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Banking and Finance
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Self-Learning Material
(SEM 1)

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PREFACE

In the ever-evolving landscape of global economics, banking and finance stand as the bedrock upon which the intricate structures of commerce are built. From the ancient practices of money lending to the modern intricacies of digital transactions, the realm of finance has journeyed through epochs of innovation, crisis, and reform.

This book endeavours to serve as a comprehensive guide through the multifaceted terrain of banking and finance, offering a blend of historical perspective, theoretical insight, and practical application. Whether you're a seasoned professional navigating the complexities of modern markets or a curious novice seeking to understand the fundamentals, this tome aims to provide a wealth of knowledge to enrich your understanding.

Within these pages, you will traverse the origins of banking, from the rudimentary systems of barter to the sophisticated mechanisms of central banking. You will delve into the intricacies of financial instruments, exploring the diverse array of securities, derivatives, and investment vehicles that shape the global economy.

Moreover, this book will examine the pivotal role of banking and finance in driving economic growth, fostering innovation, and mitigating risk. From the corridors of power in Wall Street to the bustling trading floors of international exchanges, we will uncover the mechanisms by which financial institutions allocate capital, manage liquidity, and influence economic outcomes.

In an era marked by unprecedented technological advancement and geopolitical uncertainty, the need for a nuanced understanding of banking and finance has never been more pronounced. By equipping readers with the tools to navigate this complex landscape, we aim to empower individuals and organizations to make informed decisions, mitigate risk, and seize opportunities in an ever-changing world.

It is our hope that this book will serve as a guiding beacon for all those who seek to unravel the mysteries of banking and finance, illuminating pathways to prosperity and financial resilience in the pursuit of a more prosperous future.

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Unit 1

Financial Systems & Markets

Learning Outcomes:

- Know about the banks and the functions performed by the banks.
- Evaluate the role, importance and functioning of regulatory institutions in finance and banking.
- Discuss and critically evaluate the types of financial markets.
- Integrate the money and capital market and use the advance technology.
- Express knowledge about the instruments of the money market.

Structure:

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1.1 Definition of Bank

A bank is a kind of financial institution that is permitted to accept deposits from customers and provide loans and other financial services to both individuals and companies. Banks contribute to the economy because they make it easier for savers to transfer money to borrowers and because they offer a wide range of financial services and products, such as credit cards, mortgages, loans, checking and savings accounts, and investment services. Additionally, they frequently provide services including safe deposit lockers, asset management, and currency exchange. Government agencies regulate banks to maintain stability, safeguard depositor interests, and safeguard the integrity of the financial system as a whole.

1.2 Functions of Bank

Banks perform a variety of functions within the financial system, serving the needs of individuals, businesses, and governments. Here are some of the primary functions of banks:

- **Accepting Deposits**: Banks accept deposits from individuals, businesses, and other entities. These deposits may include savings accounts, checking accounts, fixed deposits, and various other types of accounts.
- **Providing Loans and Advances**: Banks provide loans and advances to individuals and businesses for various purposes, such as purchasing homes, funding education, starting or expanding businesses, and meeting short-term financial needs. This function includes both consumer loans and commercial loans.
- **Credit Creation**: Banks have the unique ability to create credit by lending out a portion of the deposits they receive. Through the process of fractional reserve banking, banks can lend out more money than they actually hold in reserves, thereby expanding the money supply and facilitating economic activity.
- **Facilitating Payments**: Banks provide payment services that allow individuals and businesses to transfer funds to one another. These services may include electronic funds

transfers, wire transfers, check clearing, and card-based transactions such as debit and credit card payments.

- **Issuing of Credit Instruments**: Banks issue various credit instruments such as credit cards, debit cards, checks, drafts, and traveller's checks, which enable customers to make payments and access funds conveniently.
- **Providing Financial Advice and Services**: Banks offer financial advisory services and products such as investment advice, wealth management, retirement planning, insurance products, and brokerage services to help individuals and businesses manage their finances and achieve their financial goals.
- **Foreign Exchange Services**: Banks facilitate foreign exchange transactions and provide services related to currency exchange, international remittances, trade finance, and hedging against currency risks for businesses engaged in international trade.
- **Safekeeping of Valuables**: Banks offer safe deposit boxes and other secure storage facilities for customers to safeguard valuable assets such as important documents, jewellery, and other valuables.
- **Clearing and Settlement Services**: Banks participate in clearing and settlement systems that facilitate the smooth functioning of financial markets by clearing and settling transactions between banks, financial institutions, and other market participants.
- **Corporate Banking Services**: Banks provide a range of services tailored to the needs of corporate clients, including cash management, treasury services, trade finance, project finance, and corporate lending.

1.3 Financial Institutions

Financial institutions refer to organizations that facilitate the flow of funds within the financial system by offering various financial services and products. These institutions play a critical role in the economy by channelling funds from savers to borrowers, managing risks, and providing essential financial infrastructure. Here are some common types of financial institutions:

- **Banks**: As mentioned earlier, banks accept deposits from customers and provide loans and other financial services. They also offer a range of products such as checking and savings accounts, credit cards, mortgages, and investment services.

- **Credit Unions**: Credit unions are member-owned financial cooperatives that offer similar services to banks, including savings accounts, loans, and other financial products. They often cater to specific communities or groups of individuals.
- **Insurance Companies**: Insurance companies provide various types of insurance coverage to individuals and businesses, including life insurance, health insurance, property insurance, and liability insurance. They pool risks from policyholders and provide financial protection against unforeseen events.
- **Investment Banks**: Investment banks specialize in providing financial advisory services, underwriting securities offerings, facilitating mergers and acquisitions, and assisting companies with raising capital through debt and equity financing.
- **Brokerage Firms**: Brokerage firms facilitate the buying and selling of financial securities such as stocks, bonds, mutual funds, and other investment products on behalf of investors. They may also offer research, advisory, and wealth management services.
- **Asset Management Firms**: Asset management firms manage investment portfolios on behalf of individuals, institutions, and other clients. They invest in various asset classes such as stocks, bonds, real estate, and alternative investments with the goal of maximizing returns while managing risk.
- **Pension Funds**: Pension funds manage retirement savings on behalf of employees and retirees. They invest contributions from employers and employees in diversified portfolios to generate returns that fund future pension obligations.
- **Hedge Funds**: Hedge funds are investment funds that employ various strategies to generate returns for their investors. They typically cater to high-net-worth individuals and institutional investors and may use leverage and derivatives to amplify returns.
- **Venture Capital Firms**: Venture capital firms invest in early-stage and growth-stage companies with the potential for high growth and returns. They provide capital and strategic support to start-ups in exchange for equity stakes in the companies.
- **Private Equity Firms**: Private equity firms invest in established companies with the aim of improving performance, implementing operational changes, and ultimately realizing a profit through a sale or public offering. They often acquire controlling stakes in companies and actively manage their investments.

1.4 Types of financial markets

Buyers and sellers of financial assets, including stocks, bonds, currencies, commodities, and derivatives, transact on financial markets, which are platforms or systems. The pricing of financial products and the distribution of capital are made easier by these marketplaces. Financial markets come in a variety of forms, each with distinct functions and appealing to different kinds of assets and investors. These are a few typical categories of financial markets:

- **Equity market**: Shares of publicly traded corporations are bought and sold on the stock market. It gives investors a way to buy stocks and participate in the ownership of businesses. Trading in equities is made easier by stock exchanges like the Nasal and the New York Stock Exchange (NYSE).
- **Bond Market (Debt Market)**: The bond market is where debt securities such as government bonds, corporate bonds, and municipal bonds are traded. Bonds represent loans made by investors to issuers (governments or corporations) in exchange for regular interest payments and the repayment of the principal amount at maturity.
- **Foreign Exchange Market (Forex Market)**: The foreign exchange market is where currencies are traded. It facilitates the conversion of one currency into another for purposes such as international trade, investment, and speculation. The four market is decentralized and operates 24 hours a day, five days a week.
- **Commodity Market**: The commodity market is where raw materials and primary agricultural products such as gold, silver, oil, wheat, corn, and coffee are bought and sold. Commodity exchanges facilitate trading in physical commodities as well as derivative contracts based on commodities.
- **Derivatives Market**: The derivatives market consists of financial instruments whose value is derived from an underlying asset or reference rate. Derivatives include futures, options, swaps, and forwards, which are used for hedging, speculation, and risk management purposes.
- **Money Market**: The money market is where short-term debt securities with maturities of one year or less are traded. These securities include Treasury bills, commercial paper,

certificates of deposit (CDs), and repurchase agreements (repos). The money market provides liquidity to financial institutions and serves as a venue for short-term borrowing and lending.

- **Capital Market**: The bond and stock markets, where a long-term debt and equity securities are traded, belong in the capital market. It makes it less difficult for governments as well as businesses to raise funds by issuing stocks and bonds.
- **Primary Market**: New securities are originally issued and sold to investors in the primary market by issuers. Through initial public offerings (IPOs) and bond offerings, this market enables businesses and governments to raise funds by selling recently issued stocks and bonds.
- **Secondary Market**: Following their issuance in the main market, investors purchase and sell existing securities on the secondary market. Trading in secondary markets is facilitated by stock exchanges and over-the-counter (OTC) markets.
- **Alternative Investment Market**: Alternative investment markets include platforms for trading non-traditional assets such as private equity, hedge funds, real estate investment trusts (REITs), and venture capital. These markets cater to sophisticated investors seeking higher returns and portfolio diversification.

- **Knowledge Check 1**

State True or False

1. Banks primarily serve as intermediaries between depositors and borrowers.
2. Banks only provide services related to monetary transactions.
3. Facilitating payments is not a primary function of banks.
4. Banks only offer investment services to high-net-worth individuals.
5. Financial markets have no impact on the economy.

- **Outcome-Based Activity 1**

  Define the term "bank" and explain its role in the economy. Provide examples of services offered by banks that contribute to economic growth and development.

1.5 Instruments of money market

The money market is made up of different highly liquid short-term financial products with maturities of one year or less. Financial institutions, businesses, governments, and other money market participants trade these instruments. These are a few typical money market instruments:

- **Treasury Bills (T-Bills)**: Issued by governments, particularly the U.S. Treasury in the United States, Treasury bills are short-term securities with maturities ranging from a few days to one year. They are sold at a discount to face value and do not pay interest but are redeemed at face value upon maturity, providing a return to investors.
- **Certificates of Deposit (CDs):** Banks and credit unions offer CDs as time deposits. The interest rates for these have fixed terms that can vary anywhere from just a few days to a number of years, and they typically greater than regular savings accounts. Federal Insurance covers CDs. U.S. Deposit Insurance Corporation (FDIC) according to certain limitations.
- **Commercial Paper**: Commercial paper is an unsecured, short-term debt instrument issued by corporations and financial institutions to finance short-term liabilities or fund operating expenses. It typically has maturities ranging from 1 to 270 days and is sold at a discount to face value.
- **Repurchase Agreements:** Repurchase Agreements, or Repos, are short-term collateralized loans where the lender & the borrower agree to purchase back the securities at a later date at an amount that is somewhat greater after the borrower sells them to the lender. Financial institutions frequently turn to repos to handle their needs for immediate liquidity.
- **Banker's Acceptances (BAs)**: Banker's acceptances are short-term promissory notes issued by a company and guaranteed by a bank. They are used in international trade to facilitate financing of goods and services. BAs typically have maturities ranging from 30 to 180 days.
- **Federal Funds**: Federal funds are overnight loans of reserves between banks held at the Federal Reserve. Banks with excess reserves lend funds to banks in need of additional

reserves to meet reserve requirements or liquidity needs. The federal funds rate is the interest rate charged on these transactions and serves as a benchmark for short-term interest rates.

- **Short-Term Municipal Securities**: Municipalities issue short-term debt securities, such as tax anticipation notes (TANs) and revenue anticipation notes (RANs), to finance short-term cash flow needs. These securities are backed by the issuing municipality's ability to raise funds through future tax revenues or specific revenue sources.

