

Banking Systems in India



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1. Which of the following is **NOT** a function of the Reserve Bank of India?

A Issuer of currency (except one rupee notes and coins)

B Banker to the Government

C **Accepting deposits from the general public**

D Custodian of Foreign Exchange Reserves

Solution

- **Central Banking Function:** The RBI is the apex monetary institution and does not deal with the general public directly.
- **Banker to Government:** It manages the central and state governments' banking transactions.
- **Banker's Bank:** It provides lending and deposit facilities to commercial banks, acting as the 'Lender of Last Resort'.
- **Issuer of Currency:** RBI issues all currency notes except the one-rupee note and coins, which are issued by the Ministry of Finance, Government of India.
- **Foreign Exchange Manager:** It is the custodian of the country's foreign exchange reserves and manages the Foreign Exchange Management Act (FEMA).

2. If the RBI decides to decrease the Cash Reserve Ratio (CRR), what is the most likely outcome?

A Decrease in lending capacity of commercial banks

B Increase in liquidity in the banking system

C Decrease in inflation

D Increase in the government's borrowing cost

Solution

- **CRR Definition:** CRR is the percentage of a bank's Net Demand and Time Liabilities (NDTL) that it must keep as a reserve with the RBI.
- **Impact of Decrease:** A reduction in CRR means banks have to hold less money with the RBI.
- **Liquidity:** The extra funds with commercial banks are now available for lending, thus increasing the money supply and liquidity in the economy.
- **Monetary Stance:** Decreasing CRR is a sign of an expansionary monetary policy, aimed at stimulating economic activity.
- **Reverse Impact:** An increase in CRR would decrease liquidity and is an contractionary measure to control inflation.

3. **The current monetary policy framework in India is focused on which of the following primary objectives?**

A Exchange rate stability

B Maximizing employment

C Price stability and maintaining inflation within a target

D Promoting export growth

Solution

- **Monetary Policy Framework Agreement:** In 2016, the government and the RBI signed an agreement formally adopting an inflation targeting framework.
- **Primary Goal:** The primary objective of the Monetary Policy Committee (MPC) is to maintain price stability while keeping in mind the objective of growth.
- **Inflation Target:** The current target is to keep the Consumer Price Index (CPI) inflation at 4% with a tolerance band of $\pm 2\%$ (i.e., 2% to 6%).
- **MPC Composition:** The MPC has six members: three RBI officials and three external members nominated by the Government of India.
- **Decision-Making:** The MPC meets at least four times a year and decides the key policy rates like the Repo Rate.

4. **The nationalization of 14 major commercial banks took place in which year?**

A 1955

B 1969

C 1980

D 1991

Solution

- **First Phase of Nationalization:** Occurred on July 19, 1969, under Prime Minister Indira Gandhi.
- **Criteria:** Banks with deposits of over ₹50 crore were nationalized (14 banks).
- **Objective:** The primary objective was 'Social Banking'—to channel credit to priority sectors like agriculture and small industries, and to promote geographical and functional spread of banking.
- **Second Phase:** Six more commercial banks were nationalized on April 15, 1980, with deposits over ₹200 crore.
- **Impact:** This move significantly expanded the reach of public sector banking and shifted the focus from class banking to mass banking.

5. Which committee is famously associated with the comprehensive financial sector reforms introduced in India in the early 1990s?

A Vijay Kelkar Committee

B R. N. Malhotra Committee

C P. J. Nayak Committee

D Narasimham Committee

Solution

- Narasimham Committee (1991): The committee on the Financial System, headed by M. Narasimham, submitted its report in 1991.
- Core Reforms: Its recommendations paved the way for major financial sector reforms, including the introduction of capital adequacy norms (like Basel Accords), deregulation of interest rates, and the establishment of private sector banks.
- Narasimham Committee II (1998): This follow-up committee focused on banking sector reforms, primarily addressing issues like capital adequacy and asset quality.
- Goal: The reforms aimed to make the Indian financial system more stable, competitive, and efficient.
- Impact: These reforms are considered a watershed moment in the modernization of the Indian banking and financial system.

