

BANKING THEORY AND PRACTICE

(For Undergraduate Classes)

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PREFACE

This Text-Book of **Banking Theory and Practice** is specially prepared for undergraduate Students. It is prepared in accordance with the latest syllabus given in this book.

I do not claim any originality in the subject-matter of this book. I have drawn immense material from many standard books on this subject. Yet, this book is original in the exposition and presentation of the subject-matter. The subject-matter has been dealt with exhaustively and in very simple language.

I express my profound gratitude to my well-wishers for their encouragement in the preparation of this book. I am also thankful to the **United Publishers, Mangalore and United Publishers' Printing Press, Mangalore** for bringing out this book.

I shall consider my efforts amply rewarded if this book is found useful by the teachers and the students.

Suggestions for improvement of this book will be gratefully accepted.

Mangalore,

B.S. Raman

SYLLABUS
BANKING THEORY AND PRACTICE

Unit 1 : Commercial Banking :

Meaning, nature, types and systems and functions of commercial banks in India. Balance sheet of a bank, Portfolio management in banks, credit creation. New trends in commercial banking, Merchant banking, social responsibility of commercial banks, risk management - risk perception, management and mitigation-changing role of commercial banks as service providers. (12 hrs.)

Unit : II Central Banking :

Nature, functions, credit control methods - RBI and its monetary policy, Role of RBI. (12 hrs.)

Unit : III Financial Markets :

Money and Capital Markets - Constituents - Features - Defects - Instruments - Development Banks, SBI, RRBs, EXIM Bank, NABARD : Organisation, Functions and Performance: NBFIs, Banking Sector Reforms. Foreign Banks, Private Banks. (12 hrs.)

Unit IV : Banker and Customer :

Relationship - General and Special, Paying Banker, Collecting Banker, Ancillary Services of a Banker, E-Banking. (12 hrs.)

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UNIT I :

COMMERCIAL BANKING

Meaning of Commercial Banks:

Commercial banks are banks which carry on commercial banking operations, such as acceptance of deposits from the public repayable on demand or at short notice, and the granting of credit, mainly short-term credit, to trade, commerce and industry.

They are called **commercial banks**, as they finance mainly the working capital requirements of trade and commerce. They are also called **deposit banks**, as they accept deposits from the public repayable on demand or on a short notice, for the purpose of lending for short periods.

Nature of Commercial Banks in India :

The nature of commercial banks in India is indicated by their characteristics.

The main characteristics of commercial banks in India are :

- (i) Commercial banks are the most important type of banks in India in terms of functions.
- (ii) They are the oldest form of banks in India.
- (iii) They are deposit banks, i.e., they accept short-term deposits from the public and their funds consist mostly of deposits repayable on demand or at short notice.
- (iv) They mainly carry on commercial banking, i.e., they mostly finance the working capital or short-term financial requirements of trade, commerce and industry.
- (v) Besides accepting deposits and lending them for short-terms to trade, commerce and industry, they also perform a number of subsidiary, a secondary or ancillary services to their customers and the general public.
- (vi) In India, commercial banks are in the public sector as well as the private sector. But the important commercial banks are public sector banks.
- (vii) Commercial banks, especially private sector commercial banks, are more concerned with profitability.
- (viii) Commercial banks in India are on **branch banking system**, carrying on their activities with a network of branches spread throughout the country or through out one or two states.

- (ix) Of late, there has been a change in the nature of banking activities of commercial banks in India. They are engaged in mixed banking, i.e., commercial banking as well as industrial banking. They have started granting medium and long-term loans to industry.
- (x) They are not merely dealers in money, linking depositors and borrowers, but also manufacturers of money (i.e., bank money) by lending many times more than they borrow. (The excess money lent by them over what they borrowed from the depositors is the money created by them.)

Types of Commercial Banks in India:

Commercial banks in India comprise two categories. They are:

- 1. Public Sector Banks**
- 2. Private Sector Banks**

Public Sector Banks:

Public sector banks refer to commercial banks which are owned by the Central Government either directly or indirectly through the Reserve Bank of India. They are also referred to as **National Banks**. They are established by special acts passed by the parliament.