- **Money Market Mutual Funds (MMMFs)**: Money market mutual funds invest in a diversified portfolio of money market instruments, offering investors a way to access the money market with low risk and high liquidity. MMMFs typically maintain a stable net asset value (NAV) of $1 per share and pay dividends based on the yields generated by the underlying securities.

- **Knowledge Check 2**

Fill in the Blanks:

1. A bank is a financial institution that __________ from the public and provides various financial services.
    A) borrows
    B) accepts deposits
    C) lends money
2. Banks provide __________ by offering loans and credit to individuals and businesses for various purposes.
    A) investment services
    B) insurance
    C) lending
3. __________ are platforms where individuals and institutions can buy and sell financial assets such as stocks and bonds.
    A) Capital markets
    B) Money markets
    C) Derivatives markets
4. Treasury bills are short-term __________ issued by governments to raise funds.
    A) Bonds
    B) Stocks
    C) Debt securities

- **Outcome-Based Activity 2**

  What are financial systems? Define the financial instruments in bank.

1.6 Summary

Banks are financial organizations that take deposits from the general public and offer a range of financial services, such as investment, lending, and payment processing. By transferring money from savers to borrowers and by offering liquidity and financial intermediation services, they play a vital role in the economy. In addition to taking deposits, banks also facilitate payments and transactions, issue credit and loans, manage risks, offer investment services, and serve as custodians for important assets. These operations promote economic expansion and help the financial system run smoothly.

Beyond banks, a wide range of organizations are considered financial institutions, such as credit unions, asset management businesses, brokerage houses, insurance providers, and investment banks. In the financial system, they perform a variety of functions, including managing investments, underwriting securities, giving financial advice, and delivering insurance coverage.

Financial markets provide a range of venues for the purchase and sale of financial assets, including stocks, bonds, currencies, and commodities, by private citizens, corporate entities, and governmental bodies. Money markets are used for short-term debt securities, capital markets are used for long-term debt and equity securities, derivatives markets are used for financial contracts based on underlying assets, and FX markets are used for currency trading.

A portion of the financial market where short-term debt securities are exchanged is known as the money market. Treasury bills, commercial paper, certificates of deposit, repurchase agreements, and short-term bonds are among the instruments that are frequently traded in the money market. In addition to providing channels for short-term lending and borrowing, these products are essential for controlling interest rate risk and liquidity.

1.7 Keywords

- Bank
- Financial services
- Deposits
- Lending
- Investment
- Payment facilitation
- Financial institutions
- Insurance companies
- Investment banks
- Brokerage firms
- Asset management firms
- Financial markets
- Stocks
- Money markets
- Capital markets

1.8 Self-Assessment Questions

What are the primary functions of banks and how do they influence financial stability?

Unit 2

Financial Services

Learning Outcomes:

- State the various financial services available.
- Express knowledge about NBFC's and their role in financial environment.
- Evaluate the role and importance of SEBI in financial regulation.
- Examine the IPO's w.r.t the primary financial markets.
- Integrate role of KYC in provision of financial services.

Structure:

2.1 Introduction to Financial Services

2.2 Definition and role of NBFC'S

2.3 SEBI: Role & Importance

2.4 IPO

- Knowledge Check 1
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2.5 KYC

- Knowledge Check 2
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2.6 Summary

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2.9 References / Reference Reading

2.1 Introduction to Financial Services

Financial services include a wide range of products and services offered by organizations including banks, credit unions, investment businesses, insurance companies, and others. These services are intended to support companies, governments, and people in efficiently managing their financial resources. Here is a quick overview of some important financial services topics:

- **Banking Services**: Banks offer various services, including deposit accounts (such as savings and checking accounts), loans (such as mortgages, personal loans, and business loans), credit cards, and electronic fund transfers. They also provide services like currency exchange, safe deposit boxes, and financial advice.
- **Investment Services**: Investment firms provide services related to investing money in financial markets. This can include buying and selling stocks, bonds, mutual funds, and other securities on behalf of clients. Investment advisors offer guidance on portfolio management, retirement planning, and wealth management.
- **Insurance Services**: Insurance companies offer policies that protect individuals and businesses against financial losses due to unexpected events such as accidents, illness, natural disasters, or death. Types of insurance include life insurance, health insurance, property insurance, auto insurance, and liability insurance.
- **Financial Planning and Advisory Services:** Financial planners and advisers assist people and companies in creating thorough financial plans that are customized to their objectives and situation. They offer guidance on risk management, tax planning, estate planning, retirement planning, saving, investing, and budgeting.
- **Wealth Management:** High-net-worth individuals and families are served by wealth management companies, which provide individualized financial services such investment management, estate planning, tax optimization, charitable planning, and legacy planning**.**
- **Real Estate Services**: Real estate firms provide services related to buying, selling, renting, and managing residential and commercial properties. This includes property valuation, mortgage brokerage, property management, and real estate investment advice.

- **Payment Services**: Payment service providers facilitate the transfer of funds between parties, enabling transactions through various channels such as cash, checks, credit cards, debit cards, electronic wallets, and mobile payments. They also provide services like merchant processing, payment gateways, and fraud detection.
- **Financial Technology (FinTech)**: Finch companies leverage technology to offer innovative financial services and solutions, disrupting traditional banking and financial practices. Examples include peer-to-peer lending platforms, robo-advisors, crowd funding platforms, crypto currency exchanges, and mobile payment apps.

• In general, financial services are essential for promoting economic activity, controlling risk, and helping people and companies reach their financial objectives. To maintain market integrity, financial stability, and consumer protection, the industry is heavily regulated.

2.2 Definition and function of Non-Banking Financial Companies (NBFCs):

Financial organizations that offer banking services but lack a banking license are known as NBFCs. By providing a broad range of financial services and frequently targeting markets or segments that traditional banks might not be able to effectively serve, they play a vital role in the financial system. Here is a thorough explanation of their responsibilities and definition:

Definition:

Non-Banking Financial Companies (NBFCs):

- NBFCs are financial entities that engage in activities similar to banks, such as lending, investment, asset financing, and wealth management.
- They do not meet the legal definition of a bank and, therefore, do not hold a banking license.
- NBFCs are regulated by the financial regulatory authorities in each country, with specific regulations tailored to their activities and risk profiles.
- They typically cannot accept demand deposits from the public like banks but may accept term deposits or other forms of deposits.

Roles of NBFCs:

- **Credit Provision**:
  - NBFCs provide various forms of credit, including loans, advances, and credit facilities, to individuals, businesses, and other entities.
  - They often serve segments of the population or sectors of the economy that may have limited access to traditional banking services, such as small businesses, self-employed individuals, or those with poor credit histories.
- **Asset Financing**:
  - Many NBFCs specialize in asset financing, offering loans or leases to finance the purchase of assets such as vehicles, equipment, machinery, or real estate.
  - This enables individuals and businesses to acquire essential assets without needing to pay the entire cost upfront, thereby facilitating economic activity and investment.
- **Wealth Management**:
  - Some NBFCs provide wealth management services, including investment advisory, portfolio management, retirement planning, and estate planning.
  - They cater to individuals, families, and institutional investors, helping them manage their investment portfolios and achieve their financial goals.
- **Microfinance**:

  Microfinance NBFCs concentrate on offering low-income people, entrepreneurs, and small companies financial services, like small loans and savings accounts, especially in rural or underserved areas.

  o By granting access to credit and financial services, they significantly contribute to the advancement of financial inclusion and the empowerment of vulnerable populations.

- **Housing Finance**:
  - NBFCs specializing in housing finance offer loans and mortgages for purchasing, constructing, or renovating residential properties.

    - They help individuals and families fulfill their housing needs by providing tailored financing solutions, thereby promoting homeownership and real estate development.
- **Investment Activities**:
    - NBFCs engage in investment activities, including investing in stocks, bonds, debentures, and other securities.
    - They may also provide financial advisory services related to investment opportunities, asset allocation, and risk management.
- **Risk Mitigation**:
    - NBFCs often act as intermediaries in financial transactions, helping to mitigate risk for lenders and borrowers.
    - They may provide guarantees, insurance, or other risk management products to protect parties involved in financial transactions and facilitate smoother transactions.

2.3 SEBI: Role & Importance

The Securities and Exchange Board of India (SEBI) is the regulatory authority in India tasked with overseeing the securities market, protecting investors' interests, and promoting the development and regulation of the securities market. Here's an overview of SEBI's role and importance:

Role of SEBI:

- Regulatory Oversight: Stock exchanges, stockbrokers, merchant bankers, mutual funds, portfolio managers, and other intermediaries are among the securities market divisions that SEBI oversees. It creates rules, standards, and policies to control how market players behave, guaranteeing honest and open transactions in the securities market.

- **Investor Protection**: One of SEBI's primary objectives is to protect the interests of investors in the securities market.
  - It aims to ensure that investors receive accurate and timely information about securities, issuers, and market intermediaries to make informed investment decisions.
  - SEBI investigates cases of fraud, market manipulation, insider trading, and other malpractices to safeguard investors' interests and maintain market integrity.
- **Market Development**:
  - SEBI plays a pivotal role in the development and growth of the securities market in India.
  - It introduces reforms, initiatives, and policies to promote market efficiency, liquidity, and transparency.
  - SEBI encourages innovation and the adoption of best practices in the securities market to enhance its attractiveness to domestic and international investors.
- **Issuer Regulation**:
  - SEBI regulates the issuance and trading of securities by companies through measures such as the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations.
  - It ensures that companies seeking to raise capital through public offerings comply with disclosure requirements, corporate governance standards, and investor protection norms.
- **Intermediary Regulation**:
  - SEBI regulates various intermediaries in the securities market, including stockbrokers, depository participants, merchant bankers, and credit rating agencies.
  - It prescribes eligibility criteria, registration requirements, and conduct norms for intermediaries to maintain market integrity and investor confidence.
- **Market Surveillance**:
  - SEBI conducts market surveillance to detect and prevent market abuse, manipulation, and insider trading.

    - It monitors trading activities, price movements, and other market indicators to identify irregularities and take timely corrective actions to maintain market integrity.

Importance of SEBI:

- **Investor Confidence**:
    - SEBI's regulatory oversight instills confidence among investors by ensuring fair, transparent, and orderly conduct in the securities market.
    - Investors feel assured that their interests are protected, leading to increased participation and investment inflows into the market.
- **Market Integrity**:
    - SEBI's regulations and surveillance mechanisms uphold market integrity by deterring fraudulent activities, market manipulation, and insider trading.
    - Market participants adhere to ethical standards and regulatory requirements, fostering trust and credibility in the securities market.
- **Market Development**:
    - SEBI's initiatives and reforms promote the development and growth of the securities market, making it more efficient, liquid, and resilient.
    - It encourages innovation, market infrastructure development, and product diversification to enhance the market's attractiveness and competitiveness.
- **Capital Formation**:
    - SEBI's regulations and oversight facilitate capital formation by providing a conducive environment for companies to raise funds from the capital market.
    - Issuers benefit from investor confidence and regulatory compliance, enabling them to access capital at competitive costs to fuel business expansion and investment.
- In summary, SEBI plays a crucial role in regulating and developing India's securities market, safeguarding investors' interests, maintaining market integrity, and fostering market growth and innovation. Its regulatory framework and oversight mechanisms are instrumental in ensuring the stability, efficiency, and fairness of the securities market, thereby contributing to India's overall economic development.