6. Which of the following is a component of a bank's 'CASA' deposits?

A Fixed Deposits (FDs)

B Recurring Deposits (RDs)

C Current Account Deposits

D Certificate of Deposits (CDs)

Solution

- **CASA Full Form:** Current Account and Savings Account deposits.
- **Low-Cost Funds:** CASA deposits are the cheapest source of funds for a bank, as they typically carry low or no interest (Current Accounts) or very low interest (Savings Accounts).
- **Core Deposits:** They represent a stable base of deposits and are crucial for a bank's profitability and liquidity management.
- **Term Deposits:** Fixed Deposits (FDs) and Recurring Deposits (RDs) are Term Deposits or Time Liabilities, which carry a higher interest rate and are more expensive for the bank.
- **CASA Ratio:** A higher CASA ratio indicates a better cost of funds for the bank.

7. In the context of banking technology, what does 'RTGS' stand for?

A Real-Time Gross Settlement

B Reserve Trading and Government Securities

C Regional Transfer Global System

D Rapid Transaction and General Security

Solution

- **Definition:** RTGS is a system where the processing of funds transfer instructions takes place continuously (Real-Time).
- **Gross Settlement:** The instructions are processed on a one-to-one basis (Gross), without netting with other transactions.
- **Large-Value Transfers:** RTGS is primarily used for high-value transactions. The minimum amount for an RTGS transaction is ₹2,00,000 (2 lakhs).
- **Final and Irrevocable:** Once processed, the transfers are final and irrevocable.
- **Other Systems:** NEFT (National Electronic Funds Transfer) is a system that settles transactions in batches and has no minimum limit.

8. **What is the maximum insurance limit per depositor for deposits held in an insured bank in India, provided by the Deposit Insurance and Credit Guarantee Corporation (DICGC)?**

A ₹1,00,000

B ₹2,00,000

C ₹5,00,000

D ₹10,00,000

Solution

- **DICGC:** It is a wholly-owned subsidiary of the RBI and is responsible for providing deposit insurance.
- **Insurance Limit:** The insurance cover for bank deposits was increased from ₹1,00,000 to ₹5,00,000 per depositor per bank in February 2020.
- **Coverage:** This limit covers all deposits (Savings, Fixed, Current, Recurring) held by a depositor in the same right and capacity in a bank.
- **Purpose:** The insurance provides safety and security to small depositors' money in case a bank fails.
- **Types of Banks Covered:** All commercial banks (including foreign bank branches operating in India, local area banks, and RRBs) are

covered.

9. The concept of 'Priority Sector Lending (PSL)' mandates that commercial banks must direct a specified portion of their Adjusted Net Bank Credit (ANBC) or Credit Equivalent of Off-Balance Sheet Exposure (CEOBE) to certain sectors. What is the current mandatory target for total Priority Sector Lending for domestic commercial banks?

A 32%

B 40%

C 50%

D 60%

Solution

- PSL Mandate: Priority Sector Lending is an RBI mandate to ensure that certain vulnerable sectors of the economy receive credit.
- Target: The total PSL target for domestic commercial banks (and foreign banks with 20 or more branches) is 40% of ANBC or CEOBE, whichever is higher.
- Sub-Targets: This 40% includes sub-targets for Agriculture (currently 18%) and Weaker Sections (currently 10%).
- Covered Sectors: PSL covers sectors like Agriculture, MSMEs, Education, Housing, Export Credit, Social Infrastructure, and

Renewable Energy.

- **Non-Compliance Penalty:** Banks failing to meet the PSL targets are liable to pay penalties, such as contributing funds to the Rural Infrastructure Development Fund (RIDF) maintained by NABARD.

10. **What is the primary method by which commercial banks create credit/money in the economy?**

A Issuing new currency notes.

B Accepting deposits from the public.

C **Advancing loans and making investments.**

D Buying and selling government securities.

Solution

- **Credit Creation:** Commercial banks create money not by printing, but through the process of advancing loans.
- **Mechanism:** When a bank grants a loan, it credits the borrower's account, creating a deposit that is in excess of the bank's initial cash holding.
- **Deposit Multiplier:** The initial deposit leads to a chain reaction of subsequent lending, determined by the money multiplier ($LRR1$ where LRR is Legal Reserve Ratio, i.e., $CRR + SLR$).
- **RBI's Role:** The Reserve Bank of India has the sole authority to issue currency notes.
- **Limits:** The extent of credit creation is limited by the Legal Reserve Requirements (CRR and SLR) imposed by the RBI.

