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NO.1 INSTITUTE IN INDIA

INDIAN BANKING

The first bank of limited liability managed by Indians was Oudh Commercial Bank founded in 1881. Punjab National Bank was established in 1894 .

Swadeshi movement, which began in 1906, encouraged the formation of a number of commercial banks. Banking crisis during 1913 -1917 and failure of 588 banks in various States during the decade ended 1949 underlined the need for regulating and controlling commercial banks.

The Banking Companies Act was passed in February1949, which was subsequently amended to read as Banking Regulation Act, 1949.This Act provided the legal framework for regulation of the banking system by RBI. The largest bank - Imperial Bank of India - was taken over by the RBI in 1955 and rechristened as State Bank of India, followed by inclusion of its 7 Associate Banks in1959. At present SBI has five associate banks.

With a view to bring commercial banks into the mainstream of economic development with definite social obligations and objectives, the Government issued an ordinance on 19 July 1969 acquiring ownership and control of 14 major banks in the country. Six more commercial banks were nationalised from 15 April 1980.

Meaning of Bank

Bank is a lawful organisation, which accepts deposits that can be withdrawn on demand. It also lends money to individuals and business houses that need it.

Role of Banking

Banks provide funds for business as well as personal needs of individuals. They play a significant role in the economy of a nation. Let us know about the role of banking.

- It encourages savings habit amongst people and thereby makes funds available for productive use.
- It acts as an intermediary between people having surplus money and those requiring money for various business activities.
- It facilitates business transactions through receipts and payments by cheques instead of currency.
- It provides loans and advances to businessmen for short term and long-term purposes.
- It also facilitates import-export transactions.
- It helps in national development by providing credit to farmers, small-scale industries and self-employed people as well as to large business houses which lead to balanced economic development in the country.
- It helps in raising the standard of living of people in general by providing loans for purchase of consumer durable goods, houses, automobiles, etc.

TYPES OF BANKS

There are various types of banks which operate in our country to meet the financial requirements of different categories of people engaged in agriculture, business, profession, etc. On the basis of functions, the banking institutions in India may be divided into the following types:

1. **Central Bank** (RBI, in India)
2. **Commercial Banks**

- ☞ Public Sector Banks
- ☞ Private Sector Banks
- ☞ Foreign Banks

3. **Development Banks** (IFCI, SFCs)
4. **Co-operative Banks**
   - ☞ Primary Credit Societies
   - ☞ Central Co-operative Banks
   - ☞ State Co-operative Banks

5. **Specialised Banks** (EXIM Bank, SIDBI, NABARD)

Central Bank

A bank which is entrusted with the functions of guiding and regulating the banking system of a country is known as its Central bank. Such a bank does not deal with the general public. It acts essentially as Government's banker, maintain deposit accounts of all other banks and advances money to other banks, when needed. The Central Bank provides guidance to other banks whenever they face any problem. It is therefore known as the banker's bank. The Reserve Bank of India is the central bank of our country. The Central Bank maintains record of Government revenue and expenditure under various heads. It also advises the Government on monetary and credit policies and decides on the interest rates for bank deposits and bank loans. In addition, foreign exchange rates are also determined by the central bank. Another important function of the Central Bank is the issuance of currency notes, regulating their circulation in the country by different methods. No other bank than the Central Bank can issue currency.

COMMERCIAL BANKS

Commercial Banks are banking institutions that accept deposits and grant short-term loans and advances to their customers. In addition to giving short-term loans, commercial banks also give medium-term and long-term loan to business enterprises. Now-a-days some of the commercial banks are also providing housing loan on a long-term basis to individuals. There are also many other functions of commercial banks, which are discussed later in this lesson.

Types of Commercial banks:

Commercial banks are of three types i.e., Public sector banks, Private sector banks and Foreign banks.

➲ **Public Sector Banks:**

These are banks where majority stake is held by the Government of India or Reserve Bank of India. Examples of public sector banks are: State Bank of India, Corporation Bank, Bank of Baroda and Dena Bank, etc.

➲ **Private Sectors Banks:**

In case of private sector banks majority of share capital of the bank is held by private individuals. These banks are registered as companies with limited liability. For example: The ICICI Bank, Axis Bank, Federal Bank etc.

➲ **Foreign Banks:**

These banks are registered and have their headquarters in a foreign country but operate their branches in our country. Some of the foreign banks operating in our country are Hong Kong and Shanghai Banking Corporation (HSBC), Citibank, American Express Bank, Standard & Chartered Bank, Grindlay's Bank, etc. The number of foreign banks operating in our country has increased since the financial sector reforms of 1991. According to a report by RBI there are 47 Foreign Banks branches in India as on March 31, 2013.

- **Development Banks**

  Business often requires medium and long-term capital for purchase of machinery and equipment, for using latest technology, or for expansion and modernization. Such financial assistance is provided by Development Banks. They also undertake other development measures like subscribing to the shares and debentures issued by companies, in case of under subscription of the issue by the public. Industrial Finance Corporation of India (IFCI) and State Financial Corporations (SFCs) are examples of development banks in India.

- **Co-operative Banks**

  People who come together to jointly serve their common interest often form a co-operative society under the Co-operative Societies Act. **When a co-operative society engages itself in banking business it is called a Co-operative Bank**. The society has to obtain a licence from the Reserve Bank of India before starting banking business. Any co-operative bank as a society has to function under the overall supervision of the Registrar, Co-operative Societies of the State. As regards banking business, the society must follow the guidelines set issued by the ReserveBank of India.

NATIONAL BANK FOR AGRICULTURE AND RURAL DEVELOPMENT (NABARD)

INTRODUCTION

NABARD is set up as an apex Development Bank with a mandate for facilitating credit flow for promotion and development of agriculture, small-scale industries, cottage and village industries, handicrafts and other rural crafts. It also has the mandate to support all other allied economic activities in rural areas, promote integrated and sustainable rural development and secure prosperity of rural areas. In discharging its role as a facilitator for rural prosperity NABARD is entrusted with Providing refinance to lending institutions in rural areas Bringing about or promoting institutional development and Evaluating, monitoring and inspecting the client banks Besides this pivotal role, NABARD also:

Acts as a coordinator in the operations of rural credit institutions

Extends assistance to the government, the Reserve Bank of India and other organizations in matters relating to rural development

Offers training and research facilities for banks, cooperatives and organizations working in the field of rural development

Helps the state governments in reaching their targets of providing assistance to eligible institutions in agriculture and rural development

Acts as regulator for cooperative banks and RRBs

Some of the milestones in NABARD's activities are:

District Rural Industries Project (DRIP) has generated employment for 23.34 lakh persons with 10.95 lakh units in 105 districts.

It was setup with an initial capital of Rs. 100 crore, which is in henced to 4,000 crore in 2013 fully subscribed by the Government of India and RBI.

SUBSIDIARIES OF NABARD

Nab cons : NABARD Consultancy Services (Nabcons) is a wholly owned subsidiary promoted by National Bank for Agriculture and Rural Development (NABARD) and is engaged in providing consultancy in all spheres of agriculture, rural development and allied areas. Nabcons leverages on the core competence of the NABARD in the areas of agricultural and rural development, especially multidisciplinary projects, banking, institutional development, infrastructure, training, etc., internalized for more than two decades.

The Company is registered under the Company's Act, 1956, with an authorized capital of Rs 250 million (US $5.75 million) and paid up capital of Rs 50 million (US $1.15 million).

In tune with NABARD's mission to bring about rural prosperity, Nabcons has more than just commercial interest in the assignments it undertakes.

NABARD Financial Services Limited, [NABFINS] is a subsidiary of National Bank for Agriculture and Rural Development (NABARD) with equity participation from NABARD, Government of Karnataka, Canara Bank of India, Dhanalakshmi Bank and Federal Bank. It is a non-deposit taking NBFC registered with the Reserve Bank of India and shall operate throughout India. The main objectives of the Company are to provide financial services in two broad areas of agriculture and microfinance. NABFINS provides credit and other facilities for promotion, expansion, commercialization and modernization of agriculture and allied activities. NBFINS shall engage in the business of providing micro finance sections of the society for securing their prosperity in both rural and urban areas.

NABARD, which is the world renowned apex development bank of our country and pioneered the world's largest microfinance movement, while promoting NABFINS has envisaged that NABFINS shall evolve into a model Microfinance Institution to set standards of governance among the MFIs, operate with exemplary levels of transparency and operate at reasonable/ moderate rates of interest.

Agri Business Finance (AP) Limited (ABFL) was incorporated under Companies Act., 1956 on 17 February 1997. It is a state specific financial institution registered as Non Banking Finance Company. ABFL was promoted with equity participation from National Bank for Agriculture and Rural Development (NABARD), Andhra Bank, Canara Bank, Govt of Andhra Pradesh, Andhra Pradesh, State Cooperative Bank and few Industrial Houses/individuals from the State. It operates in the state of Andhra Pradesh with its registered office at Hyderabad. It is whole owned subsidiary of NABARD.

ABFL was incorporated with the objective of providing credit and to offer facilities for promotion, expansion, commercialization and modernization of enterprises engaged in Agriculture and allied activities. The organization is specifically catering to the long-term investment needs of Agriculture and allied activities since its inception from 1997.

BANKERS INSTITUTE OF RURAL DEVELOPMENT (BIRD)

Established in 1983, at Lucknow, is an autonomous institute promoted and funded by NABARD. BIRD was established primarily to cater to the training needs of RRB personnel. The Institute, has, since 1st April 1992, been catering to the training and information needs of rural bankers through its topical training programs/seminars . The Institute's mandate also includes Research and Consultancy in the related areas

FUNCTIONS OF COMMERCIAL BANKS

The functions of commercial banks are of two types.

(A) Primary functions; and

(B) Secondary functions.

- **Primary functions**

  The primary functions of a commercial bank includes:

- Accepting deposits; and
- Granting loans and advances.

ACCEPTING DEPOSITS

The most important activity of a commercial bank is to mobilise deposits from the public. People who have surplus income and savings find it convenient to deposit the amounts with banks. Depending upon the nature of deposits, funds deposited with bank also earn interest. Thus, deposits with the bank grow alongwith the interest earned. If the rate of interest is higher, public feels motivated to deposit more funds with the bank. There is also safety of funds deposited with the bank.

- **Grant of loans and advances**

The second important function of a commercial bank is to grant loans and advances. Such loans and advances are given to members of the public and to the business community at a higher rate of interest than allowed by banks on various deposit accounts. The rate of interest charged on loans and advances varies according to the purpose and period of loan and also the mode of repayment.

- **Loans**

  A loan is granted for a specific time period. Generally commercial banks provide short-term loans. But term loans, i.e., loans for more than a year may also be granted. The borrower may be given the entire amount in lump sum or in instalments. Loans are generally granted against the security of certain assets. A loan is normally repaid in instalments. However, it may also be repaid in lump sum.

- **Advances**

  An advance is a credit facility provided by the bank to its customers. It differs from loan in the sense that loans may be granted for longer period, but advances are normally granted for a short period of time. Further the purpose of granting advances is to meet the day-to-day requirements of business. The rate of interest charged on advances varies from bank to bank. Interest is charged only on the amount withdrawn and not on the sanctioned amount.

- **Types of Advances**

Banks grant short-term financial assistance by way of cash credit, overdraft and bill discounting.

- **Cash Credit**

  Cash credit is an arrangement whereby the bank allows the borrower to draw amount upto a specified limit. The amount is credited to the account of the customer. The customer can withdraw this amount as and when he requires. Interest is charged on the amount actually withdrawn. Cash Credit is granted as per terms and conditions agreed with the customers.

- **Overdraft**

  Overdraft is also a credit facility granted by bank. A customer who has a current account with the bank is allowed to withdraw more than the amount of credit balance in his account. It is a temporary arrangement. Overdraft facility with a specified limit may be allowed either on the security of assets, or on personal security, or both.

- **Discounting of Bills**

  Banks provide short-term finance by discounting bills, that is, making payment of the amount before the due date of the bills after deducting a certain rate of discount. The party gets the funds without waiting for the date of maturity of the bills. In case any bill is dishonoured on the due date, the bank can recover the amount from the customer.

- **Secondary functions**

  In addition to the primary functions of accepting deposits and lending money, banks perform a number of other functions, which are called secondary functions. These are as follows:

- Issuing letters of credit, travellers cheque, etc.
- Undertaking safe custody of valuables, important documents and securities by providing safe deposit vaults or lockers.
- Providing customers with facilities of foreign exchange dealings.
- Transferring money from one account to another; and from one branch to another branch of the bank through cheque, pay order and demand draft.
- Standing guarantee on behalf of its customers, for making payment for purchase of goods, machinery, vehicles etc.
- Collecting and supplying business information.
- Providing reports on the credit worthiness of customers.

NON BANKING FINANCIAL COMPANIES (NBFC)

A Non-Banking Financial Company (NBFC) is a company a) registered under the Companies Act. 1956, b) its principal business is lending, investments in various types of shares/stocks/bonds/debentures/securities, leasing, hire-purchase, insurance business, chit business, and c) its principal business is receiving deposits under any scheme or arrangement in one lump sum or in installments. However, a Non-Banking Financial Company does not include any institution whose principal business is agricultural activity, industrial activity, trading activity or sale/purchase/construction of immovable property. (Section 45 I (c) of the RBI Act, 1934) . One key aspect to be kept in view is that the financial activity of loans/advances as stated in 45 I (c) , should be for activity other than its own. In the absence of this provision, all companies would have been NBFCs.

NBFCs whose asset size is of Rs.100 cr or more as per last audited balance sheet are considered as systemically important NBFCs. The rationale for such classification is that the activities of such NBFCs will have a bearing on the financial stability in our country.