2.4 IPO

An Initial Public Offering (IPO) is the process through which a private company offers its shares to the public for the first time, thus becoming a publicly-traded company. Here's an overview of what an IPO involves:

Process of an IPO:

- **Preparation Stage**:
  - **Selection of Advisors**: The company selects investment banks or underwriters to manage the IPO process. These advisors help the company determine the offering price, structure the deal, and comply with regulatory requirements.
  - **Due Diligence**: The company conducts a thorough review of its financials, operations, legal matters, and other aspects to ensure compliance with regulatory standards and provide transparency to potential investors.
- **Filing of Prospectus**:
  - The company files a draft prospectus with the regulatory authority (such as the Securities and Exchange Commission in the US or SEBI in India), disclosing information about its business, financial performance, risks, and proposed offering terms.
  - The regulatory authority reviews the prospectus to ensure compliance with disclosure requirements and investor protection norms.
- **Marketing and Road show**:
  - Once the prospectus is approved, the company, along with its underwriters, embarks on a roadshow to market the IPO to potential investors.
  - Management teams present the company's business model, growth prospects, and financial performance to institutional investors, analysts, and other stakeholders to generate interest in the offering.
- **Price Setting**:
  - Based on investor feedback and market demand, the company and its underwriters determine the final offering price and the number of shares to be sold.

  - The offering price is typically set at a level that balances the company's valuation objectives with investor demand and market conditions.
- **Allocation and Allotment**:
  - The underwriters allocate shares to institutional investors, retail investors, and other stakeholders based on their investment preferences and order size.
  - The allocation process aims to ensure a fair distribution of shares among investors while maximizing the proceeds for the company.
- **Listing on Stock Exchange**:
  - Once the offering is completed, the company's shares are listed on one or more stock exchanges, enabling public trading.
  - Investors can buy and sell shares of the newly public company on the secondary market, where prices are determined by supply and demand dynamics.

Objectives and Benefits of an IPO:

- **Capital Raising**:
  - The primary objective of an IPO is to raise capital to fund business expansion, investments, debt repayment, research and development, or other corporate purposes.
  - Going public provides access to a broader investor base and potentially larger capital pools than private financing options.
- **Liquidity for Existing Shareholders**:
  - An IPO allows existing shareholders, such as founders, employees, and early investors, to monetize their investments by selling a portion of their shares in the public markets.
  - It provides liquidity and an exit opportunity for early-stage investors, potentially unlocking value and rewarding stakeholders for their contributions.
- **Enhanced Visibility and Profile**:
  - Going public increases a company's visibility, credibility, and profile in the marketplace, attracting attention from customers, suppliers, business partners, and potential employees.

    - It can enhance the company's brand reputation and facilitate business development opportunities.
- **Currency for Acquisitions and Strategic Growth**:
    - Publicly traded shares can serve as currency for acquisitions, mergers, and strategic partnerships, enabling companies to pursue growth opportunities, expand market presence, and create shareholder value.
- **Benchmark for Valuation**:
    - An IPO establishes a market value for the company's shares, providing a benchmark for future valuation assessments, stock-based compensation, and strategic decision-making.
    - Public market investors' perception of the company's value influences its ability to raise capital, attract talent, and execute strategic initiatives.

In summary, an IPO represents a significant milestone for a private company seeking access to public capital markets, liquidity for shareholders, enhanced visibility, and strategic growth opportunities. It involves a structured process of preparation, regulatory compliance, marketing, pricing, and listing, with the aim of achieving the company's financing objectives and creating long-term value for stakeholders.

- **Knowledge Check 1**
    1. Financial services encompass a wide range of activities, including banking, insurance, investment management, and payment processing.
    2. NBFC stands for Non-Banking Financial Corporation.
    3. SEBI is responsible for regulating and overseeing the functioning of stock exchanges in India.
    4. An IPO is the process through which a privately held company becomes a publicly traded company by issuing shares to the public for the first time.
- **Outcome-Based Activity 1**

  What is the SEBI? Explain the objective, role and importance of SEBI.

2.5 KYC

KYC, which stands for "Know Your Customer," describes the procedure used by companies to confirm the legitimacy of their clients before doing business with them. In order to prevent money laundering and combat the funding of terrorism, as well as to ensure regulatory compliance across a range of industries, but especially in the financial industry, the Know Your Customer (KYC) process is essential. An outline of the KYC procedure and its significance is provided below:

Key Components of KYC Process:

- **Customer Identification**:
    - Businesses collect identifying information from customers, such as name, address, date of birth, government-issued identification number (e.g., passport, driver's license), and other relevant details.
    - For corporate customers, additional information such as business registration documents, ownership structure, and authorized signatories may be required.
- **Customer Due Diligence (CDD)**:
    - CDD involves assessing the risk associated with a customer based on factors such as their financial background, nature of business activities, geographical location, and transaction history.
    - Enhanced due diligence (EDD) may be conducted for high-risk customers or transactions, involving more extensive verification and monitoring measures.
- **Risk Assessment**:
    - Businesses evaluate the risk posed by customers based on factors such as their geographic location, nature of business, transaction volume, and historical behaviour.
    - Risk assessments help businesses determine the level of scrutiny and monitoring required for each customer and tailor their compliance measures accordingly.

- **Identity Verification**:
  - Businesses verify the identity of customers using reliable and independent sources, such as government-issued identification documents, utility bills, bank statements, or biometric data.
  - Identity verification helps prevent identity theft, fraud, and unauthorized access to financial services.
- **On-going Monitoring**:
  - Businesses continuously monitor customer transactions, behaviours, and account activities to detect any suspicious or unusual patterns indicative of money laundering, terrorist financing, or other illicit activities.
  - On-going monitoring enables businesses to identify and report suspicious activities promptly to regulatory authorities.

- **Importance of KYC:**
- **Risk Mitigation**:
  - KYC helps businesses assess and mitigate the risk of financial crime, including money laundering, terrorist financing, fraud, and other illicit activities.
  - By verifying the identity of customers and conducting due diligence, businesses can prevent criminals from using their services for illegal purposes.
- **Regulatory Compliance**:
  - KYC is a legal and regulatory requirement in many jurisdictions, mandated by anti-money laundering (AML), counter-terrorism financing (CTF), and other financial regulations.
  - Compliance with KYC regulations helps businesses avoid fines, penalties, reputational damage, and legal consequences for non-compliance.
- **Protection of Reputation**:
  - Implementing robust KYC measures demonstrates a commitment to ethical business practices, integrity, and customer protection, enhancing the reputation and trustworthiness of businesses in the eyes of stakeholders, including customers, investors, and regulators.

- **Financial Stability**:
    - KYC contributes to the stability and integrity of the financial system by preventing illicit funds from entering the legitimate economy and safeguarding the integrity of financial institutions and markets.
- **Customer Trust**:
    - Effective KYC procedures reassure customers that businesses are committed to protecting their interests, privacy, and financial security.
    - Building trust through KYC helps businesses attract and retain customers, foster long-term relationships, and differentiate themselves in competitive markets.

- **Knowledge Check 2**
    1. IPO stands for (A) Initial Public Offering] or (B) Initial Private Offering.
    2. Unlike traditional banks, NBFCs primarily provide........... (credit / healthcare services) without holding a banking license.
    3. KYC stands for (A) Know Your Customer or (B) Keep Your Cash

- **Outcome-Based Activity 2**

  Explain the importance of the KYC (Know Your Customer) process in the financial industry. How does KYC help in mitigating risks associated with money laundering and terrorist financing?

2.6 Summary

Financial services encompass a broad spectrum of activities, including banking, insurance, investment management, and payment processing. These services are crucial for facilitating economic activities by providing individuals and businesses with access to capital, risk management solutions, and various financial products.

NBFCs, or Non-Banking Financial Companies, play a significant role in the financial sector by providing credit and financial services without holding a banking license. They cater to sectors

underserved by traditional banks, such as small and medium-sized enterprises (SMEs) and rural areas. NBFCs complement traditional banks by offering specialized financial products and credit facilities to specific customer segments.

SEBI, the Securities and Exchange Board of India, regulates and oversees the functioning of stock exchanges and securities markets in India. Its role includes protecting the interests of investors, promoting market integrity, and ensuring the development of the securities market. SEBI regulates both the primary and secondary markets, applying its regulations to various market participants, including listed companies, intermediaries, and market infrastructure institutions.

The process by which a privately held firm becomes a publicly listed company by first issuing shares to the public is known as an IPO, or initial public offering. Investment banks and underwriters help companies establish the selling price and underwrite the shares during initial public offerings (IPOs). An initial public offering (IPO) is typically chosen by businesses to raise money for potential development and expansion or to give current shareholders access to liquidity.

KYC, or Know Your Customer, is a regulatory requirement that mandates financial institutions to verify the identity of their clients. KYC procedures help prevent financial crimes such as money laundering and fraudulent activities by ensuring that customers' identities are legitimate. Once completed, KYC procedures may require periodic updates to ensure compliance with regulatory standards.

2.7 Keywords

- Know Your Customer (KYC)
- Risk Assessment
- Identity Verification
- On-going Monitoring
- Financial services

- Capital
- Risk management
- Financial products.
- Non-Banking Financial Companies
- Securities and Exchange Board of India
- Regulation
- Stock exchanges

2.8 Self-Assessment Questions

Analyse recent trends and developments in KYC practices, including regulatory changes, technological advancements, and emerging risks. How are businesses adapting their KYC processes to address these trends?

Unit 3

Negotiable Instruments

Learning Outcomes:

- State about the financial environment- both money and capital market along with the various financial services available.
- Express knowledge about the negotiable instruments and laws governing them.
- Evaluate the role importance and functioning of regulatory institutions in finance and banking.
- Assemble and use the latest technology in banking and critically examine the cautions to be exercised.
- Integrate the money and capital market and use the advance technology.

Structure:

3.1 Relationship between Banker & Customer

The relationship between a banker and a customer is primarily one of trust and mutual benefit. Here are some key aspects of this relationship:

- **Trust**: Customers trust bankers to safeguard their money, provide reliable financial advice, and execute transactions accurately and securely. Banks, in turn, trust customers to use their services responsibly and to fulfil their financial obligations.
- **Financial Services**: Customers of banks can get a variety of financial services from them, such as credit cards, loans, savings accounts, investment goods, and financial advice. The demands and tastes of the client determine the type of these services.
- **Confidentiality**: Bankers are bound by strict confidentiality rules that protect the privacy of their customers' financial information. This confidentiality is crucial for maintaining trust and ensuring the security of customers' assets.
- **Communication**: Effective communication is essential in the banker-customer relationship. Bankers should listen to their customers' needs, provide clear explanations of available products and services, and promptly address any concerns or questions.
- **Regulatory Compliance**: Both bankers and customers must adhere to relevant laws and regulations governing banking practices. This includes anti-money laundering laws, know-your-customer requirements, and consumer protection regulations.
- **Financial Education**: Bankers often play a role in educating customers about financial matters, helping them make informed decisions about managing their money, investing, and planning for the future.
- **Customer Service**: Providing excellent customer service is critical for maintaining a positive relationship between bankers and customers. This includes being responsive to inquiries and complaints, resolving issues promptly, and treating customers with respect and professionalism.

Overall, the relationship between a banker and a customer is built on trust, transparency, and mutual respect, with both parties working together to achieve their financial goals.

3.2 Cheques, Bills of Exchange & Promissory Notes

Cheques, bills of exchange, and promissory notes are all financial instruments used in commercial transactions, each serving different purposes and having distinct characteristics:

1. **Cheques**:
   - A cheque is a written order from an account holder (drawer) to their bank (drawee) to pay a specific sum of money to the person or entity named on the cheque (payee).
   - Cheques are commonly used for everyday transactions such as paying bills, making purchases, or transferring money to other individuals or businesses.
   - The drawer must have sufficient funds available in their account to cover the amount specified on the cheque.
   - Cheques provide a convenient and widely accepted method of payment, but they can also be subject to fraud or misuse if not handled securely.
2. **Bills of Exchange**:
   - A bill of exchange is a written order from one party (the drawer) to another party (the drawee) to pay a certain amount of money to a third party (the payee) at a specific future date.
   - Bills of exchange are commonly used in international trade transactions or when parties wish to extend credit terms for the payment of goods or services.
   - Unlike cheques, bills of exchange involve three parties: the drawer, the drawee (who accepts the bill), and the payee.
   - Bills of exchange are negotiable instruments, meaning they can be transferred or endorsed to another party, allowing for flexibility in payment arrangements.
3. **Promissory Notes**:
   - A promissory note is a written promise by one party (the maker or debtor) to pay a specific sum of money to another party (the payee or creditor) at a predetermined future date or on demand.

