capital Small Finance Bank Limited
3. Equitas Small Finance Bank Limited

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4. Suryoday Small Finance Bank Limited
5. Ujjivan Small Finance Bank Limited
6. Utkarsh Small Finance Bank Limited
7. ESAF Small Finance Bank Limited
8. Fincare Small Finance Bank Limited
9. Jana Small Finance Bank Limited
10. North East Small Finance Bank Limited
11. Shivalik Small Finance Bank Limited

Minimum Paid-Up Capital for Small Finance Bank

The RBI has assigned the minimum paid-up voting equity capital at ₹ 200 crores after changing it from ₹100 crores. The promoter of a small finance business can't hold voting equity shares for more than five years. If the promoter has an initial shareholder percentage above 40% then it is to be reduced to 40% within five years.

The small finance banks are to be listed if they achieve a net worth of ₹500 crores. The listing is supposed to happen within 3 years.

Minimum Capital for Small Finance Banks

The urban cooperative banks can function or convert themselves into a working small finance banks if they follow the guidelines mentioned by RBI to be a small finance bank. The net worth of these banks should be ₹100 crores and that is to be increased to ₹200 crore within 5 years. The small finance banks can offer up to only 15% of total capital funds as loans.

Conclusion

In the above article, it is mentioned in brief about the definition of small finance banks along with its significance and other information like who are allowed to be promoters and what amount of paid-up capital a small finance bank needs to have. The small finance banks have a huge role to play in regards to development in rural areas as these types of banks are the only mode of accessing incentives and schemes and other financial help when in need. The foreign shareholding of small finance banks is done under the guidance of Foreign Direct Investment (FDI). The small finance banks need to mention "small finance banks" in their names so they can be differentiated from other banks. They are looked after under the Reserve Bank of India Act, 1934 and the banking regulations Act 1949.

Types of Banking

Common types of banks prevalent in India include the following:

Scheduled and Non-Scheduled Banks

The banking sector is divided into scheduled and non-scheduled banks.

- Scheduled Banks are listed in the second schedule of the Reserve Bank of India (RBI) Act, 1934. The paid-up capital and collected funds of scheduled banks must be 5 Lakh and above. The RBI grants loans at the bank rate, and these banks are eligible to become clearing house members.

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- **Non-Scheduled Banks** are banks not listed in the second schedule of the RBI Act, 1934. The paid-up capital and collected funds are less than INR 5 Lakh. Such banks need not borrow funds from the RBI.

Commercial Banks

Commercial banks can be scheduled or non-scheduled and are regulated under the Banking Regulation Act, 1949. These banks accept deposits and grant loans to the general public, businesses, and even the Government. Commercial types of banking systems are:

- **Public Sector Banks:** More than 75% of the total banking business in India comes under the public sector, also known as nationalised banks. The Indian Government and RBI are the major stakeholders in this sector.
- **Private Sector Banks:** Most stakeholders of Private Sector Banks are individual investors, not the RBI or Indian Government. Nevertheless, these banks must adhere to all the RBI regulations for their operations.
- **Foreign Banks:** Foreign Banks have their headquarters in a foreign country but operate as a private entity in India. They abide by the regulations of their home country and the country in which they operate.
- **Regional Rural Banks:** These scheduled commercial banks serve the economically weaker sections, such as marginal farmers, agricultural labourers, and small businesses. Operating at regional levels, RRBs offer banking facilities like debit cards, bank lockers, complimentary insurance etc.

Small Finance Banks

Licensed under section 22 of the Banking Regulation Act, 1949, these types of banking systems cater to sections of societies not usually served by large banks. They serve micro and cottage industries and small business units.

Payments Banks

RBI restricts these banks to offer deposit facilities only, with a deposit limit of INR 1 Lakh per customer. You can avail of debit cards and e-banking facilities.

Cooperative Banks

These banks are registered under the Cooperative Societies Act, 1912, and function on a no-profit no-loss basis. They offer banking services to entrepreneurs, small businesses, and industries.

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Universal Banking

A universal bank is nothing but a commercial bank with additional authority to act as an investment house and invest its money in non-allied companies. It is a system through which banks offer their regular, retail, and high net worth customers a bouquet of comprehensive financial services, including customised or tailored investment, retail, and commercial services.

Under universal banking, you get easy access to facilities like credit requirements, deposits, securities transactions, asset management, financial analysis, and underwriting services, among other things. Essentially, you get all the required financial services under one roof. This facility reduces your transaction costs and saves you precious time as well.

Types of Universal Banking Services

Universal Banking Services in India are broadly categorised into three types based on their functionality. They are as under:

1. Investment banking services

Several public and private sector banks in India have started offering investment banking services. Such banks typically focus on providing services to various private investors and organisations. Also known as merchant banking, these banks generally offer their clients assistance with asset management, investment advisory services, raising capital, mergers and acquisitions, securities underwriting and securities trading, among other facilities. As is apparent, these functions of universal banking do not apply to everyday banking services.

2. Wholesale banking services

Wholesale Banking Services are typically designed for businesses and corporate organisations, as opposed to individual bank customers. These services usually involve lending and borrowing funds on a large scale, compared to retail banking services that deal with comparatively smaller loan amounts for individual customers. Each transaction in wholesale banking is typically in the tunes of crores of rupees and multiple accounts. For instance, a customer of a wholesale bank may need pension fund accounts for its employees. Government organisations and multinational companies are typically customers who obtain wholesale banking services.

3. Retail Banking Services

Retail banking is the most common type of universal banking service available globally. It is the type of banking that general bank customers and account holders are provided. Retail banking encapsulates the general banking facilities that include a wide variety of home, auto and personal loans and mortgage services. It also includes offering different

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types of bank accounts – Salary, Current, Savings Accounts, and more. Banks provide safe deposit lockers, fixed and recurring deposits, credit and debit cards, and other such everyday banking services under retail banking.

Conclusion

With growing competition in the banking sector, most Indian banks are adopting a universal banking model to cater to the needs of their various clients. Universal banking enables banks to broaden their customer base. As a bank customer, you can enjoy an array of facilities under one umbrella, thanks to universal banking services.

RBI Monetary Policy

Monetary policy is the procedure by which the monetary authority of a nation, normally the central bank or currency board, controls either the expense of short-term borrowing or the cash supply, focusing on inflation or the loan fee to guarantee value strength and general trust in the currency. Further goals of monetary policy are:

- to contribute to the stability of the gross domestic product,
- to achieve and maintain low unemployment, and
- to maintain predictable exchange rates with other currencies.

In India, the monetary policy is developed by the Reserve Bank of India. Hence, it is also called the Monetary Policy of RBI.

Types of Monetary Policies

1. Expansionary Monetary Policy

If a country is facing a high unemployment rate especially during a crisis period such as a slowdown or a recession, the monetary authority of the country, which is usually the central bank of the country, can opt for an expansionary policy that is aimed at increasing economic growth and expanding economic activity.

As a part of expansionary monetary policy, the subsequent monetary authority often lowers the interest rates for consumers through various measures that make money-saving relatively unfavourable and promotes spending in the market. It leads to an increase in money supply in the market, with the hope of a boost in investment and consumer spending.

2. Contractionary Monetary Policy

Contractionary monetary policy is when a central bank uses the tools of monetary policy in order to fight inflation. Since inflation is a sign of an overheated economy, the bank must slow economic growth in order to control the situation. So, the contradictory monetary policy may result in slowing down economic growth and an increase in unemployment but is often required to control inflation.

- **Monetary Policy of RBI | Monetary Policy in India**

Developing the Monetary Policy in India is a prerogative of the Reserve Bank of India. Hence, it is also called the Monetary Policy of RBI. The RBI is vested with this responsibility under the RBI Act, 1934. The Monetary policy of RBI regulates the money supply, availability of credit and interest rates. Let us look at the main goal of monetary policy and the monetary

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policy instruments that the Reserve Bank of India uses to regulate the money supply to achieve the objectives of the economic plan.

- **Main Goal of Monetary Policy of RBI**

The primary goal of monetary policy of RBI is to maintain price stability keeping in mind the objectives laid out in the economic plan. Price stability is extremely important for attaining sustainable growth. To maintain price stability, inflation must be kept in check. RBI uses various monetary policy instruments to ensure that inflation is controlled. Let us look briefly at the monetary policy instruments used by the RBI.

- **Monetary Policy Instruments | Monetary Policy of RBI**

There are several direct and indirect monetary policy instruments that help in implementing the monetary policy in India. Let's discuss each one of them in brief:

- **Repo Rate:** Repo rate is the rate at which RBI lends short term loans (less than 90 days) to commercial banks.
- **Reverse Repo Rate:** Reverse repo is the rate at which the RBI keeps the extra deposit of all banks within itself.
- **Marginal Standing Facility (MSF):** It is the rate at which banks borrow overnight loans from RBI. It can be only up to 2% of the NTDL(Net Demand and Time Liabilities). It is always 1% or 100 basis points more than the repo rate.
- **Bank Rate:** It is the rate at which RBI offers long term loans (more than 90 days) to commercial banks.
- **Cash Reserve Ratio (CRR):** It is the ratio of the bank's total deposit that every bank has to keep with the RBI. It has to be in cash form only. RBI does not offer any interest on this reserve money. It can be between 0 to 15%. RBI announces the CRR in its monetary policy.
- **Statutory Liquidity Ratio (SLR):** It is the ratio of the bank's total deposit that a bank has to maintain with itself. It can either be in cash or in liquid assets including Gold, Foreign Currency, Government Bonds, etc. It can be between 0 to 40% as announced by the RBI in its monetary policy.
- **Open Market Operations(OMO):** It refers to the buying and selling of government securities between the RBI & banks.

Different Types of Accounts

Initially, there were only four types of bank accounts that were operating in India. These included the Current Account, Savings Account, Recurring Deposit Account and Fixed Deposit Account. But later with the advancement in the banking sector, various other types of bank accounts were introduced they are

1. Savings Account
2. Current Account
3. Recurring Deposit Account
4. Fixed Deposit Account
5. DEMAT Account
6. NRI Account

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Savings Account

As the name suggests, the savings accounts can be opened by an individual or jointly by two people with an aim to save money.

The main benefit of opening a savings bank account is that the bank pays you interest for opening this type of account with them.

Given below are a few features of the Savings account:

- There is no limit to the number of times the account holder can deposit money in this account but there is a restriction on the number of times money can be withdrawn from this account.
- The rate of interest that an account holder get varies from 4% to 6% per annum
- There is no minimum balance that needs to be maintained for this type of an account
- The savings account holders can get an ATM/Debit/Rupay Card if they want to
- Savings bank account is further divided into two types: Basic Savings Bank Deposit Account (BSBDA) and the other one is Basic Saving Bank Deposit Accounts Small Scheme(BSBDS)
- The savings bank account is mostly eligible for students, pensioners and working professionals

Current Account

The second type of bank account is the current bank account. These accounts are not used for the purpose of savings.

Some important pointers related to the current bank account have been discussed below:

- This type of bank account is mostly opened by businessmen. Associations, Institutions, Companies, Religious Institutions and other business-related works, the current account can be opened
- There is no fixed number of times that money can either be deposited or withdrawn from such accounts
- Internet banking is available
- This type of bank account does not have any fixed maturity
- Overdraft facility is available for current bank accounts
- There is no interest that is paid on such accounts

Recurring Deposit Account

Recurring Deposit account or RD account is a form of account wherein the account holder needs to deposit a fixed amount every month until it reaches the fixed maturity date.

The features of the Recurring deposit account have been discussed below:

- Any individual or an Institution can open a recurring deposit account either separately or jointly
- Periodic or monthly instalments that need to be added can be as low as Rs.50/- or may vary from bank to bank
- The range of months for which an RD account can be opened varies from 6 months to 120 months
- The interest rate varies depending upon the bank you choose to open an account with
- Nomination facility is also available for RC accounts
- Passbook is issued for this type of bank account

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- Premature withdrawal of the amount is permitted, provided a sum of amount is deducted as penalty

Fixed Deposit Account

FD or a fixed deposit account is another type of bank account that can be opened in any Public or Private sector bank.

The list of important things that need to be known with respect to the fixed deposit account has been mentioned below:

- It is a one time deposit and one time take away account. Under this type of account, the account holder needs to deposit a fixed amount of sum (as per their wish) for a fixed time period
- The amount deposited in FD account can only be withdrawn all at once and not in instalments
- Banks pay interest on the fixed deposit account
- The rate of interest depends upon the amount you deposit and for the time duration of the FD
- Full repayment of the amount is available before the maturity date of FD

DEMAT Account

Shares and securities which can be held in electronic format constitute the DEMAT account. The DEMAT account also stands for Dematerialized Account.

Given below the points that need to be known by a candidate regarding the DEMAT Account:

- There are only two depository organisations which manage this type of bank account in India. This includes: National Securities Depository Limited and Central Depository Services Limited
- This helps facilitate easy trade of bonds and shares
- Helps in conducting stress-free transaction of shares
- KYC is required for opening the DEMAT Account
- Transaction cost is reduced
- Traders can work from anywhere
- The transfer of securities can be done with reduced paperwork

NRI Account

To fulfil the bank requirements of a Non-Residential Indian or a Person of India Origin, the option of NRI account is available.

The NRI Accounts are further divided into three types:

1. **NRO (Non-Resident Ordinary Rupees) Account** – This shall allow you to transfer your foreign earnings easily to India. It can be opened in the form of an FD/RD/Current/Savings account. These accounts can be opened by an individual or jointly opened
2. **NRE (Non-Resident External Rupees) Account** – When an Indian citizen moves abroad to work there, his/her account needs to be converted into an NRE account. This account can be jointly opened with an Indian resident
3. **FCNR (Foreign Currency Non-Resident) Account** – This type of account can be opened to manage an international currency. It can only be in the form of Term deposit and can be withdrawn after the maturity period only.

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Various Services Offered by Banks

Following are the few services which bank provides

- Advancements of loans
- Cheque payments
- Discounting on bills of exchange
- Collecting and paying the credit instruments
- Guarantee by banks
- Consultancy
- Credit cards
- Funds remittance
- Debit cards

Advancements of loans

Banks run on the profit they make. They are into the business of making profits. So, to generate the profit they give loans to the public and private organizations.

Thus, in return, they get an interest paid to them which helps them in making a profit. Banks need to keep a minimum cash reserve with them.

So, after deducting this cash reserve, banks provide short, medium, and long-term loans to the people who are in need of it.

Cheque Payments

The person who holds an account in the bank is provided with the cheque pads.

Thus, the account holders draw cheque upon the bank when they are required to pay the money.

So after verifying formally, banks pay for the cheques and proceed with the official procedures.

Discounting on bills of exchange

This is another popular services of banks for lending the money. In this method, the person who holds the bill of exchange gets it discounted by the bank in exchange for a bill.

The creditor gives the payment to the debtor who accepts it and agrees that the amount shall be paid upon maturity. Once the marginal deductions are made the bank pays the value to the holder of the bill.

After that, when the bill is matured the banks get their payment from the person who has accepted the bill.

Collecting and paying the credit instruments

For modern purposes, there are a variety of instruments that are used as credit instruments. This includes promissory notes, bill of exchange, cheques, etc.

These instruments are dealt with by the banks. The banks are responsible for collecting and paying the different types of credit instruments.

These credit instruments are the representative of the customers.

Guarantee by Banks

In modern banking, customers are provided with the guarantee by the banks. This happens mostly when the customers have to deposit a large fund in courts or government offices for various reasons.

The banks itself acts as a guarantee for that person.

Consultancy

Modern banks expand their businesses and also provides consultancy services to its customers.

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For this, they hire legal, financial, and market leaders and experts who can provide advice to customers regarding industry, income, trade, investment, etc.

Credit Cards

It is a service that allows the holders to make the purchase of the goods and services in exchange for a credit card.

It immediately pays off for the services and goods while the cardholder is required to pay back the amount over a period of time with a certain percentage of interest.

Funds Remittance

In this facility, banks provide the customers to transfer their funds from one account to another using cheque, drafts, etc.

Debit Cards

Debit cards withdraw the funds electronically from the cardholder accounts. To verify the transaction and keep it safe all the debit cards requires personal identification number (PIN).

The other services of banks include online banking, home banking, ATM services, and many more.

Sources of Risk in Banks

“With great risks comes great reward,” especially in banking. Banks are in the business of taking on financial risk to generate profit. However, the stakes are high, and the downside potential is huge. This includes legal repercussions, which have increased steadily since the 2008 financial crisis.

Banks have spent significant dollars on everything from regulatory compliance to litigation and compensation claims. Risk managers are feeling more pressure to build and maintain sustainable risk management frameworks that handle a wider, more comprehensive set of risk types.

Beyond traditional risks like credit, market, and liquidity risk, the impact of model risk and ESG risk is on the rise. Additionally, there's a whole host of nonfinancial risks, where the downside can be difficult to quantify. This blog lists nine common risk types that we come across when working risk clients at global banks.

Types of financial risks:

1. Credit Risk

Credit risk, one of the biggest financial risks in banking, occurs when borrowers or counterparties fail to meet their obligations. When calculating the involved credit risk, lenders need to foresee and predict the possibility of them making back the loan, principal, interest, and all.

2. Market Risk

Market risk is the risk of losing value on financial instruments on the back of adverse price moments driven by changes in equities, interest rates, credit spreads, commodities, and FX.

3. Liquidity Risk

Liquidity refers to a bank's ability to meet its collateral and cash obligations while avoiding major losses. Liquidity risk is the risk of incurring losses where certain commodity or investment cannot be traded without impacting its market price.

4. Model Risk

Model use at large banks is growing by more than 20% each year (IDC), which in turn leads to greater model risk. Banks must manage model accuracy to prevent significant financial losses when assumptions grow, models are misused, or other forms of malfunction occur.

5. Environmental, Social and Governance (ESG) Risk

Environmental, social, and governance events, from climate change to diversity and inclusion policies, can have material impact on the value of investments. Banks must proactively measure and manage these risks, integrating ESG data, scoring models, and climate models into the investment process and credit risk evaluations.

Types of non-financial risk:

6. Operational Risk

Operational risk is the risk of losses incurred by inadequate internal processes, people, and systems, or from external events.

7. Financial Crime

Money laundering, corruption, fraud are examples of financial crime, leading to economic benefits for individuals through illegal ways. Banks need to make sure they develop fool proof techniques to avoid the losses posed by financial crime.

Analyzing Banks Financial Statements

In India banks occupy a substantial portion of the overall stock market and hence, they probably form at least some part of the investment portfolios of equity investors. No matter whether an investor invests through mutual funds or directly in stocks, it is difficult for him/her to escape banks or financial firms. With credit penetration in India still remaining low, financial firms have a long runway for growth in the coming years. It translates into the growing popularity of banking and financial stocks.

However, analysing banks is very different as compared to analysing an FMCG or say an auto company because of the following reasons.

- The financial statements of banks can prove to be a black hole. Lots of numbers can lead to more confusion than any clear understanding.
- Unlike non-financial firms wherein metrics like gross margin, working-capital cycle, debt to equity, etc., are important criteria to consider, banks altogether have different metrics. To analyse a bank's financial statements, one needs to first have a clear understanding of these metrics.