The Reserve Bank of India regulates and supervises Non-Banking Financial Companies which are into the business of (i) lending (ii) acquisition of shares, stocks, bonds, etc., or (iii) financial leasing or hire purchase. The Reserve Bank also regulates companies whose principal business is to accept deposits. (Section 45I (c) of the RBI Act, 1934)

The Reserve Bank has been given the powers under the RBI Act 1934 to register, lay down policy, issue directions, inspect, regulate, supervise and exercise surveillance over NBFCs that meet the 50-50 criteria of principal business. The Reserve Bank can penalize NBFCs for violating the provisions of the RBI Act or the directions or orders issued by RBI under RBI Act. The penal action can also result in RBI cancelling the Certificate of Registration issued to the NBFC, or prohibiting them from accepting deposits and alienating their assets or filing a winding up petition.

SOCIAL BANKING IN INDIA

LEAD BANK SCHEME

To bring about all round development of the rural areas of the country a committee of Mr. Gardgil and Mr. FF Nariman recommended in 1969 that the reponsiblity of fiancial development of different districts of the country may be given to various big banks. Accordingly after consulting the public sector banks operating in the country the Reserve Bank of India assigned different districts to different public sector banks. The bank that was assigned the reponsibility to carry out allround financial development of a district, in co-ordination with the district government authorities became the lead bank for the district. To carry out the development the lead bank cordinates with the district authorities through the District Level Cordination Committee (DLCC) prepares an annual plan and implements the same through the banks operating in the district. It also collects and analyses statistical data of development taking place in the district.

While all the lead banks in the country are public sector banks, the lead bank of one district in Rajasthan viz. Mewar is ICICI Bank.

REGIONAL RURAL BANKS

The M.Narisaman committee in 1975 after studying the impact of the Lead Bank Scheme recommended the establishment of rural banks in each district that may be dedicated to rural development. The first Gramin Banks started functioning on 2nd October 1975 under an ordinance and subsquently the Regional Rural Banks Act was passed in 1976. The management of Regional Rural banks was with a public sector bank generally the lead bank of the district. The Regional Rural Bank operates within a given geographical area. The Capital for these banks was contributed by the Central Government (50%), the Sponsor Bank (35%) and the State Government (15%). Initially around 186 Gramin Bank established all over India but now in keeping with the government directive to merge the gramin banks there were 57 gramin banks as on November 2013.

FINANCIAL INCLUSION

Financial inclusion is delivery of banking services at an affordable cost to the vast sections of disadvantaged and low income groups. Unrestrained access to public goods and services is the 'sine qua non' (an essential condition) of an open and efficient society. As banking services are in the nature of public good, it is essential that availability of banking and payment services to the entire population without discrimination is the prime objective of the public policy.

The former United Nations Secretary General Mr. Kofi Annan on December 29th 2003, while addressing Unesco highlighted that 84% of the world population were not financially included. In 2004 a committe headed by Shri. Haroon Rashid Khan studied the functioning of gramin banks and found that 67% of the Indian population were not financially included. This matter was highlighted in the Reserve Bank of India term policy paper of 2005-2006 and banks were asked to take up financial inclusion for the country. The government of India has initiated a movement called Swabhiman for financial inclusion and had targeted all villages with population of 2000 or above by March 2012 and villages with population of 1000 or above by March 2015.

As result to the campaign, States or Union territories like Punducherry, Himanchal Pradesh and Kerala have announced 100% financial inclusion in all the districts. RBI's vision for 2020 is to open nearly 600 million new customers accounts and service them through a variety of channels by leveraging on IT.

The financial institutions have taken the following steps to bring in financial inclusion-

1. Publicity- Wide pulicity of the utility of financial service are being done to apprise the rural foik are the important of banks.

2.

2. Basic Saving Bank Deposit Accounts-These accounts are opened on relaxed KYC norms and need not have any balance in them. These accounts were formerly called No frill accounts but were renominated as basic saving bank deposit account by the RBI in September 2012. The main features of the account are

i. The 'Basic Savings Bank Deposit Account' should be considered a normal banking service available to all.

ii. This account shall not have the requirement of any minimum balance.
iii. The services available in the account will include deposit and withdrawal of cash at bank branch as welt as ATMs; receipt/credit of money through electronic payment channels or by means of deposit/collection of cheques drawn by Central/State Government agencies and departments;
iv. While there will be no limit on the number of deposits that can be made in a month, account holders will be allowed a maximum of four withdrawals in a month, including ATM withdrawals; and-
v. Facility of ATM card or ATM-cum-Debit Card;

- The above facilities are to be provided without any charges. Further, no charges will be levied for non-operation/activation of in'pperative 'Basic Savings Bank Deposit Account'.
- Banks are free to evolve other requirements including pricing structure for additional value-added services beyond the stipulated basic minimum services on reasonable and transparent basis and applied in a non-discriminatory manner.
- The 'Basic Savings Bank Deposit Account' is subject to RBI instructions on Know Your Customer (KYC) / Anti-Money Laundering (AMI) for opening of bank accounts issued from time to time. If such account is opened on the basis of simplified KYC norms, the account would additionally be treated as a 'Small Account' and would be subject to conditions stipulated for such accounts.
- Holders of 'Basic Savings Bank Deposit Account' will not be eligible for opening any other savings bank deposit account in that bank. If a customer has any other existing savings bank deposit account in that bank, he/ she will be required to close it within 30 days from the date of opening a ' Basic Savings Bank Deposit Account'.
- The existing basic banking 'no-frills' accounts should be converted to 'Basic Savings Bank Deposit Account'.

3. **Kisan Credit Card-** The banks are providing credit cards to the farmers having land on basis of the annual produce of their land. They amount avialable in the credit card (appropriately named Kisan Credit Card) can be drawn by the farmer any time as per his needs and has to be repaid after reaping the crop in the next croping season. Interest as applicable to agriculture loan are charged on loans given from Kisan Credit Cards. These cards are normally valid for five years.

4. **General Purpose Credit Card-**Small consumption loans are given to landless people through general purpose credit card having limits upto Rs. 15,000 and carrying an interest rate of 4%. This loan can be used by the beneficiaries for opening small bussiness.

5. **Bussiness Correspondents-** As banks were unable to open branches immediately in all villages they addopted the Bussiness Correspondent model from Jan 2006. In this model persons living near the respective villages who may be educated are used as bank's commission agents to provide door step banking to the villagers. These persons could be retired employees of banks, post offices, Railways,Armed forces etc. are could even be NGOs or SHGs. They carry with them a hand held computer and through the use of Electronic Smart Card allow withdrawal upto Rs. 10,000 from Saving Bank Accounts or Kisan Credit Cards. They can also open deposit accounts and deposit money in the accounts. The Bussiness Correspondents goes back to his base bank every day updates his computer, submits the relevant accounts.

6. **Electronic Banking-** To facility financial inclusion banks are also adopting Electronic Banking through the use of biometric Atms and mobile banking.

7. **Ultra Small Branches-** In villages serviced by the bussiness correspondent, an officer of the base branch visits the village once in a week and attends to the banking functions that could not be carried out by the bussiness correspondent. He also accepts small loan applications and sanctions them on the spot.

Financial Inclusion Index

On June 25th, 2013 CRISIL, India's leading credit rating and reasearch company launched an index to measure the status of finacial inclusion in India. The Index-Inclusix is one of its kind tool to measure the extent of inclusion in India right down to each of the 632 districts. CRISIL Inclusix is on scale of 0 to 100 and includes parameters of basic banking services-branch penetration, deposit penetration and credit penetration into one metric. The all India CRISIL Inclusix score is 40%.

Micro finance and Micro Credit
Micro credit is giving a small loan to a person. How ever if the person is trained for the project for which he is taking the loan and financial untilization and then given the loan it is called Micro Finance.
Micro Finance = Micro Credit + Financial and Project Literacy

Rural Self Employment Training Institute (RSETI)
These Institutes have been established by the Government of India in almost all districts of the country. These Institutes train the rural youth for agriculture and non-agricultural activities is through residential training of 6 to 10 days. All the expenses of these Institute are brone by the Government of India while it is generally manned by officers of the lead bank. The youth trained by these Institutes are given credit by the banks and this will amount to Micro Finance.

Financial Literacy and Counselling Centre (FLCC)
A working group under Shri. C.P. Swarnkar was constituted on 10th May 2007 to examine the procedures and processes of disbursement of agricultural loans. This group found that rural people were quiet ignorant of the types of agricultural credit facilities available to them. The group recommended the formation of Financial Literacy and Counselling Centre (FLCC) at different rural locations to help the farmers obtain credit facilities easily. These centres are generally manned by retired officers of the banks who are well versed with rural landing.

PRIORITY SECTOR CREDIT

The National Credit Council in July 1968 and the Reserve Bank of India informal study group on statastics relating to advances to priority sector in 1971, recommended that some part of the total credit given by banks should be set a side for priority sector. In terms of the directive of Reserve Bank of India domestic commercial banks, urban cooperative banks and foreign banks with 20 or more branches have to provide 40% of their addjusted net bank credit every year to the priority sector. Out of this 18% have to be set aside to agriculture credit. Foreign banks with less than 20 branches have to provide 32% of their credit to the priority sector.

Description of the Categories under priority sector
1. Agriculture 1.1. Direct Agriculture

Loans to individual farmers [including SHGs or (JLGs),] engaged in Agriculture and Allied Activities. Loans to others [corporates, partnership firms and institutions] for Agriculture and Allied Activities (dairy, fishery, piggery, poultry, bee-keeping, etc.) up to an limit of Rs. 2 crore per borrower (these loans above Rs.2 cr are indirect agriculture loans) for :

(i) Short-term crop loans. This will include traditional/non-traditional plantations, horticulture and allied activities,
(ii) Medium & long-term loans for purchase of agricultural ifnple-ments and machinery, loans for irrigation and other developmental activities at farm and development loans for allied activities),
(iii) Loans for pre-harvest and post-harvest activities viz.spraying, weeding, harvesting, sorting, gracjjng and transporting of their own farm produce.
(iv) Loans to farmers up to Rs. 50 lakh against pledge / hypothecation of agrl produce (including warehouse receipts) for a period up to 12 months. Such loans to others are indirect agriculture loans,
(v) Loans to small/marginal farmers for purchase of land for agr.
(vi) Loans to distressed farmers indebted to non-institutional lenders, against appropriate collateral,
(vii) Export credit for exporting their own farm produce.

1.2. Indirect agriculture

1. Loans to corporates, partnership firms and institutions engaged in Agriculture and Allied Activities more than Rs.2 crore Loans upto Rs.5 crore to Producer Companies set up exclusively by only small and marginal farmers for agricultural/allied activities.
2. Other indirect agriculture loans

(i) Loans up to Rs.5 crore per borrower to dealers / sellers of fertilizers, pesticides, seeds, cattle feed, poultry feed, agricultural implements and other inputs.
(ii) Loans for setting up of Agriclinics and Agribusiness Centres.
(iii) Loans to Custom Service Units to maintain a fleet of tractors, bulldozers, well-boring equipment, threshers, combines, etc., and undertake farm work for farmers on contract basis.
(iv) Loans for construction/running of storage facilities" (warehouse, market yards, godowns and silos), including cold storage units to store agriculture produce/products, irrespective of location.
Loan to MSE storage unit will be classified under loans to MSE.

2. Micro and small enterprises include:

(a) Manufacturing Enterprises (Investment in P&M): Micro max Rs.25 lac. Small Enterprises - Above Rs.25 lac up to Rs. 5 cr.
(b) Service Sector Enterprises: Micro Enterprises - Max Rs. 10 lakh. Small Enterprises - Above 10 lakh up to Rs. 2 crore.
(a) Direct Finance

1. Need based loans to Manufacturing Enterprises and loans up to Rs.5 cr to service enterprises.
2. Food/agro processing if units satisfy investment criteria.
3. Export credit to MSE units for export by them.
4. All loans to Khadi and Village Industries Sector will be classified under sub-target of 60 % for micro enterprises within MSE sector.

(b) Indirect Finance -
(i) Loans to persons assisting decentralised sector in supply of inputs & marketing of outputs of artisans, village cottage industries.
(ii) Loans to producers in the decentralised sector viz. artisans, village and cottage industries.

3. Education: Loans to individuals including vocational courses max Rs.10 lakh for studies in India and Rs. 20 lakh abroad.

4. Micro Credit: Provision of credit and other financial services and products of amounts up to Rs.50,000.

5. Housing

(i) Loans up to Rs. 25 lakh irrespective of location, to individuals for purchase / construction of a dwelling unit per family, excluding loans sanctioned by banks to their own employees,
(ii) Loans for repairs to damaged dwelling units up to Rs. 2 lakh in rural and semi-urban areas and up to Rs. 5 lakh in urban and metropolitan areas.
(iii) Loan to a governmental agency for construction of dwelling units or for slum clearance and rehabilitation of slum dwellers subject to a ceiling of loan component of Rs. 5 lakh per dwelling unit,
(iv) Loan to a non-governmental agency approved by NHB for refinance for construction / reconstruction of dwelling units or for slum clearance and rehabilitation of slum dwellers, subject to a ceiling of loan component of Rs. 10 lakh per dwelling unit.

6. Others

1. Loans up to Rs. 50,000 provided directly by banks to individuals;
2. Loans to distressed persons [other than farmers] max Rs. 50,000 per borrower to prepay their debt to non-institutional lenders.
3. Loans to SHGs / JLGs for agricultural and allied activities. Other loans to SHGs / JLGs up to Rs. 50,000 to be part of Micro Credit.
4. Loans sanctioned to State Sponsored Organisations for SC/ST for purchase and supply of inputs to and / or the marketing of the outputs of the beneficiaries of these organisations.