- Promissory notes are often used in lending arrangements, such as loans or mortgages, where one party borrows money from another and agrees to repay it according to specified terms.
- Unlike bills of exchange, promissory notes typically involve only two parties: the maker and the payee.
- Promissory notes are legally enforceable documents and can serve as evidence of a debt owed by the maker to the payee.

In summary, while cheques, bills of exchange, and promissory notes are all used in financial transactions, they have different structures, purposes, and legal implications. Cheques are orders for a bank to pay money, bills of exchange are orders for one party to pay another at a future date, and promissory notes are written promises to pay a specified amount of money.

3.3 Collection & payment of Negotiable Instruments

- There are a number of procedures involved in the collection and payment of negotiable instruments, such as promissory notes, bills of exchange, and checks, in order to guarantee correct and timely processing of the transactions. This is a quick overview of the procedure:
- **Presentment**:
  - The first step in the collection process is the presentment of the negotiable instrument to the bank or financial institution where it is drawn.
  - For cheques, this involves presenting the cheque to the drawer bank for payment.
  - For bills of exchange and promissory notes, the instrument may be presented to the drawer or maker for acceptance or payment.
- **Acceptance or Payment**:
  - Upon presentment, the drawer bank or maker of the instrument will review it to verify its authenticity and ensure that it meets the terms and conditions specified.
  - For cheques, the drawer bank will verify the signature of the drawer, check the availability of funds, and process the payment if all requirements are met.
  - For bills of exchange, the drawer may accept the bill by signing it, indicating their commitment to pay the specified amount on the maturity date.

    - For promissory notes, the maker is obligated to pay the specified amount according to the terms of the note.
- **Clearing Process**:

  o If the instrument involves many banks or financial institutions, it may go through a clearing process after acceptance or authorization of payment.

  o When it comes to checks, this usually entails the sharing of photographs of the checks and the settlement of money between the participating institutions.

  o The clearing procedure makes sure that money is quickly sent from the payer's account to the payee's account.

- **Payment to Payee**:
    - After the instrument is processed and cleared, the funds are made available to the payee or beneficiary of the instrument.
    - For cheques, this may involve crediting the payee's account with the amount specified on the cheque.
    - For bills of exchange and promissory notes, payment is made according to the terms of the instrument, either on the maturity date or upon demand.
- **Recording and Reconciliation**:
    - Banks and financial institutions maintain records of all negotiable instruments processed, including details such as the instrument number, amount, date, and parties involved.
    - Regular reconciliation processes are performed to ensure that all transactions are accurately recorded and accounted for.

Overall, the collection and payment of negotiable instruments involve a structured process to facilitate secure and efficient financial transactions between parties.

3.4 Dishonour of cheques & its legal provisions

- When a cheque is dishonored, it means that the bank has refused to honor the payment requested by the cheque due to various reasons, such as insufficient funds, a mismatched signature, a post-dated cheque being presented prematurely, or the account being closed. Here are the legal provisions regarding dishonored cheques:
- **Legal Remedies**:
    - In many jurisdictions, the dishonour of a cheque is considered a criminal offense, and legal remedies are available to the payee (the person to whom the cheque was issued) to seek recourse.
    - The legal provisions for dishonoured cheques typically aim to protect the interests of the payee and deter fraudulent or irresponsible behaviour by the drawer (the person who issued the cheque).
- **Cheque Bouncing Laws**:
    - Many countries have specific laws governing dishonoured cheques, often referred to as "cheque bouncing" laws.
    - These laws outline the consequences for the drawer of a dishonoured cheque, which may include fines, penalties, and even imprisonment in some cases.
- **Notice of Dishonour**:
    - When a cheque is dishonoured, the bank is required to provide a notice of dishonor to the payee, informing them of the reason for dishonour and any recourse available to them under the law.
    - The notice of dishonor is typically sent by the bank through mail or electronically, and it may include instructions for the payee to take further action, such as demanding payment from the drawer or initiating legal proceedings.
- **Legal Action**:
    - In cases where a dishonored cheque is not resolved through informal means, such as communication between the parties or payment of the outstanding amount, the payee may choose to take legal action against the drawer.

    - Legal remedies for dishonored cheques may include filing a complaint with law enforcement authorities, initiating civil proceedings to recover the amount owed, or pursuing criminal charges against the drawer under applicable laws.
- **Statutory Requirements**:
    - Legal provisions regarding dishonored cheques vary from country to country and may be governed by specific statutes or regulations.
    - It's important for individuals and businesses to familiarize themselves with the relevant laws and procedures governing dishonored cheques in their jurisdiction to ensure they understand their rights and obligations.
- In summary, dishonoured cheques can have serious legal consequences for the drawer, and legal provisions are in place to protect the interests of the payee and enforce accountability for financial obligations.

- ## Knowledge Check 1

State whether True or False:

1. Banks have the authority to disclose their customers' financial information to third parties without their consent. (False)
2. Cheques, bills of exchange, and promissory notes are all negotiable instruments commonly used in commercial transactions. (True)
3. Banks can refuse to honor a cheque or bill of exchange if there are insufficient funds in the drawer's account. (True)
4. The drawer of a dishonored cheque may be given a grace period to arrange for funds to cover the payment before facing legal consequences. (True)

- ## Outcome-Based Activity 1

What is a negotiable instrument? Explain the Collection & payment of Negotiable Instruments.

3.5 Salient Features of the Banking Regulation Act

The Banking Regulation Act, a crucial piece of legislation in many countries, lays down the legal framework for regulating banks and financial institutions. Here are some salient features of the Banking Regulation Act:

- **Licensing and Regulation**:
  - The Act provides for the licensing and regulation of banking companies by a central banking authority, typically the country's central bank or monetary authority.
  - It outlines the criteria and procedures for obtaining a banking license and sets standards for the establishment, ownership, and management of banks.
- **Capital Requirements**:
  - The Act mandates minimum capital requirements that banks must maintain to ensure financial stability and solvency.
  - It may specify the types of capital (such as tier 1 and tier 2 capital) and the methods for calculating capital adequacy ratios to assess a bank's ability to absorb losses.
- **Prudential Norms**:
  - The Act imposes prudential norms and guidelines on banks to promote sound banking practices and risk management.
  - These norms may cover areas such as asset classification, provisioning for bad debts, exposure limits, liquidity management, and corporate governance.
- **Regulatory Authority**:
  - The Act confers regulatory powers on the central banking authority to supervise and monitor the activities of banks.
  - It empowers the regulator to issue directives, conduct inspections and audits, impose penalties for non-compliance, and take corrective action to address issues of financial stability or consumer protection.

- **Branch Licensing and Expansion**:
    - Banks are required to obtain regulatory approval for the opening of new branches or the closure of existing branches.
    - The Act may prescribe criteria for branch expansion, taking into account factors such as financial viability, market demand, and regulatory objectives.
- **Ownership and Control**:
    - The Act may impose restrictions on the ownership and control of banks to prevent concentration of economic power and ensure diversity in the banking sector.
    - It may stipulate limits on shareholding by individuals, entities, or groups, and require approval for changes in ownership or management control.
- **Consumer Protection**:
    - The Act includes provisions aimed at protecting the interests of bank customers and depositors.
    - It may require banks to disclose information about their products and services, adhere to fair lending practices, and establish mechanisms for handling customer complaints and grievances.
- **Resolution and Winding-Up**:
    - The Act provides mechanisms for the resolution of distressed banks and the orderly winding-up of insolvent institutions.
    - It may outline procedures for the appointment of administrators or liquidators, the protection of depositors' interests, and the distribution of assets in the event of bank failure.
- **Offenses and Penalties**:
    - The Act defines offenses related to banking activities, such as fraud, embezzlement, money laundering, and violation of regulatory requirements.
    - It prescribes penalties, fines, and other sanctions for individuals or entities found guilty of such offenses, including imprisonment in certain cases.

- ## Knowledge Check 2

    1. The......................... [Banking Regulation Act] provides the legal framework for regulating banks and financial institutions.

2. Banks may refuse to honor a cheque or bill of exchange if there are................... [insufficient funds] in the drawer's account.
3. Cheques are primarily used for making................[cashless payments] between individuals.
4. Banks may impose................ [restrictions] on the withdrawal of funds from a customer's account to prevent fraudulent activities.

- **Outcome-Based Activity 2**

  Write the Salient Features of the Banking Regulation Act, 1934.

3.6 Summary

- The relationship between a banker and a customer is built on trust, confidentiality, and mutual benefit. Bankers provide various financial services to customers, including deposit accounts, loans, and investment products, while customers trust bankers to safeguard their money and provide reliable financial advice.
- Cheques, bills of exchange, and promissory notes are negotiable instruments used in commercial transactions.
- The collection and payment of negotiable instruments involve presentment to the relevant parties, acceptance or payment, clearing processes if necessary, and payment to the payee.
- Legal provisions govern the dishonour of cheques, including notice requirements, enforcement mechanisms, and penalties for non-compliance.

3.7 Keywords

- Banking Regulation
- Central Bank
- Licensing
- Regulation Authority

- Asset Classification
- Banker
- Customer Relationship
- Confidentiality

3.8 Self-Assessment Questions

What are the primary objectives of the Banking Regulation Act in your jurisdiction?

Unit 4
Financial Institutions

Learning Outcomes:

- State about the commercial banking and it's functions.
- Express knowledge about the IDBI and LICas part of the financial environment.
- Evaluate the objectives, functions and achievements of EXIM Bank.
- Examine the role of mutual funds and it's types as investment opportunity.

Structure:

4.1 Definition of Commercial Bank

- A commercial bank is a type of financial institution that provides people, companies, and governments with a broad range of banking services. Usually, these services consist of:
- **Deposits:** Consumers can make deposits into fixed deposit accounts, checking accounts (also known as current accounts), and savings accounts at commercial banks. The bank's lending operations are financed in part by these deposits.
- **Lending:** Through loans, mortgages, credit lines, and other forms of finance, commercial banks give credit to debtors. These loans can be used for a number of things, such buying houses, starting businesses, or paying for personal expenses.
- **Payment Services:** By offering payment services including wire transfers, electronic funds transfers (EFT), check clearing, and the issuance of debit and credit cards, commercial banks help to expedite the flow of money.
- **Foreign Exchange**: Many commercial banks offer foreign exchange services, allowing customers to exchange one currency for another. They may also provide currency hedging and risk management services to businesses engaged in international trade.
- **Investment Services**: Some commercial banks offer investment services, including brokerage services, wealth management, mutual funds, and retirement planning. They may also underwrite securities, provide advice on investment strategies, and manage investment portfolios for clients.
- **Treasury Operations**: Commercial banks manage their own treasury operations, which involve managing the bank's assets and liabilities, liquidity management, and risk management activities. This includes trading in financial instruments such as government bonds, currencies, and derivatives.
- **Other Financial Services**: Commercial banks may offer a range of other financial products and services, including insurance products, pension funds, trust services, and advisory services. They may also provide financing for mergers and acquisitions, project finance, and other corporate transactions.

4.2 Functions of Commercial Bank

- Commercial banks perform a variety of functions that are essential to the functioning of the economy. Here are the key functions of commercial banks:
- **Accepting Deposits**: One of the primary functions of commercial banks is to accept deposits from individuals, businesses, and government entities. These deposits may include savings accounts, current accounts (checking accounts), fixed deposits, and other types of deposit accounts.
- **Providing Loans and Advances**: Commercial banks extend credit to borrowers in the form of loans, advances, overdrafts, lines of credit, and other types of financing. They provide funds to businesses for expansion, individuals for personal needs such as education or home purchase, and government entities for infrastructure projects.
- **Facilitating Payments**: Commercial banks play a crucial role in facilitating payments and transactions within the economy. They provide various payment services such as cheque clearing, electronic funds transfers (EFT), wire transfers, debit cards, credit cards, and online banking platforms. This enables individuals and businesses to make payments to each other and conduct their financial transactions efficiently.
- **Foreign Exchange Services:** A lot of commercial banks let their clients swap one currency for another through their foreign exchange services. By offering services like currency exchange, foreign currency accounts, trade finance, and currency hedging, they promote global trade and commerce.
- **Investment Banking Services:** A few commercial banks provide investment banking services, such as portfolio management for customers, advice services, merger and acquisition facilitation, and securities underwriting. They offer financial guidance on corporate finance and investment strategies, and they assist companies in raising cash through the sale of stocks and bonds.
- **Managing Treasury Operations**: Commercial banks manage their own treasury operations, which involve managing the bank's assets and liabilities, liquidity management, and risk management activities. This includes trading in financial instruments such as government bonds, currencies, and derivatives to generate profits and manage risks.

