

# **INDIAN FINANCIAL SYSTEM**

**FOR 3<sup>RD</sup> SEM BY Prof. JJ & JD**

# **UNIT-3 FINANCIAL INSTITUTIONS (MARKS ALLOTTED-20)**

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- ▶ Commercial Banking
- ▶ Reserve Bank of India
- ▶ Financial Institutions in India
- ▶ Non Banking Financial Companies



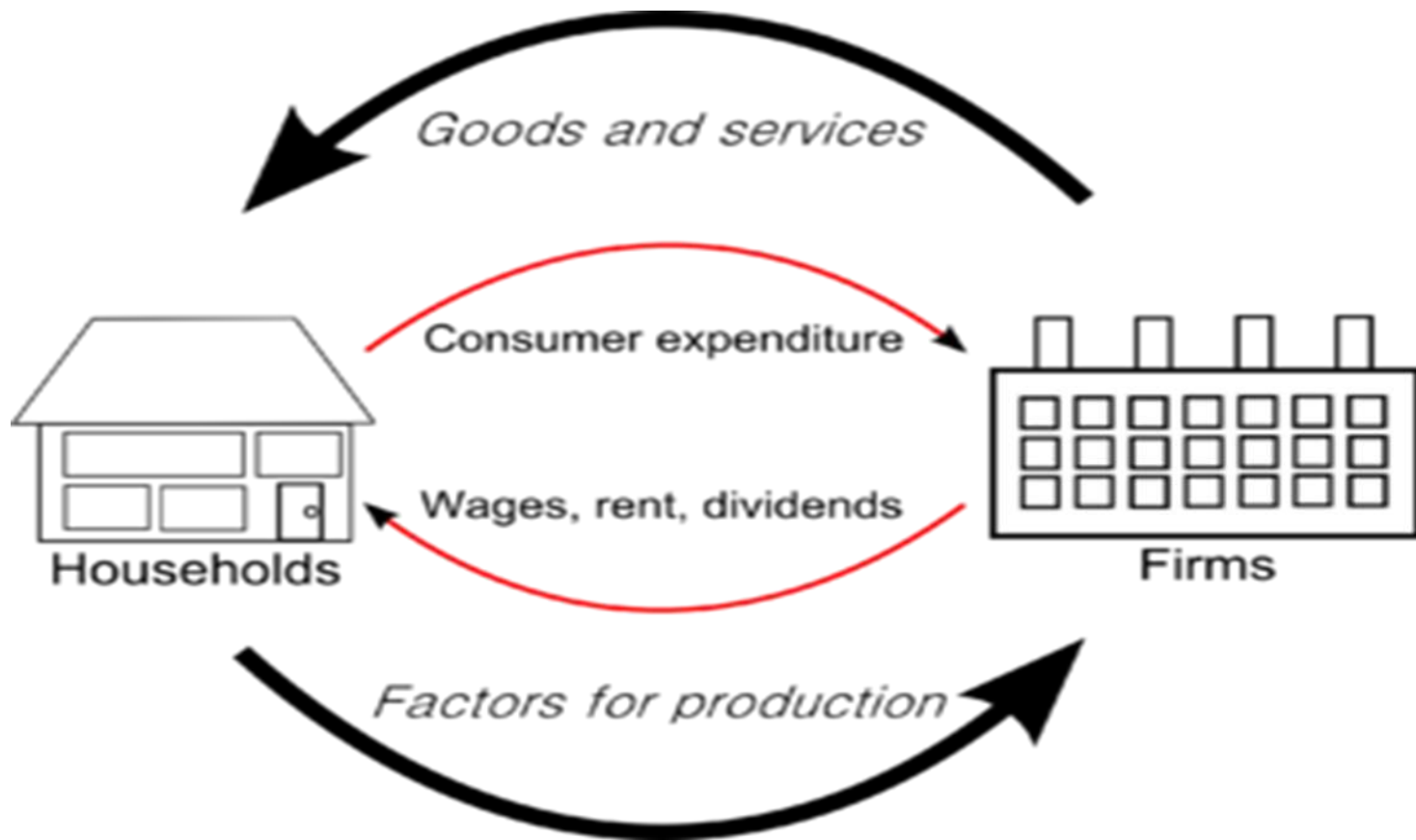
# **What is Financial System?**

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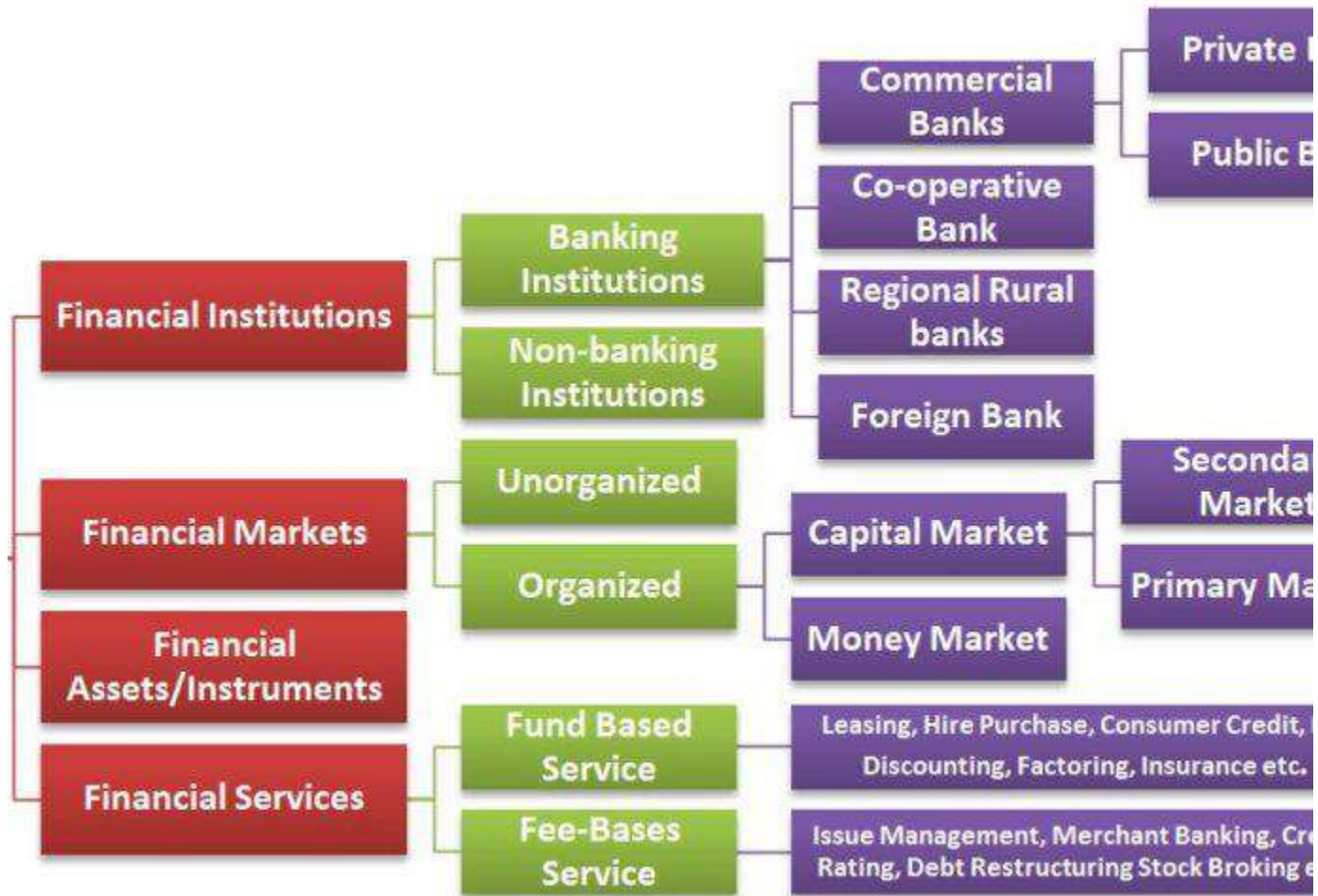
- ▶ **From economic system point of view , Financial system is a set of complex & closely related institutions, agents, practices, markets, claims etc. in an economy.**
  - ▶ **The financial system of a country is an important tool for economic development of the country as it helps in the creation of wealth by linking savings with investments.**
  - ▶ **It facilitates the flow of funds from the households (savers) to business firms (investors) to aid in wealth creation and development of both the parties.**
- 



# Diagram representing above definition



# STRUCTURE OF FINANCIAL SYSTEM



# FINANCIAL INSTITUTIONS

## Financial Institutions

Financial institutions are companies in the financial sector that provide a broad range of business and services including banking, insurance, and investment management.



# Role of Financial Institution

☐ Regulation of Monetary Supply

☐ Banking Services

☐ Insurance Services

☐ Capital Formation

☐ Act as A Government Agent for  
Economic Growth



☐ Financing the Small and  
Medium Scale Enterprises

☐ Investment Advice

☐ Pension Fund Services

☐ Trust Fund Services

☐ Investment Advice



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# **TYPES OF FINANCIAL INSTITUTIONS**