Weaker Sections: 10% of total credit to this section(a) Small and marginal farmers; (b) Artisans, village and cottage industries where individual credit limits do not exceed Rs. 50,000/-; (c) SC/ST and women; (d) Education loans to persons having monthly income not exceeding Rs.5000 (e) Loans to Self Help Groups; (f) Loans to distressed farmers indebted to non-institutional lenders; (g) Loans to distressed persons other than farmers not exceeding Rs.50,000/- per borrower to prepay their debt to non-institutional lenders; (h) Persons from minority communities as may be notified by Govt. of India.

Common guidelines for priority sector loans
Banks should comply with the following common guidelines for all categories of advances under the priority sector.

1. **Service charges :** IMo loan related and adhoc service charges/ inspection charges should be levied on loans up to Rs. 25,000/-.

2. **Receipt, Sanction/Rejection/Disbursement Register:** A register/ electronic record should be maintained by the bank, wherein the date of receipt, sanction/rejection/disbursement with reasons thereof, etc., should be recorded. The register/electronic record should be made available to all inspecting agencies.

Small and Marginal Farmers: Farmers with landholding of up to 1 hectare are considered as Marginal Farmers. Farmers with a land-holding of more than 1 hectare but less than 2 hectares are considered as Small Farmers. For the purpose of priority sector loans 'small and marginal farmers' include landless agricultural labourers, tenant farmers, oral lessees and share-croppers, whose share of landholding is within above limits prescribed for "Small and Marginal Farmer".

INTEREST SUBVENTION SCHEME

In pursuance of announcement in Budget 2012-13, Govt. of India was to provide interest subvention of 2 % p.a. to Public Sector Banks (PSBs) in case of short-term production credit up to Rs.3 lakh during the year 2012-13. This amount will be calculated on the crop loan amount from the date of disbursement/drawal up to the date of actual repayment or up to the fixed due date, whichever is earlier, subject to a maximum period of one year. The subvention is available on the condition that banks make available at ground level at 7% p.a. rate of interest.
Additional subsidy: Govt. will also provide additional interest subvention of 3% p.a. to PSBs in respect of those prompt paying farmers who repay their short-term production credit within one year of disbursement/drawal of such loans for a maximum amount of Rs.3 lakh availed of by them during the yeaf from the date of disbursement of the crop loan up to the actual date of repayment or up to the fixed due date, whichever is earlier, subject to a max period of one year from the date of disbursement. The additional subvention will be available only if the effective rate of interest is 4 % p.a. This benefit would not accrue if repayment is after one year of availing the loans. The benefits of interest subvention will also be available to small and marginal farmers having Kisan Credit Card for a further period of up to 6 months post harvest, on the same rate as available to crop loan against negotiable warehouse receipt for keeping their produce in warehouses. Claims in respect of 2% interest subvention and 3% additional interest subvention may be submitted respectively to RBI.

KHASRA, KHATUNI, KISAN BHAI

Khasra, Khatuni and Kisan Bhai are documents that establish the ownership and produce of farm land. While Khasra in-corporates the plotwise/seasonwise produce the Khatauni is the discription of plotwise ownership details. The Khasra and Khatuani are now being issued in the form of a consolidated booklet called the Kisan Bhai.

CROP LOAN

The crop loan is provided to meet all expenses involved in raising a particular crop including various agronomic practices.
Eligibility:-

Farmers cultivating owned/Registered leased lands hare croppers.

Quantum of loan:-
As per the scale of finance fixed by the Technical Committee of each district. [Depending on merits of each case, branches may sanction crop Loans 35% more than the scale of finance fixed by district technical committee. In other cases where scale of finance is not specified, the branch - will work out the credit requirements of the farmer.
Where loan limit is fixed based on scale of finance approved by Technical Committee, irrespective of loan amount - Nil
For others: [where scale of finance is not approved]
Up'oRs. 1,00,000/— Nil

Rate of Interest:-Above Rs. 1,00,000/ 10% to 15%
Repayment:- Repayment period will be less than one year for all crops except in the case oi long duration crops such as Sugarcane [Pineapple, Banana etc where if will be 12-18 months.
Security:- Up to Rs, 1,00,000/- DPN. Hypothecation of assets created and crops. Over Rs. 1,00,000.'' DPN, Hypothecation of assets created and crops, mongage of land &/or third party guarantee.
Insurance:- All eligible crops will be covered iiiic'er National Agriculture Insurance Scheme/ Rashtriya Krishi Bima Yojana.

RBI & MONETARY POLICY

The Reserve Bank of India was established on April 1, 1935 in accordance with the provisions of the Reserve Bank of India Act, 1934.
The Central Office of the Reserve Bank was initially established in Calcutta but was permanently moved to Mumbai in 1937. The Central Office is where the Governor sits and where policies are formulated. Though originally privately owned, since nationalisation in 1949, the Reserve Bank is fully owned by the Government of India.

MAIN FUNCTIONS

Monetary Authority

- Formulates, implements and monitors the monetary policy.
- Objective: maintaining price stability and ensuring adequate flow of credit to productive sectors.

REGULATOR AND SUPERVISOR OF THE FINANCIAL SYSTEM

- Prescribes broad parameters of banking operations within which the country's banking and financial system functions.
- Objective: maintain public confidence in the system, protect depositors' interest and provide cost-effective banking services to the public.

MANAGER OF FOREIGN EXCHANGE

- Manages the foreign exchange in accordance with the provision of Foreign Exchange Management Act, 1999.
- Objective: to facilitate external trade and payment and promote orderly development and maintenance of foreign exchange market in India.

ISSUER OF CURRENCY

- Issues and exchanges or destroys currency and coins not fit for circulation.
- Objective: to give the public adequate quantity of supplies of currency notes and coins and in good quality.

Developmental role

- Performs a wide range of promotional functions to support national objectives.

Related Functions

- Banker to the Government: performs merchant banking function for the central and the state governments; also acts as their banker.
- Banker to banks: maintains banking accounts of all scheduled banks.

Monetary policy

Monetary policy refers to the use of instruments under the control of the central bank to regulate the availability, cost and use of money and credit.

The goal: achieving specific economic objectives, such as low and stable inflation and promoting growth.

The main objectives of Monetary Policy in India are:

- Maintaining price stability
- Ensuring adequate flow of credit to the productive sectors of the economy to support economic growth
- Financial stability

DIRECT INSTRUMENTS

- **Cash Reserve Ratio (CRR)**

  The share of net demand and time liabilities that banks must maintain as cash balance with the Reserve Bank.

- **Statutory Liquidity Ratio (SLR)**

  Statutory Liquidity Ratio (SLR) is a term used in the regulation of banking in India. It is the amount which a bank has to maintain in the form of cash, gold or approved securities balance in current account with other commercial bank. The quantum is specified as some percentage of the total demand and time liabilities of a bank. This percentage is fixed by the Reserve Bank of India. Presently the SLR is 23%.

  The 23% is the minimum SLR (the statutory requirements to park their money in government bonds)limit the RBI can fix at present.

  The move comes ahead of the credit review by the Apex Bank, slated for January 31st.

  The objectives of SLR are 1) to restrict the expansion of bank credit 2) to augment the investment of the banks in Government securities and 3) to ensure solvency of banks.

  A reduction of SLR rates looks eminent to support the credit growth in india

  Indian banks' holdings of government securities (G-Sec) are now close to the statutory minimum banks are required to hold to comply with existing regulation. When measured in rupees, such holdings decreased for the first time in a little less than 40 years (since the nationalisation of banks in 1969) in 2005-06.

  While the recent credit boom is a key driver of the decline in banks' portfolios of G-Sec, other factors have played an important role recently. These include (i) interest rate increases; and (ii) changes in the prudential regulation of banks' investments in G-Sec. Most G-Sec held by banks are long-term fixed-rate bonds, which are sensitive to changes in interest rates. Increasing interest rates have eroded banks' income from trading in G-Sec.

- **Refinance Facilities**

  Sector-specific refinance facilities (e.g., against lending to export sector) provided to banks.

INDIRECT INSTRUMENTS

- **Liquidity Adjustment Facility (LAF)**

  Consists of daily infusion or absorption of liquidity on a repurchase basis, through repo (liquidity injection) and reverse repo (liquidity absorption) auction operations, using government securities as collateral.

- **Open Market Operations (OMO)**

  Outright sales/purchases of government securities, in addition to LAF, as a tool to determine the level of liquidity over the medium term.

- **Market Stabilisation Scheme (MSS)**

  This instrument for monetary management was introduced in 2004. Liquidity of a more enduring nature arising from large capital flows is absorbed through sale of short-dated government securities and treasury bills. The mobilised cash is held in a separate government account with the Reserve Bank.

- **Repo/Reverse Repo Rate**

  These rates under the Liquidity Adjustment Facility (LAF) determine the corridor for short-term money market interest rates. In turn, this is expected to trigger movement in other segments of the financial market and the real economy.

- **Term Repo's under Liquidity Adjustment Facility**

  On Oct 08, 2013, RBI decided to conduct auctions for Term Repos of 7-day and 14-day tenor, for a notified amount, through variable rate auction mechanism. The details are as under:

- Term Repo under the Liquidity Adjustment Facility (LAF) for 14 days and 7 days tenors will be introduced for banks (scheduled commercial banks other than RRBs) in addition to the existing daily LAF (repo and reverse repo) and MSF.
- Term repo auctions will be conducted on CBS (E-KUBER) platform through electronic bidding as is done in the case of OMO auctions.
- The total amount of liquidity injected through term repos would be limited to 0.50% of NDTL of the banking system.
- The 14 day term repo would be conducted every reporting Friday and the 7 day term repo would be conducted on every non-reporting Friday.
- In case the notified amount for the 14-day term repo is not fully subscribed, a 7-day term repo would be conducted on the following Friday for the remaining un-subscribed amount. In case of full subscription in 14-day term repo, there will be no 7 day term repo auction on following Friday.
- Banks would be required to place their bids with the term repo rate that they are willing to pay to RBI, for the tenor of the repo expressed in percentage terms up to two decimal places.
- Once the bidding time is over, all the bids would be arranged in descending order of the term repo rates quoted and the cut-off rate would be arrived at the rate corresponding to the notified amount of the auction. Successful bidders would be those, who have placed their bids at or above the cut-off rate.
- No bids would be accepted at or below prevailing Repo Rate under LAF.
- On the day prior to the auction, RBI will announce the amount to be auctioned under term repo along with its tenor. The minimum bid amount for the auction would be Rs.1 cr and multiples thereof.
- The reversal of term repo would take place at the 'start of day' on the day of completion of the term.
- The eligible collateral for term repo will remain the same as daily LAF repo and MSF i.e. for Central Government Securities on 10% discount and State Government Securities 20% discount.
- All other terms and conditions as applicable to LAF operations will also be made applicable to term repo, mutatis mutandis. These conditions will, however, be subject to review on a periodic basis.

BANK RATE

It is the rate at which the Reserve Bank is ready to buy or rediscount bills of exchange or other commercial papers. It also signals the medium-term stance of monetary policy.

National Electronic Funds Transfer (NEFT)

National Electronic Funds Transfer (NEFT) is a nation-wide payment system facilitating one-to-one funds transfer. Under this Scheme, individuals, firms and corporates can electronically transfer funds from any bank branch to any individual, firm or corporate having an account with any other bank branch in the country participating in the Scheme.

For being part of the NEFT funds transfer network, a bank branch has to be NEFT- enabled.

Individuals, firms or corporates maintaining accounts with a bank branch can transfer funds using NEFT. Even such individuals who do not have a bank account (walk-in customers) can also deposit cash at the NEFT-enabled branches with instructions to transfer funds using NEFT. However, such cash remittances will be restricted to a maximum of Rs.50,000/- per transaction. Such customers have to furnish full details including complete address, telephone number, etc. NEFT, thus, facilitates originators or remitters to initiate funds transfer transactions even without having a bank account.

Individuals, firms or corporates maintaining accounts with a bank branch can receive funds through the NEFT system. It is, therefore, necessary for the beneficiary to have an account with the NEFT enabled destination bank branch in the country.

The NEFT system also facilitates one-way cross-border transfer of funds from India to Nepal. This is known as the **Indo-Nepal Remittance Facility Scheme**. A remitter can transfer funds from any of the NEFT-enabled branches to Nepal, irrespective of whether the beneficiary in Nepal maintains an account with a bank branch in Nepal or not.

There is no limit - either minimum or maximum - on the amount of funds that could be transferred using NEFT. However, maximum amount per transaction is limited to Rs.50,000/- for cash-based remittances and remittances to Nepal.

There is no restriction of centres or of any geographical area within the country. The NEFT system takes advantage of the core banking system in banks. Accordingly, the settlement of funds between originating and receiving banks takes places centrally at Mumbai, whereas the branches participating in NEFT can be located anywhere across the length and breadth of the country.

Presently, NEFT operates in hourly batches - there are twelve settlements from 8 am to 7 pm on week days (Monday through Friday) and six settlements from 8 am to 1 pm on Saturdays.

REAL TIME GROSS SETTLEMENT (RTGS) SYSTEM

The acronym 'RTGS' stands for Real Time Gross Settlement, which can be defined as the continuous (real-time) settlement of funds transfers individually on an order by order basis (without netting). **'Real Time'** means the processing of instructions at the time they are received rather than at some later time.**'Gross Settlement'** means the settlement of funds transfer instructions occurs individually (on an instruction by instruction basis). Considering that the funds settlement takes place in the books of the Reserve Bank of India, the payments are final and irrevocable. RBI has operationalized a new ISO 20022 complaint RTGS system october 19-2-2013.