11. Which among the following is the minimum amount required for a NEFT transaction?

A ₹1,00,000

B ₹2,00,000

C ₹1

D No minimum limit

Solution

- NEFT Full Form: National Electronic Funds Transfer.
- Minimum Limit: There is no minimum limit for NEFT transactions, making it suitable for all small and medium-value fund transfers.
- Maximum Limit: While the RBI has not prescribed a maximum limit for NEFT, individual banks may set a ceiling for online banking transactions.
- Settlement: NEFT transactions are settled in a batch-wise manner at half-hourly intervals.
- Difference from RTGS: RTGS (Real-Time Gross Settlement) has a minimum limit of ₹2 lakh and is settled continuously (real-time and gross).

12. The 'Pradhan Mantri Jan Dhan Yojana (PMJDY)' is a national mission for:

A Rural Electrification

B Financial Inclusion

C Urban Housing

D Digital Literacy

Solution

- **Launch:** PMJDY was launched in August 2014.
- **Objective:** The mission's core goal is to ensure access to a minimum set of financial services, including a basic savings bank account, to every unbanked household.
- **Key Features:** It provides beneficiaries with a Basic Savings Bank Deposit Account (BSBDA) with no minimum balance, a RuPay Debit Card, a modest overdraft facility (₹10,000 to eligible accounts), and an inbuilt accident insurance cover.
- **No Frills Account:** The BSBDA is popularly known as a 'no-frills' account.
- **Vision:** It is a key initiative to bring large parts of the informal economy into the formal banking system.

13. Which one of the following is **NOT** a function of the Payment Banks in India?

A Accepting demand deposits up to ₹2 lakh.

B Issuing ATM/Debit Cards.

C Undertaking lending activities to customers.

D Facilitating money transfers (remittance services).

Solution

- Payments Banks (PBs): A new model of banks licensed by the RBI with a limited scope of operations.
- Deposits: They can accept demand deposits (Savings and Current Accounts) up to a maximum of ₹2 lakh per individual customer.
- No Lending: PBs are not permitted to undertake any lending activities, including loans and advances, or issue credit cards.
- Other Services: They can issue ATM/Debit Cards, provide remittance services, and distribute mutual fund/insurance products.
- SLR/CRR: PBs must invest a minimum of 75% of their demand deposits in Government Securities and place the remaining 25% as deposits with other Scheduled Commercial Banks.

14. **What is the full form of IFSC, which is required for NEFT/RTGS transactions?**

A Indian Financial Saving Code

B International Financial Stability Code

C Indian Foreign Security Code

D Indian Financial System Code

Solution

- **IFSC Definition:** The Indian Financial System Code is an 11-digit alphanumeric code assigned by the RBI to uniquely identify every bank branch participating in the NEFT and RTGS systems.
- **Structure:** The first four characters are alphabetic and represent the bank's name. The fifth character is always zero for future use. The last six characters are numeric and represent the specific branch code.
- **Purpose:** It is essential for routing transactions correctly between the originator and the beneficiary bank branches.
- **MICR:** The Magnetic Ink Character Recognition (MICR) code is a 9-digit code used primarily for processing cheques and clearing.
- **UBI and PNB Example:** A typical IFSC might look like UBIN0123456 (for Union Bank of India) or PUNB0012345 (for

Punjab National Bank).

15. What is the maximum period for which 'Call Money' is transacted in the Indian money market?

A 1 day

B 7 days

C 14 days

D 3 months

Solution

- Money Market: The market for short-term funds, which mature in less than one year.
- Call Money: Loans for which funds are transacted overnight (for one day).
- Notice Money: Loans for which funds are transacted for a period of 2 to 14 days.
- Term Money: Loans for which funds are transacted for a period of more than 14 days but less than a year.
- Participants: This market is crucial for banks to manage their short-term liquidity, particularly to meet the CRR requirements.