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graph TD; A[TYPES OF FINANCIAL INSTITUTIONS] --> B[Banking Institutions]; A --> C[NON-BANKING INSTITUTIONS]; B --> D[Organized sector]; B --> E[Un-organized sector]; C --> F[Organized institutions]; C --> G[Unorganized institutions];
```

**Banking  
Institutions**

**NON-  
BANKING  
INSTITUTIONS**

**Organized  
sector**

**Un-organized  
sector**

**Organized  
institutions**

**Unorganized  
institutions**



# Banking Institutions

## Organized sector

## Un-organized sector

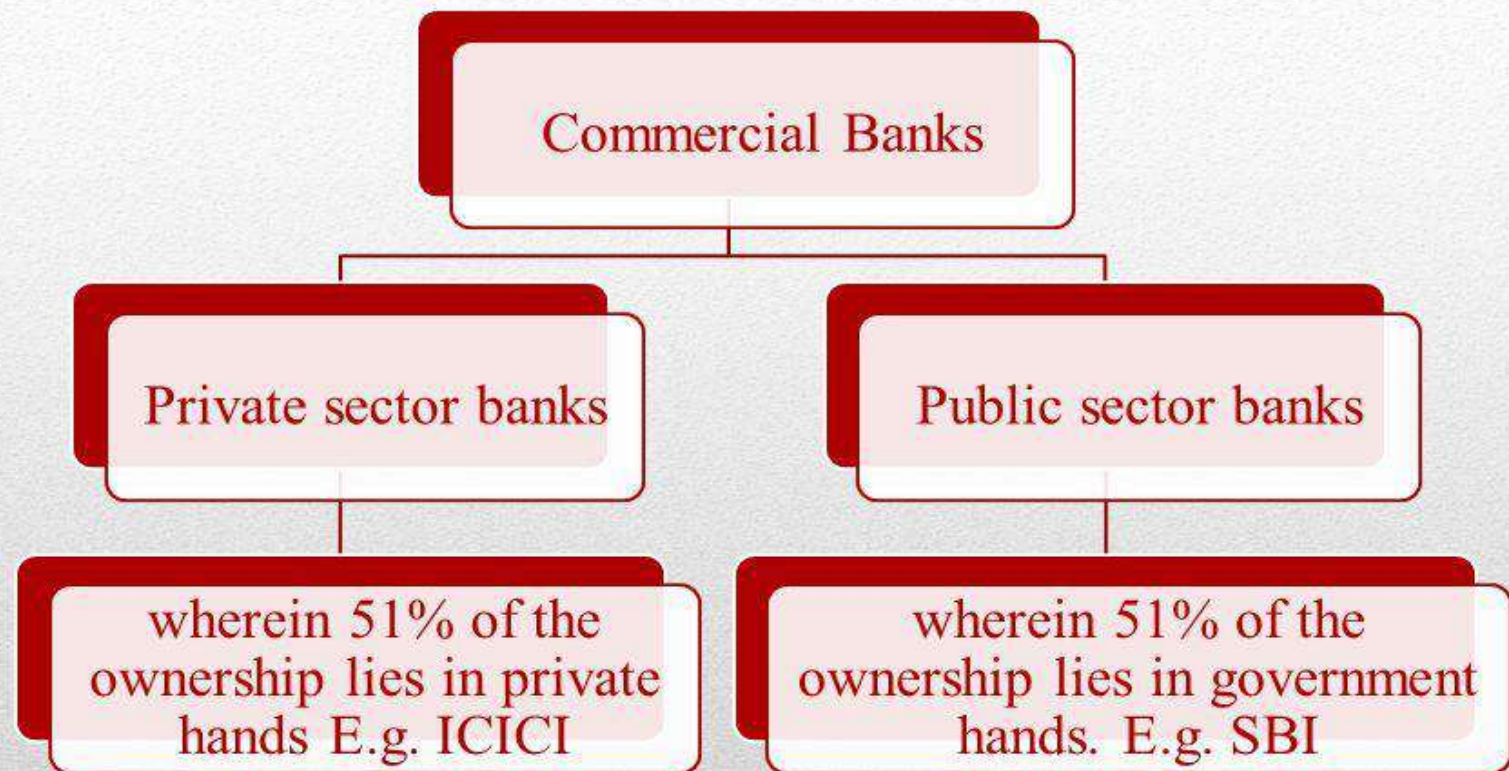
**Commercial banks**

**Co-operative banks**

**Foreign Banks**

**Indigenous bankers**

**Money lenders**



# Commercial banks

# **IMPORTANCE/ROLE OF COMMERCIAL BANK**

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- ▶ Acceptance of deposit
  - ▶ Granting Loan
  - ▶ Motivation in savings
  - ▶ Development of trade and industry
  - ▶ Assistance in foreign trade
  - ▶ Assistance in small industry
  - ▶ Assistance in financial transaction to the traders
  - ▶ Generation of employment
  - ▶ Custodian of valuable articles of depositors
  - ▶ Control inflation
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# **FUNCTION OF COMMERCIAL BANK**

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- ▶ **A. PRIMARY FUNCTIONS**
- ▶ Acceptance of deposit
- ▶ Provision of loans and advances
- ▶ Credit creation
- ▶ Discounting of bills



## **B. SECONDARY FUNCTION**

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### **▶ REPRESENTATIVE FUNCTIONS**

- ▶ Transfer of depositor's money
- ▶ Collection of depositor's money
- ▶ Purchase and sale of shares & other securities of its customers
- ▶ Act as an advisor, trustee
- ▶ Collection of money
- ▶ Preservation of valuable articles
- ▶ Agent of importer & exporter
- ▶ Underwriting function
- ▶ Credit securities





## OTHERS FUNCTIONS

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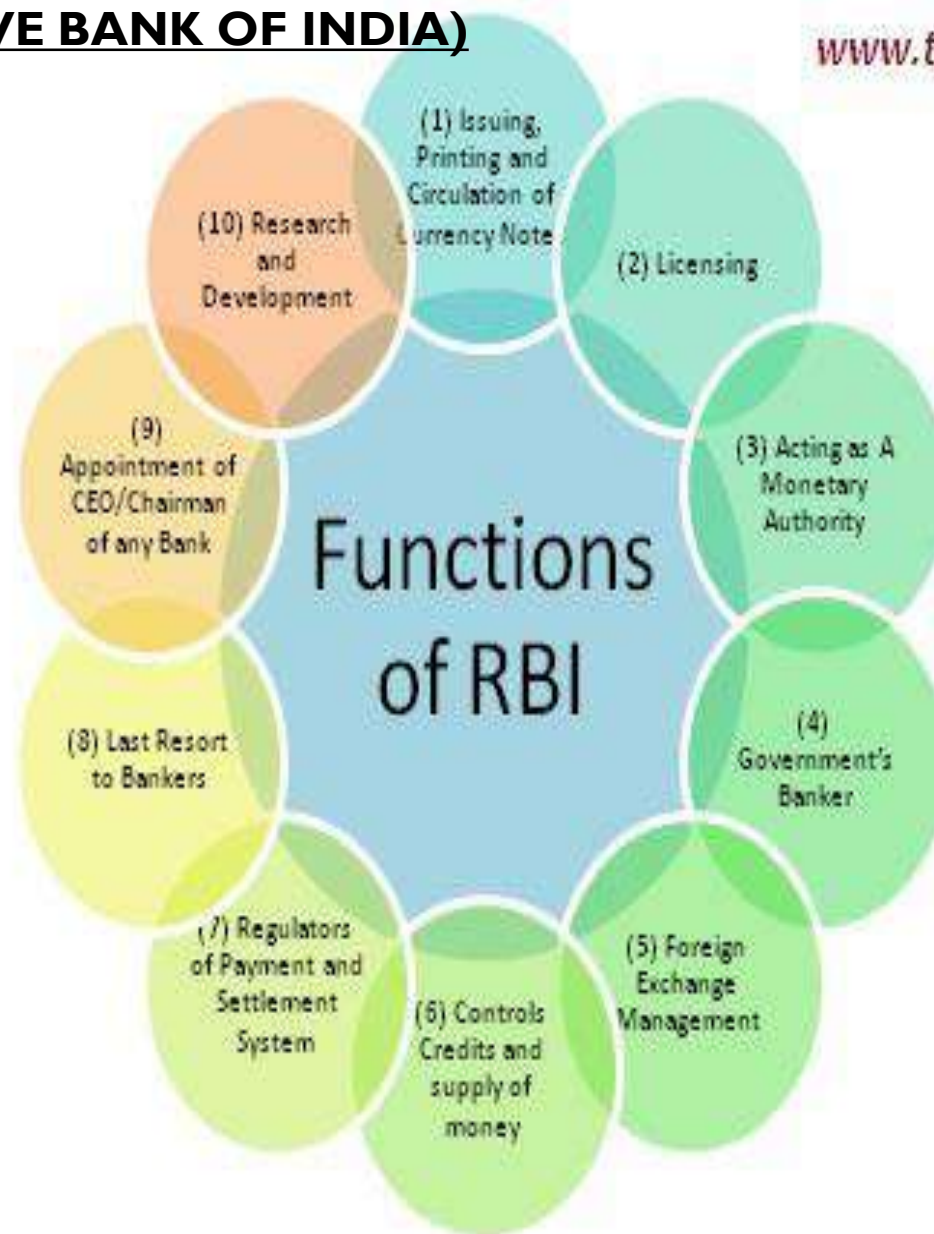
- ▶ Foreign exchange transaction
- ▶ Provide necessary information
- ▶ Participation in formulation of financial policy
- ▶ Act as intermediary
- ▶ Assistance in agriculture and industry
- ▶ Expansion of small & medium scale industries
- ▶ Participation in stock market
- ▶ Motivation in savings





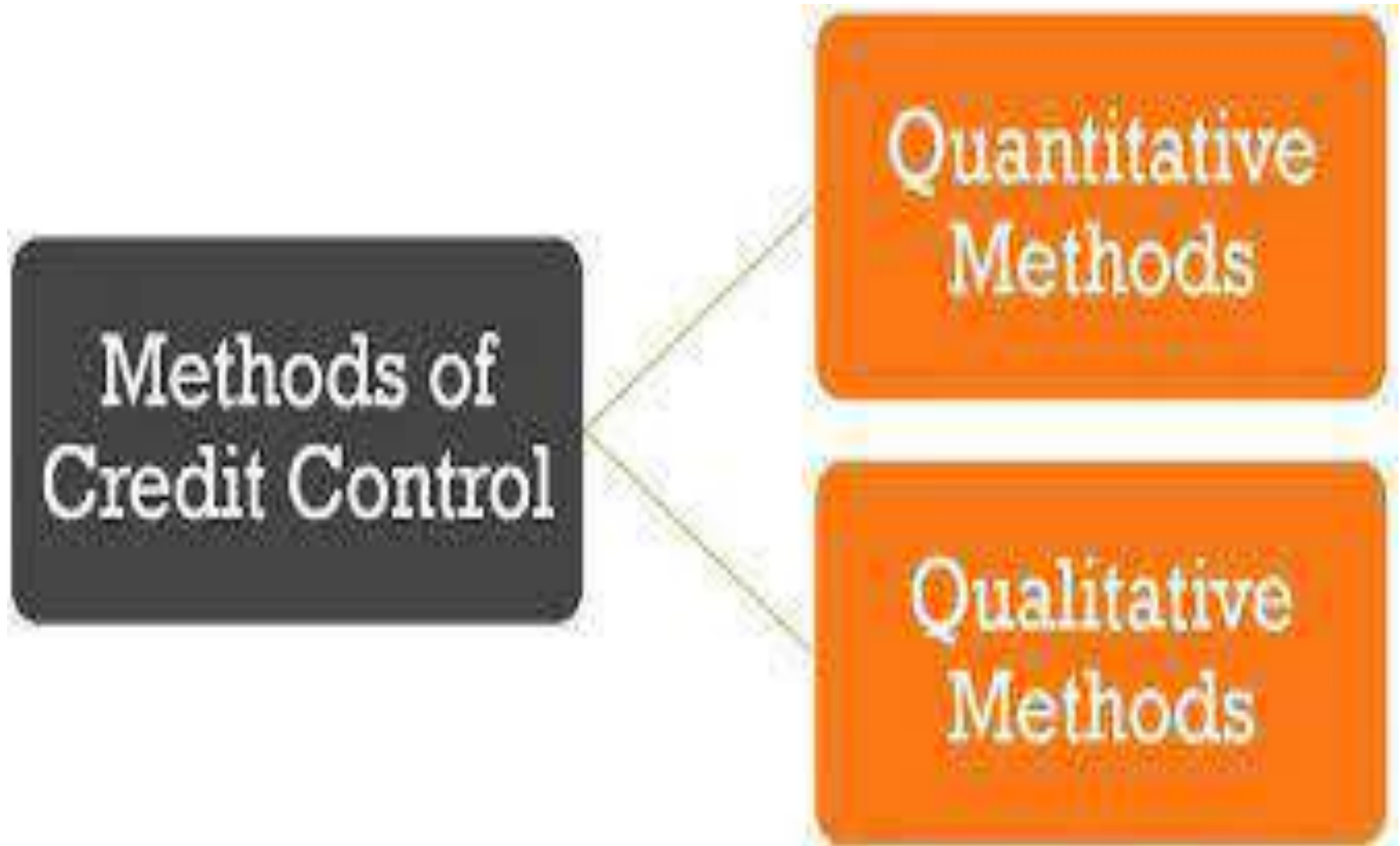
# RBI (RESERVE BANK OF INDIA)

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# CREDIT CONTROL METHODS BY RBI

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## Credit Control

### Quantitative Measures

### Qualitative Measures

#### Reserve Ratios

Cash Reserve Ratio (CRR)