In this story, we have discussed some of the most important metrics that investors need to know while researching a banking firm.

Capital adequacy ratio (CAR)

It is the measure of a bank's available capital divided by the loans (assessed in terms of their risk) given by the bank. CAR is used to protect depositors and promote the stability and efficiency of financial systems. It helps measure the financial strength or ability of the financial institution to meet its obligations by using its assets and capital. The higher the CAR, the better capitalised the bank is. In India, as per the RBI norms, Indian-scheduled commercial banks are required to

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maintain a CAR of 9 per cent, while Indian public-sector banks are emphasised to maintain a CAR of 12 per cent.

Suppose, the CAR for an XYZ Bank stood at -2.8 per cent during certain quarter. This shows that XYZ Bank had no capital to be absorbed as losses from bad loans.

Gross and net non-performing assets

Non-performing assets (NPAs) indicate how much of a bank's loan book is in danger of not being repaid. A loan turns non-performing if the interest or instalment of the principal amount is not received for a period of 90 days. NPAs are further categorised as gross and net NPAs. Gross NPA includes both the principal and interest aspects of the loan, whereas net NPA is calculated mainly by subtracting the provisions made by the bank from the gross NPA.

Public-sector banks in recent years have been plagued by bad loan problems. State Bank of India, the largest public sector bank, recorded 11 per cent of its outstanding loans as NPA (Gross NPA) as of FY18.

Provision coverage ratio

In banking, it is a fact that some portions of loans will always turn bad. Banks, therefore, make provisioning for such bad loans by setting aside funds to a prescribed percentage of their bad assets. For example, if the PCR is 70 per cent for a particular category of bad loans, banks have set aside funds equivalent to 70 per cent of those bad assets out of their profits. A high PCR means that most asset-quality issues have been taken care of.

The PCR for troubled Yes Bank stood at just 43.1 per cent as of FY19, depicting that the bank had an asset-quality issue and it wasn't able to provide adequately for bad loans.

Return on assets

In the balance of banks, loans given out to borrowers are assets whereas depositors' money is a liability. Return on assets depicts how profitable the bank is relative to its total assets. It is calculated by dividing net profit by total assets. A high ROA relative to other banks can be on account of various factors, including substantial other income, aggressive lending practices, operational efficiency and other factors.

CASA ratio

It stands for current account saving account. CASA is the per cent of deposits held by banks in current and savings accounts. Banks pay low interests on such accounts. A high CASA ratio is positive for the bank, as it is able to reduce the total borrowing rate.

Net interest margin

As the name suggests, it is the difference between the interest income generated from borrowers and the amount of interest paid to depositors, relative to total deposits. It is a profitability ratio and similar to the gross margin of a normal company.

HDFC Bank on the back of its ability to raise capital at a low cost and good lending practices has one of the best net interest margins in the banking sector. HDFC Banks NIM consistently ranged around 4.3 per cent during the past few years till FY20.

Cost to income

It is an important ratio to determine how efficiently a bank is being run. Cost to income is calculated by dividing operating expenses by the bank's operating income (interest income plus other income). There is an inverse relation between cost to income and the bank's profitability. The lower the cost-to-income ratio, the better the profitability is.

For HDFC Bank, the cost-to-income ratio has consistently decreased over the last few years and stood at 38.6 per cent as of FY20. On the other hand, SBI, which has an operating income of more than double that of HDFC Bank, is able to generate an operating profit only slightly higher than HDFC Bank, as its cost-to-income ratio stood at 52.5 per cent as of FY20. HDFC Bank is able to generate better profitability because of operational efficiency.

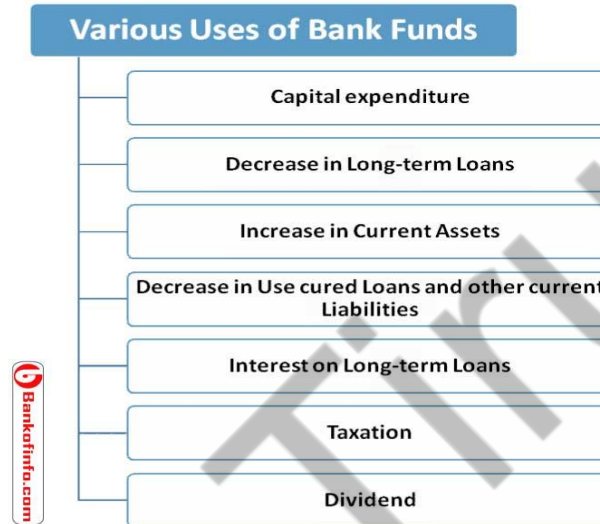
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UNIT-2

USES OF BANK FUNDS

The utilization of funds may take the form of either a) an increase in assets both fixed current, or b) a decrease in liabilities. Let's know the various uses of bank funds.

Uses of bank funds



Capital expenditure

The amounts to be spent for acquiring additional fixed assets and for normal replacement and renewals are to be shown separately under the relevant periods.

Moreover, the total of the figures relating to the project shown against this item should be equal to the figure of the capital cost of the project as shown in the statement of the cost of the project.

The decrease in long-term loans

The long-term loans raised from financial institutions are repayable in installments as per the schedule of repayment agreed upon.

Similarly, payment for plants and machinery purchased on a deferred payment basis is to be made in an agreed manner. The installments of these payments should be shown under the respective years.

Increase in current assets

Estimates about the increase in the number of book debts, stock in trade, bills receivable and other current assets are to be shown under this head.

The level of these assets increases with an increase in the level of working capital raised through short-term borrowings.

The decrease in the use of cured loans and other current liabilities

The short-term borrowings are to be repaid, as per the terms agreed upon. The cash credit limits are fixed on a year-to-year basis and are usually renewed. The number of such loans should not be shown as repaid.

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Interest on long-term loans

Interest payable on term loans (including the loan for which the application is being made) is to be shown against this item. The term loans are repayable in installments.

Hence, the amount of interest payable on the outstanding amount of loans goes on declining, as the installments are paid in subsequent years.

Taxation

As the concern starts earning profits, provision for taxation is to be taken into account. The concern may, however, take a few years time to earn profits.

Moreover, if the Government has granted any tax holiday for the concern for a certain period, no amount is payable as tax during that period.

Dividend

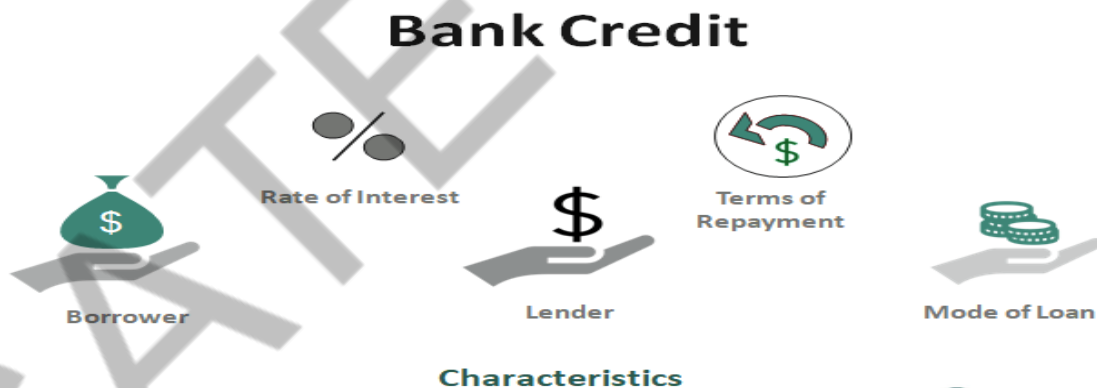
The amounts of dividends that are expected to be declared in future years out of the profits of the company are to be shown as cash outflow. Dividends are payable only when the company starts earning profits.

Moreover, a portion of the net profit is usually plowed back into the business itself to consolidate the financial position of the company and retain its funds within the business.

Here are the major uses of bank funds, there may be more uses of bank funds but these seven are the most common and important uses of bank funds.

Features of Bank Credit

The following are features of bank credit.



1. **Borrower:** Person who borrows money.
2. **Lender:** The person who lends money is usually the bank.
3. **Rate of Interest:** The interest rate can be fixed or floating rate of interest. The floating interest rate is based on benchmark rates like LIBOR or MIBOR.
4. **Terms of Repayment:** These are mentioned in the loan covenant and strictly adhere to avoid the prepayment penalty.
5. **Mode of Loan:** Normally given in cash but sometimes will be given in the form of raw material or fixed assets.

Purpose of Bank Credit

The following are the purpose of the loan.

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- **Educational Loans:** These are given for pursuing higher education, repayment of which is due after completing education. Interest gets accumulated for the loan.
- **Housing Loans:** These are given to buy a home. The repayment of principal and interest is based on the EMI principal. House is collateral for such loans, and excessive documentation is required.
- **Vehicle Loans:** These are given to purchase vehicles like cars, tempo, two-wheeler, autos, and trucks. Normally assets are hypothecated to the Bank unless and until the final installment is paid. You often see “we banked Bank” written on the backside of cars. This indicates a loan is taken from “... Bank”.
- **Vendor Financing:** This is an arrangement provided by the Bank to pay to vendors as per agreed credit terms, and in turn, the borrower will pay to the Bank after, say, 60 days or 90 days. The Bank charges an interest rate to the borrower for paying in advance to suppliers. The advantage of this is minimal documentation required by the Bank.
- **Letter of Credit Facility:** Like vendor financing but predominantly used while importing goods or making payments to overseas vendors. Terms of repayment and interest rate are mutually agreed upon between the parties.

Assessment Of Credit Worthiness Of Borrowers

Creditworthiness is an essential principle of business, signifying how deserving a customer is of getting credit. A customer is creditworthy if the company believes it can pay the debt on time. It is determined by multiple factors such as revenue, payment history, credit score, outstanding liabilities, etc.

The five Cs of creditworthiness

Businesses use multiple criteria to determine a customer's creditworthiness. The five Cs of credit is one of the most well-known techniques for evaluating creditworthiness. Understanding the **five Cs—character, capacity, capital, collateral, and conditions**—can assist in determining a customer's capability to repay the borrowed credit. Let's look at what each one signifies.

1. Character

Character assesses how dependable and trustworthy a customer is. To establish a customer's character, one must analyze their credibility and background. Credit history is one of the main factors to consider while evaluating a customer's character. It contains a detailed description of the customer's credit report and credit score. This data includes how long the customer has been in business, bankruptcies, whether they make timely payments, and more. Credit scores vary from 300 to 850, with higher scores indicating strong creditworthiness.

2. Capacity

Capacity refers to the ability of the customer to repay their debt. To evaluate the capacity of a customer, consider cash flow statements, business debt, and payment history. The Debt Service Coverage Ratio (DSCR) and Debt-to-Income ratio (DTI) help determine a company's cash flow and overall health. A DSCR of 1.25 or higher and a DTI ratio of 36% or lower is considered ideal.

3. Capital

Capital signifies the total funds and assets (both financial and non-financial) owned by a company. Before extending credit to a new customer, evaluate the worth of the customer's business in terms of their investment in fixed assets and other instruments. Review the

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customer's bank records and financial statements to get a clear picture of their capital. If these statements show a trend of strong capital growth, the customer is less risky and can be assigned a higher credit limit.

4. **Collateral**

Collaterals are assets that a customer commits to back a line of credit. These are fixed assets like inventories, corporate bonds, or real estate. Companies generally demand collateral as an assurance for extending credit. While working with a high-risk customer, always ask for collateral to limit the likelihood of bad debts.

5. **Conditions**

Conditions are terms established by a company in light of its policies or due to economic conditions or regulations prevalent in the customer's region of operations. Geographic location, industry type, currency fluctuations, and political environment are some of the factors that influence a company's payment terms and conditions. A customer with a stable geopolitical environment is more creditworthy since it faces lower economic risks.

Steps to check the creditworthiness of a new customer

Before granting credit, a company should assess the customer's competence to manage and repay outstanding debts. Collecting and analyzing information about the customer from credible sources to check creditworthiness can help you avoid the pitfalls of late payments or bad debt. Here is a step-by-step guide to determine the creditworthiness of a new customer:

Step 1: Collect relevant details to extend credit

Collecting relevant information about the client is the first step to assessing creditworthiness. The customers should fill out a business credit application form consisting of general business information, bank references, credit references, and more. These details would help to aggregate client data in one place for faster customer onboarding.

Step 2: Check credit reports

Analyzing credit reports is an ideal method to evaluate a customer's creditworthiness. A credit report contains information on the company and its financials, enabling you to generate credit scores. It depicts a company's capacity to pay by tracking its payment history and public records. Credit reports of a company are available for purchase from credit reporting agencies such as Experian, D&B, and Equifax.

Step 3: Assess financial reports

The financial report of a company provides insights into its cash position. Financial reports include the cash flow statement, income statement, and the balance sheet of the company. The financial health of a new customer should be examined thoroughly by reviewing their public financial statements.

Step 4: Evaluate the debt-to-income ratio

Analyze the DTI ratio of a customer to better understand their cash flow statement. DTI ratio indicates how much of a company's monthly income is spent on repaying debts. It helps determine the risk associated with the customer account. To calculate the DTI ratio, divide the company's monthly debt payments by gross monthly income.

A low DTI ratio indicates a healthy balance between debt and income, whereas a high DTI ratio shows that a client has more obligations than the monthly income.

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Step 5: Conduct credit investigation

You must use multiple sources to conduct further investigations to evaluate the creditworthiness of a customer. These investigations should contain:

- Customer background and history
- Credit policies
- Accounts receivable aging report
- Economic and political climate analysis
- Future business probability

All these factors contribute to better decision-making and customer authentication.

Step 6: Perform credit analysis

After gathering all necessary information about the new customer, conduct a comprehensive account analysis. Evaluate trade references, scrutinize financial statements, and apply credit analysis to predict the probability of default. While performing credit analysis, the profitability ratio, leverage ratio, and liquidity ratio are some of the key financial metrics to consider.

Different Types of Loans

Loans can be utilised for various things in today's world. It can be used for funding a start-up to buying appliances for your newly purchased house. Let us talk about the different types of loans available in the market and their specific characteristics that make these loans useful to the customers.

Personal Loans:

Most banks offer personal loans to their customers and the money can be used for any expense like paying a bill or purchasing a new television. Generally, these loans are unsecured loans. The lender or the bank needs certain documents like proof of assets, proof on income, etc. before approving the personal loan amount. The borrower must have enough assets or income to repay the loan. In case of personal loans, the application is 1 or 2 pages in length. The borrower gets to know about the denial or approval of the loan within a couple of days.

You must remember that the rate of interest associated with these loans can be on the higher side. The tenure of these loans is not that long. So, if you borrow a big amount, it can be difficult for you to repay without planning your finances properly.

Personal loans can prove to be of great help when you wish to take a small amount loan and repay it as soon as possible.

Credit Card Loans:

When you are using a credit card, you must understand that you will have to repay for all the purchases you make at the end of the billing cycle. Credit cards are accepted almost everywhere, even when you are travelling abroad. As it is one of the most convenient ways to pay for the things you buy, it has become a popular loan type.

Home Loans:

When you wish to purchase a house, applying for a home loan can help you to a great extent. It provides you the financial support and helps you buy the house for yourself and your loved ones. These loan generally come with longer tenures (20 years to 30 years). The rates offered by some of the top banks in India with their home loans start at 8.30%. Your credit score is checked

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before the loan request is approved by the lender. If you have a good credit score, there is a fair chance that you will be able to enjoy lower rates of interest with your home loan.

Home loans are primarily taken for buying new homes. However, these loan can also be used for home renovations, home extensions, purchasing land property, under-construction houses, etc.

Car Loans:

Buying a car can definitely shows a great sense of joy and happiness in you. A car will remain as your asset and it is going to be one of the biggest investments that you make. A car loan helps you to pave the path between your dream of owning a car and actually buying your car. Since credit reports are crucial for judging your eligibility towards any loan, it is good to have a high credit score when you apply for a car loan. The loan application will get approved easily and you might get a lower rate of interest associated with the loan.

Car loans are secured loans. If you fail to pay your instalments, the lender will take back your car and recover the outstanding debt.

Two-Wheeler Loans:

A two-wheeler is pretty essential in today's world. May it be going for a long ride or a busy road in a city – bikes and scooters help you to commute conveniently. A two-wheeler loan is easy to apply for. This amount you borrow under this loan type helps you to purchase a two-wheeler. But if you do not pay the instalments on time and clear your debt, the insurer will take your two-wheeler to recover the loan amount.

Small Business Loans:

Small Business Loans are loans that are provided to small scale and medium scale businesses to meet various business requirements. These loans can be used for a variety of purposes that help in growing the business. Some of these could include purchase of equipment, buying inventory, paying the salaries of employees, marketing expenses, paying off business debts, meeting administrative expenses, or even to open a new branch or take up a franchise.

The eligibility criteria for small business loans varies from lender to lender, but the common ones are the age of the business owner, the number of years the business has been operational, income tax returns, and statement of the previous year's turnover that has been audited by a Chartered Accountant (CA).

Payday Loans:

Payday loans are also called salary loans. These are unsecured short-term loans that require the customer to be employed with a steady income. They usually have high interest rates. This is based on the applicant's credit profile, age, and income. Documents required would be salary statements and other proof of income.

Cash Advances:

These loans are offered by credit card issuers and allow credit card users to withdraw cash from an ATM machine using the credit card. The amount of cash that can be withdrawn from a credit card in this way will depend on the credit limit available. The cash has to be paid back with interest, which is usually calculated from the day the cash has been withdrawn. There are also other fees associated with a cash advance, such as cash advance fees and ATM or bank fees.

Home Renovation Loan:

Home innovation loans are offered by most lenders. These can be availed to meet the expenses related to renovation, repairs, or improvement of an existing residential property. Depending on

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the lender, there is a lot of flexibility with what you can do with a home renovation loan. You can use it to buy products or pay for services. For example, you can use it to pay for the services of a contractor, architect, or interior decorator. You can also use it to buy furniture, furnishings, or household appliances such as a refrigerator, washing machine, air conditioner, etc. It can be used for painting, carpentry, or masonry work as well.

Agriculture Loan:

Agriculture loans are loans that are provided to farmers to meet the expenses of their day-to-day or general agricultural requirements. These loans can be short term or long term. They can be used for raising working capital for crop cultivation or to buy agricultural equipment.

Gold Loan:

A gold loan can be used to raise cash to meet emergency or planned financial requirements, such as business expansion, education, medical emergencies, agricultural expenses, etc. The loan against gold is a secured loan where gold is placed as security or collateral in return for a loan amount that corresponds to the per gram market value of gold on the day that the gold has been pledged. Any other metals, gems, or stones that are in the jewelry will not be calculated when determining the value of the gold loan.