16. The 'SARFAESI Act, 2002' provides the legal framework for banks to tackle which of the following issues?

A Regulation of Cooperative Banks

B Recovery of Non-Performing Assets (NPAs)

C Supervision of Foreign Banks

D Consumer Protection in Banking

Solution

- SARFAESI Full Form: Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002.
- Purpose: The Act empowers banks and financial institutions to recover their NPAs by selling the financial assets and enforcing security interests without the intervention of the court.
- Conditions: The Act applies to secured loans where the loan amount is above ₹1 lakh and the borrower's account is classified as an NPA.
- Mechanism: It allows banks to take possession of the security, manage it, or sell it to recover dues.
- Asset Reconstruction: It also provides the legal framework for the setting up of Asset Reconstruction Companies (ARCs) to take over and manage NPAs from banks.

17. **The Co-operative Credit Structure in Kerala for short-term credit is a three-tier system. Which of the following is at the State level?**

A District Co-operative Bank (DCB)

B Primary Agricultural Credit Society (PACS)

C **Kerala State Co-operative Bank (KSCB)**

D Regional Rural Bank (RRB)

Solution

- **Three-Tier Structure:** The short-term co-operative credit structure in India, and specifically in Kerala, follows a three-tier model.
- **Apex Level (State):** The Kerala State Co-operative Bank (KSCB), now merged to form Kerala Bank, operates at the state level (Apex Bank).
- **Intermediate Level (District):** The District Co-operative Banks (DCBs) (now part of Kerala Bank) operate at the district level.
- **Base Level (Village):** The Primary Agricultural Credit Societies (PACS), or Service Co-operative Banks, function at the village level and directly deal with the rural public.
- **Long-Term Structure:** The long-term structure is separate, operating on a two-tier system: State Co-operative Agricultural and Rural

Development Bank (SCARDB) and Primary Co-operative Agricultural and Rural Development Banks (PCARDBs).

18. **The Co-operative Bank which recently merged to form 'Kerala Bank' (Kerala State Co-operative Bank) was the amalgamation of:**

A

The Kerala State Co-operative Bank and all Primary Agricultural Credit Societies.

B

The Kerala State Co-operative Bank and all District Co-operative Banks.

C

The Kerala State Co-operative Bank and all Urban Co-operative Banks.

D

All District Co-operative Banks only.

Solution

- **Kerala Bank Formation:** Kerala Bank was formed to strengthen the co-operative banking structure in the state.
- **Merger:** It was formed by the amalgamation of the Kerala State Co-operative Bank (KSCB) (the state-level apex bank) and 13 out of 14 District Co-operative Banks (DCBs). (Malappuram DCB initially opted out).
- **New Structure:** This created a two-tier structure in Kerala's short-term co-operative credit system: the Kerala Bank (Apex) and the PACS (Base).
- **Objective:** To improve efficiency, access to modern technology, and competitiveness with commercial banks.
- **Timeline:** The merger was implemented in 2019-2020.

19. Which of the following is **NOT** an authorized security under the Statutory Liquidity Ratio (SLR) requirement for a co-operative bank?

A Cash in hand

B Gold

C Investment in own bank's shares

D Balances with the RBI

Solution

- **SLR Definition:** SLR mandates banks to hold a specified percentage of their deposits in liquid assets.
- **Eligible Assets:** The eligible assets include unencumbered Government securities, cash in hand, balances with the RBI (or apex bank in the co-operative structure), and gold.
- **Ineligible Assets:** A bank's own shares or shares of other institutions are generally not considered liquid and, therefore, are excluded from SLR-eligible assets.
- **Objective:** The SLR is meant to ensure a bank's solvency and meet unexpected large demands from depositors.
- **Co-operative Bank Norms:** Co-operative banks have specific norms for SLR, including holding certain balances with the apex co-

operative bank.

20. The function of the 'Lender of Last Resort' for the State Co-operative Bank is generally performed by:

A NABARD

B Commercial Banks

C Primary Agricultural Credit Societies (PACS)

D Reserve Bank of India (RBI)

Solution

- Lender of Last Resort (LLR): The function of providing emergency short-term liquidity to a solvent bank facing temporary financial difficulties.
- RBI as LLR: The RBI is the LLR for the entire organized banking system in India, including Scheduled State Co-operative Banks.
- NABARD's Role: NABARD's role is primarily to provide refinance for specific purposes (agriculture/rural development), not general emergency liquidity in its LLR capacity.
- Scheduled Status: Only Scheduled State Co-operative Banks are directly eligible for LLR facilities from the RBI.
- Ultimate Authority: The RBI maintains ultimate control over the flow of money and credit in the economy.