Statutory Liquidity Ratio (SLR)

#### Open Market Operations

#### Policy Rates

Bank Rate

Repo Rate

Reverse Repo Rate

Marginal Standing Facility

Credit Rationing  
Consumer Credit Control  
Margin Requirements  
Moral Suasion  
Direct Action

# **DEVELOPMENTAL FI IN INDIA**

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## **SIDBI**-Small Industries Development Bank of India

Small Industries Development Bank of India is the apex regulatory body for overall licensing and regulation of micro, small and medium enterprise finance companies in India. It is under the jurisdiction of Ministry of Finance, Government of India headquartered at Lucknow and having its offices all over the country.

Founded: 2 April 1990

HeadQuarter:Lucknow



# **OBJECTIVES OF SIDBI**

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- ▶ Development of small scale industries and financial assistance
- ▶ Co-ordination with other assisting financial institutions
- ▶ Acceptance of responsibility of development funds
- ▶ Development of technical standards and modernisation of small industries
- ▶ Assistance in marketing of the industrial product
- ▶ Assistance in establishment of employment oriented industries in semi urban areas



# **FUNCTIONS OF SIDBI**

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- ▶ Providing capital
- ▶ Assisting in venture capital
- ▶ Discounting and rediscounting of commercial bill
- ▶ Refinancing
- ▶ Assisting in export and marketing
- ▶ Providing financial services
- ▶ Financial support to states small industries corporation
- ▶ Finance for up gradation and modernisation of industries
- ▶ Assisting in micro finance





# NABARD


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- ▶ NABARD is a development bank focussing primarily on the rural sector of the country. It is the apex banking institution to provide finance for Agriculture and rural development. Its headquarter is located in Mumbai, the country's financial capital.
  - ▶ It is responsible for the development of the small industries, cottage industries, and any other such village or rural projects.
  - ▶ It is a **statutory body** established in 1982 under Parliamentary act-**National Bank for Agriculture and Rural Development Act, 1981**.
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- ▶ NABARD's initiatives are aimed at building an empowered and financially inclusive rural India through **specific goal oriented departments** which can be categorized broadly into three heads: **Financial, Developmental** and **Supervision**.