- **Providing Ancillary Services**: Commercial banks offer a range of ancillary services such as safe deposit boxes, insurance products, pension funds, trust services, and advisory services. They may also provide financing for specialized needs such as project finance, infrastructure financing, and export financing.
- **Financial Intermediation**: Perhaps the most crucial function of commercial banks is financial intermediation. They act as intermediaries between savers and borrowers, channeling funds from depositors to borrowers and facilitating the flow of capital within the economy. This intermediation function helps to allocate capital efficiently and promote economic growth and development.

4.3 IDBI & LIC

Meaning:

- IDBI stands for the Industrial Development Bank of India. It was established on July 1, 1964, under an Act of Parliament, the Industrial Development Bank of India Act, as a wholly-owned subsidiary of the Reserve Bank of India (RBI).
- Initially, IDBI operated as a development finance institution (DFI) with the primary objective of providing financial assistance and support to industrial enterprises in India to promote industrial growth and development.

- **Functions:**

- As a DFI, IDBI performed a range of functions aimed at fostering industrial development in the country:
  - Providing long-term finance: IDBI extended long-term loans and financial assistance to large and medium-sized industrial projects across various sectors, including manufacturing, infrastructure, and services.
  - Project financing: IDBI financed new industrial projects, expansion projects, modernization initiatives, and other capital-intensive ventures.

- Refinancing: IDBI provided refinance facilities to other financial institutions, including commercial banks and state financial corporations, to support their lending activities to industrial borrowers.
- Investment banking: IDBI offered investment banking services such as underwriting of securities, advisory services, and assistance in raising capital through public offerings or private placements.
- Promoting industrial development: IDBI played an active role in promoting entrepreneurship, innovation, and technological advancement in the industrial sector through financial support and assistance programs.

- **Objectives**:

  - The primary objectives of IDBI were aligned with the broader goals of industrialization and economic development in India:
    - Facilitating industrial growth: IDBI aimed to accelerate the pace of industrialization in India by providing timely and adequate financial support to industrial enterprises.
    - Mobilizing resources: IDBI mobilized financial resources from domestic and international sources to meet the funding requirements of industrial projects and promote investment in key sectors of the economy.
    - Promoting balanced regional development: IDBI focused on promoting balanced regional development by extending financial assistance to industrial projects in backward and underdeveloped regions of the country.
    - Supporting priority sectors: IDBI prioritized financing for sectors critical to national development, including infrastructure, agriculture, small-scale industries, and export-oriented industries.

- **Importance**:

  - IDBI played a pivotal role in the development of India's industrial sector and infrastructure by providing financial assistance, expertise, and guidance to industrial enterprises.

- It served as a key financial intermediary, channelling funds from domestic and international sources to support industrial projects and facilitate economic growth.
- IDBI contributed to job creation, technology transfer, and capacity building in the industrial sector, thereby fostering socio-economic development and reducing regional disparities.
- The transformation of IDBI into a commercial bank in 2004 (IDBI Bank Limited) marked a significant evolution in its role, enabling it to offer a broader range of banking products and services to retail and corporate customers while continuing to support industrial development initiatives.

LIC

- **Meaning**:

o The Life Insurance Corporation of India is referred to as LIC. The largest state-owned life insurance company in India, LIC was founded on September 1, 1956, under the Life Insurance Corporation Act.

O To provide a single organization for life insurance services, it was established by nationalizing the life insurance market and combining numerous already-existing insurance companies.

- **Functions**:
  - LIC performs a range of functions related to life insurance and financial services:
    - Providing life insurance coverage: LIC offers a wide range of life insurance products to individuals and groups, including term insurance, endowment plans, whole life plans, money-back plans, pension plans, and unit-linked insurance plans (ULIPs).
    - Risk coverage: LIC provides financial protection to policyholders and their beneficiaries against the risk of premature death, disability, illness, and other contingencies.

        - Wealth accumulation: LIC's insurance products also serve as investment vehicles, allowing policyholders to accumulate savings over time and build a corpus for future financial needs, such as retirement planning, education funding, or wealth creation.
        - Retirement planning: LIC offers pension plans and annuity products designed to provide a regular income stream to policyholders during their retirement years, ensuring financial security and independence in old age.
        - Health insurance: In addition to life insurance, LIC also offers health insurance products and riders to cover medical expenses, hospitalization costs, and critical illnesses.
        - Group insurance: LIC provides group insurance schemes to employers, associations, and institutions, offering life insurance coverage to their employees or members as part of employee benefits or welfare programs.
- **Objectives**:
    - The primary objectives of LIC are aligned with the broader goals of promoting insurance coverage and financial security among the Indian population:
        - Promoting life insurance awareness: LIC aims to increase awareness and understanding of the importance of life insurance as a tool for financial planning, risk management, and wealth accumulation.
        - Providing affordable insurance solutions: LIC strives to offer affordable and accessible life insurance products and services to individuals and families across different socio-economic segments, including rural and urban areas.
        - Enhancing financial inclusion: LIC plays a vital role in promoting financial inclusion by extending life insurance coverage to underserved and marginalized communities, thereby empowering them to protect their families and secure their future.
        - Supporting national development: LIC contributes to the socio-economic development of the country by mobilizing long-term savings, channeling funds into productive investments, and fostering economic growth and stability.

- **Role and Importance**:
  - LIC plays a crucial role in India's insurance sector and financial system, serving as a key provider of life insurance coverage and financial protection to millions of policyholders.
  - It helps individuals and families mitigate financial risks, secure their loved ones' future, and achieve their long-term financial goals through life insurance and investment-linked products.
  - LIC's extensive network of agents, branches, and offices across India enables it to reach customers in both urban and rural areas, promoting insurance penetration and financial literacy.
  - As a significant institutional investor in the Indian capital markets, LIC plays a pivotal role in supporting capital formation, liquidity, and stability in the financial markets through its investment activities.
  - LIC's role as a state-owned enterprise also extends to supporting government initiatives and programs aimed at promoting socio-economic development, including infrastructure projects, rural development schemes, and social welfare programs.

4.4 EXIM Bank – objectives, functions and achievements.

The Export-Import Bank of India (EXIM Bank) is the premier export finance institution in India, established in 1982 under the Export-Import Bank of India Act. It serves as the principal financial institution for facilitating international trade and investment, particularly the export-import trade of goods and services. Here are the objectives, functions, and achievements of EXIM Bank:

Objectives:

- **Facilitating Export and Import Trade**: EXIM Bank aims to promote and facilitate India's international trade by providing financial assistance and support to exporters and importers.

- **Promoting Export Competitiveness**: The bank works towards enhancing the competitiveness of Indian exporters by offering financial products and services that address their unique needs and challenges.
- **Boosting Export Credit**: EXIM Bank focuses on extending export credit facilities to Indian exporters, including pre-shipment and post-shipment finance, export credit insurance, and guarantees.
- **Supporting Export Promotion Initiatives**: The bank collaborates with various government agencies and industry associations to support export promotion initiatives, trade exhibitions, buyer-seller meets, and market development activities.
- **Facilitating Export-Import Financing**: EXIM Bank facilitates trade finance transactions by providing export-import financing, trade credits, and lines of credit to exporters, importers, and overseas buyers.
- **Promoting Cross-Border Investments**: The bank supports Indian companies' overseas expansion and investments by offering financial products such as buyer's credit, supplier's credit, project finance, and investment advisory services.

Functions:

- **Export Finance**: EXIM Bank provides a range of export finance products, including pre-shipment and post-shipment credit, export bills rediscounting, and export credit guarantees, to support exporters' working capital needs and mitigate credit risks.
- **Import Finance**: The bank offers import finance facilities, such as import letters of credit, import bills financing, and import loans, to facilitate imports of capital goods, raw materials, and intermediate goods required by Indian businesses.
- **Export Credit Insurance**: EXIM Bank provides export credit insurance to protect exporters against payment risks associated with non-payment or default by overseas buyers, thereby promoting export credit flows and enhancing exporters' confidence.
- **Project Finance**: The bank supports Indian companies' overseas investments and projects by providing project finance, buyer's credit, and supplier's credit for infrastructure projects, construction projects, and overseas acquisitions.

- **Trade Facilitation Services**: EXIM Bank offers various trade facilitation services, including trade information, advisory services, export-import data analysis, and trade finance training programs, to assist Indian exporters and importers in navigating international trade dynamics.

Achievements:

- **Facilitating Export Growth**: EXIM Bank has played a significant role in promoting India's export growth by providing financial assistance, credit support, and advisory services to exporters across sectors.
- **Supporting Overseas Investments**: The bank has facilitated Indian companies' overseas investments and acquisitions by offering project finance, buyer's credit, and financial advisory services for strategic projects and initiatives.
- **Promoting Export Diversification**: EXIM Bank's initiatives have helped Indian exporters diversify into new markets and product categories, thereby reducing dependency on traditional export destinations and enhancing export competitiveness.
- **Enhancing Trade Finance Availability**: The bank has contributed to enhancing the availability of trade finance in India by providing export-import financing, credit insurance, and trade facilitation services to exporters, importers, and trade intermediaries.
- **Strengthening Trade Ties**: EXIM Bank's partnerships and collaborations with international financial institutions, export credit agencies, and trade promotion organizations have strengthened India's trade ties with key trading partners and facilitated trade and investment flows.

Knowledge Check 1

- A commercial bank offers a limited range of banking services compared to other types of financial institutions. (True /False)
- One of the functions of a commercial bank is to accept deposits from customers..
  (True /False)
- Both IDBI and LIC are state-owned financial institutions in India.(True /False)
- The primary objective of EXIM Bank is to promote domestic trade within India.

(True /False)

Outcome-Based Activity 1

What are the commercial banks? Explain it's functions and objectives.

4.5 Mutual Funds and it's types

- Mutual funds are investment vehicles that combine the capital of several participants to buy a variety of securities, including bonds, equities, money market instruments, and other assets. Professional fund managers oversee them and decide on investments on the clients' behalf. With relatively small investment amounts and expert administration, mutual funds give investors access to a diverse range of securities.

  Mutual funds come in a variety of forms, each with unique risk profiles, asset allocation plans, and investment goals. Several typical mutual fund kinds are as follows:

- **Equity Funds**: The main asset class of equity funds is stocks and other equity assets of businesses. They are appropriate for investors who are ready to assume greater levels of risk in exchange for long-term capital gains.
- **Debt Funds:** These funds make investments in fixed-income assets such money market instruments, corporate and government bonds, and treasury bills. Compared to equities funds, they are more appropriate for investors looking to preserve capital and receive monthly income at lower risk levels. Liquid funds, short-term funds, gilt funds, income funds, and credit opportunity funds are a few examples.
- **Hybrid Funds**: Investing in a combination of debt and equity assets, hybrid funds are also referred to as balanced funds or asset allocation funds. They are appropriate for investors looking for a balance between capital appreciation and yielding returns by providing diversification across asset types. and income generation. Examples include balanced funds, monthly income plans (MIPs), and dynamic asset allocation funds.

• **Index Funds:** These investment vehicles seek to mimic the performance of a particular market index, such the Sensex or the Nifty 50. They match the index they monitor by investing in the same securities in the same proportion. With little tracking error, index funds provide investors with an inexpensive means of getting exposure to the larger market.