21. The term 'Indira Awas Yojana' is related to a scheme that used to be a part of which priority sector lending category?

A Agriculture

B Export Credit

C Housing

D Education

Solution

- Indira Awas Yojana (IAY): It was a major social welfare program by the Government of India for providing houses to the rural poor.
- Current Scheme: IAY was restructured and renamed as the Pradhan Mantri Awas Yojana-Gramin (PMAY-G) in 2016.
- PSL Classification: Loans granted for construction/purchase of dwelling units and repairs/upgradation are part of the Housing category under Priority Sector Lending.
- Co-operative Relevance: Co-operative Banks, especially the long-term structure, also finance rural housing, making this a relevant PSL concept for the exam.
- Social Objective: The scheme aligns with the 'social banking' objective of the banking sector.

22. Which of the following is an example of an asset for a bank?

A Loans and Advances given to customers

B Deposits from customers

C Borrowings from the RBI

D Share capital of the bank

Solution

- **Assets vs. Liabilities:** In banking, an asset is something the bank owns and is expected to generate future economic benefits (income), while a liability is something the bank owes to others.
- **Loans as Assets:** Loans and Advances (money lent to customers) are assets because they generate interest income for the bank.
- **Deposits/Borrowings as Liabilities:** Customer deposits and borrowings from the RBI are liabilities because the bank owes these amounts to depositors and the central bank, respectively.
- **Capital:** Share capital is part of the bank's net worth or owner's equity.
- **Balance Sheet:** A bank's balance sheet structure is crucial for understanding its financial health.

23. The term 'Banker's Lien' is primarily associated with:

A A bank's right to claim a customer's property for non-repayment of a loan.

B

The right of the bank to retain the goods or securities belonging to the debtor customer.

C The right of the bank to sell the collateral pledged by the borrower.

D The duty of the bank to maintain the secrecy of customer accounts.

Solution

- Lien: A legal claim or right against an asset that is typically used as collateral to satisfy a debt.
- General Lien: A Banker's General Lien is the statutory right of a bank to retain any goods or securities belonging to a customer until the general balance due from the customer is paid.
- Implied Pledge: The general lien is often described as an implied pledge.
- Set-Off: The right of the bank to adjust the debit and credit balances in a customer's different accounts is called the right of set-off.
- Specific Lien: A specific lien gives the right to retain only those goods or securities that are connected to a particular debt.

24. Which of the following is considered a quantitative tool of credit control by the RBI?

A Moral Suasion

B Rationing of Credit

C Statutory Liquidity Ratio (SLR)

D Direct Action

Solution

- **Quantitative Tools:** These tools affect the overall volume of credit in the economy (e.g., Repo Rate, Reverse Repo Rate, CRR, SLR, Bank Rate).
- **SLR Definition:** SLR is the percentage of NDTL that a bank must maintain in the form of liquid assets (like gold, cash, or unencumbered approved securities).
- **Qualitative Tools:** These tools selectively direct credit towards specific sectors (e.g., Margin Requirements, Moral Suasion, Direct Action).
- **Impact:** An increase in SLR reduces the funds available for commercial banks to lend, thus controlling credit.
- **Statutory Mandate:** SLR is mandated under Section 24 of the Banking Regulation Act, 1949.

25. The term 'Scheduled Commercial Bank' refers to a bank that is included in the:

- A** First Schedule of the Banking Regulation Act, 1949
- B** Second Schedule of the Reserve Bank of India Act, 1934
- C** Third Schedule of the Companies Act, 2013
- D** Fourth Schedule of the Negotiable Instruments Act, 1881

Solution

- **Scheduled Bank Status:** A bank that is included in the Second Schedule of the RBI Act, 1934, is a Scheduled Bank.
- **Benefits/Obligations:** Scheduled banks enjoy facilities like financial accommodation (loans) from the RBI and membership in clearing houses.
- **Regulatory Requirement:** They are subject to specific regulatory requirements, like maintaining the CRR with the RBI.
- **Scheduled vs. Non-Scheduled:** A non-scheduled bank is one that does not meet the requirements for inclusion in the Second Schedule.
- **Classification:** Scheduled Commercial Banks include Public Sector Banks, Private Sector Banks, Foreign Banks, and Regional Rural Banks.