  - ▶ It provides **refinance support** for building rural infrastructure.
  - ▶ It prepares **district level credit plans** to guiding and motivating the banking industry in achieving these targets.

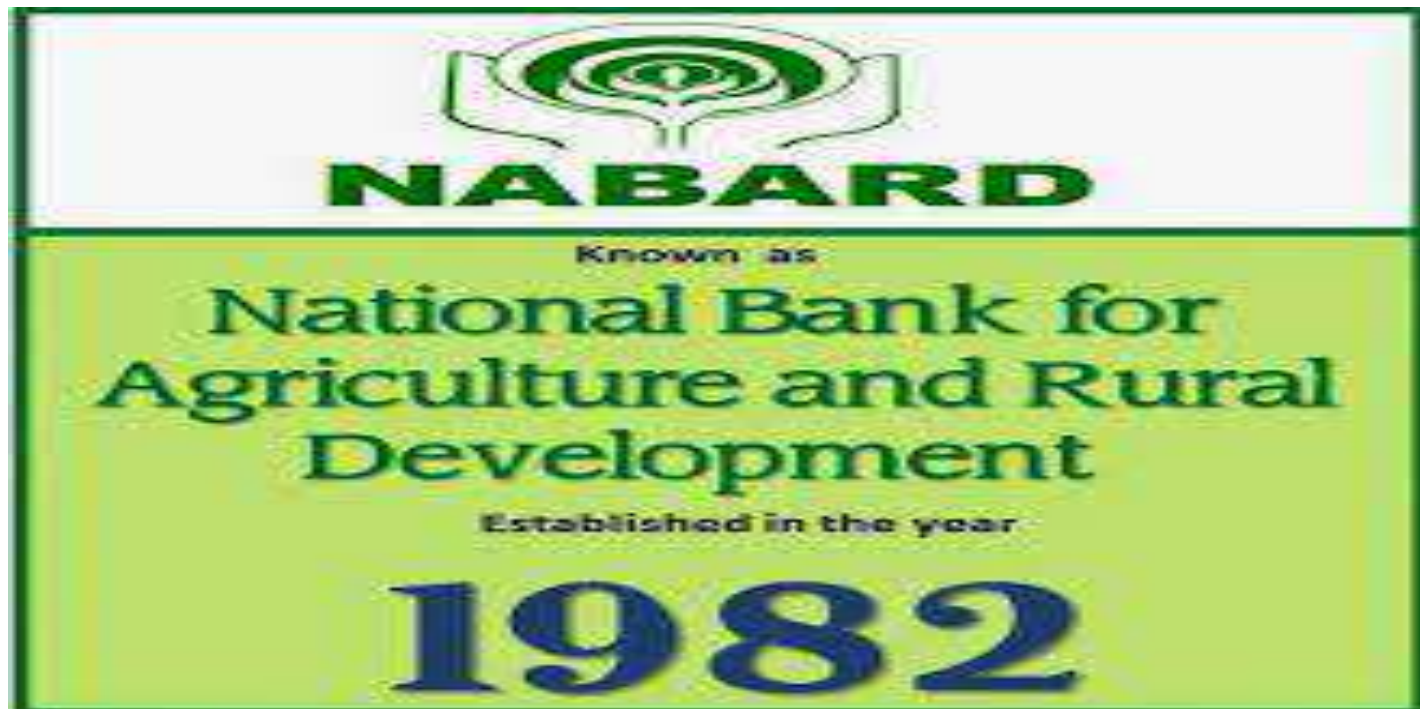


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- ▶ It **supervises Cooperative Banks and Regional Rural Banks (RRBs)** and helping them develop sound banking practices and integrate them to the **CBS (Core Banking Solution) platform.**
  - ▶ **Core Banking Solution (CBS)** is **networking of branches**, which enables Customers to operate their accounts, and avail banking **services from any branch of the Bank** on **CBS network**, regardless of where he maintains his account. The customer is no more the customer of a Branch. **He becomes the Bank's Customer.**
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- ▶ It is involved in designing Union government's development schemes and their implementation.
  - ▶ It provides **training to handicraft artisans** and helps them in developing a **marketing platform** for selling these articles.
  - ▶ NABARD has various **international partnerships** including leading global organizations and **World Bank-affiliated institutions** that are breaking new ground in the fields of rural development as well as agriculture.
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- ▶ These international partners play a **key consultant's role** in providing advisory services as well as **financial assistance** designed to ensure uplifting of rural peoples as well as optimization of various agricultural processes.



# **OBJECTIVES OF NABARD**

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- ▶ Providing Loan
- ▶ Rural Development
- ▶ Supervision of rural credit
- ▶ Coordination
- ▶ Refinancing





# **FUNCTIONS OF NABARD**

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- ▶ Rural development
- ▶ Arrangement of long term loan
- ▶ Coordination
- ▶ Refinancing
- ▶ Supervision of credit system
- ▶ Research work
- ▶ Inspection of activities
- ▶ Development function



# **EXIM-Export & Import Bank**

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- ▶ Export-Import Bank of India (Exim Bank) was set up in 1982 by an Act of Parliament for the purpose of financing, facilitating and promoting India's foreign trade. It is the principal financial institution in the country for coordinating the working of institutions engaged in financing exports and imports. Exim Bank is fully owned by the Government of India.