The RTGS system is primarily meant for large value transactions. The minimum amount to be remitted through RTGS is Rs.2 lakh. There is no upper ceiling for RTGS transactions.

Under normal circumstances the beneficiary branches are expected to receive the funds in real time as soon as funds are transferred by the remitting bank. The beneficiary bank has to credit the beneficiary's account within two hours of receiving the funds transfer message.

The remitting bank receives a message from the Reserve Bank that money has been credited to the receiving bank. Based on this the remitting bank can advise the remitting customer that money has been delivered to the receiving bank.

It is expected that the receiving bank will credit the account of the beneficiary instantly. If the money cannot be credited for any reason, the receiving bank would have to return the money to the remitting bank within 2 hours. Once the money is received back by the remitting bank, the original debit entry in the customer's account is reversed.

The RTGS service window for customer's transactions is available from 9.00 hours to 16.30 hours on week days and from 9.00 hours to 13.30 hours on Saturdays for settlement at the RBI end. However, the timings that the banks follow may vary depending on the customer timings of the bank branches.

With a view to rationalize the service charges levied by banks for offering funds transfer through RTGS system, a broad framework has been mandated as under:

- **Inward Transactions**

  Free, no charge to be levied.
- **Outward Transactions**

  Rs. 2 lakh to Rs. 5 lakh - not exceeding Rs. 30 per transaction

  Above Rs. 5 lakh - not exceeding Rs. 55 per transaction

DeMat Account

A DeMat account is one that allows you to buy, sell as well as transact without the need of any paperwork. DeMat accounts are very safe, convenient and secure.

What is a DeMat Account?

DeMat is nothing but a dematerialized account. If one has to save money or make cheque payments, then he/she needs to open a bank account. Similarly, one needs to open a DeMat account if he/she wants to buy or sell stocks. Thus, DeMat account is similar to a bank account wherein the actual money is being replaced by shares. In order to open a DeMat account, one needs to approach the Depository Participants [DPs].

In India, a DeMat account is a type of banking account that dematerializes paper-based physical stock shares. The DeMat account is used to avoid holding of physical shares: the shares are bought as well as sold through a stock broker. In this case, the advantage is that one does not need any physical evidence for possessing these shares. All the things are taken care of by the DPs.

This account is very popular in India. Physically only 500 shares can be traded as per the provision given by SEBI. From April 2006, it has become mandatory for any person holding a DeMat account to possess a Permanent Account Number (PAN).

MARGINAL STANDING FACILITY - SCHEME

As announced in the Monetary Policy for the year 2011-12, a new Marginal Standing Facility (MSF) is being introduced with effect from May 9, 2011.

The Scheme will be operationalized on the lines of the existing Liquidity Adjustment Facility - Repo Scheme (LAF - Repo). The salient features of the Scheme are as under:

- This facility is effective from May 9, 2011.
- Eligibility

  All Scheduled Commercial Banks having Current Account and SGL Account with Reserve Bank, Mumbai will be eligible to participate in the MSF Scheme.

- **Tenor and Amount**

  Under the facility, the eligible entities can avail overnight, up to one per cent of their respective Net Demand and Time Liabilities (NDTL) outstanding at the end of the second preceding fortnight. But for the intervening holidays, the MSF facility will be for one day except on Fridays when the facility will be for three days or more, maturing on the following working day. In the event, the banks' SLR holdings fall below the statutory requirement up to one per cent of their NDTL, banks will not have the obligation to seek a specific waiver for default in SLR compliance arising out of use of this facility in terms of notification issued under sub section (2A) of Section 24 of the Banking Regulation Act, 1949.
- **Timing**

The Facility will be available on all working days in Mumbai, excluding Saturdays between 3.30 P.M. and 4.30 P.M.

- **Rate of Interest**

The rate of interest on amount availed under this facility will be 100 basis points above the LAF repo rate, or as decided by the Reserve Bank from time to time.

- **Discretion to Reserve Bank**

The Reserve Bank will reserve the right to accept or reject partially or fully, the request for funds under this facility.

- **Mechanics of Operations**

- The requests will be submitted electronically in the Negotiated Dealing System (NDS). Eligible members facing genuine system problem on any specific day, may submit physical requests in sealed cover in the box provided in the Mumbai Office, Reserve Bank of India, to the Manager, Reserve Bank of India, Securities Section, Public Accounts Department (PAD), Mumbai Office by 4.30 P.M.
- The NDS provides for submission of single or multiple applications by the member. However, as far as possible only one request should be submitted by an applicant.
- The MSF will be conducted as "Hold-in-Custody" repo, similar to LAF - Repo.
- On acceptance of MSF requests, the applicant's RC SGL Account will be debited by the required quantum of securities and credited to Bank's RC SGL Account. Accordingly, the applicant's current account will be credited with the MSF application amount. The transactions will be reversed in the second leg. In case the second leg falls on a holiday, the reversal date will be the next working day.
- The MSF transactions between Reserve Bank and counter parties which would involve operation of the RC SGL Account would not require separate SGL forms.
- Pricing of all securities including Treasury Bills will be at face value for MSF operations by Reserve Bank. Accrued interest as on the date of transaction will be ignored for the purpose of pricing of securities.

- **Minimum Request Size**

Requests will be received for a minimum amount of Rs. One crore and in multiples of Rs. One crore thereafter.

- **Eligible Securities**

MSF will be undertaken in all SLR-eligible transferable Government of India (GoI) dated Securities/Treasury Bills and State Development Loans (SDL).

- **Margin Requirement**

A margin of five per cent will be applied in respect of GoI dated securities and Treasury Bills. In respect of SDLs, a margin of 10 per cent will be applied. Thus, the amount of securities offered on acceptance of a request for Rs.100 will be Rs.105 (face value) of GoI dated securities and Treasury Bills or Rs.110 (face value) of SDLs.

- **Settlement of Transactions**

The settlement of all applications received under the MSF Scheme will take place on the same day after the closure of the window for acceptance of applications.

- **SLR and Securities held in Repo SGL Account**

  The extant instructions issued by the Department of Banking Operations and Development (DBOD) of the Reserve Bank will apply on the securities offered by scheduled commercial banks for MSF operations.

BASEL COMMITTEE

The Basel Committee on Banking Supervision provides a forum for regular cooperation on banking supervisory matters. Its objective is to enhance understanding of key supervisory issues and improve the quality of banking supervision worldwide. It seeks to do so by exchanging information on national supervisory issues, approaches and techniques, with a view to promoting common understanding. The Committee's Secretariat is located at the Bank for International Settlements (BIS) in Basel, Switzerland.

NEED FOR SUCH NORMS

The first accord by the name .Basel Accord I. was established in 1988 and was implemented by 1992. It was the very first attempt to introduce the concept of minimum standards of capital adequacy. Then the second accord by the name Basel Accord II was established in 1999 with a final directive in 2003 for implementation by 2006 as Basel II Norms. Unfortunately, India could not fully implement this but, is now gearing up under the guidance from the Reserve Bank of India to implement it from 1 April, 2009.

Basel II Norms have been introduced to overcome the drawbacks of Basel I Accord. For Indian Banks, its the need of the hour to buckle-up and practice banking business at par with global standards and make the banking system in India more reliable, transparent and safe. These Norms are necessary since India is and will witness increased capital flows from foreign countries and there is increasing cross-border economic & financial transactions.

FEATURES OF BASEL II NORMS

Basel II Norms are considered as the reformed & refined form of Basel I Accord. The Basel II Norms primarily stress on 3 factors, viz. Capital Adequacy, Supervisory Review and Market discipline. The Basel Committee calls these factors as the Three Pillars to manage risks.

Pillar I: Capital Adequacy Requirements

Under the Basel II Norms, banks should maintain a minimum capital adequacy requirement of 8% of risk assets. For India, the Reserve Bank of India has mandated maintaining of 9% minimum capital adequacy requirement. This requirement is popularly called as Capital Adequacy Ratio (CAR) or Capital to Risk Weighted Assets Ratio (CRAR).

Pillar II: Supervisory Review

Banks majorly encounter with 3 Risks, viz. Credit, Operational & Market Risks. Basel II Norms under this Pillar wants to ensure that not only banks have adequate capital to support all the risks, but also to encourage them to develop and use better risk management techniques in monitoring and managing their risks. The process has four key principles:

- Banks should have a process for assessing their overall capital adequacy in relation to their risk profile and a strategy for monitoring their capital levels.
- Supervisors should review and evaluate bank's internal capital adequacy assessment and strategies, as well as their ability to monitor and ensure their compliance with regulatory capital ratios.
- Supervisors should expect banks to operate above the minimum regulatory capital ratios and should have the ability to require banks to hold capital in excess of the minimum.

- Supervisors should seek to intervene at an early stage to prevent capital from falling below minimum level and should require rapid remedial action if capital is not mentioned or restored.

Pillar III: Market Discipline:

Market discipline imposes banks to conduct their banking business in a safe, sound and effective manner. Mandatory disclosure requirements on capital, risk exposure (semiannually or more frequently, if appropriate) are required to be made so that market participants can assess a bank's capital adequacy. Qualitative disclosures such as risk management objectives and policies, definitions etc. may be also published.

BASEL III

The Reserve Bank released, guidelines outlining proposed implementation of Basel III capital regulation in India. These guidelines are in response to the comprehensive reform package entitled "Basel III: A global regulatory framework for more resilient banks and banking systems" of the Basel Committee on Banking Supervision (BCBS) issued in December 2010.

The major highlights of the draft guidelines are:

Minimum Capital Requirements

- Common Equity Tier 1 (CET1) capital must be at least 5.5% of risk-weighted assets (RWAs);
- Tier 1 capital must be at least 7% of RWAs; and
- Total capital must be at least 9% of RWAs.

Capital Conservation Buffer

- The capital conservation buffer in the form of Common Equity of 2.5% of RWAs. A such minimum Capital Adequacy ratio for banks will be 11.5% after full application of the capital conservation buffer by 31 March 2018.

Transitional Arrangements

- It is proposed that the implementation period of minimum capital requirements and deductions from Common Equity will begin from January 1, 2013 and be fully implemented as on March 31, 2018.
- Capital conservation buffer requirement is proposed to be implemented between March 31, 2014 and March 31, 2018.
- The implementation schedule indicated above will be finalized taking into account the feedback received on these guidelines.
- Instruments which no longer qualify as regulatory capital instruments will be phased-out during the period beginning from January 1, 2013 to March 31, 2022.

Enhancing Risk Coverage

- For OTC derivatives, in addition to the capital charge for counterparty default risk under Current Exposure Method, banks will be required to compute an additional credit value adjustments (CVA) risk capital charge.

Leverage Ratio

- The parallel run for the leverage ratio will be from January 1, 2013 to January 1, 2018, during which banks would be expected to strive to operate at a minimum Tier 1 leverage ratio of 5%. The leverage ratio requirement will be finalized taking into account the final proposal of the Basel Committee.

KNOW YOUR CUSTOMER

The Reserve Bank of India (RBI) has advised banks to follow 'KYC guidelines', wherein certain personal information of the account-opening prospect or the customer is obtained. The objective of doing so is to enable the Bank to have positive identification of its customers. This is also in the interest of customers to safeguard their hard earned money.

The KYC guidelines of RBI mandate banks to collect three proofs from their customers. They are-

- Photograph
- Proof of identity
- Proof of address

What is KYC?

Know Your Customer - KYC enables banks to know/ understand their customers and their financial dealings to be able to serve them better

Who is a customer of the Bank?

For the purpose of KYC Policy, a Customer is defined as:

- A person or entity that maintains an account and/or has a business relationship with the Bank;
- One on whose behalf the account is maintained (i.e. the beneficial owner);
- Beneficiaries of transactions conducted by professional intermediaries, such as Stock Brokers, Chartered Accountants, Solicitors, etc. as permitted under the law, and
- Any person or entity connected with a financial transaction, which can pose significant reputation or other risks to the Bank, say, a wire transfer or issue of a high value demand draft as a single transaction

CAMEL RATING OF BANKS

CAMEL model of rating was first developed in the 1970s by the 3 federal banking supervisors of the U.S (the Federal Reserve, the FDIC and the OCC) as part of the Regulators' "Uniform Financial Institutions Rating System", to provide a convenient summary of bank condition at the tirfie of its on-site examination.

The banks were judged on 5 different components under the acronym C-A-M-E-L: Capital adequacy, Asset quality, Management, Earnings and Liquidity. The banks received a score of '1' through '5' for each component of CAMEL and a final CAMEL rating representing the composite total of the component CAMEL scores as a measure of the bank's overall condition. The system of CAMEL was revised in 1996, when agencies added an additional parameter 'S' for assessing "sensitivity to market risk", thus making it 'CAMELS' that is in vogue today.

In india the Padhmanabhan Committee (1996) recommended the application of CAMEL RATING for compliance of norms by Indian Banks. Thus CAMELS means

C- Capital Adequacy
A- Asset Quality
M- Management Quality
E- Earnings
L- Liquidity
S- Sensivity to Market Risk

RBI plans to change system in order to make the process more forward-looking. Indian financial sector would be evaluated under a dynamic risk-based mechanism, an aspect the present CAMELS rating system lacked. RBI proposes to replace CAMELS with INROADS (Indian Risk-Oriented and Dynamic Rating System) from the next round of annual financial inspection.

MONEY

Money is a thing that is usually accepted as payment for goods and services as well as for the repayment of debts.