26. What is 'Microfinance' in the context of the Indian financial system?

A Providing large loans to major industries.

B Providing small loans, savings, and other financial services to low-income individuals or groups.

C Offering complex financial derivatives to High Net Worth Individuals (HNIs).

D Funding only government-sponsored infrastructure projects.

Solution

- **Definition:** Microfinance involves the provision of financial services to clients usually excluded from the formal financial system, mainly due to their low-income status.
- **Target Group:** Low-income households, particularly women organized into Self-Help Groups (SHGs) or Joint Liability Groups (JLGs).
- **Key Services:** Small loans (microcredit), micro-savings, micro-insurance, and remittance facilities.
- **Regulation:** Microfinance Institutions (MFIs) are regulated by the RBI.
- **Significance:** It is a powerful tool for financial inclusion, poverty reduction, and women's empowerment, particularly in rural and

semi-urban areas.

27. Which is the lowest tier in the short-term Co-operative Credit Structure, directly dealing with the rural borrower?

A Primary Agricultural Credit Society (PACS)

B State Co-operative Bank

C District Co-operative Bank

D Urban Co-operative Bank (UCB)

Solution

- **PACS as Base:** The PACS forms the grassroots level of the co-operative credit system.
- **Function:** They provide short and medium-term loans, distribute agricultural inputs, and offer various services directly to farmers and rural residents.
- **Direct Interaction:** They are the primary source of formal credit for the majority of the rural population covered by the co-operative sector.
- **Funding Channel:** Funds flow from the State Co-operative Bank → District Co-operative Banks → PACS → ultimate borrower.
- **Local Scope:** Their operations are generally confined to a single village or a small group of villages.

28. **What is the primary role of the State Co-operative Union in Kerala's co-operative movement?**

- A** Providing finance to Co-operative Banks
- B** Supervising and regulating Co-operative Banks
- C** Co-operative education, training, and publicity
- D** Auditing the accounts of Co-operative Societies

Solution

- **Non-Credit Function:** State Co-operative Unions are generally non-credit organizations.
- **Core Mandate:** Their main function is the promotion of the co-operative movement through education, training, and propaganda (publicity).
- **Training:** They often run Co-operative Training Colleges and Centers to impart training to co-operative employees and members.
- **Auditing:** Auditing of co-operative societies is primarily done by the Co-operative Department or independent auditors appointed by the department.
- **Finance/Supervision:** Finance is handled by the financial structure, and supervision is shared between the RBI and the RCS.

29. The principle of 'one member, one vote' is characteristic of which banking system?

A Commercial Banks

B Public Sector Banks

C Payments Banks

D Co-operative Banks

Solution

- **Co-operative Principle:** The 'one member, one vote' principle is the third fundamental principle of co-operation, as defined by the International Co-operative Alliance (ICA).
- **Democratic Control:** It ensures democratic control and equality among members, irrespective of the number of shares held by them.
- **Contrast with Commercial Banks:** In commercial banks, voting rights are generally based on the number of shares held (one share, one vote).
- **Purpose:** This principle ensures that the co-operative serves the needs of its members, rather than just the interests of major shareholders.
- **Exception:** Some minor exceptions may exist for institutional members, but the spirit remains democratic.

30. Which of the following types of loan is a characteristic long-term loan provided by Primary Co-operative Agricultural and Rural Development Banks (PCARDBs)?

A Crop loans (seasonal)

B Gold loans (short-term pledge)

C Loans for irrigation development and farm mechanization

D Consumption loans

Solution

- **Long-Term Focus:** PCARDBs specialize in providing long-term investment credit for development purposes.
- **Investment Credit:** This includes financing for activities that yield returns over a long period, such as digging wells, installing irrigation systems, purchasing tractors (farm mechanization), and development of plantations.
- **Short-Term Credit:** Crop loans and short-term gold loans are the domain of PACS (the short-term credit structure).
- **Repayment Period:** The repayment tenure of PCARDB loans usually extends from 5 to 15 years.
- **Developmental Role:** Their core role is capital formation in the agriculture sector.



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