• **Exchange-Traded Funds (ETFs):** Traded on stock exchanges like individual equities, ETFs are comparable to index funds. They give investors the freedom to purchase and sell shares at market prices at any time during the trading day. ETFs give investors variety and liquidity by tracking a range of indices, industries, commodities, or asset classes.

• **Sector Funds:** These funds invest in the stocks of businesses that are involved in a certain industry or sector, including technology, They offer investors targeted exposure to a particular sector's growth prospects but may carry higher levels of risk and volatility associated with sector-specific factors.

• **Tax-saving Funds (ELSS):** Under Section 80C of the Income Tax Act, equity-linked savings schemes (ELSS)—a type of mutual fund focused on equity—offer tax advantages. With a three-year lock-in period and a focus on equity investments, they offer investors the chance to benefit from both tax savings and long-term capital growth.

• **Fund-of-Funds:** Rather than investing in individual assets, fund-of-funds make investments in other mutual funds. They provide investors with diversification among several mutual fund schemes run by various fund companies or with various investment goals. With only one investment, FoFs offer accessibility to a diverse portfolio and ease**.**

Knowledge Check 2

- A commercial bank is a __________ institution that offers a wide range of banking services.
- One of the primary functions of a commercial bank is to accept __________ from customers.
- IDBI was initially established as a development finance institution before transforming into a __________.

- EXIM Bank provides export and import finance, export credit insurance, project finance, and trade facilitation services to __________ and importers.
- One of the common types of mutual funds is __________ funds, which primarily invest in stocks or equity securities of companies.

Outcome-Based Activity 2

What are the mutual funds? Describe the types of mutual funds.

4.6 Summary

- Commercial banks are financial institutions that offer a broad range of banking services to individuals, businesses, and government entities.
- The functions of commercial banks encompass accepting deposits from customers, providing loans and advances, facilitating payments and transactions, managing foreign exchange operations, offering investment products and services, and providing other financial services like treasury operations and risk management.
- IDBI, initially established as a development finance institution, has evolved into a commercial bank providing comprehensive banking services.
- EXIM Bank is India's premier export finance institution, aimed at facilitating international trade and investment, promoting export competitiveness, supporting overseas investments by Indian companies, and contributing to India's economic growth.
- Mutual funds are investment vehicles that pool funds from investors to invest in a diversified portfolio of securities.

4.7 Keywords

- Commercial Bank
- IDBI
- LIC
- EXIM Bank

- Mutual Funds
- Equity Funds
- Financial Institutions
- Export Finance

4.8 Self-Assessment Questions

Explain the process of accepting deposits and providing loans in a commercial bank.

Unit 5

Regulatory Institutions

Learning Outcomes:

- Know about the objectives and organization of RBI.
- Express the roles and functions of RBI as an Indian Central Bank.
- Evaluate the role of RBI as a regulatory body for credit control.
- Examine NABARD as a regulatory institution.
- Evaluate the objectives and functions of SEBI.

Structure:

5.1 RBI: Objectives & Organization

- As the nation's central banking organization, the Reserve Bank of India (RBI) is essential to the development of monetary policy in the nation and the supervision of the financial system. Below is a summary of its goals and structure:

  Goals:

- **Monetary Stability**: The RBI's major goals are to keep prices stable and keep inflation within predetermined bounds. To accomplish end, it creates and carries out monetary policies.
- **Financial Stability**: Another important goal is to guarantee the stability of the financial system. In order to protect the integrity of the financial system and avert systemic risks, the RBI oversees and regulates banks and other financial institutions.
- **Exchange Rate Management:** In order to promote external commerce and preserve the Indian rupee's competitiveness in the global market, the Reserve Bank of India (RBI) controls the rupee's exchange rate relative to other major currencies.
- **Credit Control**: Using a variety of tools, including as the repo rate, cash reserve ratio (CRR), statutory liquidity ratio (SLR), etc., it controls the amount and cost of credit available to the economy.
- **Developmental Role**: By encouraging financial inclusion, supporting financial sector innovation, and guaranteeing the efficient operation of payment and settlement systems, RBI also contributes to development.

Organization:

- **Central Board**: The highest decision-making body of the RBI is the Central Board. It is headed by the Governor of RBI and consists of four Deputy Governors, other official directors nominated by the Government of India, and non-official directors appointed by the Government to represent various fields of the Indian economy.

- **Governor**: The Governor is the chief executive officer of the RBI and is responsible for the overall management and functioning of the bank. The Governor is appointed by the Government of India.
- **Deputy Governors**: There are typically four Deputy Governors who assist the Governor in various functions and oversee different departments within the RBI.
- **Departments and Offices**: RBI has several departments and offices responsible for different functions such as monetary policy, banking regulation and supervision, currency management, economic research, financial markets, and others.
- **Regional Offices**: RBI has regional offices located in major cities across India, which oversee the functioning of banks and financial institutions in their respective regions and implement RBI policies at the grassroots level.
- **Subsidiaries**: RBI has subsidiaries like the National Housing Bank (NHB) and Deposit Insurance and Credit Guarantee Corporation (DICGC), which perform specific functions related to housing finance and deposit insurance, respectively.

5.2 RBI: Roles & Functions

The Reserve Bank of India (RBI) plays a pivotal role in India's financial system and economy. Its roles and functions are diverse and encompass various aspects of monetary policy formulation, banking regulation, currency management, and financial stability. Here's a detailed overview:

1. **Creating Monetary Policy:**

• **Interest Rate Management:** To control the cost and availability of credit in the economy, the RBI sets important policy rates such as the repo rate, reverse repo rate, and marginal standing facility (MSF) rate.

• **Open Market Operations (OMOs):** By purchasing and disposing of government securities, RBI OMOs control liquidity in the banking sector.

• **Statutory Liquidity Ratio (SLR) and Cash Reserve Ratio (CRR):** The RBI establishes the SLR and CRR standards for banks in order to regulate their lending capacity and uphold financial stability.

2. Banking Regulation and Supervision:

- **Licensing and Regulation**: RBI issues licenses to banks and regulates their operations to ensure sound banking practices and protect the interests of depositors.
- **Prudential Norms**: It prescribes prudential norms related to capital adequacy, asset classification, and provisioning to maintain the stability of the banking sector.
- **Bank Inspections and Audits**: RBI conducts inspections and audits of banks to assess their financial health, compliance with regulations, and risk management practices.

3. **Currency Management:**

•**Money Issuance:** The Reserve Bank of India (RBI) is the exclusive authority for issuing currency notes in India. It also oversees the distribution and supply of money to satisfy the demand for cash in the economy.

• **Cash Distribution:** It oversees the process of distributing cash through banks and currency chests and guarantees that there are authentic, clean notes in circulation.

4. Financial Stability: In order to avert crises and maintain stability, the RBI monitors and evaluates systemic risks in the financial system.

• Financial Institution Resolution: In order to protect depositor interests and preserve financial stability, it is able to step in and resolve financial institutions that are in trouble.

5. Payment and Settlement Systems:

- **Regulation of Payment Systems**: RBI regulates and supervises payment and settlement systems to ensure efficiency, safety, and reliability in financial transactions.
- **Development of Payment Infrastructure**: It promotes the development of payment infrastructure and fosters innovation in payment systems to enhance financial inclusion and facilitate digital transactions.

6. Developmental Role:

- **Financial Inclusion**: RBI promotes financial inclusion by encouraging banks to reach underserved areas and population segments through various initiatives like priority sector lending and microfinance.
- **Developmental Institutions:** In order to encourage sector-specific growth, it manages and assists specialist organizations like the Small Industries growth Bank of India (SIDBI) and the National Bank for Agriculture and Rural Development (NABARD).

5.3 RBI: Credit Control

Credit control is a significant function of the Reserve Bank of India (RBI) aimed at regulating the availability, cost, and direction of credit within the Indian economy. The RBI employs various tools and mechanisms to influence credit creation by banks and financial institutions. Here's an overview of how RBI controls credit:

1. Monetary Policy Tools:

- **Repo Rate:** The interest rate at which the RBI lends money to commercial banks in exchange for government assets is adjusted periodically. The RBI affects banks' cost of borrowing by adjusting the repo rate, which has an effect on the rates at which banks lend money to consumers.

- **Reverse Repo Rate:** The RBI will accept banks' excess funds at this rate for storage. The RBI can change the amount of credit available to banks overall in the economy by adjusting the reverse repo rate, which can either encourage or discourage banks from keeping surplus liquidity.
- **Marginal Standing Facility (MSF):** By pledging authorized government securities, banks can borrow money from the RBI during times of emergency. Because the MSF rate is usually higher than the repo rate, banks are discouraged from borrowing on a regular basis.
- **Open Market Operations (OMOs)**: RBI conducts OMOs by buying or selling government securities in the open market. By purchasing securities, RBI injects liquidity into the system, encouraging credit flow, while selling securities reduces liquidity, restraining credit expansion.

2. Reserve Requirements:

• Cash Reserve Ratio (CRR): Commercial banks must keep cash reserves with the RBI equal to a predetermined portion of their net demand and time liabilities. The RBI manages the liquidity that banks have available for lending by changing the CRR. While lowering the CRR increases liquidity and credit availability, raising it decreases banks' lendable funds and stifles credit expansion.

• Statutory Liquidity Ratio (SLR): Banks are required to hold authorized securities, such as gold, government bonds, or cash, as a fraction of their deposits. Akin to the CRR, modifications to SLR criteria impact banks' capacity to extend credit and have an impact on credit generation.

3. Directives and Guidelines:

- **Credit Policy**: RBI issues periodic credit policies outlining its stance on interest rates, liquidity management, and credit growth targets. These policies provide guidance to banks regarding their lending practices and credit allocation.

- **Sectorial Guidelines**: RBI may issue specific directives or guidelines to regulate credit flow to priority sectors like agriculture, small-scale industries, export-oriented industries, etc., to ensure equitable credit distribution and promote inclusive growth.

4. Moral Suasion:

- RBI also employs moral suasion, which involves informal persuasion and communication with banks to encourage compliance with its credit control objectives. Through dialogues, meetings, and advisories, RBI seeks to influence banks' lending behavior and credit policies.

5.4 NABARD

In India, a specialist financial organization with an emphasis on agriculture and rural development is called the National Bank for Agriculture and Rural Development (NABARD). NABARD, which was founded on July 12, 1982, by an Act of Parliament, is vital to the nation's efforts to advance rural development and livelihoods centered on agriculture. This is a synopsis of NABARD:

Objectives:

- **Promotion of Agriculture and Rural Development**: NABARD aims to promote agriculture, rural industries, and rural livelihoods by providing financial and developmental support to various stakeholders, including farmers, rural artisans, and entrepreneurs.
- **Financial Inclusion**: NABARD works towards enhancing financial inclusion in rural areas by facilitating credit access to underserved communities, promoting self-help groups (SHGs), and supporting microfinance institutions (MFIs).
- **Infrastructure Development**: It supports the development of rural infrastructure such as irrigation, rural roads, warehousing, and cold storage facilities, thereby improving agricultural productivity and market access for farmers.

- **Institution Building**: NABARD assists in building and strengthening rural financial institutions like cooperative banks, regional rural banks (RRBs), and primary agricultural credit societies (PACS) to ensure the efficient delivery of financial services in rural areas.
- **Policy Advocacy and Research**: NABARD conducts research, surveys, and studies on various aspects of agriculture and rural development and provides policy recommendations to the government to address the challenges faced by rural communities.