Types of Money

- **Commodity Money -**

  Commodity money value is derived from the commodity out of which it is made. The commodity itself represents money and the money is the commodity. For instance, commodities that have been used as mediums of exchange include gold, silver, copper, salt, peppercorns, rice, large stones, etc.
- **Representative Money -**

  Representative Money includes token coins, or any other physical tokens like certificates, that can be reliably exchanged for a fixed amount/quantity of a commodity like gold or silver.
- **Fiat Money -**

  Fiat money, also known as fiat currency is the money whose value is not derived from any intrinsic value or any guarantee that it can be converted into valuable commodity (like gold). Instead, it derives value only based on government order (fiat).
- **Commercial Bank Money -**

  Commercial bank money or the demand deposits are claims against financial institutions which can be used for purchasing goods and services.

Narrow and Broad Money

Money supply, like money demand, is a stock variable. The total stock of money in circulation among the public at a particular point of time is called money supply. RBI publishes figures for four alternative measures of money supply, viz. M1, M2, M3 and M4.

They are defined as follows -

M1 = CU + DD

M2 = M1 + Savings deposits with Post Office savings banks

M3 = M1 + Net time deposits of commercial banks

M4 = M3 + Total deposits with Post Office savings organisations (excluding National Savings Certificates)

where, CU is currency (notes plus coins) held by the public and DD is net demand deposits held by commercial banks. The word 'net' implies that only deposits of the public held by the banks are to be included in money supply.

The interbank deposits, which a commercial bank holds in other commercial banks, are not to be regarded as part of money supply.

M1 and M2 are known as narrow money. **M3 and M4 are known as broad money**.These gradations are in decreasing order of liquidity. M1 is most liquid and easiest for transactions whereas M4 is least liquid of all. M3 is the most commonly used measure of money supply. It is also known as aggregate monetary resources.

ANTI MONEY LAUNDERING

Prevention of Money Laundering Act, 2002

Prevention of Money Laundering Act in Indian Law was passed in 2002, to prevent money-laundering and to provide for confiscation of property derived from money-laundering. The main objective of this act are to prevent money-laundering as well as to provide for confiscation of property either derived from or involved in, money-laundering.

Salient Features

Punishment for Money-laundering : The act prescribes that any person found guilty of money-laundering shall be punishable with rigorous imprisonment from three years to seven years. He could also be liable to fine of upto Rs. 5 lakh.

Powers of Attachment of Tainted : Property Appropriate authorities, appointed by the Government of India, can provisionally attach property believed to be 'proceeds of crime' for 90 days. Such an order is required to be confirmed by an independent adjudicating authority.

Adjudicating Authority : It is the authority appointed by the Central Government. It decides whether any of the property attached or seized is involved in money-laundering.

Appellate Tribunal : It is the body appointed by Government of India. It has given the power to hear appeals against the orders of the adjudicating authority and any other authority under the act. Orders of the tribunal can be appealed in appropriate High Court (for that jurisdiction) and finally to the Supreme Court.

Special Courts : The trial for the offences mentioned in the act are conducted by a special court, also called 'PMLA Court'. The Central Government (in consultation with the Chief Justice of the High Court), designates a Session Court as Special Court Any appeal against order passed by PMLA court can directly be filed in the High Court (for that jurisdiction).

Burden of Proof : A person, who is accused of having committed the offence of money-laundering, has to prove that alleged proceeds of crime are in fact lawful property.

Money laundering occurs in three stages

- Placement: refers to the initial point of entry for funds derived from any criminal activities.
- Layering: refers to the creation of a complex network of transactions which attempts to obscure the link between the initial entry point and the end of the laundry cycle
- Integration: refers to the return of funds to the legitimate economy for later extraction.

SWIFT

The Society for Worldwide Interbank Financial Telecommunication ("SWIFT") operates a worldwide financial messaging network which exchanges messages between banks and other financial institutions. SWIFT also markets software and services to financial institutions, much of it for use on the SWIFT Net Network, and ISO 9362 bank identifier codes (BICs) are popularly known as "SWIFT codes".

The majority of international interbank messages use the SWIFT network. As of September 2010, SWIFT linked more than 9,000 financial institutions in 209 countries and territories, who were exchanging an average of over 15 million messages per day. SWIFT transports financial messages in a highly secure way, but does not hold accounts for its members and does not perform any form of clearing or settlement.

SWIFT does not facilitate funds transfer, rather, it sends payment orders, which must be settled via correspondent accounts that the institutions have with each other. Each financial institution, to exchange banking transactions, must have a banking relationship by either being a bank or affiliating itself with one (or more) so as to enjoy those particular business features.

INFLATION

DEFINITION

Inflation is defined as a sustained increase in the general level of prices for goods and services. It is measured as an annual percentage increase. As inflation rises, every rupee you own buys a smaller percentage of a good or service.

The value of a rupee does not stay constant when there is inflation. The value of a rupee is observed in terms of purchasing power, which is the real, tangible goods that money can buy. When inflation goes up, there is a decline in the purchasing power of money. For example, if the inflation rate is 2% annually, then theoretically a Re 1 pack of gum will cost Rs 1.02 in a year. After inflation, your money can't buy the same amount of goods it could beforehand.

DiFference between WPI and CPI

WPI and CPIs differ in terms of their weighting pattern. First, food has a larger weight in CPI ranging from 46 per cent in CPI-IW to 69 per cent in CPI-AL whereas it has a weight of only 27 per cent in WPI. The CPIs are, therefore, more sensitive to changes in prices of food items. Second, the fuel group has a much higher weight in the WPI (14.2 percent) than the CPIs (5.5 to 8.4 per cent). As a result, movement in international crude prices has a greater bearing on WPI than on the CPIs. Third, services are not covered under WPI while they are, to different degrees, covered under CPIs. Consequently, service price inflation has a greater influence on CPIs. In general, revision of base in every 5 years is an accepted principle in major developed and emerging countries.

NEW WPI SERIES

Following the recommendation of the Working Group for Revision of Wholesale Price Index under the Chairmanship of Prof. Abhijit Sen, the base year has been revised to 2004-05 from September 2010. The proposed basket of manufactured products in the new series covers significantly a higher number of commodities and integrates items from both organised and un-organised manufacturing sectors. The revised WPI basket, however, does not include services prices. An Expert Group (Chairman: Prof. C. P. Chandrasekhar) is looking into process of developing a service price index. In order to enhance the representativeness of WPI index, it is important to expand the coverage to include services. The new WPI series aimes at capturing the price movement in a more realistic way in keeping with the times. The basic difference between the two series is that the new WPI index with 2004-05 as the base year has a total of 676 items instead of 435 items under the old series which had 1993-94 as the base year. Among the 241 items added to the basket for better reflection of the inflationary spiral are consumer items - essentially used by the middle-class - such as ice-cream, mineral water, readymade food, refrigerators, VCDs, dish antennas, microwave ovens, washing machines, computers and computer stationery and gold as well as silver.

Under the primary article group, there are 102 items in the new series against 98 in the old index although the number of items in the fuel and power category remains unchanged at 19. A substantial increase is in the number of manufactured products that have been included in the index - 555 items as compared to 318 items in the basket under the old series.

PRODUCER PRICE INDEX

India revised the WPI, but still don't have a Producer Price Index (PPI). The PPI covers price changes faced by the producers on primary, intermediate and finished goods and services ready for the market. The primary difference between the WPI and the PPI is, in addition to the coverage, that the WPI reflects changes in the average cost of production including mark-ups and taxes, while the PPI measures price changes of transacted goods at the gate excluding taxes. The purpose of the PPI is to provide a measure of prices received by producers of commodities. The PPI usually covers the industrial (manufacturing) sector as well as public utilities (electricity, gas and communications).

NEW CONSUMER PRICE INDEX

At the retail level, CPI is meant to reflect the cost of living conditions and is computed on the basis of the changes in the level of retail prices of selected goods and services on which consumers spend the major part of their income. Therefore, a broad based CPI for the country as a whole, including both services and manufacturing products, has greater relevance for monetary policy formulation.In India, however, data on CPI relates to different segments of the population rather than the entire population. With a view to addressing this issue, the Reserve Bank had taken the initiative and prepared an approach paper on CPI (Urban) and CPI (Rural).

Subsequently, the Central Statistical Organisation (CSO) has taken up the work for generating data on CPI (Urban) and CPI (Rural). The new CPIs once complied will go a long way in filling a major data gap in price statistics.

MONEY MARKET IN INDIA

The money market is the market in which short term funds are borrowed and lent. The lending money market institutions are -

- Government of India and other sovereign bodies
- Banks and Development Financial Institutions
- PSUs [Public Sector Undertakings]
- Private sector organizations
- The Government /Quasi government owned non-corporate entities.

Large numbers of instruments that are traded in the money market are issued by Government of India, State governments and other statutory bodies. Instruments that are issued by the Development Financial Institutions [DFI] and banks carry the highest credit ratings amongst non-government issuers mainly due to their connection with the Indian Government.

INSTRUMENTS OF MONEY MARKET

- **Call Money -** Call or notice money is an amount borrowed or lent on demand for a very short period. If the period is greater than one day and up to 14 days it is called Notice money; otherwise the amount is known as Call money. No collateral security is needed to cover these transactions.

  The call market enables the banks and institutions to even out their day-to-day deficits and surpluses of money. Co-operative banks, commercial banks and primary dealers are allowed to borrow and lend in this market for adjusting their cash reserve requirements.

  This is a completely inter-bank market. Interest rates are market determined. In view of the short tenure of these transactions, both borrowers and lenders are required to have current accounts with Reserve Bank of India.
- **Treasury Bills -** These are the lowest risk category instruments for the short term. RBI issues treasury bills [T-bills] at a prefixed day and for a fixed amount. There are 3 types of treasury bills.

  -91-day T-bill: maturity is in 91 days, it is auctioned on every Friday of every week and the notified amount for auction is Rs. 100 crores.

  -182-day T-bill: maturity is in 182 days, it is auctioned on every alternate Wednesday, which is not a reporting week and the notified amount for auction is Rs. 100 crores.

  -364-day T-bill: maturity is 64 days, it is auctioned on every alternate Wednesday which is a reporting week and the notified amount for the auction is Rs. 500 crores.
- **Certificates of Deposits -** After treasury bills, the next lowest risk category investment option is Certificate of Deposit (CD) issued by banks and Financial Institutions (FI). Allowed in 1989, CDs were one of RBI's measures to deregulate the cost of funds for banks and FIs. A CD is a negotiable promissory note, secure and short term, of up to a year, in nature.

  A CD is issued at a discount to the face value, the discount rate being negotiated between the issuer and the investor. Although RBI allows CDs up to one-year maturity, the maturity most quoted in the market is for 90 days.
- **Commercial Papers -** Commercial papers [CPs] are negotiable short-term unsecured promissory notes with fixed maturities, issued by well-rated organizations. These are generally sold on discount basis. Organizations can issue CPs either directly or through banks or merchant banks [called as dealers]. These instruments are normally issued in the multiples of five crores for 30/45/60/90/120/180/270/364 days.
- **Inter-Corporate Deposits -** An Inter-Corporate Deposit or ICD is an unsecured loan extended by one corporate to another. Existing mainly as a refuge for low rated corporate, this market allows funds surplus corporate to lend to other corporate.

  A better rated corporate can borrow from the banking system and lend in this market. As the cost of funds for a corporate is much higher than a bank, the rates in this market are higher than those in other markets. ICDs are unsecured, and therefore the risk inherent is high. The ICD market is not well organized with very little information available about transaction details.
- **Ready Forward Contracts -** These are transactions in which two parties agree to sell and repurchase the same security. Under such an agreement the seller sells specified securities with an agreement to repurchase the same at a mutually decided future date and price. Similarly, the buyer purchases the securities with an agreement to resell the same to the seller on an agreed date in future at a predetermined price.

  Such a transaction is called **Repo when viewed from the prospective of the buyer of securities that is the party acquiring fund**. It is called **reverse repo when viewed from the prospective of supplier of funds**.
- **Commercial Bills -** Bills of exchange are negotiable instruments drawn by the seller or drawer of the goods on the buyer or drawee of the good for the value of the goods delivered. These bills are called **trade bills**. **These trade bills are called commercial bills when they are accepted by commercial banks**. If the bill is payable at a future date and the seller needs money during the currency of the bill then the seller may approach the bank for discounting the bill.
- **Pass through Certificates -** This is an instrument with cash flows derived from the cash flow of another underlying instrument or loan. The issuer is a Special Purpose Vehicle (SPV), which only

receives money, from a multitude of, may be several hundreds or thousands, underlying loans and passes the money to the holders of the PTCs. This process is called **securitization**.

Legally speaking PTCs are promissory notes and hence tradable freely with no stamp duty payable on transfer. Most PTCs have 2-3 year maturity because the issuance stamp duty rate makes shorter duration PTCs unviable.

- **Dated Government Securities -** These are securities issued by the Government of India and State Governments. The date of maturity is specified in the securities therefore they are known as **dated securities**. The Government borrows funds through the issue of long term dated securities, the lowest risk category instruments in the economy. They are issued through auctions conducted by RBI, where RBI decides the coupon or discount rate based on the response received. Most of these securities are issued as fixed interest bearing securities, although the government sometimes issues zero coupon instruments and floating rate securities.