  - ▶ The Bank provides financial assistance to export-oriented Indian companies by way of term loans in Indian rupees or foreign currencies for setting up new production facilities, expansion/modernization or upgradation of existing facilities and for acquisition of production equipment or technology.
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- ▶ The Bank lays special emphasis on extension of Lines of Credit (LOCs) to overseas entities, national governments, regional financial institutions and commercial banks. The Bank also extends Buyers' credit and Suppliers' credit to finance and promote country's exports.



## LIC & GIC

Basis of Comparison	Life insurance	General insurance
Meaning	Life insurance is an insurance contract, wherein the insurance company promises to compensate the insured individual for uncertainties of life that are death. Life insurance provides protection against life risk.	General insurance is an insurance contract, wherein the insurance company promises to compensate the insured individual or entity for the financial loss or damage caused due to an unfortunate event. General insurance gives protection for all the valuable things that are important to you.
Term of contract	Long-term contract	Short-term contract
Nature of contract	Life insurance is not a contract of indemnity. It is considered as an investment	General insurance is a contract of indemnity

<b>Insurable interest</b>	<b>Life insurance requires the beneficiary to have an insurance interest in the person who is being insured. That means, insurable interest needs to be present at the time of underwriting</b>	<b>In general insurance policies, insurance interest is expected to exist both at the time of underwriting and at the time of loss.</b>
<b>Payment of claim</b>	<b>Benefits under the policy are paid on the occurrence of an insured event or on maturity</b>	<b>Financial loss caused due to the insured event is remembered on the occurrence of the particular event</b>
<b>Compensation value</b>	<b>The compensation value is dependent on the premium payable under the policy</b>	<b>The compensation value is the actual loss incurred in the insured event (maximum amount payable is subjected to the policy limit)</b>



<b>Premium payment</b>	<b>Premiums need to be paid periodically over the years for a specified term</b>	<b>Premium is paid in a lump sum as the policy is purchased for short-term and plans need to be renewed on expiry</b>