Functions:

- **Refinancing**: NABARD refinances commercial banks, RRBs, and other financial institutions for providing loans to agriculture and rural sectors at concessional rates of interest.
- **Direct Lending**: It directly extends loans and financial assistance to state governments, cooperative banks, and rural development institutions for specific projects and programs aimed at rural development.
- **Credit Monitoring and Evaluation**: NABARD monitors the flow of credit to the agricultural and rural sectors and evaluates the impact of various developmental programs and schemes on rural livelihoods and agricultural productivity.
- **Capacity Building**: It conducts training programs, workshops, and capacity-building initiatives for stakeholders involved in agriculture and rural development to enhance their skills and knowledge.
- **Promotion of Self-Help Groups (SHGs)**: NABARD supports the formation and capacity-building of SHGs to empower rural women and marginalized communities and promote their participation in economic activities.
- **Developmental Initiatives**: NABARD implements various developmental initiatives such as watershed development projects, dairy development programs, rural infrastructure projects, and sustainable agriculture practices to promote holistic rural development.

Knowledge Check 1

- The Central Board of RBI consists of a maximum of 20 members.(True/False)
- Currency management is not a function of RBI.(True/False)
- SEBI regulates the insurance sector in India.(True/False)
- SEBI is responsible for promoting fair and transparent dealings in the securities market.(True/False)

Outcome-Based Activity 1

- What are the primary objectives of the Reserve Bank of India (RBI), and how is its organizational structure designed to achieve these objectives effectively?

5.5 SEBI

The Indian securities market is governed by the Securities and Exchange Board of India (SEBI). Its main goals were to safeguard investor interests and advance the growth of the securities market when it was founded on April 12, 1992, in accordance with the SEBI Act, 1992. This is a synopsis of SEBI:

Objectives:

1. **Investor Protection** SEBI works to protect investors' interests by enforcing honest and open transactions in the securities market and eliminating dishonest and unfair business practices.
2. **Regulation and Development**: To encourage orderly and healthy market circumstances favorable to investor trust and capital development, it regulates a number of securities market areas, including stock exchanges, brokers, merchant bankers, and mutual funds.
3. **Promotion of Fair Practices**: By enforcing strict regulatory measures, SEBI encourages ethical and professional standards in the securities sector and fair competition among market participants.
4. **Market Development**: Through the introduction of new products, the improvement of market infrastructure, and the promotion of innovation and technical advancement, SEBI is a key player in the development and regulation of the securities market.

5. **Education and Awareness**: SEBI educates investors about investment opportunities, risks, and rights through investor awareness programs, seminars, and publications to empower them to make informed investment decisions.

Functions:

1. **Regulatory Oversight**: SEBI regulates various entities and intermediaries operating in the securities market, including stock exchanges, brokers, sub-brokers, depositories, and clearing corporations, to ensure compliance with regulatory norms and standards.
2. **Registration and Regulation**: It registers and regulates market intermediaries such as stockbrokers, merchant bankers, portfolio managers, investment advisers, credit rating agencies, and mutual funds to ensure their conduct is in line with regulatory requirements.
3. **Market Surveillance**: SEBI monitors and supervises the securities market through surveillance mechanisms to detect and prevent market manipulation, insider trading, and other fraudulent activities that could undermine market integrity.
4. **Enforcement Actions**: SEBI takes enforcement actions against entities and individuals found violating securities laws and regulations, including imposing penalties, initiating legal proceedings, and issuing warnings and directions to ensure compliance.
5. **Policy Formulation**: SEBI formulates policies and regulations governing the securities market, including listing requirements, disclosure norms, takeover regulations, and corporate governance guidelines, to promote investor confidence and market integrity.
6. **Investor Education and Protection**: SEBI undertakes initiatives to educate investors about market risks, rights, and responsibilities and establishes investor grievance redresses mechanisms such as SCORES (SEBI Complaints Redress System) to address investor complaints and grievances promptly.

Knowledge Check 2

- The primary objective of the Reserve Bank of India (RBI) is to ensure financial stability.(True/False)
- Monetary policy formulation is one of the key functions of the RBI..(True/False)
- RBI is not involved in regulating the banking sector..(True/False)

- NABARD primarily focuses on urban development initiatives..(True/False)

Outcome-Based Activity 2

What are the key challenges faced by SEBI in regulating the securities market, and what are its future directions and priorities?

5.6 Summary

- RBI, established in 1935, serves as the central banking institution of India, responsible for monetary policy formulation, regulation of the financial system, and currency management.
- NABARD, established in 1982, is a specialized financial institution in India focused on agricultural and rural development.
- SEBI regulates various segments of the securities market, including stock exchanges, brokers, merchant bankers, and mutual funds, through regulatory oversight, registration, surveillance, enforcement actions, policy formulation, and investor education.
- Its regulatory framework encompasses listing requirements, disclosure norms, corporate governance guidelines, and other measures aimed at promoting market efficiency, transparency, and investor protection.

5.7 Keywords

- Monetary Stability
- Financial Stability
- Exchange Rate Management,
- Credit Control
- Banking Regulation
- Supervision

5.8 Self-Assessment Questions

- What are the primary objectives of the Reserve Bank of India (RBI)?
- What are the main objectives of NABARD and how does it contribute to rural development?

Unit 6

Banking Innovation

Learning Outcomes:

- State the new technological advancements in banking.
- Express knowledge about the credit and debit cards.
- Evaluate the growth in internet banking
- Examine the various types of the modern baking technologies.
- Integrate the role of CRM in the banking sector.

Structure:

6.1 New Technology in banking

6.2 E-services: Credit & Debit Cards

6.3 Internet Banking

6.4 Types of modern banking technologies

- Knowledge Check 1
- Outcome-Based Activity 1

6.5 CRM in banking

- Knowledge Check 2
- Outcome-Based Activity 2

6.6 Summary

6.7 Keywords

6.8 Self-Assessment Questions

6.9 References / Reference Reading

6.1 New Technology in banking

1. **Digital Banking:** The transition from traditional brick and mortar banking to online and mobile banking platforms is referred to as "digital banking."· Through websites or mobile apps, customers can check their accounts, transfer money, pay bills, and carry out a variety of banking operations.· Customers may manage their finances anytime, anywhere with the ease, flexibility, and accessibility that digital banking provides.
2. **Fintech**: Fintech, an acronym for financial technology, refers to a broad category of cutting-edge firms and technologies that challenge established banking services. Digital wallets, robo-advisors, peer-to-peer lending, crowdfunding platforms, and mobile payments are examples of fintech solutions. The goals of these technologies are to improve client experiences, lower costs, increase efficiency, and improve financial services.
3. **Blockchain Technology:** Blockchain is a decentralized digital ledger system that securely and openly records transactions across numerous machines. Blockchain is mostly related to cryptocurrencies, like as Bitcoin and Ethereum, in the financial industry. These allow for safe peer-to-peer transactions without the need for middlemen. Beyond only cryptocurrency, blockchain is useful for cross-border payments, trade finance, identity verification, and smart contracts, among other things.
4. **Artificial Intelligence (AI):** By enabling tailored customer experiences, increasing operational efficiency, and strengthening risk management, AI is transforming the banking industry. AI-driven chatbots offer round-the-clock client service, responding to questions, helping with transactions, and giving financial guidance. Artificial intelligence (AI) systems examine enormous volumes of data to identify fraudulent activity, evaluate creditworthiness, and personalize product recommendations depending on consumer behavior.
5. **Biometric Authentication:** Unique physical traits like fingerprints, facial features, or iris patterns are used in biometric authentication to confirm a customer's identification. By supplanting more vulnerable techniques like passwords and PINs, biometric authentication improves security. To offer safe and easy authentication processes, banks use biometric authentication in branches, ATMs, and mobile banking apps.
6. **Big Data Analytics**: o To obtain useful insights and enhance decision-making, big data analytics makes use of substantial amounts of both structured and unstructured data. Banks

use consumer data analysis to forecast behavior, comprehend preferences, and provide tailored goods and services. Big data analytics also assist banks with risk management, fraud detection, campaign optimization, and improving operational effectiveness.

7. **Contactless Payments:** Contactless payments: Using Near Field Communication (NFC) technology, a contactless card, smartphone, or wearable device can be tapped or waved to conduct a safe transaction. Contactless payments eliminate the need for actual currency or card swipes by being quick, easy, and safe. The emergence of mobile wallets, transit networks, and retail stores that accept contactless payments has sped up the adoption of contactless payments.
8. **Open Banking:** Open banking is a banking paradigm that uses Application Programming Interfaces (APIs) to give third-party financial service providers access to consumer financial data. By enabling fintech entrepreneurs and developers to create new financial goods and services, open banking fosters innovation, competition, and teamwork. To obtain personalized content, customers can safely share their financial information with approved third parties.
9. **Robotic Process Automation (RPA):** RPA is the process of automating repetitive, rule-based tasks in banking operations through the use of software robots, or bots. RPA simplifies back-office tasks including loan processing, account reconciliation, data entry, and compliance reporting. RPA increases operational effectiveness, lowers mistake rates, and frees up staff to concentrate on higher-value work by automating manual operations.
10. **Cybersecurity Solutions:** o As banking services become more digitally connected, cybersecurity becomes even more important to safeguard client information, financial assets, and digital infrastructure. Banks make investments in cutting-edge cybersecurity technologies like intrusion detection systems, multi-factor authentication, encryption, and security analytics.

Continuous monitoring, threat intelligence, employee training, and regulatory compliance are essential components of a robust cybersecurity strategy. These technological advancements are reshaping the banking landscape, driving innovation, and improving the overall customer experience while addressing challenges such as security, efficiency, and regulatory compliance.

6.2 E-services: Credit & Debit Cards

E-services related to credit and debit cards encompass a wide range of digital offerings aimed at enhancing convenience, security, and flexibility for cardholders. Here's a detailed overview:

1. **Online Account Management:**
   - Cardholders can access their account details, view transaction history, check balances, and make payments online through the bank's website or mobile app.
   - Online account management allows users to monitor their spending, track rewards or cashback points, and set up alerts for suspicious activities or payment due dates.
2. **Mobile Wallet Integration:**
   - Many banks offer mobile wallet applications that allow users to link their credit and debit cards for easy access to funds.
   - Mobile wallets enable contactless payments using Near Field Communication (NFC) technology, allowing users to pay for purchases in-store or online securely with their smartphones.
3. **Virtual Cards:**
   - Virtual credit and debit cards provide an additional layer of security for online transactions by generating one-time-use card numbers.
   - Users can create virtual cards linked to their primary account for online purchases, reducing the risk of fraud and unauthorized transactions.
4. **Card Controls and Alerts:**
   - E-services often include features that allow cardholders to customize their card usage preferences and receive real-time alerts for transactions.
   - Card controls enable users to set spending limits, block specific merchant categories, or temporarily freeze their cards in case of loss or theft.
5. **Cardless ATM Withdrawals:**
   - Some banks offer cardless ATM withdrawal options through their mobile apps, allowing users to withdraw cash from ATMs using a unique code or QR scan instead of a physical card.

- Cardless ATM withdrawals provide added security and convenience, especially in situations where users forget their cards or need to access cash urgently.

6. **Instant Card Issuance:**
    - E-services may include instant card issuance capabilities, allowing users to request and receive a new or replacement credit or debit card instantly at select bank branches or through mobile apps.
    - Instant card issuance eliminates the need to wait for physical cards to be mailed, providing immediate access to funds and enabling seamless card activation.
7. **Fraud Monitoring and Protection:**
    - Banks employ advanced fraud detection algorithms and machine learning technologies to monitor card transactions in real-time and detect suspicious activities.
    - E-services include fraud protection measures such as zero-liability policies, transaction alerts, and two-factor authentication to safeguard cardholders against unauthorized use and fraudulent transactions.
8. **Rewards and Loyalty Programs:**
    - Many credit and debit card issuers offer rewards and loyalty programs that provide cardholders with incentives such as cashback, points, miles, or discounts on purchases.
    - E-services allow users to track their rewards earnings, redeem points for merchandise or travel, and receive personalized offers and promotions based on their spending patterns.

These e-services associated with credit and debit cards contribute to a seamless and secure banking experience, empowering users with greater control, convenience, and protection over their financial transactions.

6.3 Internet Banking

The term "internet banking," sometimes referred to as "online banking" or "e-banking," describes the digital platform that banks offer their clients so they can conduct a variety of financial operations online. This is a thorough note about online banking:

Synopsis: Online banking has completely changed how people and companies handle their money since it offers safe, convenient, and accessible banking services from anywhere at any time. Customers no longer need to visit physical bank branches in order to access a wide range of banking services, including checking account balances, transferring payments, and paying bills, thanks to internet banking systems.