MONEY MARKET CONCEPTS

- **Issued Capital:** that part of a company's capital that has been subscribed to by shareholders. It is a broader concept than paid up capital.
- **Paid Up capital:** It is that part of the issued capital of a company, paid up by the shareholders (promoters). It is that part, invested by the promoters. Therefore, an issued capital may or may not be a paid up capital.
- **Authorized Capital:** It is the amount of share capital fixed in the Memorandum of an Association and the Articles of the Association of a company as required by the Company's act. They are also known as **nominal capital**.
- **Repo Operations:** In order to absorb and to neutralize excess liquidity from the system and even to out call money rates a system of announcing calendar of Repos auctions on a monthly basis was introduced with effect from January 13,1997.
- **Fixed Rate Repos:** The fixed rate repo was introduced with effect from November 29,1997. The repo rate and the period of repo is announced by the RBI in the evening of the previous day.
- **Net Asset Value (NAV) :** The investment efficiency of the mutual fund can be measured in terms of the NAV values and Net Sales. NAV is the indicator of the investment performance and it indicates the amount each unit holder will get per unit on redemption or winding up of mutual fund. Net Sales given by the difference between the total sales and total repurchases of the units of a fund.
- **Floating Rate Note :** It adopts a reference rate of interest which reflects the market rate of interest. The interest rate of FRN then in certain percentage points over the reference rate or benchmark rate.
- **Stock-Invest:** Under this scheme a provision of special payment system for investors in the primary market. Stockinvest is a non-negotiable bank instrument and its validity is for four months from the date of the issue.
- **Zero -Cupon Bonds:** It is issued at a discount to face value. No interest is paid during the period of the bond. But at the time of maturity full payment or bullet payment of the face value would be done.
- **Deep-Discount Bonds:** It was first introduced by IDBI in June 1994 followed by ICICI. It is similar to zero-coupon bonds with longer maturity.
- **Jumboo Lot:** It is issued in primary and secondary market to reduce the paper work connected with the processing. The certificates are issued in bulk.
- **Book Building:** This is the first draft or preliminary prospectus, which carries the information of the company and the project.
- **Dabba Trading:** The illegal badla trading, banned since 1993, has resurfaced in the form of Dabba Trading, a modified form of CFTS. It is based on bucketing system. It is an illegal practice where a stockbroker executes a customer's trade without taking it to a stock exchange with the hope of earning profit in future. The Dabba trader keeps record in a separate book. The trades to be settled on Friday.

  SEBI has conducted raids on large scale on dabba trading and investigations are on. These trading have intensified the speculative nature of the market. Therefore, despite the fact that market has a cash market with T + 1 rolling settlement and derivatives market with four types of options and futures products, a huge amount of illegal mode is also adopted in the transactions of stock market.

NEGOTIABLE INSTRUMENTS

Definition of Negotiable Instrument

According to section 13 of the Negotiable Instruments Act, 1881, a negotiable instrument means "promissory note, bill of exchange, or cheque, payable either to order or to bearer".

Types of Negotiable Instruments

According to the Negotiable Instruments Act, 1881 there are just three types of negotiable instruments i.e., promissory note, bill of exchange and cheque. However many other documents are also recognized as negotiable instruments on the basis of custom and usage, like hundis, treasury bills, share warrants, etc., provided they possess the features of negotiability. In the following sections, we shall study about Promissory Notes (popularly called pronotes), Bills of Exchange (popularly called bills), Cheques and Hundis (a popular indigenous document prevalent in India), in detail.

Promissory Note

Suppose you take a loan of Rupees Five Thousand from your friend Ramesh. You can make a document stating that you will pay the money to Ramesh or the bearer on demand. Or you can mention in the document that you would like to pay the amount after three months. This document, once signed by you, duly stamped and handed over to Ramesh, becomes a negotiable instrument. Now Ramesh can personally present it before you for payment or give this document to some other person to collect money on his behalf. He can endorse it in somebody else's name who in turn can endorse it further till the final payment is made by you to whosoever presents it before you. This type of a document is called a Promissory Note.

Bill of Exchange

Suppose Rajiv has given a loan of Rupees Ten Thousand to Sameer, which Sameer has to return. Now, Rajiv also has to give some money to Tarun. In this case, Rajiv can make a document directing Sameer to make payment up to Rupees Ten Thousand to Tarun on demand or after expiry of a specified period. This document is called a Bill of Exchange, which can be transferred to some other person's name by Tarun.

Section 5 of the Negotiable Instruments Act, 1881 defines a bill of exchange as 'an instrument in writing containing an unconditional order, signed by the maker, directing a certain person to pay a certain sum of money only to or to the order of a certain person, or to the bearer of the instrument'.

Cheques

Cheque is a very common form of negotiable instrument. If you have a savings bank account or current account in a bank, you can issue a cheque in your own name or in favour of others, thereby directing the bank to pay the specified amount to the person named in the cheque.

Therefore, a cheque may be regarded as a bill of exchange; the only difference is that the bank is always the drawee in case of a cheque.

The Negotiable Instruments Act, 1881 defines a cheque as a bill of exchange drawn on a specified banker and not expressed to be payable otherwise than on demand. Actually, a cheque is an order by the account holder of the bank directing his banker to pay on demand, the specified amount, to or to the order of the person named therein or to the bearer.

Types of Cheque

- **Open cheque:** A cheque is called 'Open' when it is possible to get cash over the counter at the bank. The holder of an open cheque can do the following:
- Receive its payment over the counter at the bank,
- Deposit the cheque in his own account
- Pass it to some one else by signing on the back of a cheque.
- **Crossed cheque:** Since open cheque is subject to risk of theft, it is dangerous to issue such cheques. This risk can be avoided by issuing another types of cheque called 'Crossed cheque'. The payment of such cheque is not made over the counter at the bank. It is only credited to the bank

account of the payee. A cheque can be crossed by drawing two transverse parallel lines across the cheque, with or without the writing 'Account payee' or 'Not Negotiable'.

- **Bearer cheque:** A cheque which is payable to any person who presents it for payment at the bank counter is called 'Bearer cheque'. A bearer cheque can be transferred by mere delivery and requires no endorsement.
- **Order cheque:** An order cheque is one which is payable to a particular person. In such a cheque the word 'bearer' may be cut out or cancelled and the word 'order' may be written. The payee can transfer an order cheque to someone else by signing his or her name on the back of it.

Hundis

A Hundi is a negotiable instrument by usage. It is often in the form of a bill of exchange drawn in any local language in accordance with the custom of the place. Some times it can also be in the form of a promissory note. **A hundi is the oldest known instrument used for the purpose of transfer of money without its actual physical movement**. The provisions of the Negotiable Instruments Act shall apply to hundis only when there is no customary rule known to the people.

INDIA'S FOREIGN TRADE

Each country has to keep economic transaction with other countries of the world and India also has a healthy trade relationship with several countries. Foreign trade brings into play the commercial transaction of payment and receipt for goods and services sent (export) or received (import). The difference between these two creates the concept of Balance of Payment and Balance of Trade.

According to Benham,"Balance of Payments of a country is a record of the monetary transactions over a period with rest of the world."

Ordinarily, a country has to deal with other countries in respect of three items, namely;

(i) Visible items, which include all types of physical goods exported and imported.

(ii) Invisible items, which include all those services, whose export and import are not visible.

(iii) Capital transfer, which are concerned with capital receipts and capital payments.

Each country has to workout a balance in respect of its dealings, in all the above three items with other countries of the world in a given period. Such a balance may assume any one of the three positions

(i) balanced (ii) negative (unfavourable) (iii) positive (favourable)

Balance of Trade (BoT)

When the difference in the value of imports and exports of only physical goods or visible items, is taken into account, it is called Balance of Trade or Net Exports.

Balance of trade may be

(i) **Surplus or Favourable** In this situation, exports are greater than imports,

(ii) **Deficit or Unfavourable** In this situation, imports are greater than exports,

(iii) **Equilibrium in Balance of Trade** In this situation, total value of goods exported is equal to the total value of goods imported by a country.

Balance of Payments (BoP)

When the difference in the value of imports and exports of all the three items i.e., visible, invisible and capital transfers, is taken into account, it is called Balance of Payments (BoP). Balance of Payments (BoP) is thus an overall record of all economic transactions of a country in a given period, with rest of the world.

Balance of Payments (BoP) account broadly comprises of the following components (i) Current account transaction and (ii) Capital account transaction.

Current account transactions: These are the transactions relating to inflows and outflows of forex of a routine transactions such as exports of goods and services, remittances received from non-resident Indians, foreign tourists visiting India and bringing forex into India and outflows in the form of imports of goods and services, remittances by expatriates to their home countries, expenses of resident Indians travelling abroad. These inflows and outflows never match. When the outflows exceed the inflows, a country has current account deficit.

Components of Current Account

Current account records the following transactions

(i) Export and import of goods (or of visible items).

(ii) Export and import of services (or of invisible items),

(iii) Uniliteral transfers from one country to the other.

7n the context of current account BoP, following are some important observations

- All exports (of goods and services), are recorded ;as positive (+) items as these result in the flow of foreign exchange into the country.
- All imports (of goods and services), are recorded as negative (-) items as these cause the vflow ofjforeign exchange out of the country.
- Balance occuring o/fcaccount of export and import of goods is regarded as balance'of visible trade.
- Balance occuring on account of export and import of services is recorded as balance of invisible trade.
- Receipts of uniliteral transfers are recorded as positive items.
- Payments of uniliteral transfers are recorded as negative items.
- Net value of the three balances
  (a) balance of visible trade,
  (b) balance of invisible trade,
  (c) balance of uniliteral transfers is recorded as balance on current account.
- Current Account Balance = Balance of Visible Trade + Balance of Invisible Trade + Balance of Uniliteral Transfers

Capital account transactions : These are the transactions that lead to change in asset or liability position of residents of a country, outside their own country. These are longer-term flows in the form of borrowings (ECB), investments (FDI), assistance by India to other countries or to India by other countries etc. The difference between outflows & inflows is either the capital account surplus or capital account deficit. If there is current account deficit, it will be covered by the capital account surplus. But if the capital account surplus is not enough to cover the current account deficit, the country will have to use the forex reserves leading to reduction in forex reserves.

Components of Capital Account

Following are the principal forms of capital account transactions

1.Foreign Investment : It has two sub-components

(i) Foreign Direct Investment (FDI) referring to the purchase of assets in the rest of the world, which allows control over that assets.

Example Purchase of a firm by TATA in the rest of the world.

(ii) Portfolio Investment referring to purchase of an asset in the rest of the world, without any control over that asset. Portfolio investment into India also consists of Foreign Institutional Investment (FII).

Example Purchase of some shares of a company by TATA in the rest of the world.

2. Loans : It has two sub-components

(i) Commercial Borrowings referring to borrowing by a country (including government and the private sector), from the international money market. This involves market rate of interest without considerations of any concession,

(ii) Borrowings as External Assistance referring to borrowing by a country with considerations of assistance. It involves lower rate of interest compared to that prevailing in the open market.

3. Banking Capital Transactions : referring to transactions of external financial assets and liabilities of Commercial Banks and Cooperative Banks operating as authorised dealers in foreign exchange. These transactions include NRI deposits.

4. Reserve Account : The official reserve account records the change in stock of reserve assets (also known as foreign exchange reserves) at the country's monetary authority.

5. Net Errors and Omissions : This is the last component of the Balance of Payments and principally exists to correct any possible errors made in accounting for the three other accounts. They are often referred to as 'balancing items'.

- All capital transactions causing flow of foreign exchange into the country are recorded as positive items in the capital account of BoP.

  Example Loans from rest of the world, foreign direct investment or portfolio investment by the non-residents in our country.
- All capital transactions causing flow of foreign exchange out of the country are recorded as negative items in the capital account of BoP.
- While FDI and portfolio investments are non-debt creating capital transactions, borrowings are debt-creating capital transactions.

SIGNIFICANCE OF CURRENT ACCOUNT DEFICIT

CAD measures the dependence of an economy on the capital inflows from abroad, to cover its current requirements. If dependence high, it can create problem, because the inflow of long term capital is uncertain and there is obligation to service the long term capital in the form of interest payments, dividend payments and return of principal amount, in case it is borrowing and not the investment. ;

The dependency level is judged on the basis of CAD as percentage to gross domestic product of a country (and not by amount of CAD). In case of India, it is around 4.8% currently which is significantly higher than about 1.3% in 2007-08. There area no. of causes for higher demand foreign currency including import of oil and gold while the supply could not keep pack due to declining exports.

In normal circumstances, the increasing CAD would have been funded by inflow of foreign capital in the form of FDI and/or FII, but due to various reasons including policy paralysis, political uncertainty, sliding industrial output and a weakening economy, that did not happen.

This demand-supply mismatch of foreign currencies particularly of US dollars, is the basic reason of US currency becoming more expensive.

FOREIGN INVESTMENT

Foreign Direct Investment (FDI) - It refers to direct investment in the productive capacities of a country by someone from outside the country. Such an investment can be in the form of setting up a new plant or through purchase of shares of a company, where the shareholding gives the foreign entity control over the business of the company. IMF defines control in such a case as, holding 10 % or more of ordinary shares or voting power in an incorporated firm. A foreign company can set up its business in India in two ways, by setting up a company under the Companies Act or by setting up an unincorporated entity like liaison office, project office or branch office.

Two concepts associated with FDI are Greenfield and Brownfield investment

Greenfield Investment It's a form of foreign direct investment, where a parent company starts a new venture in a foreign country by constructing new operational facilities from the ground up.

Brownfield Investment It happens, when a company or government entity purchases or leases existing production facilities to launch a new production activity.

Foreign Institutional Investment (Fll) These are investments by entities from outside the country into the financial assets like debts and shares of companies from a different country, in which they are incorporated. FIIs are required to register with SEBI (Securities and Exchange Board of India) and any foreign individual wanting to invest into India has to co^pie through one of these FIIs.

Participatory Notes (P-Notes) These are financial instruments used by investors or hedge funds that are not registered with the Securities and Exchange Board of India to invest in Indian securities. Indian-based brokerages buy India-based securities and then issue participatory notes to foreign investors. Any dividends or capital gains collected from the underlying securities go back to the investors.