Savings	Many life insurance plans come with a savings element which helps the insured to build corpus or create wealth for future	General insurance plans have no savings component as it's an indemnity contract wherein you incur the premium cost to avail the protection





## **Functions of LIC**

- ▶ The major functions of LIC are as follows:-
- ▶ Collect people's savings in exchange for an insurance policy and promote savings in the country.
- ▶ Protect the capital of the people by investing funds into government securities.
- ▶ Issue insurance policies at affordable rates
- ▶ Provide various loans like direct loans to industries, housing loans, loans to various national projects at reasonable interest rates.

## **Objectives of LIC**

- ▶ LIC aims to spread awareness about the importance of life insurance among people living in rural areas and people who are a part of socially and economically backward classes.
  - ▶ It aims to meet several life insurance needs of the community people who are subjected to change with the changing social and economic environment.
  - ▶ It aims to conduct business economically while taking into consideration that the money belongs to the policyholders.
  - ▶ It aims in maximization of the mobility of people's savings through attractive insurance-linked savings.
  - ▶ It aims in providing utmost job satisfaction to all the agents and employees of the corporation and promotes building a co-operative work environment to deliver efficient service with courtesy to its insured public.
  - ▶ It aims to deploy the funds to the best advantage of the investors and the community as well.
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**Objective of the GIC:** To carry on the general insurance business other than life, such as accident, fire etc.

- ▶ To aid and achieve the subsidiaries to conduct the insurance business and
- ▶ To help the conduct of investment strategies of the subsidiaries in an efficient and productive manner.

**Role and Functions of GIC** Carrying on of any part of the general insurance, if it thinks it is desirable to do so.

- ▶ Aiding, assisting and advising the acquiring companies in the matter of setting up of standards of conduct and sound practice in general insurance business.
- ▶ Rendering efficient services to policy holders of general insurance.
- ▶ Advising the acquiring companies in the matter of controlling their expenses including the payment of commission and other expenses.
- ▶ Advising the acquiring companies in the matter of investing their fund.
- ▶ Issuing directives to the acquiring companies in relation to the conduct of general insurance business.