Key Features:

1. **Account Management:** Customers can view account balances, transaction history, and statements online, providing real-time access to their financial information.
2. **Fund Transfers:** Internet banking allows users to transfer funds between their own accounts, to other accounts within the same bank, or to accounts at different banks through electronic funds transfer (EFT) mechanisms.
3. **Bill Payments:** Users can pay bills, utilities, loans, credit card dues, and other expenses online, either as one-time payments or through scheduled recurring payments.
4. **Mobile Banking Integration:** Many internet banking platforms offer seamless integration with mobile banking apps, allowing customers to access banking services on smartphones and tablets for added convenience.
5. **Alerts and Notifications:** Customers can set up alerts and notifications for various banking activities, including account transactions, low balances, bill due dates, and security alerts.
6. **Online Statements and Documents:** Internet banking provides access to electronic statements, documents, and tax forms, reducing the need for paper-based communications and document storage.

7. **Account Customization:** Users can customize their banking experience by setting preferences, updating personal information, managing beneficiaries, and adding or removing services as needed.
8. **Security Features:** Internet banking platforms incorporate robust security measures such as encryption, multi-factor authentication, biometric authentication, and secure sockets layer (SSL) protocols to protect customer data and transactions from unauthorized access and fraud.

Benefits:

1. **Convenience:** Internet banking offers 24/7 access to banking services, eliminating the constraints of banking hours and physical branch locations.
2. **Accessibility:** Customers can bank from anywhere with an internet connection, whether at home, work, or while traveling, using computers, laptops, smartphones, or tablets.
3. **Time-saving:** Online banking saves time by reducing the need to visit bank branches for routine transactions, enabling users to manage their finances efficiently.
4. **Cost-effective:** Internet banking reduces the need for paper-based transactions, postage, and administrative overheads, resulting in cost savings for both banks and customers.
5. **Enhanced Control:** Users have greater control over their finances with real-time access to account information, transaction tracking, and customizable alerts and notifications.
6. **Environmental Sustainability:** By promoting paperless transactions and digital document storage, internet banking contributes to environmental conservation and sustainability efforts.

Challenges:

1. **Security Concerns:** Users must be aware of the risks associated with internet banking and take precautions against phishing attacks, malware, and data breaches.
2. **Digital Divide:** Access to internet banking may be limited in regions with inadequate internet infrastructure or among populations lacking digital literacy skills, widening the digital divide.

3. **Technical Issues:** Users may encounter technical glitches, system downtimes, or compatibility issues with internet banking platforms, affecting the reliability and usability of online banking services.

Future Trends:

1. **Biometric Authentication:** Increasing adoption of biometric authentication methods such as fingerprints, facial recognition, and voice recognition for secure and frictionless login experiences.
2. **Artificial Intelligence (AI):** Integration of AI-powered chatbots and virtual assistants for personalized customer support, financial advice, and predictive analytics.
3. **Open Banking:** Expansion of open banking initiatives and API-driven ecosystems to promote collaboration, innovation, and interoperability among banks and third-party fintech providers.
4. **Blockchain Technology:** Exploration of blockchain applications for secure and transparent financial transactions, digital identity management, and cross-border payments.

In conclusion, internet banking has emerged as a transformative force in the banking industry, offering a comprehensive suite of digital services that empower customers with greater control, convenience, and accessibility over their financial affairs. While internet banking presents numerous benefits and opportunities, it also poses challenges related to security, inclusivity, and technological advancements, necessitating ongoing innovation, regulation, and collaboration to ensure a secure and seamless banking experience for all users.

6.4 Types of modern banking technology

Modern banking technology encompasses a diverse array of innovations aimed at enhancing efficiency, security, and customer experience in the financial services industry. Here are some key types of modern banking technology:

1. **Digital Banking Platforms:**
    - Digital banking platforms provide customers with online access to banking services through web portals and mobile apps.
    - These platforms enable account management, fund transfers, bill payments, loan applications, and other banking transactions from anywhere with internet access.
2. **Mobile Banking Apps:**
    - Mobile banking apps allow customers to access banking services directly from their smartphones or tablets.
    - Users can perform various transactions, receive alerts, view account balances, deposit checks remotely, and access additional features such as budgeting tools and financial insights.
3. **Contactless Payments:**
    - Contactless payment technology enables users to make secure transactions by tapping or waving their contactless-enabled credit or debit cards, smartphones, or wearables at point-of-sale terminals.
    - Near Field Communication (NFC) technology facilitates fast and convenient payments without physical contact, enhancing the speed and convenience of transactions.
4. **Biometric Authentication:** Using distinctive physical traits like fingerprints, face recognition, or iris scans, biometric authentication verifies the identity of clients. By reducing the need for conventional authentication techniques like passwords or PINs, biometric authentication improves security and provides a more convenient and safe user experience.
5. **Blockchain and Distributed Ledger Technology (DLT):**

Decentralized, transparent, and safe solutions for recording and confirming transactions are offered by blockchain technology and DLT. Blockchain is utilized in banking to increase efficiency, security, and transaction trust in a variety of applications, including trade finance, digital identity management, smart contracts, and cross-border payments.

6. **Machine learning (ML) and artificial intelligence (AI):**

o In banking, artificial intelligence (AI) and machine learning (ML) are used for activities like risk management, tailored recommendations, fraud detection, credit scoring, and customer service automation.

o AI-powered chatbots use machine learning and natural language processing (NLP) to offer round-the-clock customer service, including query answering, issue resolution, and personalized help.

7. **RPA, or Robotic Process Automation:** RPA is the process of automating repetitive, rule-based tasks in banking operations through the use of software robots, or bots.
8. **Open Banking and APIs:**
   - Open banking initiatives and application programming interfaces (APIs) enable banks to securely share customer data and services with third-party developers and fintech companies.
   - Open banking fosters collaboration, innovation, and competition in the financial services industry, leading to the development of new products, services, and business models.
9. **Cloud Computing:**
   - Cloud computing technology allows banks to store, process, and analyze large volumes of data securely over the internet.
   - Cloud-based solutions offer scalability, flexibility, and cost-effectiveness, enabling banks to deploy innovative applications, improve agility, and enhance customer experiences.
10. **Cyber security Solutions:**
    - Advanced cyber security technologies such as encryption, multi-factor authentication, intrusion detection systems, and security analytics are crucial for protecting banking systems, data, and customer information from cyber threats and attacks.

- Continuous monitoring, threat intelligence, employee training, and regulatory compliance are essential components of a comprehensive cybersecurity strategy in banking.

These types of modern banking technology represent a transformative shift in the industry, enabling banks to adapt to changing customer preferences, streamline operations, mitigate risks, and drive innovation in the digital era.

- **Knowledge Check 1**
  1. New technology in banking is limited to traditional services and has not significantly impacted the industry. (False)
  2. E-services related to credit and debit cards include features like online account management, mobile wallet integration, and virtual cards. (True)
  3. Internet banking allows customers to perform various banking transactions online, including fund transfers, bill payments, and account management. (True)

- **Outcome-Based Activity 1**

  Explain how these e-services enhance convenience, security, and flexibility for cardholders.

6.5 CRM in Banking

Customer Relationship Management (CRM) in banking refers to the strategies, processes, and technologies implemented by banks to manage and improve interactions with customers throughout their lifecycle. Here's an overview of CRM in banking:

1. **Understanding Customer Needs:**
   - CRM starts with understanding the needs, preferences, and behaviors of bank customers. Banks collect and analyze customer data from various sources, including transactions, interactions, and demographic information.
2. **Segmentation and Targeting:**

- CRM helps banks segment customers based on factors such as demographics, behavior, and profitability. By categorizing customers into segments, banks can tailor products, services, and marketing campaigns to specific customer groups.

3. **Personalized Marketing and Communication:**
    - CRM enables banks to deliver personalized marketing messages, offers, and communications to customers through various channels such as email, SMS, mobile apps, and online banking portals. Personalization enhances customer engagement and loyalty by delivering relevant content and promotions.
4. **Customer Service and Support:**
    - CRM systems centralize customer information and interactions, enabling bank employees to provide more efficient and personalized customer service. CRM platforms facilitate case management, issue resolution, and customer inquiries across multiple channels, including phone, email, chat, and social media.
5. **Cross-Selling and Upselling:**
    - CRM helps banks identify cross-selling and upselling opportunities by analyzing customer data and transaction history. By understanding customer needs and preferences, banks can recommend relevant products and services to customers, increasing revenue and customer satisfaction.
6. **Customer Retention and Loyalty:**
    - CRM plays a crucial role in customer retention and loyalty by nurturing relationships and addressing customer needs proactively. Banks use CRM data to identify at-risk customers, offer loyalty rewards, and implement retention strategies to reduce churn and increase customer lifetime value.
7. **Lead Management and Sales Automation:**
    - CRM systems streamline lead management and sales processes by automating tasks such as lead capture, qualification, and tracking. Banks use CRM workflows and pipelines to manage sales opportunities, forecast revenue, and track performance metrics.
8. **Data Analytics and Insights:**
    - CRM platforms provide banks with valuable insights and analytics to understand customer behavior, preferences, and trends. Banks leverage CRM analytics to

optimize marketing campaigns, improve product offerings, and enhance customer experiences.

9. **Compliance and Regulatory Reporting:**
    - CRM systems help banks comply with regulatory requirements by capturing and maintaining customer data in a secure and compliant manner. CRM platforms enable banks to track customer consent, manage privacy preferences, and generate reports for regulatory audits and compliance purposes.
10. **Integration with Other Systems:**
    - CRM systems integrate with other banking systems and applications such as core banking, marketing automation, and data analytics platforms. Integration enables seamless data exchange and workflow automation, improving operational efficiency and data accuracy.

- **Knowledge Check 2**
    1. New technology in banking includes innovations such as .... (blockchain), ... (artificial intelligence (AI)), and ....(biometric authentication).
    2. ....(Customer Relationship Management) in banking refers to the strategies, processes, and technologies implemented by banks to manage and improve interactions with customers throughout their lifecycle.

- **Outcome-Based Activity 2**

  Provide an overview of modern banking technologies, such as digital banking platforms, mobile banking apps, and cloud computing.

6.6 Summary

New Technology in Banking explores the latest technological advancements shaping the banking industry, such as blockchain, artificial intelligence, and biometric authentication. These technologies are revolutionizing banking operations, enhancing security, and improving customer experiences.

E-services related to credit and debit cards are discussed, including online account management, mobile wallet integration, and virtual cards. These services offer customers convenience and flexibility in managing their finances and making transactions.

Internet banking allows customers to conduct various banking transactions online, including fund transfers, bill payments, and account monitoring. It provides customers with 24/7 access to banking services from anywhere with an internet connection.

A range of modern banking technologies, including digital banking platforms, mobile banking apps, and cloud computing are available for use today. These technologies enhance operational efficiency, streamline processes, and enable banks to deliver personalized services to customers.

Customer Relationship Management (CRM) in banking focuses on building and maintaining strong relationships with customers. It involves strategies, processes, and technologies to understand customer needs, personalize interactions, and enhance customer satisfaction and loyalty. CRM plays a critical role in driving business growth and competitiveness in the banking industry.

6.7 Keywords

- Technology
- Blockchain,
- Artificial Intelligence
- Biometric Authentication
- Digital Transformation
- Mobile Wallet
- Virtual Cards
- Digital Banking Platforms
- Mobile Banking Apps
- Cloud Computing
- Customer Relationship Management

6.8 Self-Assessment Questions

1. How do banks use CRM strategies to improve customer satisfaction and loyalty?
2. What role do mobile banking apps play in providing convenience and accessibility to customers?
3. How does internet banking provide convenience and accessibility to customers?
4. Can you describe a situation where e-services for credit and debit cards would be particularly useful?

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