Loan Against Credit Card:

Loan against credit card is like a personal loan that is taken against your credit card. These are usually pre-approved loans that do not require any additional documentation. Depending on the lender, this can be converted into a personal loan that is interest free within a certain period of time. After that, it will attract a certain percentage of interest. There is a processing fee associated with converting the credit limit that is pre-assigned into a loan.

Education Loan:

An education loan is availed specifically to finance educational requirements towards school or college. Depending on the lender, it will cover the basic fees of the course, the exam fees, accommodation fees, and other miscellaneous charges. The student is the borrower with any other close relative being the co-applicant, such as a parent, grandparent, spouse, or sibling. It can be availed for courses in India or abroad. It can be taken for a wide variety of 28 recognized courses which are either part time or full time. They cover vocational courses as well as undergraduate and postgraduate courses.

Consumer Durable Loan:

Consumer durable loans are loans that are availed to finance the purchase of consumer durables such as electronic gadgets and household appliances. Depending on the lender, they can be used to buy anything from mobile phones to television sets. Loan amounts range from Rs.5,000 to Rs.5 lakh. There is no security deposit required usually. Some lenders offer 0% interest on consumer durable loans with instant approvals and minimal documentation required as well.

Loan Against the Insurance Schemes:

If your insurance scheme is eligible for a loan, you can avail the loan amount from your insurer. You may also use the investment for insurance as collateral. Generally, loans cannot be availed right from the commencement of the insurance policy. After 3 years into the scheme, you can apply for a loan against insurance.

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Loan Against Fixed Deposits:

This is a type of loan where your fixed deposit is the collateral. For example, if you have a fixed deposit of Rs.10 lakh in the bank, you can avail a loan of up to Rs.8 lakh. However, the rate of interest associated with this kind of a loan is usually higher than the fixed deposit rate.

Loan Against Mutual Funds and Shares:

Certain lenders provide loan against your mutual fund value and share value. However, you will not be able to borrow huge amounts under this type of loans.

Priority Sector Lending and Sectoral Limits

Priority Sector refers to those sectors which the Government of India and Reserve Bank of India consider as important for the development of the basic needs of the country. They are assigned priority over other sectors. The banks are mandated to encourage the growth of such sectors with adequate and timely credit.

The Priority Sector Lending classifications and guidelines released by the RBI are intended to align with emerging national priorities and bring a sharper focus on inclusive development, building a consensus among all stakeholders.

It enables better credit penetration to credit deficient areas, increased lending to small and marginal farmers and weaker sections, boost credit to renewable energy, and health infrastructure and allied sectors that need credit boost, which is otherwise difficult to avail.

What are the Different Categories of the Priority Sector?

- Agriculture
- Micro, Small and Medium Enterprises
- Export Credit
- Education
- Housing
- Social Infrastructure
- Renewable Energy
- Others

Agriculture

- The lending to the agriculture sector includes Farm Credit (Agriculture and Allied Activities), lending for Agriculture Infrastructure and Ancillary Activities.
- Crop loans include loans for traditional/non-traditional plantations, horticulture and allied activities.
- Loans for pre and post-harvest activities viz. spraying, harvesting, grading and transporting their own farm produce.
- Loans to distressed farmers indebted to non-institutional lenders.

Micro, Small and Medium Enterprises (MSMEs)

- Micro enterprises are the ones where the investment in plant and machinery or equipment does not exceed one crore rupees and turnover does not exceed five crore rupees.
- Small enterprises are the ones where the investment in plant and machinery or equipment does not exceed ten crore rupees and turnover does not exceed fifty crore rupees.
- Medium enterprise, where the investment in plant and machinery or equipment does not exceed fifty crore rupees and turnover does not exceed two hundred and fifty crore rupees

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Education

- Loans to individuals for educational purposes, including vocational courses, not exceeding Rs 20 lakh are considered eligible for priority sector classification.
- Loans currently classified as a priority sector would continue till maturity.

Housing

- Loans to individuals up to Rs 35 lakh in metropolitan centres.
- Up to Rs 25 lakh in other areas apart from Urban centres for purchase/construction of a dwelling unit per family.
- The overall cost of the dwelling unit in the metropolitan centre and at other centres should not exceed Rs 45 lakh and Rs 30 lakh respectively.
- The housing loans to banks' employees are excluded.

Social infrastructure

- Loans up to a limit of Rs 5 crore per borrower for setting up schools, drinking water facilities and sanitation facilities.
- It includes the construction/ refurbishment of household toilets and water improvements at the household level.

Renewable Energy

- Loans up to Rs 30 crore to borrowers for purposes such as solar-based power generators, biomass-based power generators, windmills, micro-hydel plants.
- Non-conventional renewable energy-based public utilities like street lighting systems and remote village electrification.
- For individual households, the loan limit is Rs 10 lakh

Others

- Loans not exceeding Rs 1.00 lakh per borrower are provided directly by banks to individuals and individual members of SHGs when they fulfill certain criteria of annual income.
- Loans not exceeding Rs 2.00 lakh provided directly by banks to SHG for activities other than agriculture or MSME, such as meeting social needs, construction or repair of houses, construction of toilets or any viable common activity started by the SHGs.

Loan Pricing

Loan pricing is the process of determining the interest rate for granting a loan, typically as an interest spread (margin) over the base rate, conducted by the book runners. The pricing of syndicated loans requires arrangers to evaluate the credit risk inherent in the loans and to gauge lender appetite for that risk.

For market-based loan pricing, banks incorporate credit default spreads as a measure of borrowers' credit risks. It is standard procedure in loan pricing to benchmark a loan against recent comparable transactions ("comps") and select the base rate on which the financing costs are pegged. A comparable deal is one with a borrower in the same industry, country and of the same size with the same credit rating, for which a certain market rate of return is required.

A bank's credit rating has a direct impact on its cost of funding and, thus, the pricing of its loans. Banks with a high credit rating generally have access to lower cost funds in debt markets

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and low counterparty margins in swap and foreign exchange markets. The lower cost of funds can be passed on to borrowers in the form of lower loan pricing.

Banks compete for lead arranger mandates on syndication strategy and pricing. Some banks are very effective at pricing loans, while others have better bargaining power, are more effective in borrower monitoring, or have better incentive-inducing scheme.

Pricing of Fixed and Floating Rate Loans

A fixed rate of interest or floating rate of interest are terms that will be introduced to you when you are in the market for a new loan. Whether it is a home loan or a personal loan, understanding these terms can help you make an informed choice as to which is the right type of interest rate for you, keeping in mind your financial requirements and repayment capacity. Here is everything you need to know about these two terms.

What is Fixed Interest Rate?

A fixed rate of interest means that your interest rate remains the same throughout your loan repayment tenure. It does not vary even if there is any change in the lending rates of banks or repo rates of the Reserve Bank of India (RBI). Equated Monthly Instalments (EMI) will remain the same throughout the tenure. Some lenders offer loans that have a fixed rate of interest only for the first few years of the tenure, switching to a floating interest rate later.

Benefits of Fixed Interest Rate

These are the benefits of a fixed interest rate based on various parameters:

- **Interest rate:** The interest rate remains constant throughout the entire loan tenure and is not affected by market conditions.
- **EMI:** Since this interest rate doesn't fluctuate over time, your EMI remains fixed, making it easier to more accurately plan your monthly budget and long-term financial savings or investments.

Drawbacks of Fixed Interest Rate

Some of the drawbacks of a fixed interest rate are as follows:

- The fixed interest rate is usually 1% to 2.5% higher than the floating interest rate offered by a bank or non-banking financing company (NBFC).
- Even if the fixed interest rate reduces after an announcement from the Government or Reserve Bank of India (RBI), it doesn't affect the loans already borrowed using the previous interest rate. The borrower will have to continue repayment at the higher interest rate even after a rate cut.
- Many a times, the fixed rate of interest is only valid for a couple of years after which the interest rate gets revised according to the ongoing rate.

Why choose a Fixed Interest Rate?

These are some of the scenarios in which a fixed rate of interest may be beneficial for you:

- You prefer a fixed repayment schedule and are comfortable paying the current interest amount. You should ensure that your monthly installment isn't more than 30% of your net monthly salary.
- You foresee a rise in the interest rate in the future and, therefore, want to ensure that your interest amount doesn't increase more than what you are currently paying. In such a

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scenario, the fixed interest rate can be used to lock in the current rate of interest being offered by the lender.

- In cases where there has been a decline in the interest rates and it is likely to remain the same for a few more years.

What is Floating Interest Rate?

A floating interest rate varies with the market scenario. The interest will be calculated on a base rate with a floating element being added so that when the base rate changes, the floating rate also changes.

Benefits of Floating Interest Rate

The benefits of a floating interest rate are as follows:

- Floating interest rates are usually set 1% to 2.5% lower than the fixed interest rate offered by the same lender.
- The floating interest rates offered by a bank or non-banking financing company is usually lower than the fixed rates it offers its customers. Therefore, it means that even if the floating interest rate increases, it can still be less than the previous fixed interest rate offered.
- In case the floating interest rate exceeds the interest rate, it will not be for the entire loan tenure. There are chances that the floating rates might come down after a certain period of time.

Drawbacks of Floating Interest Rate

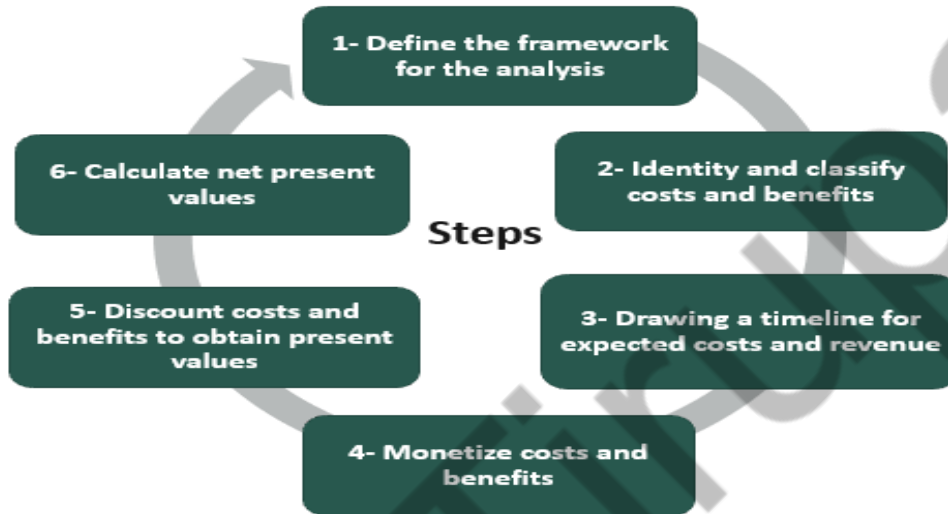
The drawbacks of a floating interest rate are as follows:

- Due to the fluctuating nature of floating interest rates, the monthly installments of a particular amount of loan will vary throughout the entire loan tenure.
- Attributed to the uneven monthly installments, it is very difficult to budget a loan with floating rate of interests.
- Since it is not possible to have a fixed repayment schedule under this interest rate option, it can lead you to pay more than you are comfortable paying. This can, therefore, cause you to have less savings and no budget plan.

Cost Benefits

The cost-benefit analysis compares the costs and benefits of a project and then makes a decision on whether or not to proceed with the project. The project's costs and benefits are measured in monetary terms after adjusting for the time value of money, thus providing a true picture of the costs and benefits. Net Present Value and Benefit-Cost Ratio are the two most common methods of doing a cost-benefit analysis. The NPV model chooses the project with the highest NPV. The benefit-cost ratio model chooses the project with the highest benefit-cost ratio.

Cost-Benefit Analysis



We all know it's quite simple to make an investment decision when the benefits overshadow the costs, but only a few of us know the other key elements that go into the analysis. The steps to create a meaningful model are:

The steps to create a meaningful Cost-Benefit Analysis model are:

1. Define the framework for the analysis.

Identify the state of affairs before and after the policy change or investment on a particular project. Analyze the cost of this status quo. We need to first measure the profit of taking up this investment option instead of doing nothing or being on ground zero. Sometimes the status quo is the most lucrative place to be in.

2. Identity and classify costs and benefits.

It is essential to costs and benefits are classified in the following manner to ensure that you understand the effects of each cost and benefit.

- Direct Costs (Intended Costs/Benefits)
- Indirect Costs (Unintended Costs/Benefits),
- Tangible (Easy To Measure And Quantify)/
- Intangible (Hard To Identify And Measure), And
- Real (Anything That Contributes To The Bottom Line Net-Benefits)/Transfer (Money Changing Hands)

3. Drawing a timeline for expected costs and revenue.

When it comes to decision making, timing is the most crucial element. Mapping needs to be done when the costs and benefits will occur and how much they will pan out over a phase. It solves two major issues. Firstly, a defined timeline enables businesses to align themselves with the expectations of all interested parties. Secondly, understanding the timeline allows them to plan for the impact that the cost and revenue will have on the

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operations. This empowers businesses to better manage things and take steps ahead of any contingencies.

4. **Monetize costs and benefits.**

We must ensure to place all costs and all benefits in the same monetary unit.

5. **Discount costs and benefits to obtain present values.**

It implies converting future costs and benefits into present value. It is also known as discounting the cash flows or benefits by a suitable discount rate. Every business tends to have a different discount rate.

6. **Calculate net present values.**

It is done by subtracting costs from benefits. The investment proposition is considered efficient if a positive result is obtained. However, there are other factors to be considered, as well.

Principles of Cost-Benefit Analysis

- **Discounting the costs and benefits** – The benefits and costs of a project have to be expressed in terms of equivalent money of a particular time. It is not just due to the effect of inflation but because a dollar available now can be invested, and it earns interest for five years and would eventually be worth more than a dollar in five years.
- **Defining a particular study area** – The impact of a project should be defined for a particular study area. E.g., A city, region, state, nation, or the world. It's possible that the effects of a project may “net out” over one study area but not over a smaller one.
- The specification of the study area may be subjective, but it can impact the analysis to a significant extent.
- **Addressing uncertainties precisely** – Business decisions are clouded by uncertainties. It must disclose areas of uncertainty and discretely describe how each uncertainty, assumption, or ambiguity has been addressed.
- **Double counting of cost and benefits must be avoided** – Sometimes though each of the benefits or costs is seen as a distinct feature, they might be producing the same economic value, resulting in the dual counting of elements. Hence these need to be avoided.

Importance of Cost-Benefit analysis

- **Determining the feasibility of an opportunity:** Nobody wants to incur losses in business. When a massive sum of money is invested in a project or initiative, it should at least break even or recover the cost. To determine whether the project is in the positive zone, the costs and benefits are identified and discounted to present value to ascertain the viability.
- **To provide a basis for comparing projects:** With so many investment choices around, there has to be a basis for choosing the best alternative. Cost-benefit analysis is one the aptest to tools to pick through the available options. When one out of the two options seems more beneficial, the choice is simple. However, a problem arises when there are more than two alternatives to evaluate. This model helps businesses to rank the projects according to their order of merit and go for the most viable one.
- **Evaluating Opportunity Cost:** We know that the resources at our disposal are finite, but investment opportunities are many. Cost-benefit analysis is a useful tool for comparing and selecting the best option. However, while choosing the most viable project, it is also imperative to be aware of the Opportunity Cost or the cost of the next best alternative

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foregone. It helps businesses to identify the benefits that could have arisen if the other option was chosen.

- **Performing Sensitivity Analysis for the various real-life scenarios:** Situations are not always the same, and the exact outcome cannot be predicted. The discount rate can be tested over a range. Sensitivity analysis can be instrumental in improving the credibility of a Cost-benefit analysis and is mainly used where there is ambiguity over the discount rate. The investigator may change the discount rate and the horizon value to test the sensitivity of the model.

Securitisation

Securitization can be defined as a process of converting illiquid financial assets into a combined investment instrument that reduces the risk of non-payment.

In other words, a bank has a long-term loan that cannot be converted into cash quickly. Hence, this loan is then used to issue an investment instrument (security) through a particular purpose vehicle to the investors who will get interest income from the security issued.

The entire process of converting an asset into securities, or investment instruments, is called securitization.

Purpose of the Securitization

- The primary purpose is to mitigate the credit risk of non-payment or default of the loans given to the borrowers lying as assets in the bank's balance sheet.
- Through securitization, the banks can raise capital and add more loans to their assets.
- Securitization helps increase liquidity by pooling the debt/financial assets into securitized investment instruments.

Key Players of Securitization

Broadly, in the entire securitization process, three key players make the process working. So, let's understand who these players are.

1. Asset Originator

The asset originator is the bank or a financial institution that has lent money to the borrowers and has loans such as housing, student, personal loans, etc., on the asset side of its balance sheet.

2. Issuing Entity (Special Purpose Vehicle)

The assets getting securitized by the banks or financial institutions are done by issuing agents or entities that create a special purpose vehicle (SPV). SPV helps in the conversion of illiquid assets into tradable securities and is the key to any securitization process without which it is incomplete.

3. Investors

Finally, the debt pooled through SPVs is converted into investment instruments which are then sold to the investors who buy such securities in exchange for a fixed income. The fixed income is paid as the original borrower pays off the loans to the asset originator (banks).

The Process of Securitization: How Does it Work?

The securitization process is quite similar, be it either banks, financial institutions, or any corporate.

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The securitized instruments are also called collateralized Debt Obligations as they are created by pooling debt/financial assets. Understanding the process will help you with a better knowledge of the concept of securitization.

1. Identifying Illiquid Assets

The preliminary idea of the securitization process is to convert the illiquid assets into an investment instrument that generates more capital to increase such assets.

Illiquid assets are those assets that take quite an extended period to get converted into physical cash. Long-term loans such as housing, student, and personal loans are illiquid as the tenure of such loans is pretty long.

Banks and financial institutions have such loans in large numbers, and they generally try to convert them into securitized instruments.

2. Combining the Illiquid Assets

Once the illiquid assets are identified, they are combined to create a pool. One more reason why they are combined is that an individual asset may have higher credit risk, but when they are combined, the risk reduces essentially.

3. Converting Illiquid Assets into Investment Instruments

The SPVs discussed earlier come into the picture in this step, where they help such illiquid assets be converted into securitized investment instruments.

Typically, such instruments offer fixed interest to investors. This is called the securitization of illiquid assets.

4. Issuing Investment Instruments to the Investors

After the pool is created, they are issued, and interested investors invest in such securitized instruments. The securitization process helps both the investors and the banks get a return, and the banks can raise capital.

Conclusion

It may sound a bit complicated at once, but the securitization process is an interesting one.

Once it is understood, we make better investment decisions as well. While banks can raise capital through such a process, the investors also get an investment instrument that pays higher returns than FDs at a fixed rate at fixed intervals.

Syndication

Meaning and Definition of Loan/Credit Syndication

The loan syndication is the leading and conventional way of cross border lending. If there is requirement of large amount of loan then the different banks combines themselves to grant loan.

It is also known as credit syndication. It was evolved in U.S. by the law of U.S. which has defined a particular limit on lending facility of a single bank on a single borrower.

It is a contract between two or more banks or lending institutions to grant loan to the borrower on the same loan documents.