- ▶ Issuing directions and encouraging competition among the acquiring companies in order to render their services more efficiently.



# MUTUAL FUNDS

- ▶ A mutual fund is a type of financial vehicle made up of a pool of money collected from many investors to invest in securities like stocks, bonds, money market instruments, and other assets. Mutual funds are operated by professional and money managers, who allocate the fund's assets and attempt to produce capital gains or income for the fund's investors. A mutual fund's portfolio is structured and maintained to match the investment objectives stated in its prospectus.

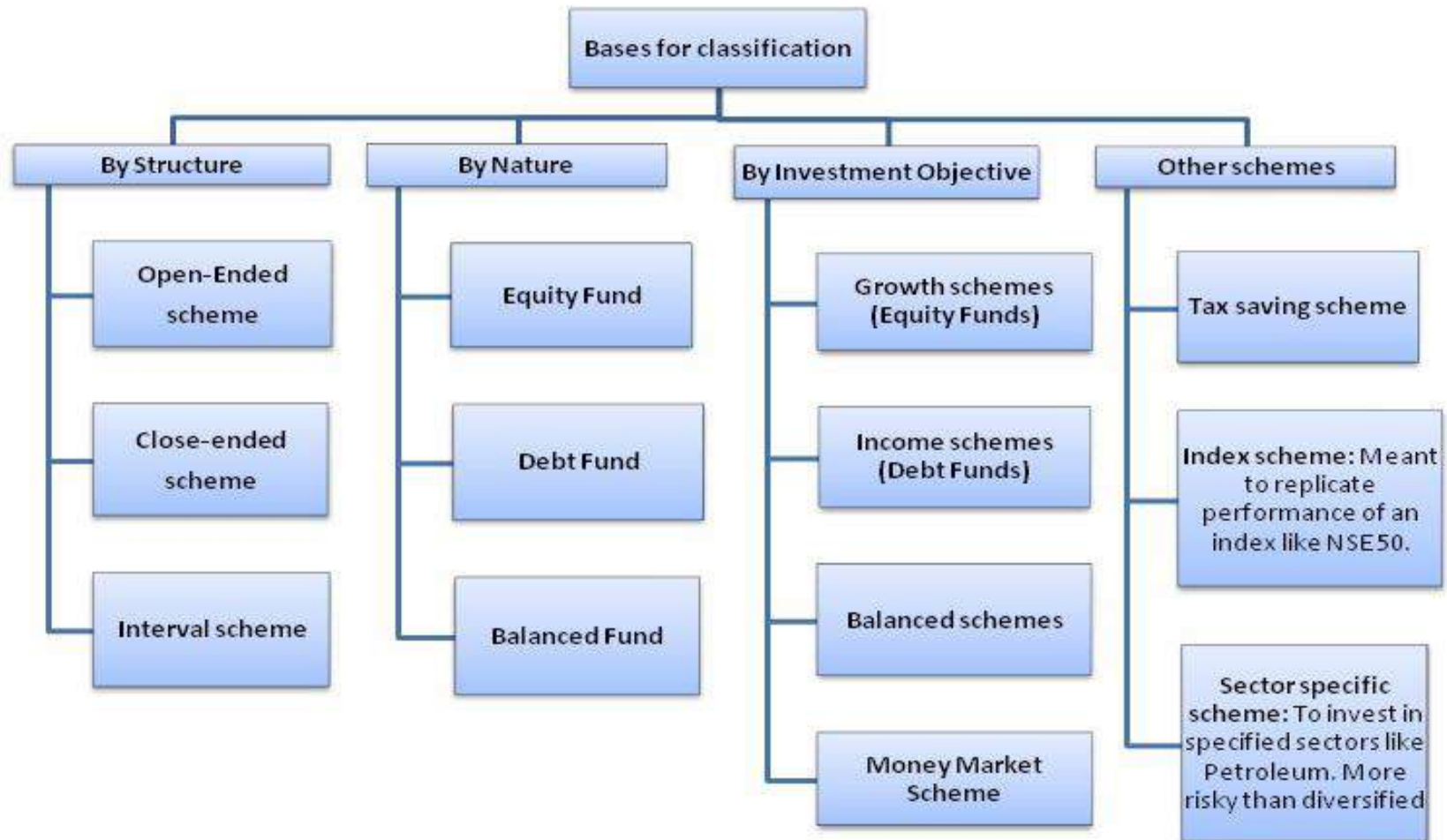
## **ADVANTAGES**

- ▶ Diversification
- ▶ Reduction of risk
- ▶ Expertise supervision
- ▶ Safety of investment
- ▶ Reduced operating cost
- ▶ Liquidity of investment
- ▶ Tax benefit
- ▶ Transparency
- ▶ Convenience

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# TYPES OF MUTUAL FUNDS

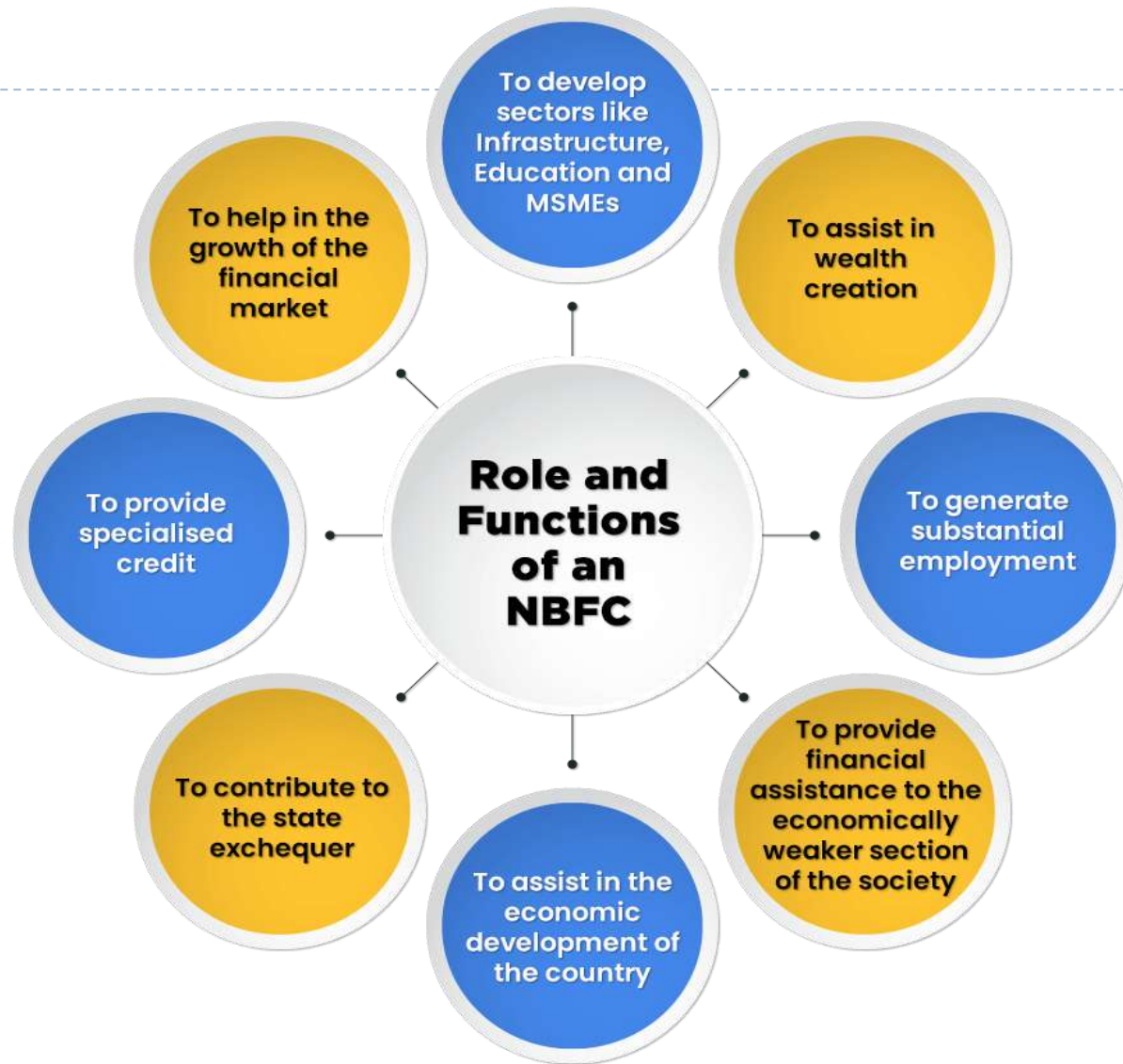


## NBFC



Basis for Comparison	Bank	NBFC
Meaning	Bank is a government authorized financial intermediary that aims at providing banking services to the general public.	An NBFC is a company that provides banking services to people without holding a bank license.
Incorporated under	Banking Regulation Act, 1949	Companies Act 1956 or Companies Act 2013
Loan sanction process	Comparatively Stringent	Easier and faster
Demand Deposit	Accepted	Not Accepted
Deposit insurance facility	Available	Not available
Overdraft Facility	Available in some banks such as SBI	Not Available
Maintenance of Reserve Ratios	Compulsory	Not required
Credit creation	Banks create credit	NBFC do not create credit
Transaction services	Provided by Banks	Not provided by NBFC
Foreign Investment	Allowed up to 74% for private sector banks	Allowed up to 100%





## **REGULATION OF RBI OVER NBFC**

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- ▶ RBI has been given powers to register, lay down policy, issue directions, inspect, regulate, supervise and exercise surveillance over NBFSs.
- ▶ RBI can penalize NBFC's for violating the provisions of the RBI Act.
- ▶ Deposit accepting NBFC's also have to comply with the statutory liquidity requirements.
- ▶ The NBFC's are allowed to accept public deposits for a minimum period of 12 months and maximum period of 60 months. They cannot accept deposits repayable on demand. Actions may be taken by RBI if any NBFC violates this rule.





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THANK YOU!