Global Depository Receipts (GDRs) These are equity instruments issued in international markets like London, Luxembourg etc. Indian companies use GDRs to raise capital from abroad. GDRs are designated in dollars, euros etc.

American Depository Receipts (ADRs) These are the equity instruments issued to American retail and institutional investors. They are listed in New York, either on Nasdaq or New York Stock Exchange.

Indian Depository Receipts (IDRs) These are similar to ADR/GDR. They are used by non-Indian companies in the Indian stock markets for issuing equity to Indian investors.

INDIA'S FDI POLICY

To encourage FDI inflows, India has continued to be fine-tuned and progressively liberalised, allowing FDI in more and more industries under the automatic route. In the year 2000, government allowed FDI up to 100% on the automatic route for most activities; a small negative list was notified, where either the automatic route was not available or there were limits on FDI. Since then, the policy has been gradually simplified and rationalised and more sectors have been opened up for foreign investment.

FDI is prohibited under the government route as well as the automatic route in the following sectors, where FDI is not allowed

1. Atomic Energy
2. Lottery Business
3. Gambling and Betting
4. Business of Chit Fund
5. Nidhi Companies
6. Agricultural (excluding floriculture, horticulture, development 01 seeds, animal husbandry, pisciculture and cultivation of vegetables, mushrooms, etc under controlled conditions and services related to Agro and Allied Sectors) and plantatioi activities (other than tea plantations).
7. Housing and Real Estate business (except development > townships, construction of residential/commercial premises. roads or bridges to the extent specified in Notification No. FEMA 136/2005-RB dated July 19, 2005).
8. Trading in Transferable Development Rights (TDRs).
9. Manufacture of cigars, cheroots, cigarillos and cigarettes, of tobacco or of tobacco substitutes.

Approval Mechanism Under FDI Policy

There are two routes for FDI to enter into India.

AUTOMATIC ROUTE

In most sectors, FDI is permitted on the automatic route. FDI in such sectors does not require any prior approval and only requires notification of RBI.

Government Approval Route

Limited activities are required to prior government approval. Proposals of FDI are considered by FIPB. (Foreign Investment Promotion Board), now functioning under the Department of Economic

Affairs and decisions are conveyed in most cases within 6 to 8 weeks of receipt of complete application.

Sector Specific Limits of FDI into India

Sector	Limit	Route
Defence	49%	FIPB*
Banking (Private) Sector	74%	Automatic
Insurance	49%	Automatic
Single Brand Retail	100%	Automatic
Multi Brand Retail	51%	FIPB
Telecom	49%	Automatic
Civil Aviation	49%	Automatic

Note :

* Higher investment may be considered in state of the art technology production by Cabinet Committee on Security (CCS)

FOREIGN INSTITUTIONAL INVESTORS [FII]

[FII] that invest in the Indian capital markets. These flows are large in magnitude and have a great impact on capital market and the exchange rate.

However, there is also the danger that if FIIs pull out, the stock markets could crash which in turn can adversely impact the economy. This danger is not only on account of the impact of share prices but also because of the impact on exchange rate, which can adversely affect foreign trade and consequently the price level in the country.

DIFFERENCE BETWEEN FDI AND FII

In order to remove the ambiguity that prevails on what is Foreign Direct Investment (FDI) and what is Foreign Institutional Investment (FII) the Finance Minister in his budget speech of 2013 clarified as under--

“I propose to follow the international practice and lay down a broad principle that where an investor has a stake of 10% or less in a company, it will be treated as FII and, where an investor has a stake of more than 10%, it will be treated as FDI. A committee will be constituted to examine the application of the principle and to work out the details expeditiously.

- FIIs will be allowed to participate in the exchange traded currency derivative segment to the extent of their rupee exposure in India.
- FIIs will also be permitted to use there investment in corporate bonds and Government securities as collateral to meet their margin requirements.

QUANTITATIVE EASING & ITS TAPERING

Following the 2008 crisis, the US Fed resorted to bond-buying as a means of boosting the economy. When the Fed buys up bonds, it amounts to releasing more money into the markets that leads to reducing interest rates. This is called ‘quantitative easing’ measure or QE.

This made borrowing in the US cheaper and hence incentivized borrowers to invest (in housing or in their businesses). In June 2013, Fed chief signalled that the QE process might be tapered off which would imply that interest rates in the US will climb again. That could lead to investors investing in US and pulling out their investment from emerging markets, including India.

CAPITAL MARKET IN INDIA

A capital market is a market for securities (debt or equity), where business enterprises (companies) and governments can raise long-term funds. It is defined as a market in which money is provided for periods longer than a year,as the raising of short-term funds takes place on other markets (e.g., the money market). The capital market includes the stock market (equity securities) and the bond market (debt).

The capital market has 3 components - the equity market, the debt market, and the derivative market. It consists of all those connected with issuing and trading in equity shares and also medium and long term debt instruments, namely, bonds and debentures. It is well accepted that tenures less than one year are considered as short term; while tenures more than one year and up to three years may be taken as medium term while more than three years can be considered as long term.

Both equity and debt market have 2 segments - the primary market dealing with new issues of equity and debt instruments and the secondary market which facilitates trading in equity and debt instruments thereby imparting liquidity to the instruments and making it possible for people with different liquidity preferences to participate in the market.

The capital market operations are regulated by the Securities and Exchange Board of India [SEBI].

SEBI [SECURITIES AND EXCHANGE BOARD OF INDIA]

ESTABLISHMENT OF SEBI

The Securities and Exchange Board of India was established on April 12, 1992 in accordance with the provisions of the Securities and Exchange Board of India Act, 1992.

PREAMBLE

The Preamble of the Securities and Exchange Board of India describes the basic functions of the Securities and Exchange Board of India as "…..to protect the interests of investors in securities and to promote the development of, and to regulate the securities market and for matters connected therewith or incidental thereto"

Primary Market

The primary market is that part of the capital market that deals with the issuance of new securities. Companies, governments or public sector institutions can obtain funding through the sale of a new stock or bond issue. This is typically done through a syndicate of securities dealers.

Secondary Market

The secondary market, also known as the **aftermarket**, is the financial market where previously issued securities and financial instruments such as stock, bonds, options and futures are bought and sold.The term “secondary market” is also used to refer to the market for any used goods or assets, or an alternative use for an existing product or asset where the customer base is the second market (for example, corn has been traditionally used primarily for food production and feedstock but a “second” or “third” market has developed for use in ethanol production).

Sensex

Sensex is an index based on shares traded on the BSE. The Sensex and Nifty are the barometers of the Indian markets. The indices are composite in nature in that they cover a large segment of industries.

Commodity Market

Commodity markets are markets where raw or primary products are exchanged. These raw commodities are traded on regulated commodities exchanges, in which they are bought and sold in standardized contracts.

Bull Market

A bull market is associated with increasing investor confidence, and increased investing in anticipation of future price increases (capital gains). A bullish trend in the stock market often begins before the general economy shows clear signs of recovery.

Bear Market

A bear market is a general decline in the stock market over a period of time. It is a transition from high investor optimism to widespread investor fear and pessimism.

Blue Chip (Stock Market)

According to the New York Stock Exchange, a blue chip is stock in a corporation with a national reputation for quality, reliability and the ability to operate profitably in good times and bad. **The most popular index which follows US blue chips is the Dow Jones Industrial Average**. The Dow Jones Industrial Average is a price-weighted average of 30 blue-chip stocks that are generally the leaders in their industry. It has been a widely followed indicator of the stock market since October 1, 1928.

RIGHTS ISSUE

A rights issue is basically when a company offers existing shareholders a right to purchase additional shares of the company at a given price, which is at a discount to the prevailing market price of the stock, to make the offer enticing for the shareholder and to ensure that the rights offer is fully subscribed to.

PREFERENCE SHARES

Preference shares are those shares which are given preference as regards to payment of dividend and repayment of capital. Preference shareholders are given preference over equity shareholders as in the case of winding up of the company, their capital is paid back first and then the equity shareholders are paid. Preference shareholders cannot exercise their voting rights on all the matters. They can vote only on the matters affecting their own interest.

DEBENTURES

A debenture is a document which either creates a debt or acknowledges it. Debenture issued by a company is in the form of a certificate acknowledging indebtedness. The debentures are issued under the Company's Common Seal. Debentures are one of a series issued to a number of lenders. The date of repayment is specified in the debentures. Debentures are issued against a charge on the assets of the Company. Debentures holders have no right to vote at the meetings of the companies.

MUTUAL FUND

A mutual fund is a professionally managed type of collective investment scheme that pools money from many investors to buy stocks, bonds, short-term money market instruments, and/or other securities.

CROSS SELLING

Cross-selling stands for being able to offer to the existing bank customers, some additional banking products, with a view to expand banking business, reduce the per customer cost of operations and provide more satisfaction and value to the customer. For instance, when a bank is in a position to sell to a deposit customer (say saving bank or term deposit), a loan product such as housing loan, credit card, personal loan or vice-versa, this would result into additional business and lead to low per customer cost and higher per customer earning.

Mergers and Acquisitions

Mergers and acquisitions refers to the aspect of corporate strategy, corporate finance and management dealing with the buying, selling, dividing and combining of different companies and similar entities that can help an enterprise grow rapidly in its sector or location of origin, or a new field or new location, without creating a subsidiary, other child entity or using a joint venture. The distinction between a "merger" and an "acquisition" has become increasingly blurred in various respects (particularly in terms of the ultimate economic outcome), although it has not completely disappeared in all situations.

JOINT VENTURE

A Joint Venture (JV) is a cooperative enterprises entered into by two or more business entities. Sometimes the joint venture creates a separate corporation, limited liability company, or partnership. In other cases, the individual entities retain their individuality and they operate under a joint venture agreement. In any case, the parties in the JV share in the management, profits, and losses, according to a joint venture agreement (contract).

AMALGAMATION

Amalgamation is a restructuring phenomenon in which two or more companies are liquidated and a new company is formed to acquire business. In simpler terms, it means that a new company is formed that buys the business of minimum two companies.

PUBLIC FINANCE

'Budget System' was introduced in India on 7th April, 1860. James Wilson the first Indian Finance Member delivered the budget speech expounding the Indian financial policy as an integral whole for the first time.

The financial year for the Union and the State Governments in India is from April to March. Each financial year is, therefore, spread over two calendar years. The period of financial year as from April to March was introduced in India from 1867. Prior to that, the financial year in India used to commence on 1st May and ended on 30th April (L.K. Jha Committee's Report of the Committee On Change in Financial Year).

Although the Indian Constitution does not mention the term 'Budget', it provides that the President shall in respect of every financial year cause to be laid before both the Houses of Parliament, the House of People (Lok Sabha) and the Council of States (Rajya Sabha), **a statement of the**

estimated receipts and expenditure of the Government for that year. This statement known as the ‘Annual Financial Statement’ is the main fiscal or budgetary document of the Government. Budget has been described in **Article-112** of the Indian Constitution as Annual Financial Statement. **Article-110 describes Money Bill**

CONCEPTS OF BUDGET

On the budget day, the finance minister tables 14 documents. Of these, the main and most important document is the Annual Financial Statement.

ANNUAL FINANCIAL STATEMENT:

Article 112 of the constitution requires the government to present to the Parliament a statement of estimated receipts and expenditure in respect of every financial year, April 1 to March 31. This statement is the annual financial statement. The annual financial statement is usually a white 10-page document. It is divided into three parts, Consolidated Fund, Contingency Fund and Public Account. For each of these funds, the government has to present a statement of receipts and expenditure.

CONSOLIDATED FUND:

This is the most important of all the government funds. All revenues raised by the government, money borrowed and receipts from loans given by the government flow into the consolidated fund of India. All government expenditure is made from this fund, except for exceptional items met from the Contingency Fund or the Public Account. Importantly, no money can be withdrawn from this fund without Parliament’s approval.

CONTINGENCY FUND:

As the name suggests, any urgent or unforeseen expenditure is met from this fund. The Rs 500-crore fund is at the disposal of the President. Any expenditure incurred from this fund requires a subsequent approval from Parliament and the amount withdrawn is returned to the fund from the consolidated fund.

PUBLIC ACCOUNT:

This fund is to account for flows for those transactions where the government is merely acting as a banker, for instance, provident funds, small savings and so on. These funds do not belong to the government. They have to be paid back at some time to their rightful owners. Because of this nature of the fund, expenditures from it are not required to be approved by Parliament.

REVENUE DEFICIT:

The excess of disbursements over receipts on revenue account is called revenue deficit. This is an important control indicator. All expenditure on revenue account should ideally be met from receipts on revenue account; the revenue deficit should be zero. When revenue disbursement exceeds receipts, the government would have to borrow. Such borrowing is considered regressive as it is for consumption and not for creating assets. It results in a greater proportion of revenue receipts going towards interest payment and eventually, a debt trap. The FRBM Act, which we will take up later, requires the government to reduce fiscal deficit to zero by 2008-09.

RECEIPTS in the capital account of the consolidated fund are grouped under three broad heads - public debt, recoveries of loans and advances, and miscellaneous receipts.

FISCAL DEFICIT:

When the government’s non-borrowed receipts (revenue receipts plus loan repayments received by the government plus miscellaneous capital receipts, primarily disinvestment proceeds) fall short of its entire expenditure, it has to borrow money from the public to meet the shortfall. The excess of total expenditure over total non-borrowed receipts is called the fiscal deficit.

PRIMARY DEFICIT:

The revenue expenditure includes interest payments on government's earlier borrowings. The primary deficit is the fiscal deficit less interest payments. A shrinking primary deficit would indicate progress towards fiscal health.