There is the single loan agreement of the syndicated loan provided by the banks which are known as participants to the borrower. The loan is controlled by an agent and an agent can also

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be participants. The participants give certain amount of loan and receive same amount of repayments. The organizing of the loan is done by an arranger.

Also, the loan syndication is the type of joint venture whereas all the type of joint venture is not same like syndication. In simple words, a syndicated loan is the group of people which contribute money to buy a land or other property for attaining profit. They can be a person or an institution who is planner of the group.

For example, there is syndicator when the person or entity assemble the deal together and then give chance to the other people and institutions to: contribute for achieving the development or acquisition.

The Loan Syndication Service is the project financial service given by the merchant banker in which financial service is planned and obtained from various financial institutions, banks or other lending institutions. It is done for arranging capital both for fixed capital and working capital. It is also known as 'Loan/Credit Syndication Service' as there is inclusion of various lending institutions for granting loan.

It is basically done when there is requirement of large amount of loan, the syndication lets numerous lenders grant loan and also maintain the more reasonable and manageable credit options as they are the only creditor.

Participants in Loan Syndication

The various participants in loan syndication are the following :

1) Lead Bank :

The lead bank is the bank which contributes the highest amount in the loan.

2) Managing Bank :

The managing bank is selected by the borrower which requires loan. The managing bank organises loan. It helps in filing loan application, it discusses the terms and conditions with other banks and organises the syndicate. After getting the signature from the borrower and participating banks the work of the managing bank is ended.

3) Agent Bank :

The agent bank is the bank employed by the participating bank for safeguarding the interest after the loan agreement is signed. They come after the managing bank.

4) Participating Bank :

The banks which are participating are divided into two types. The types are as follows :

- The wholesale large commercial banks which grant loan and take the highest share.
- The retail sector small bank which grants loan take any percentage of share as given to them.

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Features of Loan Syndication

The features of loan syndication are as follows :

1) Required for Large Amount of Loan :

The loan syndication is only required for the large amount of loan. It cannot be used for small amount of loan as it can be given by the single bank.

2) No Separate Agreement Requirement :

All the lending institutions involved in loan syndication: work on the single agreement. It does not require the separate agreement for all the lending institutions.

3) High Repute Borrowers :

As the loan syndication is done for huge amount so the loan is granted only to the high reputed borrowers. There is basically the big corporate house as the borrower of loan syndication. It is done for long time period i.e. from 3 to 15 years.

4) Less Risk :

There is less risk involved in loan syndication as if the borrowers is not able to pay the loan amount, than the single landing institutions will not bear all the loss/risk but instead all the bank in syndication group will share the loan according to the amount contributed by all the lending institutions.

Types of Loan Syndication

The various types of loan syndication's are as follows :

1) Term Loan Facility :

Term loan facility is the type of loan syndication in which the certain amount of capital is granted by the lending institution for certain time period as specified in the term loan facility. The repayment is done according to the Loan Market Association (LMA) in which the borrower pays either in installment or one payment at the end of time period. The term loan facility finishes as the loan is repaid. The single payment term is known as a bullet repayment.

2) Revolving Loan Facility :

In the revolving loan facility, the borrowers will be capable of borrowing till the maximum amount of the syndicated loan is repaid and he can further withdraw the advanced capital at the time of converting term loan facility. It can also be resolved by extending the time period like from) two month to nine months. By the end of the time period, it is usually due for repayment but is refined as the "rollover loan".

3) Underwritten Transactions :

It is also known as a 'Bought Deal' in this the overall amount of the facility is given to the borrower according to the pre-decided terms and conditions. The underwriting of the loan is carried out by an arranger which takes the overall risk and will be part of the syndicate process. It is required when there is short changing time period like at the time of acquisition. It helps the borrowers by providing the fast grant of loan and also saving the confidential and price-saving information. The borrowers are supposed to pay higher fee to the arranger than the normal fees. There is two or three joint arrangers if the amount of loan is high.

4) Arranged or Best Efforts Transactions :

In this the arranger grant the loan for only some amount as possible and manages the leftover amount from the syndicate. It is helpful for borrowers who are sure that they will get the whole amount by the loan syndication and will also increase the banking relationship. The borrower is related with the market risk and it is not certain that all the amount will be granted as loan and has to pay the small amount as a fee to the arranger.

5) Club Deals :

In the club deals, borrower does not appoint the arranger but by the help of its own relationship with the banks arranges for the loan syndication. The borrower act both as the arranger and agent for itself. The relationship with the bank of the borrower needs to be strong for getting finance for the project. There are different situation which bring different structure but they agreement with all the banks will remain the same.

Concept of Gross and Net NPA'S

NPA expands to non-performing assets (NPA). Reserve Bank of India defines NPA as any advance or loan that is overdue for more than 90 days. "An asset becomes non-performing when it ceases to generate income for the bank," said RBI in a circular form 2007. To be more attuned to international practises, RBI implemented the 90 days overdue norm for identifying NPAs has been made applicable from the year ended March 31, 2004. Depending on how long the assets have been an NPA, there are different types of non-performing assets as well.

What is an asset for a bank?

Asset means anything that is owned. For banks, a loan is an asset because the interest we pay on these loans is one of the most significant sources of income for the bank. When customers, retail or corporates, are not able to pay the interest, the asset becomes 'non-performing' for the bank because it is not earning anything for the bank. Therefore RBI has defined NPAs as assets that stop generating income for them.

Categories of NPA

There are different types of non-performing assets depending on how long they remain in the NPA category.

a) Sub-Standard Assets

An asset is classified as a sub-standard asset if it remains as an NPA for a period less than or equal to 12 months.

b) Doubtful Assets

An asset is classified as a doubtful asset if it remained as an NPA for more than 12 months.

c) Loss Assets

An asset is considered as a loss asset when it is "uncollectible" or has such little value that its continuance as a bankable asset is not suggested. However, there may be some recovery value left in it as the asset has not been written off wholly or in parts.

NPA Provisioning

Keeping aside the technical definition, provisioning means an amount that the banks set aside from their profits or income in a particular quarter for non-performing assets; such assets that may turn into losses in the future. It is a method by which banks provide for bad assets and to maintain a healthy book of accounts.

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Provisioning is done according to which category the asset belongs to. The categories have been mentioned in the above section. Not only the type of asset, but provisioning also depends on the type of bank. Like, Tier-I banks and Tier-II banks have different provisioning norms.

Concept of Gross and Net NPA'S

What is Gross Non-Performing Assets?

Gross non-performing assets is a term used by financial institutions to refer to the sum of all the unpaid loans which are classified as non-performing loans.

Credit institutions offer loans to their customers who fail to be honoured and within ninety days, financial institutions are obligated to classify them as non-performing assets because they are not receiving either principle or net payments.

What is Net Non-Performing Assets?

Net non-performing assets is a term used by credit institutions to refer to the sum of the non-performing loans less provision for bad and doubtful debts. Credit institutions tend to provide a precautionary amount to cover the unpaid debts.

Therefore, if one deducts provision for unpaid debts from the unpaid debts, the resulting amount refers to the net non-performing assets.

Difference between Gross NPA and Net NPA

1. Meaning

One of the main difference between gross non-performing assets and net non-performing assets arises from the meaning. Gross non-performing assets refer to the total amount of the debts that an organization has failed to collect or the people owing the organization has failed to honor their contractual obligations of paying both the principal and interest amount.

On the other hand, net-non performing loans is the amount that results after deducting provision for doubtful and unpaid debts from the sum of the loans defaulted. It is the actual loss that the organization incurs after loan defaults.

2. Default Period

Credit institutions offer a grace period after which an individual is required to start paying the loan and its associated interests. If the payment duration expires, the institution is obligated to write-off those debts which are not paid.

Non-performing loans are listed as default after ninety days which is internationally recognised. Any amount that is due after the ninety-day grace period is classified as a default. However, net-non performing asset does not have a grace period and is immediately calculated and classified as a net non-performing asset.

3. Method of Calculation

Gross non-performing loans are the sum of all the loans that have been defaulted by the individuals who have acquired loans from the financial institution. This means that all loans defaulted are added together to form gross non-performing assets.

$$\text{Gross NPA} = (A_1 + A_2 + A_3 \dots\dots\dots + A_n) / \text{Gross Advances}$$

Where A_1 stands for loans given to person number one.

On the other hand, net non-performing assets are the amount that is realized after provision amount has been deducted from the gross non-performing assets.

$$\text{Net NPA} = (\text{Total Gross NPA}) - (\text{Provision for Unpaid Debts}) / \text{Gross Advances}$$

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4. Actual Loss

The other difference between gross non-performing assets and net non-performing assets is what the organization refers to as the actual loss facing the company. Gross non-performing assets do not constitute the actual loss facing the organization.

Net non-performing assets constitute the actual loss experienced by the organization after debts have defaulted. Since the credit institution has already provided for unpaid loans, the provided amount is deducted from default amount which results in the actual loss experienced by the organization.

5. Causes of Gross NPA and net NPA

There are some significant factors that have been highlighted to be the extreme causes of gross non-performing assets include poor government policies, industrial sickness, natural calamities, willful defaults, and ineffective recovery tribunal among others.

Although net non-performing assets are principal products of gross non-performing assets, there is a significant difference in that the amount provided by the credit institution to cover for unpaid debts plays a vital role in determining the amount of net non-performing assets.

6. Effects of Gross NPA and Net NPA

Some of the significant causes of gross non-performing assets include the bad effect on the goodwill of the company and bad effect on the equity value of the organization.

A company with bad equity value experiences difficulties in attracting investors due to low return on investment and low share value of the company.

On the hand, net non-performing assets have significant impacts on profitability and liquidity of the company. Low liquidity means that the company does not have enough cash to meet its obligations when they fall due which means the company cannot afford to run the daily activities.

Difference between Gross NPA and Net NPA

GROSS NPA VERSUS NET NPA

Basis For Difference	Gross NPA	Net NPA
Meaning	Sum of loans Defaulted	Default Loans – Provision for Default
Default Period	Ninety Days	Immediately
Actual Loss	Not Actual Loss	It is the Actual Loss
Causes	Poor government policies, industrial sickness, natural calamities etc.	Low Provision for Unpaid Debts
Effects	Equity and Company Goodwill	Profitability and Liquidity

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Causes of NPA's

1. **Willful Defaults:-** The Indian Public Sector Banks are worst hit by these defaults. It is a default in repayment obligation. Kingfisher Airlines Ltd. Is one among many of those willful defaulters. Other are Beta Napthol, Winsome Diamonds & Jewellery Ltd., Rank Industries Ltd., XL Energy Ltd. etc.
2. **Industrial Crisis:-** Industries depend on banks to fulfill their projects. If industry is in crisis, it is bound to hit the banking sector and their NPA will rise.
3. **Credit distribution Mis-management:-** Often ill-minded borrowers bribe bank officials to get loans with an intention of default.
4. **Lenient Lending Norms:-** One of the main reasons of rising NPAs is the lenient Lending Norms especially for corporate honchos where their financial status and credit rating is not analysed properly.

Recovery of NPA's

Recovery mechanism is a process of carrying out the recovery procedures and mechanisms required to restore the financial assets in the event of failure to repay by the borrower. An NPA as explained above is an asset that has ceased to generate income and returns which if not dealt with correctly and promptly can be detrimental to the bank and therefore the recovery of NPAs plays an important role to sustain the banking industry.

Mainly recovery is done through the following aspects:

1. Lok Adalats

The Lok Adalat is one of the alternative dispute redressal mechanisms set up by the government. It is a forum where disputes or cases pending in the court of law or at pre-litigation stage are settled mutually. Lok Adalats have been given statutory status under the Legal Services Authorities Act, 1987. Under the said Act, the decision made by the Lok Adalats is deemed to be a decree of a civil court and is final and binding on all parties and no appeal against such an award lies before any court of law.

If the parties are not satisfied with the award of the Lok Adalat though there is no provision for an appeal against such an award, however they can initiate litigation by approaching the appropriate court by filing a case by following the required procedure exercising their right to litigation. The jurisdiction of the Lok Adalats is in cases/disputes of less than 10 lakh rupees in value.

The persons deciding the cases in the Lok Adalats are called the Members of the Lok Adalats and they have the role of statutory conciliators only and do not have any judicial role. Therefore, they can only persuade the parties to come to a conclusion for settling the dispute outside the court in the Lok Adalat and shall not pressurize or coerce any of the parties to compromise or settle cases or matters either directly or indirectly.

The Lok Adalat cannot decide the matter referred to it on its own but instead it is to be decided on the basis of the compromise or settlement between the parties. The members shall assist the parties in an independent and impartial manner in their attempt to reach amicable settlement of their dispute. Mobile Lok Adalats are also organized in various parts of the country which travel from one location to another to resolve disputes in order to facilitate the resolution of disputes through this mechanism.

As on 30.09.2015, more than 15.14 lakhs Lok Adalats have been organized in the country since its inception. More than 8.25 crore cases have been settled by this mechanism so far.[6]

2. Debt Recovery Tribunals (DRTs)

The Recovery of Debts Due to Banks and Financial Institutions Act, 1993 (RDDBFI Act) made provisions for speedy redressal to lenders and borrowers through filing of Original Applications also known as OAs in the Debt Recovery Tribunals (DRTs) and appeals in Debts Recovery Appellate Tribunals (DRATs). Therefore, under the RDDBFI Act the DRTs and DRATs have been established to help provide for the need of speedy redressal for banks against NPAs.

The DRT also has the power to decide upon the applications filed against the secured creditors by the borrower or mortgager for the action taken by them under the Securitization Act. As of today, the government has established 39 DRTs and 5 DRATs, which are single Member Tribunals. The problem plaguing the DRTs like several other debt recovery mechanisms is that they are slow to work out on pending disputes as the process is very long which results in a high number of pending cases.

3. Sarfaesi Act

The Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 better known as the SARFAESI Act was formed after the considerations carried out by committees constituted by the government to examine the reforms and changes that are needed in the banking and legal systems for better functioning of the debt recovery mechanisms.

The main purpose of this Act is to provide speedy recovery of defaulted loans and help reduce the mounting stress on the banks due to the increase in NPAs. The act provides the banks and financial institutions with a mechanism to better recovery of assets by enabling them to take possession of securities and sell them to reduce the burden of the Non-Performing Asset.

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The Act aims to achieve recovery of NPAs through three major ways which are the following:

i. Securitization:

The Section 7 of the SARFAESI Act gives an outlook of what exactly happens in securitization, it states that any securitization company or reconstruction company, may, after acquisition of any financial asset offer security receipts to qualified institutional buyers, (other than by offer to public) who are those who have expertise and sound knowledge to evaluate and make their investment in the Capital Markets, for subscription in accordance with the provisions of those Acts.

A securitization company or reconstruction company may raise funds from the qualified institutional buyers by formulating schemes for acquiring financial assets and shall keep and maintain separate and distinct accounts in respect of each such scheme for every financial asset acquired out of investments made by a qualified institutional buyer and ensure that realizations of such financial asset is held and applied towards redemption of investments and payment of returns assured on such investments under the relevant scheme. The main advantage of securitization is that it allows the institutions to raise finances by selling assets or income streams.

ii. Asset Reconstruction:

In Asset Reconstruction the Securitization companies or Reconstruction Companies buy the NPAs from the banks and take measures to recover the bad loans from the borrower by carrying certain functions according to the powers vested in them by the Act.

Section 9 of the SARFAESI Act gives measures for asset reconstruction such as:

- a. The proper management of the business of the borrower;
- b. Changing or taking over the management of the business of the borrower;
- c. The sale or lease of a part or the whole of business of the borrower;
- d. Rescheduling the payment of debts payable by the borrower;
- e. Enforcement of security interest in accordance with the provisions of the SARFAESI Act;
- f. Settlement of dues payable by the borrower;
- g. Taking possession of secured assets in accordance with the provisions of the SARFAESI Act.

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Thus, Asset Reconstruction helps the banks reduce the burden of NPAs on banks as when a Securitization company or Reconstruction Company takes over the NPA the banks and financial institutions can get returns on the NPA which reduces the stress of bad loans on banks and other institutions.

iii. **Enforcement of Security Interests:**

The Section 13 of the SARFAESI Act makes provisions for enforcement of security interests it states that notwithstanding anything contained in section 69 or section 69A of the Transfer of Property Act, 1882 any security interest created in favour of any secured creditor may be enforced, without the intervention of court or tribunal, by such creditor in accordance with the provisions of this Act.

Where any borrower, who is under a liability to a secured creditor under a security agreement, makes any default in repayment of secured debt or any instalment thereof, and his account in respect of such debt is classified by the secured creditor as non-performing asset, then, the secured creditor may require the borrower by notice in writing to discharge in full his liabilities to the secured creditor within sixty days from the date of notice failing which the secured creditor may take recourse to one or more of the following measures to recover his secured debt, namely:

- a. take possession of the secured assets of the borrower including the right to transfer by way of lease, assignment or sale for realizing the secured asset;
- b. take over the management of the business of the borrower including the right to transfer by way of lease, assignment or sale for realizing the secured asset;
- c. appoint any person (hereafter referred to as the manager), to manage the secured assets the possession of which has been taken over by the secured creditor;
- d. require at any time by notice in writing, any person who has acquired any of the secured assets from the borrower and from whom any money is due or may become due to the borrower, to pay the secured creditor, so much of the money as is sufficient to pay the secured debt.

The section 14 of the SARFAESI act is another provision to help the secured creditors, it states that chief metropolitan magistrate or district magistrate shall assist the secured creditor in taking possession of the secured asset.

The secured creditor can for the purpose of taking possession or control of

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any secured asset make a request in writing to the Chief Metropolitan Magistrate or the District Magistrate within whose jurisdiction any such secured asset or other documents relating to the secured asset may be situated or found, to take possession of the said asset or documents and the Chief Metropolitan Magistrate or the District Magistrate shall on such request being made to him:

- a. take possession of such asset and documents relating thereto; and
- b. forward such assets and documents to the secured creditor.

The section goes further to state that for the purpose of securing compliance with the provisions the Chief Metropolitan Magistrate or the District Magistrate may take or cause to be taken such steps and use, or cause to be used, such force, as may, in his opinion, be necessary. It also states that no act of the Chief Metropolitan Magistrate or the District Magistrate done in pursuance of this section shall be called in question in any court or before any authority.

4. Insolvency And Bankruptcy Code (IBC)

Before the Insolvency and Bankruptcy Code, 2016 came into force there were multiple laws and institutions that were overlapping in jurisdiction and functioning which lead to a lot of confusion in dealing with the insolvency and bankruptcy proceedings against individuals and companies. There was no legal framework which provided an efficient procedure to help the debt recovery process in India which was hurting the banks and other financial institutions and affecting the flow of credit. To overcome these hurdles the government introduced the Insolvency and Bankruptcy Code Bill in 2015 which was then passed in 2016 and came into force.

There were first 4 forums which dealt with matters of insolvency and bankruptcy which were the High court, Board for Industrial and Financial Reconstruction (BIFR), Debt Recovery Tribunal (DRT) and Company Law Board (CLB), upon the enforcement of the IBC the burden of these forums was reduced as now all the matters in relation to the code were to be filed in the National Company Law Tribunal (NCLT). The main purposes of the IBC is to provide speedy remedies for the banks against NPAs and also to reduce the burden of the long pending cases in courts.