Public sector banks comprise two categories. They are:

- 1. State Bank Group**
- 2. Nationalised Banks**

State Bank Group:

State Bank Group comprises the State Bank of India and its seven subsidiaries, viz., (1) The State Bank of Bikaner and Jaipur, (2) The State Bank of Patiala, (3) The State Bank of Indore, (4) The State Bank of Saurashtra, (5) The State Bank of Hyderabad, (6) The State Bank of Mysore and (7) The State Bank of Travancore.

Nationalised Banks:

Nationalised banks include the Indian commercial banks nationalised under the following two enactments:

(A) Fourteen commercial banks with deposits of Rs.50 crores or more nationalised by the Government of India on 19th July, 1969 under the

Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970. Those 14 nationalised banks are:

1. The Central Bank of India Ltd., nationalised as Central Bank of India.
2. The Bank of India Ltd., nationalised as Bank of India.
3. The Punjab National Bank Ltd., nationalised as Punjab National Bank.
4. The Bank of Baroda Ltd., nationalised as Bank of Baroda.
5. The United Commercial Bank Ltd., nationalised as United Commercial Bank.
6. The Canara Bank Ltd., nationalised as Canara Bank.
7. The United Bank of India Ltd., nationalised as United Bank of India.
8. The Dena Bank Ltd., nationalised as Dena Bank.
9. The Union Bank of India Ltd., nationalized as Union Bank of India.
10. The Allahabad Bank Ltd., nationalised as Allahabad Bank.
11. The Syndicate Bank Ltd., nationalised as Syndicate Bank.
12. The Indian Overseas Bank Ltd., nationalised as Indian Overseas Bank.
13. The Indian Bank Ltd., nationalised as Indian Bank.
14. The Bank of Maharashtra Ltd., nationalised as Bank of Maharashtra.

(B) Six commercial banks with demand and time liabilities exceeding Rs. 200 crores as on 31st March, 1980 , nationalised by the Government of India on 15th April, 1980 under the Banking Companies (Acquisition and Transfer of Undertakings) Act, 1980. Those 6 banks are:

1. The Andhra Bank Ltd., nationalised as Andhra Bank.
2. The Corporation Bank Ltd., nationalised as Corporation Bank.
3. The New Bank of India Ltd., nationalised as New Bank of India.
4. The Oriental Bank of Commerce Ltd., nationalised as Oriental Bank of Commerce.

5. The Punjab and Sindh Bank Ltd., nationalised as Punjab and Sindh Bank.
6. The Vijaya Bank Ltd., nationalised as Vijaya Bank.

It may be noted that, as a result of the merger of New Bank of India with Punjab National Bank, the number of nationalised commercial banks has come down from 20 to 19. Today, there are only 19 nationalised commercial banks in India.

Private Sector Banks:

Private sector banks refer to commercial banks other than public sector commercial banks. In other words, private sector banks are those commercial banks which are owned and controlled by private entrepreneurs.

Private sector banks comprise two categories of banks. They are:

1. **Private Sector Indian Banks**
2. **Private Sector Foreign Banks**

Private Sector Indian Banks:

Private sector Indian banks refer to commercial banks owned and controlled by private Indian entrepreneurs.

Private sector Indian banks are of two categories. They are (1) Old Private Sector Indian Banks and (ii) New Private Sector Indian Banks formed after 1994.

Today, there are 22 Old Private Sector Indian banks.

There are 8 New Private Sector Indian banks. They are the HDFC Bank Ltd., the ICICI Bank Ltd., the UTI Bank Ltd., renamed as the Axis Bank Ltd., the IdusInd Bank Ltd., the Centurian Bank Ltd., the IDBI Bank Ltd., the Kotak Mahindra Ltd., and the Yes Bank Ltd.

Private Sector Foreign Banks:

Private sector foreign banks refer to commercial banks incorporated outside India, i.e., in foreign countries, but have places of business in India. Formerly, these banks were called foreign exchange banks. There are 40 foreign banks carrying on business in India. Some of the foreign banks carrying on business in