The Budget document also mentions the deficit as a percentage of the GDP.

HIGHLIGHTS OF UNION BUDGET 2013-14

THE ECONOMY AND THE CHALLENGES

- Getting back to potential growth rate of 8% is the challenge facing the country.
- Slowdown in Indian economy has to be seen in the context of global economic growth from 3.9% in 2011 to 3.2% in 2012.
- Of the large countries of the world only China and Indonesia growing faster than India in 2012-13. In 2013-14, only China projected to grow faster than India.
- llth Plan period had average growth rate of 8 percent, highest during any Plan period.

THE PLAN AND BUDGETARY ALLOCATIONS

- Budget for 2013-14 to have one overarching goal of creating opportunities for our youth to acquire education and skills that will get them jobs or self-employment.

SC, ST, Women and Children

- Rs. 97,134 crore allocated for programmes relating to women and Rs. 77,236 crore allocated for programmes relating to children.

Health and Education

- Rs. 37,330 crore allocated to the Ministry of Health & Family Welfare.
- New National Health Mission to get an allocation of Rs. 21,239 cr.
- Allocation of Rs. 65,867 cr to Ministry" of Human Resource Development, an increase of 17% over the RE of the current year.
- Rs. 27,258 crore provided for Sarva Shiksha Abhiyaan (SSA).
- An increase of 25.6% over RE of the current year for investments in Rashtriya Madhyamik Shiksha Abhiyan (RMSA). - I
- Mid Day Meal Scheme (MDM) to be provided Rs. 13,215 crore.

Rural Development

- Allocation of Rs. 80,194 crore in 2Q13-14 for Ministry of Rural Development (an increase of 46for over RE 2012-13).(MGNREGS will get Rs.33,000 crore, PMGSY'toill get Rs.21,700 crore, and IAY will get Rs.15,184 crore.)

AGRICULTURE

- Rs. 27,049 crore allocated to Ministry of Agriculture (increase of 22% over the RE of current year).

Agricultural Credit

- For 2013-14, target of agricultural credit kept at Rs. 7 lakh crore.

- Interest subvention scheme for short-term crop loans to be continued scheme extended for crop loan is borrowed from private sector scheduled commercial banks.

Green Revolution

- Bringing green revolution to eastern India a remarkable success. Rs. 1,000 crore allocated in 2013-14.
- Rashtriya Krishi Vikas Yojana and National Food Security Mission provided Rs. 9,954 crore and Rs. 2,250 crore respectively.
- Allocation for integrated watershed programme increased from Rs. 3,050 crore in 2012-13 (BE) to Rs. 5,387 crore.

Farmer Producer Organizations

- Matching equity grants to registered Farmer Producer Organization (FPO) upto a maximum of Rs. 10 lakhs per FPO to enable them to leverage working capital from financial institutions.
- Credit Guarantee Fund to be created in the Small Farmers'Agri Business Corporation with an initial corpus of Rs. 100 crore.

Food Security

- Additional provision of Rs. 10000 cr for National Food Security Act.

INVESTMENT, INFRASTRUCTURE AND INDUSTRY

- Infrastructure Debt Funds (IDF) to be encourged,
- Infrastructure tax-free bond of *Rs.* 50,000 crore in 2013-14,
- Raising corpus of 19th tranche Rural Infrastructure Development Fund (RIDF) to Rs. 20,000 crore and
- Rs. 5,000 crore to NABARD to finance construction for warehousing.

Cabinet Committee on Investment

- The Cabinet Committee on Investment (CCI) has been set up. Decisions have been taken in respect of a number of gas, power and coal projects.

New Investment

- Companies investing Rs. 100 crore or more in plant and machinery during the period 1.4.2013 to 31.3.2015 will be entitled to deduct an investment allowance of 15% of the investment.

Savings

- Rajiv Gandhi Equity Savings Scheme to be liberalised (by raising the income ceiling from Rs.10 lac to Rs.12 lac).
- Additional deduction of interest upto Rs. 1 lakh for a person taking first home loan upto Rs. 25 lakh during period 1.4.2013 to 31.3.2014
- In consultation with RBI, instruments protecting savings from inflation to be introduced.

Industrial Corridors

- Plans for 7 new cities have been finalised and work on 2 new smart industrial cities at Dholera, Gujarat and Shendra Bidkin, Maharashtra will start duing 2013-14

Ports

- Two new major ports will be established in Sagar, West Bengal and in Andhra Pradesh to add 100 million tonnes of capacity.

- A new outer harbour to be developed in the VOC port at Thoothukkudi, Tamil Nadu through PPP at an estimated cost of Rs. 7,500 crore.

Micro, Small and Medium Enterprises

- Benefits or preferences enjoyed by MSME to continue upto 3 years after they grow out of this category.
- Refinancing capacity of SIDBI raised to Rs. 10,000 crore.
- Another sum of Rs. 100 crore provided to India Microfinance Equity Fund.
- A corpus of Rs. 500 crore to SIDBI to set up a Credit Guarantee Fund for factoring.

Textiles

- Technology Upgradation Fund Scheme (TUFS) to continue in 12th Plan with an investment target of Rs. 1,51,000 crore.
- A new scheme called the Integrated Processing Development Scheme will be implemented in the 12th Plan to address the environmental concerns of the textile industry.
- Working capital and term loans at a concessional interest of 6% to handloom sector.

FINANCIAL SECTOR

- A standing Council of Experts to be constituted in the Ministry of Finance to analyse the international competitiveness of the Indian financial sector.

Banking

- Compliance of public sector banks with Basel III regulations to be ensured. Rs. 14,000 crore provided in BE 2013-14 for infusing capital.
- All branches of public sector banks to have ATM by 31.3.2014.
- Proposal to set up India's first Women's Bank as a public sector bank. Provision of Rs. 1,000 crore as initial capital.
- Rs. 6,000 crore to Rural Housing Fund in 2013-14.
- National Housing Bank to set up Urban Housing Fund. Rs. 2,000 crore to be provided to the fund in 2013-14.

Insurance

- A multi-pronged approach to increase the penetration of insurance, both life and general, in the country.
- An office of at least one public sector general insurance company in towns with population of 10,000 or more.
- Rashtriya Swasthya Bima Yojana to be extended to other categories such as rickshaw, auto-rickshaw and taxi drivers, sanitation workers, rag pickers and mine workers.

Capital Market

- Designated depository participants, authorised by SEBI, may register different classes of portfolio investors, subject to compliance with KYC guidelines.
- SEBI will simplify the procedures and prescribe uniform registration and other norms for entry for foreign portfolio investors.
- Rule that, where an investor has a stake of 10% or less in a company, it will be treated as FII and, where an investor has a stake of more than 10%, it will be treated as FDI will be laid.
- FIIs will be permitted to participate in the exchange traded currency derivative segment to the extent of their Indian rupee exposure in India.
- FIIs will also be permitted to use their investment in corporate bonds and Govt. securities as collateral to meet their margin requirements.

- Small and medium enterprises, to be permitted to list on the SME exchange without being required to make an initial public offer.

Defence

- Allocation for Defence increased to Rs. 2,03,672 crore including Rs. 86,741 crore for capital expenditure.

Broadcasting

- All cities having *a* population of more than 1,00,000 will be covered by private FM radio services.

Post Offices

- An ambitious IT driven project to modernise the postal network at a cost of Rs. 4,909 crore. Post offices to become part of the core banking solution aYidjq£fe?real time banking services.

Three promises: (made to woman, youth and poor)

- We stand in solidarity with our girl children and women. A fund -"Nirbhaya Fund"- to be setup with Government contribution of Rs. 1,000 crore.
- Youth to be motivated to voluntarily join skill development programmes. National Skill Development Corporation to set the curriculum and standards for training in different skills. Rs. 1000 crore set apart for this scheme.
- To the poor of India direct benefit transfer scheme will be rolled out throughout the country during the term of the UFA Government with the motive "Aapka paisa aapke haath".

Fiscal discipline:

- By 2016-17 fiscal deficit to be brought down to 3%, revenue deficit to 1.5% and effective revenue deficit to zero%.

TAX PROPOSALS

- Tax Administration Reforms Commission to be set up.
- In short term need to reclaim peak of 11.9% of tax GDP ratio achieved in 2007-08.

DIRECTTAXES

- No case to revise either theslabs or the ratesof Personal Income Tax. Even a moderate increase in the threshold exemption will put hundreds of thousands of Tax Payers outside Tax Net.
- However, relief for Tax Payers in the first bracket of Rs.2 lakhs to Rs. 5 lakhs. A tax credit of Rs. 2000 to every person with total income upto Rs.5 lakhs.
- Surcharge of 10% on persons (other than companies) whose taxable income exceed Rs. 1 crore to augment revenues.
- Increase surcharge from 5 to 10% on domestic companies whose taxable income exceed Rs, 10 crore.
- In case of foreign companies who pay a higher rate of corporate tax, surcharge to increase from 2 to 5%, if the taxabale income exceeds Rs. 10 crore.
- In all other cases such as dividend distribution tax or tax on distributed income, current surcharge increased from 5 to 10%.
- Additional surcharges to be in force for only one year.
- Education cess to continue at 3%.

- Permissible premium rate increased from 10% to 15% of the sum assured by relaxing eligibility conditions of life insurance policies for persons suffering from disability and certain ailments.
- Contributions made to schemes of Central and State Governments similar to Central Government Health Scheme, eligible for section SOD of the Income tax Act.
- Donations made to National Children Fund eligible for 100% i deduction.
- Investment allowance at the rate of 15% to manufacturing companies that invest more than Rs. 100 crore in plant and' machinery during the period 1.4.2013 to 31.3.2015.
- Concessional rate of tax of 15% on dividend received by an Indian company from its foreign subsidiary proposed to continue for one more year. ,
- TDS at the rate of 1% on the value of the transfer of immovable properties where consideration exceeds Rs. 50 lakhs. Agricultural land to be exempted.
- A final withholding tax at the rate of 20% on profits distributed by unlisted companies to shareholders through buyback of shares.
- Proposal to increase the rate of tax on payments by way of royalty and fees for technical services to non-residents from 10% to 25%.
- Reductions made in rates of Securities Transaction Tax in respect of certain transaction (Equity futures - from 0.017% to 0.01%, MF/ETF redemptions at fund counters - from 0.25% to 0.001%, MF/ETF purchase/sale at exchanges - from 0.1% to 0.001%, on the seller).
- Proposal to introduce Commodity Transaction Tax (LI i) in a limited way (at 0.01%). Agricultural commodities will be exempted.
- Modified provisions of GAAR will come into effect from 1.4.2016.

Indirect Taxes

- No change in the normal rates of 12% for excise duty and service tax.
- No change in the peak rate of basic customs duty of 10% for non-agricultural products.
- Duty free gold limit increased to Rs. 50,000 in case of male passenger and Rs. 1,00,000 in case of a female passenger subject to conditions.

Service Tax

- Out of nearly 17 lakh registered assesses under Service Tax only 7 lakhs file returns regularly. A onetime scheme called 'Voluntary Compliance Encouragement Scheme' proposed to be introduced, j Defaulter may avail of the scheme on condition that he files truthful declaration of Service Tax dues since 1st October 2007.
- Tax proposals on Direct Taxes side estimated to yield to Rs. 13,300 crore and on the Indirect Tax side Rs.4,700 crore.

Good and Services Tax

- A sum of Rs. 9,000 crore towards the first instalment of the balance of CST compensation provided in the budget.

NATIONAL INCOME

DEFINITION

Annual income of a family is the sum total of income it receives from various sources during a year. It is on this basis that the economic position of a family is determined. Factors of production like land, labour and capital are owned by Households and they generate income in the form of rent, wages, interest and profit respectively. An economy is divided mainly into three sectors - Agricultural sector, Industrial sector and Service sector. Therefore, when we calculate the annual income of a nation, naturally we have to take into account the income from various sectors. These sectors produce innumerable items of goods and services ranging from ball pins to space shuttles during a year. The sum total of these goods and services is the gross production of the country. When we express the value of these goods and services in terms of money, we get national income. Gross National Product and Net National Product help us to understand economic progress.

J.M.Keynes, a famous economist defined national income as follows. **“National Income is the money value of all goods and services produced in a country during a year”**

While family income reflects the economic position of households, national income shows the economic position of a nation. The basic objective of an economy is to achieve economic progress. This is achieved by coordinating natural resources, human resources, capital, technology etc. National income will help to assess and compare the progress achieved by a country over a period of time.

GDP = Money value of total goods and services + Income from abroad

Income Method

Factors of production together produce output and income. The income received by the factors of production during a year can be obtained by adding rent to land, wages to labour, interest to capital and profit to organisations. This will be equal to the income of the nation. In other words, total income is equal to the reward given to various factors of production. By adding the money sent by the Indian citizens from abroad to the income of the various factors of production, we get the gross national income.

GDP = Rent + Wage + Interest +Profit + Income from abroad

This method will help us to know the contributions made by different agents like landlords, labourers, capitalists and organizers to national income.

EXPENDITURE METHOD

National income can also be calculated by adding up the expenditure incurred for goods and services. Government as well as private individuals spend money for consumption and production purposes. The sum total of expenditure incurred in a country during a year will be equal to national income.

GDP = Individual Expenditure + Government Expenditure

This method will help us to identify the expenditure incurred by different agents.

Any one of the above methods can be used for calculating national income.

Production method = Income method = Expenditure method

SOME MACROECONOMIC IDENTITIES

Gross Domestic Product (GDP)

Gross Domestic Product measures the aggregate production of final goods and services taking place within the domestic economy during a year.

GDP Value of all services produced within the country + value of all goods produced within the country.