The IBC has made a provision for the formation of the Insolvency and Bankruptcy Board of India which is responsible for implementation of the Code that consolidates and amends the laws relating to reorganization and insolvency resolution of corporate persons, partnership firms and individuals in a time bound manner for maximization of the value of assets of such persons, to promote entrepreneurship, availability of credit and balance the interests of all the stakeholders. The IBC also makes provisions to make a formal Insolvency Resolution Process (IRP).

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Asset Recovery Companies

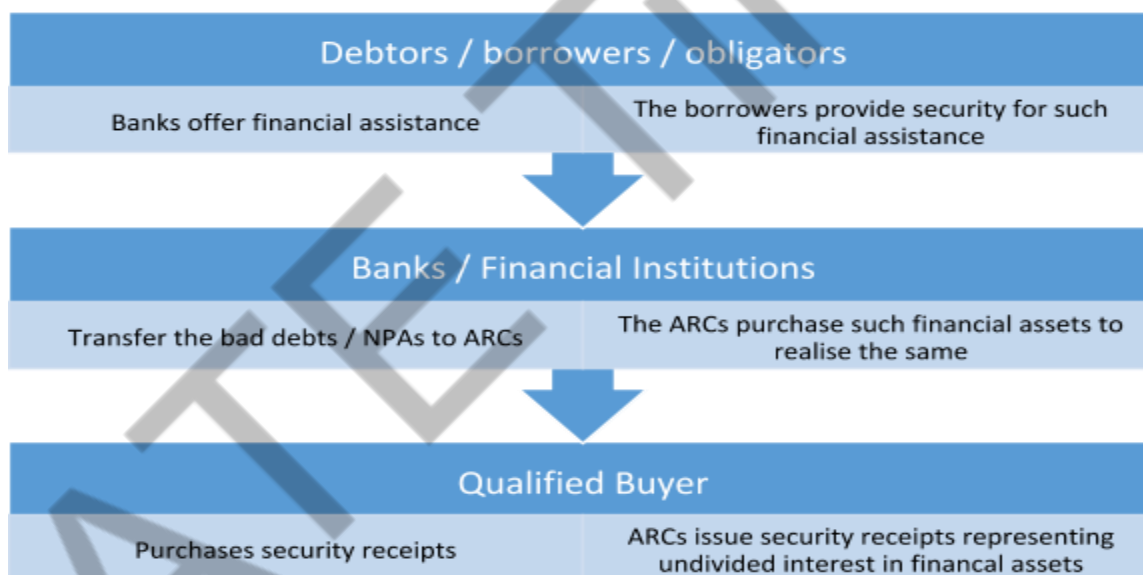
An asset reconstruction company is a special type of financial institution that buys the debtors of the bank at a mutually agreed value and attempts to recover the debts or associated securities by itself.

The asset reconstruction companies or ARCs are registered under the RBI and regulated under the Securitisation and Reconstruction of Financial Assets and Enforcement of Securities Interest Act, 2002 (SARFAESI Act, 2002).

The ARCs take over a portion of the debts of the bank that qualify to be recognised as Non-Performing Assets. Thus ARCs are engaged in the business of asset reconstruction or securitisation or both.

All the rights that were held by the lender (the bank) in respect of the debt would be transferred to the ARC. The required funds to purchase such debts can be raised from Qualified Buyers.

The working of the ARC can be summarized by the following diagram:



The business of asset reconstruction or securitisation may be commenced only after obtaining a registration certificate under Section 3 of the SARFAESI Act, 2002. The main requirement in this regard is that the 'net owned funds' as prescribed in the RBI Act should be Rs. 100 crore or more.

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Bad Bank

A Bad Bank houses Bad loans or Non-Performing Assets (NPA). The idea of Bad Bank was implemented in countries like Sweden, Finland, France, Germany, Indonesia etc. Even with Bad Bank structure, the Non-Performing Assets (NPA) losses do not go away. It needs to be shared between investors, taxpayers of these banks in general and those of the bad bank.

The bad bank will manage Non-Performing Assets in suitable ways, some may be liquidated, others may be restructured, etc. In the meantime, it would work towards suitably disposing of the toxic assets. This concept has been successfully implemented in many western European countries post the 2007 financial crisis like Ireland, Sweden, France etc.

Recent Proposal of Bad Banks by Indian Banking Association (IBA)

Indian Banking Association (IBA) has submitted a proposal to both the Government and the Reserve Bank of India (RBI) to set up a 'Bad Bank.'

As per IBA estimates the 'Bad Bank' would require approximately Rs 10,000 crore of capital initially. The exact quantum of capital and amount of bad loans to be housed in the proposed 'Bad Bank' would only be finalised after discussions with the Government and Reserve Bank of India (RBI).

Bad Bank – Origin of Concept

The concept of a bad bank was pioneered at the Pittsburgh-headquartered Mellon Bank in 1988. Bad Bank would set up as a separate entity that would buy the Non-Performing Asset from other banks to free up their books for fresh lending. It is focused on the task of recovery.

A bank may accumulate a large portfolio of debts or other financial instruments which unexpectedly become at risk of partial or full default. A large volume of non-performing assets usually make it difficult for the bank to raise capital, for example through sales of bonds.

In these circumstances, the bank may wish to segregate its "good" assets from its "bad" assets through the creation of a bad bank.

How Does 'Bad Bank' Work?

1. Banks will be able to demarcate their assets into good assets and toxic or bad assets.
2. Good assets are ones in which loans are repaid as per schedule, and defaulted ones are classified as toxic assets or bad assets.
3. Toxic assets can be removed from Banks books and transferred to Bad Bank which has the sole purpose of aiding the recovery of risky assets.
4. Hence the banks will clean up and reduce their exposure to risky assets.
5. Bad Bank will absorb all the toxic assets of banks at a price below the book value of these loans.

What is the Need for a Bad Bank?

Investors would see large NPA's as a sign of Banks ill-health or financial weakness. If the NPA's are high, then the Bank loses its ability to borrow, lend or conduct business.

Bad Bank Structure – IBA Proposal

The 'Bad Bank' will be a 2 tiered structure.

Tier 1:

1. There will be an Asset Reconstruction Company (ARC) backed by the Government which would buy bad loans from banks and issue Security Receipts to the Banks.
2. As per RBI guidelines, ARC will hold Security Receipts of 15%.

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3. Banks will get 15% of the cash and will hold 85% of Security Receipts. Hence it is called 15:85 structure.

Tier 2:

1. There will be an Asset Management Company (AMC).
2. AMC would be run by public and private bodies which includes banks as well.
3. Turnaround professionals.

Past Debates on Bad Banks

The idea of Bad Bank is not new. Currently, this is in the news due to the problem caused by COVID-19. Earlier the topic of Bad Bank was a matter of debate in the banking and finance circles when former Interim Finance Minister Piyush Goyal had put forward the idea when a committee headed by Sunil Mehta was formed to study the feasibility of National Asset Reconstruction Company. Even in 2017 Economic Survey had mooted the idea by suggesting the creation of Public Sector Asset Rehabilitation Agency (PARA). Even former RBI governor Raghuram Rajan had started a debate on Bad Banks in 2015 as a possible solution to the problems of Non Performing Assets.

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UNIT-3

Regulation and Innovation in Banking System

The onset of the pandemic has caused an unpredicted increase in the demand among consumers for digital banking, including instant access to banking services, products, and information. In such circumstances, there can be no better time than the present to welcome the future of banking with digital bank, particularly when the world is stricken by the ever-increasing variants of the covid-19 virus and its ensuing plague that requires the restriction of free movement and avoidance of public spaces.

The growing use of technology has also led to tremendous changes in conventional ways of finance and keeping its eye on the advancement of digital technology around the globe. India has kept its pace with the rest of the world in technology innovation for digital inclusion in the financial sector.

The Reserve Bank of India (RBI), the primary regulator of the financial sector in India, has been conscious of the importance of technology-based innovations and its growing use in India. In 2019, the RBI issued its “Enabling framework for regulatory sandbox” guidelines. Under this, fintech companies – including startups, banks, financial institutions and any other company partnering with or providing support to financial services businesses – which also satisfy the eligibility criteria, are selected to test their products in the regulatory sandbox. This allows for the testing of new products, innovations and technologies in a live environment within specified parameters and timeframes under the aegis of the RBI.

Regulation of Banks

The financial system in India is regulated by independent regulatory bodies in different fields namely banking, capital market, insurance, commodity market, and pension funds. However, the Government of India plays an important role in influencing the regulatory framework of these institutions, at least to some extent.

Primarily, in India, the regulation of banks and financial institutions are governed by the Banking Regulation Act, 1949. It was passed as Banking Companies Act, 1949, and came into effect from March 16, 1949. Further, the name was changed to the Banking Regulation Act from March 1, 1966.

For a banking job aspirant, it is pertinent to know about the working and regulation of the financial institutions in India. From the examination viewpoint, objective questions can be asked regarding the Chairperson of regulatory bodies, the location of headquarters, year of establishment, etc.

Moreover, questions on the Banking Regulation Act and recent developments related to it can also be asked in Main and Interview.

Let us now briefly discuss the regulations of banks and financial institutions in detail:

Banking Regulation Act, 1949

Following are the important points regarding the Banking Regulation Act, 1949:

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1. It regulates all banking institutions in India. Initially, it was applicable only to banking companies, but was amended in 1965 to bring the cooperative banks under its purview. Cooperative banks are formed and run by the state government, but the licensing and regulation are under the control of the RBI.
2. This Act gives the RBI the power to license banks, and have regulation over the shareholding; regulate the operations of banks; supervise the appointment of Board and management; lay down audit instructions; issue directives in the interest of public good; control moratorium, mergers, liquidations, and acquisitions; and impose penalties.

Important Banking Regulatory Bodies in India

Regulatory Body	Sector	Headquarters
Reserve Bank of India (RBI)	Banking & Finance	Mumbai
Securities & Exchange Board of India (SEBI)	Stock & Capital Market	Mumbai
Insurance Regulatory & Development Authority of India (IRDA)	Insurance	Hyderabad
Pension Fund Regulatory & Development Authority (PFRDA)	Pension	New Delhi
National Bank for Agriculture & Rural Development (NABARD)	Financing Rural Development	Mumbai
Small Industries Development Bank of India (SIDBI)	Financing Micro, Small & Medium Enterprises (MSMEs)	Lucknow

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National Housing Bank Financing Housing New Delhi
(NHB)

Insolvency and Insolvency Proceedings New Delhi
Bankruptcy Board of
India (IBBI)

Let us now discuss some important regulatory bodies:

The Reserve Bank of India (RBI)

Established under the RBI Act, 1934, RBI is the central bank of India; and is vested with various responsibilities under the Banking Regulation Act, 1949. Following are some of its primary functions:

1. Issuance of banknotes
2. Banker to the government
3. Custodian of cash reserves of commercial banks
4. Custodian of foreign exchange reserves
5. Controller of credit
6. Lender of the last resort

Basel Accords I, II, and III

Basel accords are introduced by Basel Committee of Banking Supervision (BCBS), a committee of banking supervisory authorities that was incorporated by the central bank governors of the Group of Ten (G-10) countries in 1975. The main objective of this committee is to provide guidelines for banking regulations. BCBS has issued 3 accords named Basel 1, Basel 2 and Basel 3 so far with the intention of enhancing banking credibility by strengthening the banking supervision worldwide. The key difference between **Basel 1 2 and 3 is that Basel 1 is established to specify a minimum ratio of capital to risk-weighted assets for the banks whereas Basel 2 is established to introduce supervisory responsibilities and to further strengthen the minimum capital requirement and Basel 3 to promote the need for liquidity buffers (an additional layer of equity).**

What is Basel 1?

Basel 1 was released in July 1988 to provide a framework to address risk management from a bank's capital adequacy perspective. The principle concern here was the capital adequacy of banks. One of the main reasons for the same was the Latin American debt crisis during the early 1980s, where the committee realized that capital ratios of international banks are diminishing over time. A minimum ratio of capital to risk-weighted assets of 8% was stated to be implemented effective from 1992.

Basel 1 also specified the general provisions that can be included in the calculation of the minimum required capital.

E.g. The accord specified guidelines on how to recognize the effects of multilateral netting (an agreement between two or more banks to settle a number of transactions together as it is cost effective and time-saving as opposed to settling them individually) in April 1995.

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What is Basel 2?

The main objective of Basel 2 was to replace the minimum capital requirement with a need to conduct a supervisory review of the bank's capital adequacy. Basel 2 consist of 3 pillars. They are,

- Minimum capital requirements, which sought to develop and expand the standardised rules set out in the Basel 1
- Supervisory review of an institution's capital adequacy and internal assessment process
- Effective use of disclosure as a lever to strengthen market discipline and encourage sound banking practices

The new framework was designed with the intention of improving the way regulatory capital requirements reflect underlying risks and to better address the financial innovation that had occurred in recent years. The changes aimed at rewarding and encouraging continued improvements in risk measurement and control.

What is Basel 3?

The need for an update to Basel 2 was felt especially with the financial collapse of Lehman Brothers – a global financial services company which was declared bankrupt in September 2008. Pitfalls in corporate governance and risk management have led to the development of this accord which will be effective from 2019 onwards. The banking sector entered the financial crisis with too much leverage and inadequate liquidity buffers. Thus, the main objective of Basel 3 is to specify an additional layer of common equity (a capital conservation buffer) for banks. When breached, restricts payouts to help meet the minimum common equity requirement. Additionally, the following guidelines are also included in Basel 3.

- A countercyclical capital buffer, which places restrictions on participation by banks in system-wide credit booms with the aim of reducing their losses in credit busts
- A leverage ratio – a minimum amount of loss-absorbing capital relative to all of a bank's assets and off-balance sheet exposures regardless of risk weighting
- Liquidity requirements – a minimum liquidity ratio, the Liquidity Coverage Ratio (LCR), intended to provide enough cash to cover funding needs over a 30-day period of stress; a longer-term ratio, the Net Stable Funding Ratio (NSFR), intended to address maturity mismatches over the entire balance sheet
- Additional proposals for systemically important banks, including requirements for supplementary capital, augmented contingent capital and strengthened arrangements for cross-border supervision and resolution

Banking Innovations

Allowing a customer access to full banking services in real time, through any channel they choose is one of the results coming out of EU legislation known as the second Payment Services Directive (PSD2). Whether it's from an online terminal in a bank branch, an ATM, a voice call or online it allows customers the freedom of choice to access their accounts whenever and from wherever they choose.

Traditional banks are spending vast amounts of money to develop new systems and features so that they can keep up with the rapidly changing demands of their customers. As well, the institutions are looking for ways to streamline their own operations, improve performance and reduce overheads – any bank that fails to do this will quickly lose out in the face of competition both from traditional banks and from the new fintech players.

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Completely ‘digital only’ financial institutions also provide customers with seamless access to the whole range of activity, even though these banks do not compete with traditional banks in regular business fields such as credit, overdrafts, mortgages and so on. They can generally offer several distinct advantages over brick-and-mortar banks in the form of reduced costs, user friendly interfaces, wider range of features and easy account openings.

Retail banking innovation 2023

Retail banking, also known as consumer banking or personal banking, refers to the banking services that are provided to individual consumers, as opposed to businesses or other organizations. Retail banking innovation refers to the development and implementation of new ideas, technologies, and approaches in the retail banking sector.

Some examples of retail banking innovation include:

1. **Mobile banking:** Many banks now offer mobile banking apps that allow customers to manage their accounts, make payments, and conduct other banking tasks using their smart phones.
2. **Online banking:** Many banks now offer online banking platforms that allow customers to manage their accounts and conduct other banking tasks using their computers or other devices.
3. **Virtual assistants:** Some banks are using artificial intelligence (AI) and chat bot technology to provide customers with personalized assistance and support through virtual assistants.
4. **Contactless payment systems:** Many banks now offer contactless payment systems, such as near field communication (NFC) and QR code scanners, that allow customers to make payments using their mobile devices or smart watches.
5. **Personal financial management tools:** Some banks are offering personal financial management tools that help customers track and manage their spending, create budgets, and achieve their financial goals.

Overall, the goal of retail banking innovation is to improve the customer experience and make banking more convenient, efficient, and secure for consumers

Digital banking innovation ideas 2023

There are many potential ideas for digital banking innovation, including:

1. Mobile banking apps that allow customers to manage their accounts, make payments, and transfer money on the go.
2. Integration with popular payment platforms such as Apple Pay, Google Pay, and PayPal.
3. Use of artificial intelligence and machine learning to improve customer service, such as through chat bots that can answer common questions and provide personalized recommendations.
4. Implementation of biometric authentication methods, such as facial recognition or fingerprint scanning, to improve security and make it easier for customers to access their accounts.
5. Offering investment and wealth management services, such as robo-advisors, to help customers grow their wealth.
6. Integration with wearable devices, such as smart watches, to enable customers to make payments and check their account balances directly from their wrists.

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7. Implementing block chain technology to improve the security and efficiency of financial transactions.
8. Offering virtual reality or augmented reality experiences to enhance the customer experience and make banking more interactive and engaging.
9. Using data analytics to better understand customer needs and preferences, and to develop customized products and services.

Digital Banking

Digital Banking is the automation of traditional banking services. Digital banking enables a bank's customers to access banking products and services via an electronic/online platform. Digital banking means to digitize all of the banking operations and substitute the bank's physical presence with an everlasting online presence, eliminating a consumer's need to visit a branch.

Benefits of Digital Banking

Advancing to a more technologically sophisticated way of doing things, it goes without saying that the benefits long outweigh the costs. Similarly, digital banking as a technological by-product aims to make life easier for the customers of a bank. Digital banking has the following benefits:

- Digital banking enables consumers to perform banking functions from the comfort of their homes, be it an elderly person who is tired of waiting in lines or a working-class professional who is caught up with work, or a regular person who does not want to visit the bank's branch to run a single errand. It also **offers convenience**.
- Elaborating on the convenience offered, digital banking lets a user carry out banking work around the clock, with **24*7 availability of access** to banking functions.
- One of the biggest drawbacks of traditional banking was the overly placed importance on paper. Banking has become **paperless** with the development of digital banking as a service. A user can log into their account at any point in time to monitor records.
- Digital banking allows a user to **set up automatic payments** for regular utility bills such as electricity, gas, phone, and credit cards. The customer no longer has to make a conscious effort of remembering the due dates. The customer can opt for alerts on upcoming payments and outstanding dues.
- Online shopping has become a cakewalk with payment channels becoming well-integrated with the online shopping portals. Internet banking has significantly contributed to **online payments**.
- Digital banking extending **services to remote areas** is seemingly a step toward holistic development. With smart phones at affordable prices and internet access in remote areas, the rural population can make the most out of digital banking services.
- Digital banking-enabled fund transfers **reduce the risk of counterfeit currency**.
- With the help of digital banking, a user can report and block misplaced credit cards at the click of a button. This benefit greatly **strengthens the privacy** and security available to a bank's customer.
- By promoting a cashless society, digital banking **restricts the circulation of black money** as the Government can keep a track of fund movements. In the long run, digital banking is expected to lower the minting demands of a currency.

