# DEPARTMENT OF ECONOMICS

POORNAPRAJNA COLLEGE, UDUPI

# ROLE OF RBI

# 1. ISSUER OF CURRENCY

- Sole authority of currency issue
- Issue department looks after issuing currency
- Banking department looks after circulation and withdrawal of currency

# 2. BANKER TO THE GOVERNMENT

- To both central and state government
- Short term credit to government
- Advises govt. on financial matters

# 3. MANAGING GOVERNMENT SECURITIES

- Financial institutions are required by law to invest minimum portion in govt. securities
- RBI administers these

# 4. BANKER TO OTHER BANKS

✓Holds cash reserves

✓Lends short term funds

✓Provides clearing and remittance facilities

# 5. CONTROLLER OF MONEY SUPPLY AND CREDIT

- Regulates the claims of competing banks
- Meets the credit requirement
- Ensure maximum output, price stability, economic growth

# 6. EXCHANGE MANAGER AND CONTROLLER

- Manages exchange control
- Represents India as a member of IMF

## 7. PUBLISHER OF MONETARY DATA AND OTHER DATA

- Maintains and provides banking and economic data
- Collects, collates and publishes data
- Users avail weekly statements, monthly bulletins, annual reports on currency and finance

# 8. DEVELOPMENTAL AND PROMOTIONAL ROLE

i. Development of the financial system

ii. Development of agriculture

iii. Provision of industrial finance

iv. Provision of training

v. Collection of data

vi. Publication of the reports

vii. Promotion of banking habits

viii. Promotion of export through refinance

# TOOLS USED BY RBI

- **Quantitative Credit Control Methods**

  - Bank Rate Policy

As per 2020 – 4.25%

  - Open Market Operations

RBI has announced of the purchase of 10000 govt. securities this year

- Cash Reserve Ratio (CRR)
  - Current CRR is 3%
- Statutory Liquidity Ratio
  - 18.00%
- Repo rate and Reverse repo rate
  - Repo rate- 4.00%
  - Reverse Repo rate- 3.35%

## ❑Qualitative methods

- Ceiling on credit
- Margin requirements
- Discriminatory interest rate
- Directives
- Direct actions
- Moral suasion

# BANKING SECTOR REFORMS

## A ROAD MAP OF RBI

# FIRST PHASE- NARASIMHAN COMMITTEE REPORT 1991

- 4 tier hierarchy for banking structure
- Phased reduction in SLR
- Phased achievement of 8% CAR
- Abolition of branch licensing policy
- Proper classification of assets and full disclosure of accounts

- Deregulation of interest rates
- Delegation of direct lending activity of IDBI to a separate lending body.
- Competition among financial institution
- Setting up asset reconstruction fund

# MEASURES OF GOVERNMENT

- Lowering SLR and CRR
- Prudential Norms
- Capital Adequacy Norms
- Deregulation of interest rates
- Recovery of debts

- Competition from new private sector banks
- Phasing out of directed credit
- Access to Capital Market
- Freedom of operation
- Local Area banks
- Supervision of commercial banks

# SECOND PHASE 1998

- strong Banking system in the context of CAC
- 2/3 banks be given international orientation and global character
- 8/10 national banks & large no. of local banks
- New and higher norms for capital adequacy
- Asset Reconstruction Fund

- BFRS to supervise banks & financial institutions
- Review of RBI Act, Banking Regulation Act etc.
- Net Non-Performing Assets be brought down to 3% by 2002
- Rationalization of bank branches and staffs
- Foreign banks be allowed to set up subsidiaries and joint ventures

# REFORMS TAKEN BY GOVERNMENT

- New areas
- New Instruments
- Risk Management
- Strengthening Technology
- Increase inflow of credit

- Increase in FDI limit
- Universal Banking
- Adoption of global standards
- Information technology
- Base rate system of interest rates

- Management of NPAs
- Mergers and Amalgamation
- Guidelines for Anti-Money laundering
- Managerial autonomy
- Customer Service

# CAPITAL ADEQUACY FOR INDIAN BANKS

Requirements:

- Sufficient to finance bank’s operation
- Adequate to provide protection to depositors and other creditors

- Sufficient to inspire confidence in customers, employees, management and regulators
- Adequate to ensure safety, soundness and systematic stability of organization
- Sufficient to cover the risk associated with assets of bank.

# RECOGNITION OF IMPORTANCE OF CAR

In the past, banks did not build adequate capital for the following reasons

- ❑Government ownership was considered enough
- ❑Indian banks with limited exposure to international banking business
- ❑Low level of profit

In recent years growing globalization and expanding international banking business, attention is given to capital adequacy

# CAPITAL ADEQUACY RATIO SYSTEM

The system of judging the adequacy of capital in relation to risk adjusted assets, known as the capital adequacy ratio system or capital risk-weighted assets ratio system, was developed by Committee on Banking Regulation & Supervisory Practices in July 1988.

# INTRODUCTION OF CAR IN INDIA

- RBI on the recommendation of Narasimhan Committee, introduced in April, 1992 the risk-weighted assets ratio system (CAR)
- Paid-up capital and reserves of a bank should form an adequate percentage of its total assets such as investment, loans, advances

# INCOME RECOGNITION

- RBI has specified interest income on NPA should not be recognized on actual basis.
- Should be recognized only when it is received
- Assets of bank classified into

- Performing assets
- Non Performing Assets

## Performing assets

If interest is served i.e., received promptly and there is nothing irregular in the account.

## Non Performing Assets

An asset which ceases to generate income for the bank.  A credit facility in respect of which the interest or installment of principal is delayed and not received before a stipulated time.

# GUIDELINES OF RBI FOR TREATING NPA

- For Term Loans
- For Cash Credit and Overdrafts

An account is to be treated as out of order if,

- Outstanding balance remains excess of sanctioned limit
- no credit continuously for 90 days/ the credits are not enough to cover the interest debited during same period

- For bills purchased and discounted
- For Agricultural advances
- For Other Accounts

# CLASSIFICATION OF ADVANCES

Banks are required to make provisions for advances and classify their loans:

1. Standard Assets
2. Sub Standard Assets
3. Doubtful Assets
4. Loss Assets

# PROVISIONS AGAINST LOAN  ASSETS

Provisions to be made are:

- Provisions against standard assets
- Provisions against sub-standard assets
- Provisions against doubtful assets
- Provisions against loss assets

# AUTONOMY FOR COMMERCIAL BANKS

To make public sector banks more market driven, GOI allowed more operational freedom through an autonomy package in March 2005

4 parameters are:

- CAR more than 9%
- Net NPA less than 9%
- Net profit over last 3 yrs.
- Minimum owned funds of Rs. 100 crore.

# Additional Parameters

- Net NPA less than 4%
- Minimum owned funds of Rs. 300 crore

# REGULATORY GUIDELINES

- Making suitable acquisition
- Deciding human resource issue
- Prescription of standards
- Prescription of academic, minimum standards, & modality of recruitment & promotion
- Perusing new lines of business

# RATING OF BANKS

S. Padmanabhan committee suggested the supervision of banks should focus on parameters of soundness, financial, managerial & operational efficiency.

Recommended bank should be rated on a 5- point scale of A to E on lines of international CAMELS rating method.

C- CAR

A- Asset Quality

M- Management effectiveness

E- Earning or Profitability

L- Liquidity asset- Liquidity management.