Digital Banking products

If an individual has access to a stable internet connection and an internet-enabled smart device, digital banking has a lot to offer.

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Digital Product services

Digital banking services	Utility
1. Obtain bank statements	View and download your bank statements for any specified period.
2. Transfer of Funds	With alternatives such as NEFT, RTGS, and IMPS available, the need to issue cheques and DDs has been eradicated.
3. Mobile banking	Mobile banking is digital banking through an application optimized for smartphones and tablets.
4. Cash withdrawals	ATMs facilitate cash withdrawals at any point in time. Moreover, ATMs are widely present in every locality.
5. Bill payments	Auto-debit feature for bill payments lets a user setup monthly debits in favor of regular utility payment.
6. Finance	Invest, raise loans, open fixed deposit accounts – all through digital banking. De-mat accounts can be linked to your bank accounts to provide a seamless flow of funds so you can invest promptly.
7. Manage cheques	Intervene in the cheque clearing process using digital banking to stop the cheque if the need arises.
8. Monitor transaction records	Banks send transaction alerts to the linked mobile number or email addresses. Transactions are updated almost as soon as executed. Digital banking also lets you monitor account balances or outstanding at the click of a button.

Types of Digital banking payments

- **Banking cards:** Cards are not only used to withdraw cash but also enable other forms of digital payment. Cards can be used for online transactions and on Point of Sale (PoS) machines. Prepaid cards can also be issued by the banks; such cards are not linked to the bank account but function through the money loaded onto them.
- **Unstructured Supplementary Service Data (USSD):** By dialing the number *99#, mobile transactions can be carried out without an application and internet connection. The number holds nationwide applicability and promotes greater financial inclusion on the ground level. The service lets the caller surf through an interactive voice menu and chooses the desired option on the mobile screen. The only catch is the mobile number of the caller should be the one linked to the particular bank account.
- **Aadhaar Enabled Payment System (AEPS):** AEPS lets the client initiate banking instructions following the successful verification of the Aadhaar number.
- **Unified Payments Interface (UPI):** UPI is the most trending form of digital banking presently. UPI makes use of a virtual payment address (VPA) so the user can transfer funds without entering bank account details or IFSC code. Another striking feature of UPI is that the applications let you consolidate all your bank accounts in one place. Funds can be transferred and received around the clock with no time restrictions. UPI-based apps in India are BHIM, PhonePe, and Google Pay. BHIM application, in addition to the transfer of funds to other virtual addresses and bank accounts, also lets the user transfer funds to another Aadhaar number. More importantly, UPI-based payments are free of cost.

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- **Mobile Wallets:** Mobile wallets have eliminated the need to remember four-digit card pins or enter CVV details or carry loose cash. Mobile wallets store bank account and card credentials to easily add funds to the wallet and make payments to other merchants with similar applications. Popular mobile wallets are Paytm, Freecharge, Mobiwik, etc. Mobile wallets, however, generally have a limit on how much can be deposited in the wallet. A small fee may also be charged on depositing the funds from the mobile wallet back into the bank account.
- **PoS terminals:** Typically, PoS machines are portable devices that read a card to authorize and complete the payment. Supermarkets and gas stations opt for this method of payment. However, with digital banking thriving, PoS terminals have evolved into more than physical PoS devices. Virtual and Mobile PoS terminals have surfaced, which makes use of the mobile phone's NFC feature and web-based applications to initiate payment.
- **Internet and Mobile Banking:** Commonly known as e-banking, internet banking refers to obtaining certain banking services over the internet, such as fund transfers, and opening and closing accounts. Internet banking is a subset of digital banking because internet banking is only limited to core functions. Similarly, mobile banking is availing banking services through mobile-based applications.

Plastic Money

Money is an indispensable part of our lives. But where did the need for money arise from? You may recall learning about a barter system, in which commodities were traded for goods, followed by an age when gold and silver coins were introduced. As humanity progressed, we began to use paper notes and coins for commercial transactions. With time, we also used technology to pay for commodities.

The use of plastic money came through technology. Plastic money is your debit or credit card, although it can also refer to the wire transfers of funds from one bank to another. Let us get a more holistic idea of what plastic money is.

What do you mean by plastic money?

Cards are increasingly being used in place of actual cash. Plastic money refers to these cards. Debit and credit cards represent plastic money. Plastic money has made it easier for us to carry out transactions in our daily lives. It has replaced cash payments across the world and established itself as a necessary form of instant money. It has made it simpler for us to buy items with some of the best credit cards in the market, which we could not otherwise afford.

Benefits of plastic money

Plastic money comes with many benefits, including:

1. Cashless living

Plastic money has not only made our lives easier but has also alleviated the hassles that come with carrying currency. Some of the best credit cards allow us to move around the world without worrying about carrying cash.

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2. Better security

One advantage of using credit or debit cards is the decrease in robberies and crimes. Hacking a card's PIN is difficult and necessitates the knowledge of certain procedures. As a result, credit and debit cardholders can be reasonably confident of the security of their funds.

3. Financial freedom

Credit cards allow a person to make a transaction and pay for it even when they do not have the funds. It is incredibly beneficial especially when you are short on cash. Credit cards also reduce the need to rely on others for financial assistance in an emergency. You can use the credit card to fund your requirement and later payback in instalments. Further, a credit card is easy to get. All you need to do is meet your bank's credit card eligibility criteria, and the card is yours.

4. Ease of doing transactions

Credit cards and debit cards can help make online payments, fund transfers, and other transactions with ease. It is incredibly simple to make payments with plastic money from any location. Furthermore, several online businesses provide discounts when paying using credit and debit cards.

5. Exciting deals and discounts

Every credit and debit card providers offers deals and discounts on shopping. They can help you save more and earn cashback on purchases.

6. Saving on travel

Travelling can be expensive without plastic money. Credit and debit cards provide lounge access and incredible deals on travel bookings. You cannot enjoy the same benefits while using cash, making plastic money a must if you are travelling.

Drawbacks of plastic money

Plastic money also has some downsides, such as:

1. Does not work everywhere

There may be certain venues and stores where only cash is accepted. For example, buying products from a small merchant or buying vegetables or newspapers.

2. Can land you in debt

If a person is not careful with plastic money, they can often overstep their spending limit and spend more than they can repay. This can land them in debt.

If you are in the market for credit and debit cards and want to transition from cash to plastic money, look no further than IDFC FIRST Bank. You will receive unsurmountable benefits if you use cards from IDFC FIRST Bank. From unlimited lounge access to huge discounts, the world is

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your playing field with IDFC FIRST Bank. So, wait no more; get your card from IDFC FIRST Bank today! Use our mobile banking apps to unlock the benefits of our manifold cards.

National Electronic Funds Transfer (NEFT)

The National Electronic Fund Transfer (NEFT) is a payment platform which is used nationwide by many banks. This allows the easy and hassle-free transfer of money from one bank account to another bank account. With the world slowly shifting to online banking, the concept of NEFT has become very popular in the country and is an easy way of transferring funds. It eliminates the need to visit the bank to transfer funds, as you can transfer funds while at home.

NEFT - Transaction Timings

Fund transfer through NEFT service can be used any time and, on any day, of the year. NEFT services are conducted every 30 minutes throughout the day in batches and processed by 9:30 am for any transaction made prior to this time.

How to make an NEFT transfer

The procedure for National Electronic Funds Transfer (NEFT) is mentioned below:

Step 1: First login to your net banking account. If you do not have a net banking account then register for it on the website of your bank.

Step 2: Add the beneficiary as a payee. To do so, you have to enter the following details about the beneficiary in the 'Add New Payee' section:

- Account Number.
- Name.
- IFSC Code.
- Account Type.

Step 3: Once the payee is added, choose NEFT as mode of Fund Transfer.

Step 4: Select the account you wish to transfer money from, the payee, enter the amount that you wish to transfer, and add remarks (optional).

Step 5: Click on submit.

Benefits of Using NEFT for Fund Transfer

NEFT offers a lot of benefits. Let's look into a few of these:

- The system allows the one-way cross-border transfer of funds from India to Nepal. This is under the Indo-Nepal Remittance Facility Scheme.
- With NEFT, you can easily transfer funds from one bank account of any branch to another account.
- It avoids the need for a physical instrument to transfer funds.
- There is no need for any physical presence of parties.
- NEFT is easy, simple and efficient.
- Money can be transferred via NEFT on holidays and weekends as well.
- You can initiate internet banking from any location.
- The confirmation of a transaction will be received via email and SMS notifications
- The real-time transactions of NEFT give assurance to both parties.

Real Time Gross Settlement RTGS

Real-Time Gross Settlement (RTGS) is a fund transfer method via which money is sent immediately without any delays. RTGS is typically meant for larger value transactions and the minimum amount that can be sent via this mode is Rs.2 lakh.

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You can use the net banking or mobile banking facility to transfer money via RTGS. You need the bank details of the individual to transfer money via this mode. Transfers can be scheduled in advance as well.

The following information is required for an RTGS transaction:

- The amount that needs to be transferred.
- Name of the payee/beneficiary as in the bank account,
- IFSC code of the payee/beneficiary.
- Account number of the payee/beneficiary.
- Name of beneficiary bank and bank branch.

Money can be sent using RTGS through net banking. To initiate such a transaction, it is important to collect some details from the payee such as account number, bank name, **IFSC code**, and account holder name. Another interesting feature of this wire transfer method is that transactions can be scheduled in advance.

The following information is required for an RTGS transaction:

- The amount that needs to be transferred in rupees
- Name of the payee/beneficiary as in the bank account
- IFSC code of the payee/beneficiary
- Account number of the payee/beneficiary
- Name of beneficiary bank and bank branch

RTGS Fund Transfer Process(Stepwise)

The step-by-step procedure to transfer funds via RTGS is mentioned below:

Step 1: Log in to your respective bank's internet banking account by entering your username and password.

Step 2: Go to the home page and click on the Funds Transfer option.

Step 3: Proceed to choose RTGS, key in beneficiary/payee details such as account number, IFSC code, etc.

Step 4: Review all details and then submit. The funds will be credited immediately to the payee's account.

Features and Benefits of RTGS Transactions

The main features and benefits of RTGS transactions are mentioned below:

- Realtime online fund transfer
- Used for high value transactions
- Safe and secure
- Reliable and backed by the RBI
- Immediate clearing
- Funds credited on a one-on-one basis
- Transactions executed on an individual and gross basis

Mobile Banking

M-banking refers to the use of the internet and mobile technology to bring financial services to customers. Customers use m-banking through a USSD, SMS, or mobile app to access banking services. As a result, it has eliminated the customers' need to visit the bank branch for every other financial necessity.

Busy lifestyle and, more recently, the COVID pandemic have forced people to opt for mobile banking. Round-the-clock banking services at the fingertips provide customers with an

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easy, quick, and hassle-free experience. At the same time, banks also benefit from a reduction in operating costs due to savings in time and resources.

Though beneficial, m-banking is exposed to security threats like hacking that raise safety concerns among customers. In order to secure transactions, banks keep updating the security features of their m-banking app regularly. In addition, they also use a virtual private network (VPN), biometric login, and two-step OTP-based verification to ensure safety of customers.

To access m-banking, customers must download the bank's m-banking app from the app store. Then, proceed to create an online account to register for the same. It involves answering some questions, selecting a username and password, and setting up security preferences. After that, set an MPIN to be used every time a transaction is made.

Once the bank verifies the credentials, the customer becomes the registered user and can perform all the financial transactions using the mobile app. It includes shopping online, paying utility bills, making account information inquiries, transferring funds, using forex-related services, and booking tickets.

History

Let us discuss the m-banking history to know its origin. The earliest form of m-banking was performed using SMS in the 1990s. However, with the introduction of the mobile web and smartphones with wireless access protocol (WAP) in 1999, banks in Europe started offering m-banking platforms to their account holders.

Until 2010, banks were utilizing the mobile web and SMS to offer banking services on the customer's mobile. But after 2010, the advent of the following factors revolutionized the m-banking completely:

- Development of iOS by Apple and Android by Google for smartphones
- Emergence of web-based technologies (WBT) like CSS3, HTML 5, and JavaScript

WBT enabled the launch of web-based and mobile-based applications for banks on Android and Apple devices. As a result, banks started incorporating advanced features in their apps to attract customers. The enhanced functionality of apps with easy accessibility worked as bait for the customers. Thus, over the years, these m-banking apps emerged as the new normal globally.

Types of Mobile Banking Services

M-banking allows banks to offer a range of financial services to customers. From accessing account information to utilizing transaction, investment, loan, and support services, m-banking has assumed all roles traditionally requiring the help of a bank representative.

#1 – Account Information

The account holders can:

- Extract the details related to accounts like bank statements
- Enable or disable SMS alerts of transactions
- Manage the fixed deposits and recurring deposits
- Know the loan details and statements
- Get debit card details
- Obtain credit card statements
- Understand and invest in insurance details
- Perform investment in securities

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#2 – Transaction

Customers can transfer funds between self-operated accounts, make payments to third-party bank account holders, and undertake utility bill payments, premium payments, and loan repayment using the mobile-based application. Moreover, many banking apps also integrate online shopping for the ease of customers laced with offers, cash backs, and rewards upon using these services.

#3 – Investments

Many banks offer the facility of managing the investments like deposits, insurance, and equities from their m-banking interface embedded in the app.

#4 – Loans

Banks provide the window of loans management to their customers. Customers can check the status of their loans, pay their EMIs, and even avail small digital loans using the app-based mobile utility.

#5 – Customer Support

All banks provide a dedicated menu in their m-banking app to submit requests for services like cheque book, debit & credit card, and loan applications. The account holders can also check their ATM card and credit card reward points from the banking app.

#6 – Content services

Several banks serve their customers with various loyalty programs, online shopping discounts, recharge offers, and other finance-related news through m-banking.

#7 – Consumer Complaints

Customers can lodge complaints about any forgery or invalid transaction from their accounts using the app.

Mobile Banking Features

M-banking has features that ensure customers can access their accounts and carry out financial transactions on the go. Some key features of m-banking are:

#1 – Accessibility

M-banking offers 24-hour access to all customers. Customers can log in to their app and view and track their account balances anytime. Besides, they can engage in fund transfers even during bank holidays.

#2 – Security

The banks recognize the importance of providing a secure environment to customers for transactions based on the banking app. Hence, m-banking asks for SMS access, location access, biometric access, and application password from the customers to ensure their privacy and security.

#3 – Transferability

Transferring funds from one bank account to another is the most basic m-banking activity. All the banking app-based transfers are now secured using two-step verification via app password and OTP-based transactions. The two-step verification is applicable in fund transfers, utility bill payments, and online shopping for the safety and convenience of customers.

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#4 – Investment Management

Many big banks offer the facility of securities trading through their banking app. It makes it easier for the customers to trade hassle-free. Also, m-banking enables customers to track their deposits and other investments from the convenience of their homes.

#5 – Digital Payments

At present, all m-banking apps have a QR code reader for payment at merchant locations. So the customer has to point at the QR code of the merchant at their shops and pay the price of the goods using the account details from the QR code.

#6 – Customer Service

M-banking provides personalized service to customers through live chat, phone, notifications, etc. This helps customers to get the required assistance without visiting the bank directly.

M-banking Advantages and Disadvantages

Like every other technology, m-banking can be advantageous as well as disadvantageous to customers. Therefore, one must know its pros and cons to stay safe.

Advantages

- Offers 24-hour accessibility to banking
- Saves time
- Provides a convenient way of making fund transfers and payments
- Enables easy tracking and monitoring of bank accounts
- Facilitates quick reporting of any illegal transaction or fraudulent activity
- Allows swift redressal of consumer complaints
- Increase request processing speed
- Makes online shopping possible
- Allows trouble-free management of investments
- Sends notification of bill or loan payments
- Encourages customers to stay indoors during a pandemic
- Eliminates the need to carry cash all the time
- Reduces chances of theft

Disadvantages

- Causes inconvenience for less tech-savvy account holders
- Removes human touch from banking
- Raises security concerns and online fraud
- Results in delays or losses in transactions due to mistakes
- Gives rise to comprehension issues due to the complex app interface
- Makes follow up on fraud reports difficult
- Delays service requests in case of internet issues

M WALLETS

Customers use mobile wallets to make in-store payments, and it is a convenient payment method compared to paying with cash or carrying physical credit cards. Mobile wallets are accepted as a method of payment in stores that are listed with mobile service providers.

The most popular mobile wallets include Google Pay, Apple Pay, and Samsung Pay. The wallets are integrated into mobile devices, or users can download the application from app stores.

Understanding Mobile Wallets

The information stored in a mobile wallet is encrypted, making it difficult for cybercriminals to execute fraudulent activities with them. While physical credit and debit cards can be stolen or duplicated, mobile wallets are difficult to steal since they come with encrypted keys that may not reveal any useful information.

Once a customer installs a mobile wallet on their mobile device, they are required to provide their credit card details, reward cards, and coupons. The information is then linked to an accepted personal identification format, such as a key or a scannable QR code.

When a customer makes an in-store payment, the mobile app uses near-field communication (NFC) technology to communicate between devices. The NFC uses a QR code, key, or another personal identification format to process the payment at the payment terminal. The action is triggered when the user taps or waves the NFC-enabled device at the merchant's point-of-service terminal.

Types of Mobile Wallets

The following are the main types of mobile wallets:

1. Open wallets

An open wallet is used directly by a bank or through a third party. Open wallets allow customers to use the funds in the mobile wallet for making payments for transactions or withdrawing the funds deposited to the account in cash. An example of an open mobile wallet is PayPal, which allows users to make payments for in-store and online purchases and still withdraw the funds in cash.

2. Closed wallets

Closed wallets are linked to specific merchants, and users can only use the funds to make payments for transactions initiated with the specific merchant. Users cannot use the money to make payments for transactions with other merchants and third-party service providers or withdraw the funds in cash. An example of a closed wallet is Amazon Pay.

3. Semi-closed wallets

Semi-closed mobile wallets allow users to use the funds in the wallet to make payments for transactions with multiple merchants, as long as there is an existing contract between the merchant and the mobile wallet company. Users can also withdraw the funds into a bank account. However, semi-closed wallets do not allow users to withdraw funds in cash.

How to Use a Mobile Wallet

After choosing your preferred mobile wallet, it is easy to set it up and use it to make payments. Start by downloading the mobile app in the app store onto your smartphone, tablet, or other compatible devices. Then, launch the app, and start adding the information you want to add to your wallet – credit cards, debit cards, coupons, reward cards, etc.

While it is possible to load information for multiple cards onto the wallets, only one card will be selected as the default payment option to be used to make payments. If a user wants to use a different card to make the transaction, they must change the default card before making the payment.

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When making an in-store purchase, find merchants that accept your chosen payment gateway. Usually, merchants that accept mobile wallet payments can be identified through a contactless payment indicator (usually a sideways Wi-Fi symbol).

When making a payment, users are required to tap or wave their device to the NFC-enabled terminal. After making the payment, a message is sent to the merchant regarding the payment. The merchant must honor the message alert for the payment to be transferred from the consumer's account to the merchant's account.

Benefits of Mobile Wallets

1. Secured access

One of the benefits of a mobile wallet is its secured access. Before making a payment, the user is required to unlock the mobile device using a password or fingerprint. The app also requires users to type a passcode, use their fingerprint, or use the face scan to unlock the mobile wallet.

In the case of theft, it will be impossible for anyone to use the mobile device to make a payment without providing the required security credentials. It makes mobile wallets more secure than carrying physical credit cards and cash, which can easily be compromised.

2. Accessible and convenient

Mobile wallets are also quickly accessible and convenient, making it easier for users to make payments. They are preferred by consumers who want more convenience in paying for in-store purchases, instead of carrying physical wallets and cash to stores. Once credit card information is added to the mobile wallet, users can use the funds to pay bills and make purchases on the go.

Net Banking

Net-banking, also known as internet banking, is an electronic system managed by banks which enables customers to access financial as well as non-financial banking products online. Earlier, customers had to visit the banks even for a small service. However, after the arrival of internet banking, almost all the services and products can be accessed online. From fund transfer to requesting demand draft, net-banking facilities, and all banking essentials. It is not just convenient but also a secure method of banking.

How does Net Banking Work

To benefit from net-banking, customers are required to register for internet banking at the bank.

- Individuals having a savings account or current account at any bank can register for internet banking
- For net-banking to work properly, you need a personal computer, laptop or mobile, and good internet connection
- After registering, a unique customer ID and password are issued by the bank using which one can log-in to the net-banking portal

Features of Net Banking

Given below are some of the key features of Net Banking:

- A secure and convenient method of banking
- Password-protected banking system
- Easy access to financial and non-financial banking products/services
- Access your bank account anytime anywhere
- Track and manage bank balance, last transactions, statements, etc.
- Transfer funds online via NEFT, RTGS, IMPS anytime

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- Process bill payments quickly
- Keep a track of payments, personal loans, home loans, business loans, credit cards, savings account, etc.
- Channelize or cancel automatic payments

How to Register for Net Banking

Most of the banks open an internet banking account for the customers as and when they apply for a new bank account. If you do not have an internet banking account already,

- You can submit the Internet Banking Application Form at your home branch along with required documents such as a copy of your bank passbook, Aadhaar card, etc.
- The bank will verify all the information and then issue a customer ID and password for internet banking
- The net-banking application form can be downloaded from your bank's official website
- After receiving the credentials, you can log-in and access net-banking

How to Register for Net Banking Online

Besides offline registration, which involves the submission of the application form at the bank, users can register for net-banking online from the respective bank's official website. However, it should be noted that not all banks offer online registration for internet banking services.

Step 1: Visit your bank's official net-banking website

Step 2: Click on the 'login' button under personal/retail banking option

Step 3: On the next screen, click on the 'New User? Register Here' option

Step 4: If you have already obtained the customer ID and password from the bank, enter and proceed to login. Otherwise, click 'Next'

Step 5: Now, you will be required to fill a 'Self Registration Form'. Enter details such as account number, registered mobile number, email address, branch code, CIF number, debit card details, etc. After that, click on 'Submit'

Step 6: Authenticate your registration using a one-time password sent to your registered mobile number

Step 7: On the next screen, your temporary customer ID and password will be displayed

Step 8: Log-in using your temporary credentials. You need to create a new log-in password after logging in for the first time

Note: Login and transaction password should be changed every 2 months to safeguard the net-banking account.

Steps for Net Banking Login

After successful registration, you can follow the given steps to log into your net banking account-

1. Visit your bank's official net-banking website. (Make sure the URL of the website starts with 'https://'. This means that the URL is secure)
2. If you are a retail user, choose 'Personal Log-in'. If you are a corporate user, choose 'Corporate Log-in'
3. Now, on the next screen, enter your customer ID and password
4. Enter Captcha and click on 'Login'
5. Your Net Banking dashboard will be displayed on the next screen

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Types of Fund Transfers available on Net Banking

Net-banking allows the transfer of funds from one account to another through three different ways- NEFT, RTGS and IMPS. Let us understand these three methods in details-

NEFT

National Electronic Fund Transfer (NEFT) is one of the most commonly used payment methods which enables one-to-one fund transfer. It is a time-restricted process at the bank, but available 24×7 on the net-banking portals. Generally, it takes about 30 minutes for the funds to be successfully transferred via NEFT. However, the time can even stretch to 2-3 hours.

RTGS

Real-Time Gross Settlement (RTGS) refers to a continuous settlement of funds individually on an order-by-order basis. This implies that the RTGS system ensures that the beneficiary's account is credited with the funds immediately. Transactions via RTGS are monitored by the RBI which suggests that successful transfers are irrevocable. This method is used to transfer a minimum of Rs.2 lakh. Just like NEFT, RTGS is also a time-restricted service at the bank, but accessible 24×7 via net-banking.

IMPS

Immediate Payment System (IMPS) also deals in the real-time transfer of funds. It is most commonly used to transfer funds instantly within banks across India via mobile, internet and ATM. One can transfer funds via IMPS just with the mobile number of the beneficiary.

E Rupee

Simply put, the retail e-rupee – or the Central Bank Digital Currency-retail (CBDC-R) – is a **digital version of cash**. It is legal tender issued by the central bank, but in electronic form. The e-rupee will be issued in the same denominations as currently available banknotes and coins. Users can transact via a digital wallet offered by their banks.

How is it different from UPI?

One of the motivations behind launching a digital currency is to reduce settlement risk in the system. In the case of UPI transactions, the transfer of money involves a settlement process, where you place a request with your bank and the funds are then deducted from your account and transferred to the beneficiary's account.

But with e-rupee transfers, there is no intermediary. It is literally the electronic equivalent of handing cash over to another person. The money is never 'in transit'; nor is there any need for inter-bank settlement.

The e-rupees are simply transferred from one wallet to another and the funds become the property of the receiving party: this is the concept of 'settlement finality'.

What does it mean for users?

We could be looking at a **whole new era of reach and convenience** in digital payments. Transferring funds will be the literal equivalent of handing cash over. The process will be instantaneous. The RBI has even mentioned an 'offline' feature, which means that transactions can occur even without a mobile network. This could have serious implications for remote areas, where the penetration of digital payments has suffered.

A digital currency would reduce the dependence on cash and help reduce fraud in digital transactions. Further, the government could use the e-rupee to improve the mechanism of directly transferring funds to beneficiaries of schemes.

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One feature of physical cash transactions is **anonymity**: there is no digital trail. While the idea of anonymity while transacting in ‘digital’ rupees may sound infeasible, the RBI has suggested that “reasonable anonymity for small value transactions” could be a “desirable option for CBDC-R.” This means that you could, potentially, transfer funds without leaving any record. However, such anonymous transactions will likely be capped at a certain value.

Another point to note is that e-rupees will likely not bear any interest, with the RBI arguing that it would be “logical” to offer CBDCs without interest since physical cash does not carry any interest either.

How do we start using the e-rupee?

For now, the trial will only cover selected consumers and businesses in a closed user group, with only certain cities and banks involved. When the e-rupee is rolled out, users will be able to download an app – for example, Yes Bank has launched its digital rupee app – from their banks and transact in digital rupees.

Why was the e-rupee introduced?

The RBI, in its concept document, mentioned a few principal motivations: 1. Reducing the cost associated with physical cash management (printing, storage, transportation etc.), 2. Increasing the adoption of digital payments, 3. Supporting financial inclusion (especially via the offline feature in remote parts of the country with poor connectivity) and 4. Providing Indians a safe digital currency without any of the risks associated with crypto currency.

The future

The e-rupee could have a transformative effect, deepening and widening the reach of digital payments in India. It could herald a new era of ease and convenience in digital payments in the country’s farthest corners. It is important, though, to note that the e-rupee is intended by the RBI to “complement, rather than replace, current forms of money”.

Central Bank Digital Currency

The Reserve Bank of India (RBI) has roped in at least five lenders including State Bank of India, ICICI Bank, IDFC First Bank and HDFC Bank to work on the retail pilot project of the central bank digital currency (CBDC). The central bank commenced the pilot project of India's very own digital currency —Digital Rupee — for the wholesale segment from November 1, 2022. "The use case for this pilot is settlement of secondary market transactions in government securities," the regulator mentioned in a notification on October 31, 2022. The RBI has identified nine banks including State Bank of India, Bank of Baroda, Union Bank of India, HDFC Bank, ICICI Bank, Kotak Mahindra Bank, YES Bank, IDFC First Bank and HSBC

Features of Digital Rupee

- 1) CBDC is a sovereign currency issued by central banks in alignment with their monetary policy.
- 2) It appears as a liability on the central bank’s balance sheet.

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- 3) It must be accepted as a medium of payment, legal tender, and a safe store of value by all citizens, enterprises, and government agencies.
- 4) CBDC is freely convertible against commercial bank money and cash.
- 5) CBDC is a fungible legal tender for which holders need not have a bank account.
- 6) CBDC is expected to lower the cost of issuance of money and transactions.

Types of CBDC that could be introduced

The Central Bank Digital Currency can be classified into two types — general purpose or retail (CBDC-R) and wholesale (CBDC-W). Retail CBDC can be used by all including the private sector, non-financial consumers, and businesses. Wholesale CBDC is designed for restricted access to select financial institutions.

While retail CBDC is an electronic version of cash primarily meant for retail transactions, the wholesale CBDC is designed for the settlement of interbank transfers and related wholesale transactions.

"It is believed that retail CBDC can provide access to safe money for payment and settlement as it is a direct liability of the central bank. Wholesale CBDC has the potential to transform settlement systems for financial transactions and make them more efficient and secure. Going by the potential offered by each of them, there may be merit in introducing both CBDC-W and CBDC-R,"

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UNIT-4

Non-Banking Finance Companies

Non-Banking Financial Company (NBFCs) may be defined as a company registered under the Companies Act, 1956 and under the provisions of section 45-IA of the Reserve Bank of India Act, 1934. NBFCs provides banking services without meeting the legal definition of a bank such as holding a banking license.

Section 45-I of the Reserve Bank of India Act, 1934 defines “non-banking financial company” as–

- (i) a financial institution which is a company;
 - (ii) a non-banking institution which is a company and which has as its principal business the receiving of deposits, under any scheme or arrangement or in any other manner, or lending in any manner;
 - (iii) such other non-banking institution or class of such institutions, as the Bank may, with the previous approval of the Central Government and by notification in the Official Gazette, specify.
- Following are the business in which NBFCs are engaged:

- Loans and advances
- Acquisition of shares/stocks/bonds/debentures/securities issued by the government or local authority or other securities of like marketable nature,
- Leasing
- Hire-purchase
- Insurance business,
- Chit business

But does not include any institution whose principal business is that of agricultural activity or any industrial activity or sale, purchase or construction of immovable property.

Classification of NBFCs based on the nature of its business

Depending upon the nature of the business NBFCs registered under RBI are divided into four categories depending upon its nature of business:

- hire-purchase company;
- equipment leasing company;
- loan company;
- investment company;
- infrastructure finance company

Types of Non-Banking Financial Companies

- **Asset Finance Company (AFC):** Financing of physical assets supporting productive or economic activity that includes automobiles, tractors and generators.
- **Investment Company (IC):** Acquiring securities with the purpose of re-selling.
- **Loan Company (LC):** Provides finance by extending loans or for any activity than its own. However, this does not include an Asset Finance Company.
- **Infrastructure Finance Company (NBFC-IFC):** Provides loans for projects linked to infrastructure.
- **Infrastructure Debt Fund (NBFC-IDF):** Facilitates the flow of long-term debt into projects that deal with infrastructure.

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- **Systemically Important Core Investment Company (CIC-ND-SI):** Acquires shares and securities for the investment in equity shares primarily.
- **Micro Finance Institution (NBFC-MFI):** Extends credit to the economically disadvantaged groups. Additionally, they extend their support to Micro, Small and Medium Enterprises (MSMEs).
- **NBFC Non-Operative Financial Holding Company (NOFHC):** Permits promoters or promoter groups to set up a new bank.
- **Factor (NBFC-Factor):** Engages in the business of acquiring receivable of an assignor or extending loans against the security interest of the receivables at a reduction.
- **Mortgage Guarantee Company (MGC):** Undertakes mortgage activities.
- **Account Aggregator (NBFC-AA):** Collects and offers information on a customer's financial assets in a consolidated, organised and retrievable method to the customer or others as required by the customer.
- **NBFC Peer to Peer Lending Platform (NBFC-P2P):** Provides an online platform in order to bring lenders and borrowers together onto a single space to help mobilise unsecured finance.

Operations of Non-Banking Finance Companies

The following guidelines are to be adhered to by NBFCs once they obtain their licenses.

- NBFCs are not permitted to receive deposits that are payable on demand.
- The interests charged by an NBFC cannot exceed the threshold prescribed by the RBI.
- The public deposits that they can take must be for a minimum of 12 months and a maximum of 60 months.
- The RBI would not guarantee the repayment of any amount so taken by the NBFC.
- The deposits taken by the public would be unsecured.
- Every information about the company and the changes in the composition of the same has to be furnished to the RBI.
- It is essential that the company submits its audited balance sheet annually.
- Quarterly return on the company's liquid assets has to be furnished.
- It is necessary that a statutory return on the deposits taken by an NBFC has to be furnished through Form NBS-1 annually.
- The auditors have to legally state that the NBFC is capable of paying back all the deposits or funds taken from the public.
- A credit rating of the company has to be taken every six months and submitted to the RBI.
- A half-yearly Asset Liability Management (ALM) return has to be given by the company which has a Public Deposit of Rs. 20 Crore and above or has assets worth Rs. 100 Crore and above. A company which has a public deposit of INR 20 Crores and more, or has assets worth INR 100 Crores and more, has to submit a half-yearly Asset Liability Management return.
- An NBFC is required to maintain a minimum level of 15% of the public deposits in terms of liquid assets.

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Micro Finance Companies

Microfinance companies, as the name suggests, are financial institutions that provide finances to low-income groups, where the finance requirement is lesser as compared to other sectors of the society. These sectors generally do not have access to traditional financial institutions such as banks and other financial institutions.

Need for Microfinance Companies

In India, there are many institutions like banks that grant loans to finance businesses. So why do we need microfinance companies? The need arises as it serves the following purposes:

- It provides financial assistance to enterprises that cannot place collateral
- It encourages women entrepreneurship
- It provides startups with much-needed support
- It offers assistance even for nominal amounts which generally are funded as hand loans
- It formalizes the process of lending and hence brings about discipline in borrowing by low-income groups. This prevents over-borrowing and reduces complications arising out of high future debts.

Formation of Microfinance Companies

Ideally, only a Non-Banking Finance Company (NBFC) is authorized by the Reserve Bank of India to conduct financial business. However, certain exemptions are provided by RBI to particular businesses to perform financial activities up to a specified limit. Therefore, a microfinance company registration can happen in the following two ways:

- Non-Banking Finance Companies (NBFC) duly registered with RBI
- Section 8 companies (companies formed under Section 8 of the Companies Act 2013)

Microfinance Company Registration as an NBFC

Given the differences in the two models for forming a microfinance company, the registration process also varies considerably. The following are the steps involved in the registration of a microfinance company through an NBFC:

- **Register a company:** To be registered as an NBFC microfinance company, the first step is to form a private or a public company. To form a private company, at least 2 members and a capital of Rs 1 lakh is required. To form a public company, at least 7 members are required.
- **Raise capital:** The subsequent step is to raise the required minimum net owned funds of Rs 5 crore. For the northeastern region the requirement is of Rs 2 crore.
- **Deposit the capital:** On collection of capital, the next step is to deposit the capital in a bank as a fixed deposit and obtain a 'No lien' certificate for the same.
- **Apply for license:** Finally, the NBFC must fill an online application for the license and submit it along with all the certified documents. A hard copy of the application and license must also be submitted at the regional office of Reserve Bank of India. The documents that must be available with the NBFC at the time of filing are:
 - Memorandum of Association and Articles of Association
 - Incorporation certificate of the company
 - Board resolution copy

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- Copy of Auditor's report of receipt of fixed deposit receipt
- Banker's Certificate of No Lien stating the net owned fund
- Banker's report about the company
- Recent credit report of the directors
- Net worth certificate of the directors
- Education/professional qualification proof of the director
- KYC and income proof of the director
- Proof of work experience in the financial sector
- Structure plan of the organization

Microfinance Company Registration as a Section 8 Company

The other option is to register a company as a Section 8 company. The procedure to be followed for the same is as follows:

- **Apply for Digital Signature Certificate (DSC) and Director Identification Number (DIN):** To form a company, the first process is to apply for a DSC and DIN. The DSC is essential for authorizing the e-forms.
- **Apply for name approval:** The next step is to apply for name approval in Form INC-1. The name must suggest that it is registered as a Section 8 company. So it must have the words sanstha, foundation or micro credit.
- **File Memorandum of Association (MOA) and Articles of Association (AOA):** Post the name approval; the company must draft the MOA and AOA and file it along with necessary documents.
- **File all relevant documents:** The last step is to file all relevant documents along with the incorporation certificate, and Form INC -12 to obtain a license. The primary basic documents required for registering a company under both the models are:
 - PAN Card copy of all directors/promoters
 - Documents for identity proof
 - Documents for address proof
 - Photograph of all directors/promoters
 - Proof of ownership of registered office or rental agreement for the same
 - NOC from the owner
 - Applicable stamp duty as mandated by the state
 - Any other documents as required

Regulation of Micro Finance Companies

Types of Regulation

Financial institutions are generally subject to prudential and non-prudential regulation. Prudential regulation ensures the financial soundness of the industry. This regulation provides the appropriate legal framework for financial operations to help prevent and reduce financial sector instability. A

financial authority directly sanctions microfinance institutes and assumes the responsibility for the soundness of regulated institutions. Non-prudential regulation, on the other

hand, encompasses regulations about the institution's business operations. A financial authority does not sanction the business, but offers guidelines and invokes standards that do not involve the implicit guarantee of the financial authority. Examples of non-prudential regulation could include truth in lending laws, fraud and financial crimes prevention, interest rate policies, among others. These rules serve to protect the consumer. The type and level of regulation depends on how the microfinance institute is formed and what services it provides.

Benefits of Regulation

The advantages of regulation in the microfinance industry for the customer and financial markets are numerous. Regulation serves to ensure the financial soundness of an MFI, reducing the chance of failure and reinforcing the public's trust in these financial institutions. Regulations in the form of capital adequacy requirements, reserve requirements, loan loss provisions, and loan documentation are all examples of measures to ensure an MFI will be able to maintain its operations. Regulations also serve to protect borrowers by preventing profit maximization at the client's expense. MFI's can often have considerable local market power which can result in monopolistic lending practices. These practices can result in usurious interest rates and expensive fees. For MFI's that take deposits, regulation helps to prevent a loss of client savings from failure of the MFI. For the poor, these savings can be vital to deal with economic uncertainties and their loss can have grave effects. In addition, regulation and supervision may promote the development of the microfinance industry, attracting greater borrowing and more deposits from the public.

Microfinance, in All Shapes and Sizes

Regulation of the microfinance industry has its many benefits, though it can be an involved process due to the variety of MFI's. Very generally, microfinance institutes can be divided into non-bank and bank MFI's. Within these two divisions, however, are numerous types, including cooperative societies, commercial banks (both state-owned and private) and development banks, Non-governmental Organizations (NGOs) and International NGOs (INGOs). The many types of MFI's also differ in the nature of their business and the services they provide. Given the breadth of this industry, there is often no single body to regulate and supervise the operations of all MFI's. The regulatory requirements and standards for each of these regulatory bodies are different, complicating the regulatory framework.

Costs of Regulation

Regulation has many obvious advantages, however it can come at a price. The breadth and diversity of the microfinance industry can lead to difficulties and great expenses in order to administer and monitor all of the MFI's. Also, establishing regulatory rules intended to service microfinance customers and markets, can potentially harm MFI's and their customers as well.

Cost of supervision. Regulatory authorities will need to supervise a growing number of MFI's in a country. Given the variety of MFI types and the different regulatory requirements and standards for each, supervision can often be costly. These costs are partly passed on to MFI's in the form of licensing fees, making it more expensive for the MFI to operate. The microfinance industry already endures high operating expenses in relationship to its loan portfolio size, and these additional costs add greater difficulty to maintaining operations.

MFI's are often small, numerous, located in remote regions, and have poor record keeping. The administration and reporting requirements for the MFI can involve high levels of supervision and can be burdensome and expensive. This added work and expense will partly be borne by the

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clients in the form of higher interest rates and fees. In addition, higher costs may slow the growth of financial services offered to disadvantaged groups. Ultimately borrowing will become more expensive and more limited for the already poor clients.

Control of interest rates. Regulatory institutions can impose interest rate caps. MFI's naturally bear high costs as they provide small loans in remote areas. Often higher interest rates are charged to compensate the MFI for the added expenses in servicing its clientele. Limiting interest rates can prevent usurious lending, however it can also limit the customer base and the geographical scope for the MFI. Higher interest rates may be the only way MFI can operate in a sustainable manner. Limiting interest rates may adversely affect the very poor and those who live in remote places by discouraging microfinance services in these areas and for those people.

Capital requirements. A minimum capital requirement can limit entrance into the industry. Capital requirements might also restrict future operations in terms of cost and outreach. These requirements can limit the start-up of a new MFI to service clients and can limit existing MFI's in terms of how widely they can operate. These limitations can reduce the reach of MFI's and may reduce the competition in the industry, preventing potential borrowers from receiving financial services or making financial services more expensive.

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Credit Information Bureaus

Credit Information Bureau (India) Limited (CIBIL) is a credit bureau or credit information company, engaged in maintaining the records of all the credit-related activities of companies as well as individuals, including credit cards and loans.

The registered member banks and several other financial institutions periodically submit their information to CIBIL. Based on the information and records provided by these institutions, CIBIL issues Credit Information Report (CIR) and credit score to applicants and financial institutions.

CIBIL is a credit information database and does partake in any kind of lending decisions. It provides data to the banks and other lenders to quickly and efficiently filter the loan applications which they receive in the course of their business.

Product offerings by CIBIL

CIBIL offers three products viz. credit score, a credit report for individuals and credit report for companies:

Credit score

A credit score refers to a 3 digit numeric value that represents the creditworthiness of an individual. The creditworthiness ranges between 300 to 900 with 900 being the highest and 300 being the least. This score is computed with the help of the credit history of an individual.

Banks and most financial institutions prefer extending credit to an individual whose score is 750 and more. Individuals with good credit scores are less likely to default on their loan payments.

Credit report

The credit report contains the credit information that CIBIL fetches from various financial institutions. This detailed report contains information about an individual's history of borrowing and repayment routine, including defaults and delays.

The important parts of this report are credit Score, individual's personal information, employment details, contact information and account details.

Credit report for companies

Credit report for companies constitutes details about a company's credit history. The several segments in a company credit report speak about potential lenders, existing credit which the company has, any pending lawsuits and outstanding amount.

A good credit report is essential for approval of any loans, whereas a bad report could damage/reduce the chances of the loan being granted to the company.

Factors influencing a CIBIL score

Repayment History

Your CIBIL score would tell the loan providers if you are capable of dealing with the debt burden and whether you can repay the loan obligation. A repayment history with EMI defaults or late payments could negatively affect your credit score.

Credit Utilisation Ratio

This is another key factor that could impact your CIBIL score. Credit utilization ratio refers to the total amount of credit that you use against the total amount of credit that you've been authorized.

Financial experts suggest that individuals should try and keep the credit utilization ratio in the range of 25-30 % for maintaining a good CIBIL score report.

Excess Personal Loans/Credit Cards

Credit cards and personal loans both are unsecured loans. Too many credit cards and a high amount of personal loans with no secured loans such as an auto loan or home loan could have a negative impact on your CIBIL score.

So, if you have a balance of both the secured as well as unsecured loans, it might lead to a positive impact on the CIBIL score.

New Accounts

An increase in the number of credit cards and loans sanctioned to you imply a rise in your debt burden. In case numerous credit cards and loans are sanctioned over a short time period, your credit score would be negatively affected.

Building and preserving a good CIBIL score isn't rocket science, however, people tend to mess up their credit usage which does substantial harm to CIBIL scores. If you're mindful of your own physical health and do everything for keeping yourself healthy, maintain a financial discipline and you would find that your financial health is healthy too.

Credit Scores

A credit score is a number representative of an individual's financial and credit standing and ability to obtain financial assistance from lenders. Lenders use the credit score to assess a prospective borrower's qualification for a loan and the specific terms of the loan. Essentially, it is used to determine the borrower's ability to pay back the borrowed amount in due time. The credit score assessment is provided by a consumer credit reporting agency such as Equifax or TransUnion.

Who Uses Credit Scores?

Any organization that lends money as a source of business uses credit scores to assess the eligibility of a borrower. Such organizations specifically include banks, credit card companies, fintech-based lenders, insurance companies, landlords, government agencies, and mortgage companies.

It can be any individual or organization that seeks to lend someone money or enter into a contract that will require another party to pay them back in a predetermined time.

What is a Good Credit Score?

A credit score ranges from 300 to 850. The higher your credit score, the better your standing as a borrower is. A respectable credit score is above **670**.

How to Improve your Credit Score

1. Pay your bills on time

Paying off what is due on time consistently will establish your credibility as a borrower. Building your credit history takes time and steadily paying off what you owe in a timely manner is considered one of the biggest indicators of your creditworthiness.

For lenders, past behavioral patterns are considered key indicators of the future. Therefore, proving to lenders that you are capable of paying back on time helps improve your credit score.

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2. Reduce your overall loan amounts

Proactively paying off more than what is due will ultimately help you showcase yourself as a credible borrower, who not only pays back, but who does so ahead of the due date. Doing that can also decrease any interest payments on borrowed funds.

For example, if you have the means to prepay your mortgage, then by doing so, you are coming across as a credible borrower and your credit score will improve.

3. Manage credit cards effectively:

Credit cards, if used diligently, are an excellent way to improve your credit score. Ideally, you should not spend more than 35% of your credit limit. Following this practice will help keep your total debt amount in check and also help ensure that you are able to easily pay back financing extended to you. Lenders specifically look at how much of your available credit you have actually borrowed. Again, to rate higher with lenders, it's a good idea to access no more than 35% of your available credit at any given time. So, for example, if you have a credit card with a \$5,000 line of credit, you shouldn't allow your outstanding balance for that card to get above \$1,700-\$1,800.

4. Do not buy what you can't afford

As a golden rule, do not purchase things that you can't immediately pay off. While buying things on credit is convenient, if there is something you cannot afford immediately with the funds available to you, it is generally better to look in the other direction.

Maintaining financial health is all about making the correct decisions for yourself in the broad scheme of things and not indulging in impulse purchases that you may regret later.

Credit Repository of Large Clients

RBI has constituted a Central Repository of Information on Large Credits (CRILC) to collect, store, and publish data on all borrowers' credit exposures. Banks/Financial Institutions are expected to report findings to CRILC. Banks will have to provide credit information to CRILC about their borrowers with an aggregate fund-based and non-fund based exposure of and over Rs.5 Crores (Rs.50 million). Banks should also report the SMA status of their borrowers to the Central Repository of Information on Large Credits. As a way to impart knowledge about credit discipline, mainly regarding reduction in NPA level in banks, banks have been suggested to refer the information provided in CRILC instead of limiting the due carefulness to looking for NOC (No Objection Certificate) from the bank with whom the customer is availing credit facilities as per the presented declaration. The CRILC was built in 2014 precisely to help financial institutions and banks to assess their non-performing assets (NPAs) and also share this information with other institutions. The idea behind the creation of the CRILC was for financial institutions to notify the status of their stressed borrowers and submit the information to a central database of the Reserve Bank of India. There are also guidelines to separate borrowers as SMAs (Special Mention Accounts) of different levels to assess their probability of going delinquent. In January 2016, RBI imposed a fine of Rs.1 crore on the State Bank of Travancore (SBT) for violating some guidelines regarding the Central Repository of Information on Large Credits.

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Account Aggregator

An Account Aggregator (AA) is a type of RBI regulated entity (with an NBFC-AA license) that helps an individual securely and digitally access and share information from one financial institution they have an account with to any other regulated financial institution in the AA network. Data cannot be shared without the consent of the individual. There will be many Account Aggregators an individual can choose between. Account Aggregator replaces the long terms and conditions form of 'blank cheque' acceptance with a granular, step by step permission and control for each use of your data.

The Account Aggregator system can make lending and wealth management a lot faster and cheaper.

Eight banks that have joined AA network

The individual's bank just needs to join the Account Aggregator network. Eight banks already have are- Axis, ICICI, HDFC, IndusInd Bank, State Bank of India, Kotak Mahindra Bank, IDFC First Bank, and Federal Bank.

How will the new Account Aggregator network improve an average person's financial life?

India's financial system involves many hassles for consumers today -- sharing physical signed and scanned copies of bank statements, running around to notarise or stamp documents, or having to share your personal username and password to give your financial history to a third party. The Account Aggregator network would replace all these with a simple, mobile-based, simple, and safe digital data access & sharing process. This will create opportunities for new kinds of services -- eg new types of loans.

Account aggregators that have received approval

Some of the account aggregators that have received approval from the RBI include CAMSFinServ, Cookiejar Technologies Pvt Ltd, FinSec AA Solutions Pvt Ltd and NSEL Asset Data Ltd, among others.

Can a consumer decide they don't want to share data?

Yes. Registering with an AA is fully voluntary for consumers. If the bank the consumer is using has joined the network, a person can choose to register on an AA, choose which accounts they want to link, and share their data from one of their accounts for some specific purpose to a new lender or financial institution at the stage of giving 'consent' via one of the Account Aggregators. A customer can reject the consent to share a request at any time. If a consumer has accepted to share data in a recurring manner over a period (eg during a loan period), it can also be revoked at any time later as well by the consumer.

How can a customer get registered with an AA?

You can register with an AA through their app or website. AA will provide a handle (like username) that can be used during the consent process.

Today, four apps are available for download (Finvu, OneMoney, CAMS Finserv, and NADL) with operational licenses to be AAs. Three more have received in-principle approval from RBI (PhonePe, Yodlee, and Perfios) and maybe launching apps soon.

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Credit Guarantee Options

Credit markets for small and medium size enterprises (SMEs) are characterized by market failures and imperfections.

Up to 68% of formal SMEs in emerging markets are either unserved or underserved by financial institutions, with a resulting credit gap estimated to be close to \$1 trillion.

Public credit guarantee schemes (CGSs) are a common form of government intervention to unlock finance for small and medium enterprises (SMEs). More than half of all countries in the world have a CGS for SMEs and the number is growing.

A credit guarantee scheme provides third-party credit risk mitigation to lenders through the absorption of a portion of the lender's losses on the loans made to SMEs in case of default, typically in return for a fee.

However, the international community lacks a common set of principles or standards that can help governments establish, operate and evaluate CGSs for SMEs.

Now, the World Bank Group and the FIRST Initiative have launched a new tool to help governments implement public credit guarantee schemes. The tool is intended to become the standard for effectively and efficiently establishing and running public CGSs for SMEs around the world.

The 16 principles cover four key areas that are critical for the success of CGSs.

Legal and regulatory framework

1. Establish the CGS as an independent legal entity.
2. Provide adequate funding and keep sources transparent.
3. Promote mixed ownership and treat minority shareholders fairly.
4. Supervise the CGS independently and effectively.

Corporate governance and risk management

5. Clearly define the CGS mandate.
6. Set a sound corporate governance structure with an independent board of directors.
7. Design a sound internal control framework to safeguard the operational integrity.
8. Adopt an effective and comprehensive enterprise risk management framework.

Operational framework

9. Clearly define eligibility and qualification criteria for SMEs, lenders, and credit instruments.
10. Ensure the guarantee delivery approach balances outreach, additionality, and financial sustainability.
11. Issue partial guarantees that comply with prudential regulation and provide capital relief to lenders.
12. Set a transparent and consistent risk-based pricing policy.
13. Design an efficient, clearly documented, and transparent claim management process.

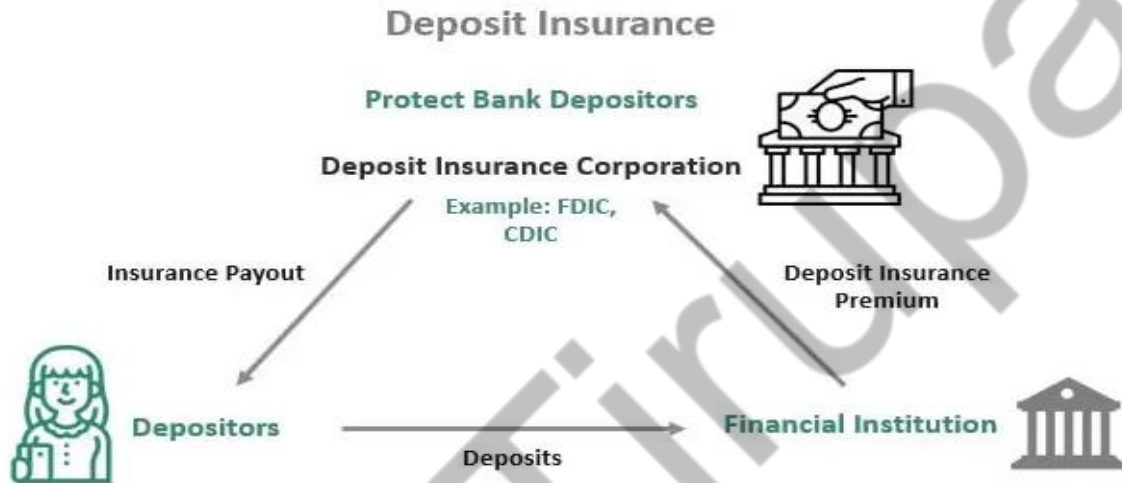
Monitoring and evaluation

14. Set rigorous financial reporting requirements and externally audit financial statements
15. Publicly disclose non-financial information periodically.
16. Systematically evaluate the CGS' performance and publicly disclose the findings.

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Deposit Insurance

Deposit insurance is a type of insurance that protects depositors against loss in the event of a bank failure. It was first launched in the United States during the 1930s Great Depression to shield bank depositors from loss.



It is an element of the financial safety net since it offers protection against banking crises and funding to lessen their effects. The institutions that offer deposit insurance can be government-run, a part of a nation's central bank, a private institution, or private institutions with government support.

How Does Deposit Insurance Work?

The deposit insurance program contributes to the overall well-being of the banking sector and the economy. As a result, depositors can feel confident even during periods of financial turbulence because of solid consumer safety. In addition, it promotes economic stability by lowering the possibility of a significant number of bank depositors withdrawing their funds at once. The member banks' and institutions' contributions are placed in a fund and used to fund the deposit insurance program.

Deposit insurance is based on the theory that people will refrain from trying to withdraw their money even if they learn that the bank is insolvent because they are confident that the government-backed entity will reimburse them in the event of a bank failure. It is done to stop bank runs on institutions reported as insolvent or having financial problems. Additionally, bankrupt banks won't need to sell their assets rapidly to obtain money.

Advantages And Disadvantages

Let's look into the advantages and disadvantages of deposit insurance.

Some of the advantages are the following:

- The main benefit for individuals is the peace of mind associated with knowing that their deposits won't become inaccessible if their bank goes bankrupt or is rendered insolvent. In addition, it indicates that individuals are more likely to deposit money into their bank accounts than other investments.
- It contributes to the economic stability of the nation.

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- It helps to gain and retain the trust and confidence of people in the banking system.
- Banks can benefit from the protection element of this offering. If banks take on too many questionable investments or overstretch themselves and fail, they don't always go extinct. Instead, the FDIC will take them up and put them under a new administration. As a result, the bank's management loses control of it yet does not entirely fail as they could otherwise.

Some of the disadvantages are the following:

- Banks have always been subject to moral hazard because they make money from the deposits of others, money they borrowed, or investors' money. As a result, banks are encouraged to take more significant risks when their depositors are covered.
- It weakens depositors' incentives to keep an eye on the risk posed by management's actions and to take corrective action, such as withdrawing deposits when the danger rises, reducing market discipline.

Supervisory College

In an increasingly globalised world – as so clearly demonstrated by the financial crisis – it is crucial that banks operating in more than one country are supervised as effectively as possible. Supervisory colleges play an important role in this regard, helping to improve the supervision of cross-border banks.

“Supervisory college” in a nutshell

A supervisory college is essentially a permanent, though flexible, structure comprised of an international bank's “home” and “host” supervisors: the Basel Committee on Banking Supervision uses the term very broadly as the set of ongoing relationships among these supervisors, covering any contact, be it in the form of teleconferences, videoconferences, letters, emails, or communication via secure websites.

The underlying objective is to help college members develop a better understanding of a cross-border bank's risk profile and vulnerabilities and to provide them with a framework for addressing the key issues that are relevant from a supervisory perspective. Information sharing and cooperation on an ongoing basis are essential tools for strengthening the supervision of such banks.

Information sharing in practice

The extent of interaction between supervisory college members varies depending upon the particular banking group and supervisors concerned, and a proportional approach is applied. Here are some examples of the information that may be shared among college members:

- Supervisory risk assessments, the main findings of supervisory reviews as well as any significant supervisory actions taken
- Analyses of the impact of the operating environment in key markets/countries on the banking group and the results of stress tests
- Crisis preparedness plans
- Capital and liquidity position/plans
- Strategic plans for the whole banking group and its subsidiaries
- Information on exogenous factors that may be useful for college members, such as regulatory developments and macro prudential information.