Banking and Finance
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RBI Role and it’s functions

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RBI and Its Role

- Objectives and Functions of RBI,
- Bank Rates and Interest Rates,
- Objectives of Credit Control,
- Organized and Unorganized Money Market,
- Capital Market and Money Market,
- Open Market Operations,
- Quantitative and Qualitative Measures for Credit Control
Objectives of RBI

The Important Objectives of RBI is as follows -

- To Stabilize the Internal Price Level (Controlling Inflation)
- To Stabilize the Rate of Foreign Exchange
- To Stabilize the Money Market in the Country
- To Control the Activities of Business Cycle and Others.
- Promotion of Economic Growth in Shortest Possible Period:
- To Meet Business Needs:
Objectives of RBI

- **To Stabilize the Internal Price Level:**

The important objective of credit control is to establish stability in the internal price-level. But this is possible only when if there is a proper adjustment between the demand and supply of credit.

- **If the supply of credit is less than the commercial requirements, i.e., demand, there is sure to be a decline in the price-level.**

- **On the contrary, if the supply of credit exceeds the commercial requirements, i.e., demand, the internal price-levels are bound to go up.**

- **Therefore, the Central Bank should try to bring about a proper adjustment between the supply of credit and the commercial requirements of the country.**
Objectives of RBI

- **Stabilize the Rate of Foreign Exchange:**

  The second important objectives of credit control are to maintain stability in the foreign exchange rates.

  - The instability in exchange rates can have harmful repercussions on the foreign trade of the country. Therefore, the Central Bank in those countries whose foreign trade is important should pay special attention to the elimination of volatile fluctuations in foreign exchange rates through credit control policy.

- **Stabilize the Money Market in the Country:**

  Next important point to consider is that the credit control policy of the Central Bank should aim at the stabilization of the money market in the country. To achieve this point the Central Bank should neutralize seasonal variations in the demand for funds.
Objectives of RBI

- **Control the Activities of Business Cycle:**

  Business cycles are a common phenomenon of capitalist countries which lead to periodic fluctuations in production, prices and employment.

  - Therefore, the credit control policy of the Central Bank should be to eliminate or at least to reduce the havoc caused by the business cycle. By varying the supply of credit, the Central Bank can, to some extent, control the operation of the business cycle.
Objectives of RBI

- **Promotion of Economic Growth in Shortest Possible Period:** It should be remembered that the chief objectives of the credit control policy in underdeveloped countries should be to promote economic growth within the shortest possible period.

  - For economic growth backward countries suffer from financial crisis. Therefore, the Central Bank in those countries should try to solve the problem of financial crisis through planned expansion of bank credit.

- **Meet Business Needs:**

  “Credit is needed to meet the requirements of trade and industry.

  - **As business expands large quantity of credit is needed and when business Contracts Less Credit is needed.** Therefore it is the Central Bank only which can need the requirements of business by controlling credit.”
Functions of RBI

- Note Issuing Agency
- Banker's Bank
- Controller of Credit
- Lender of Last Resort
- Banker to the Government
- Manages Price Stability
- Manages Exchange Rate/Currency.
A Central Bank performs many important and essential functions, which are described below:

- **Traditional Functions**
- **Developmental Functions**

### Traditional Functions

- **Note Issuing Authority**
  Note-issue is the sole privilege of the Central Bank in a country and its notes became full legal tender. In issuing notes, the Central Bank must follow rules laid down by law. It has compulsorily to maintain reserves of gold, silver, and selected securities in fixed proportions to inspire confidence among the people in the paper currency to maintain its internal and external value.

- **The system of note-issue differs from country to country and is governed by its peculiar circumstances.** Thus in India, the Reserve Bank of India (RBI) which is its central bank, is now (since October 1957) required to keep a minimum reserve of Rs. 200 crores, of which not less than Rs. 115 crores must be in gold.
Functions of RBI

Traditional Functions

- Government Banker:
  Previously Governments in a country had to maintain many treasuries all over the country. **Now their funds are kept with the Central Bank free of interest. This is a privilege for the Bank as well as a responsibility. It receives payment on behalf of the government and makes payments on its behalf.**

- A Central Bank is required to lend money to Central and State governments when called upon to do so. Taxes flow to Government only in certain parts of the year, while funds are always wanted. Hence, Government borrows temporarily from the Central Bank in times of need.

- These loans are called “**ways and means advances**”. Besides these, all other government loans, temporary (like treasury bills) and permanent, are floated through the Central Bank. In addition, it remits government funds, purchases foreign currencies, as well as manages the public debt. It also acts as the financial adviser of the government. The Reserve Bank of India performs all these functions for the Central and State Governments in India.
Functions of RBI

Traditional Functions

▪ Bankers’ Bank:
All other banks in the country are bound either by law or by convention to keep a certain proportion of their total deposits as reserve with the Central Bank.

▪ These reserves help the Central Bank to control the issue of credit by commercial banks. They also keep their spare cash with the Central Bank on which they draw as and when needed. This is how the Central Bank serves as a bankers’ bank.

▪ Lender of Last Resort:
The other banks in the country depend upon the Central Bank for support in times of emergency. This help may be in the form of a loan on the security of approved securities or through a rediscount of bills of exchange.

▪ The Central Bank is thus the “lender of last resort” for other banks in difficult times, because on such occasions, there is no hope of getting help from any competing institution.
Functions of RBI

**Traditional Functions**

- Control of Credit:

Perhaps the most important function of a Central Bank today is the control of credit, i.e., regulating the volume and direction of bank loans.

- On the volume of credit depends largely the level of employment and the level of prices in the country

- Maintenance of Exchange Rate:

Another very important function of a Central Bank is to keep stable the external value of the home currency. A stable exchange rate is necessary to maintain and promote a country’s foreign trade and to encourage the inflow of foreign investments, which is so essential for accelerating the pace of economic growth, particularly in the under-developed countries.
Functions of RBI

Traditional Functions

- **Maintenance of Exchange Rate:**

  - In order to maintain the rate of exchange stable, a Central Bank is always prepared to buy and sell foreign currencies at the rates fixed by it.

  - However, when the cost-price situation in the country as also the balance of payments position, undergo a substantial change, the old rate of exchange may have to be changed.
Functions of RBI

Traditional Functions

▪ Custodian of National Reserves:

It is the Central Bank which serves as the custodian of nation’s reserves of gold and international currency. It is its duty to take appropriate measures to safeguard these reserves.

▪ Provision of Clearing House Facilities:

The Central Bank performs the duty of a Clearing House for cheques. It settles the accounts of commercial banks and enables them to clear their dues by the process of book entries.

• The Reserve Bank of India is now a government-owned bank and whatever be its profits, they go to the government treasury.
Functions of RBI

Developmental Functions:

In the under-developed countries, whose main concern is faster economic development, the Central banks have a very important role to play, which is not merely regulatory to maintain stability, but developmental and promotional.

The main task of Central Banks in such countries is to bring about a rapid expansion of banking facilities and to make adequate funds available to finance development programmes in respect of agriculture, trade, transport and industry, and to create specialized financial institutions for the purpose.

- Development of the Financial System The financial system comprises the financial institutions, financial markets and financial instruments. The sound and efficient financial system is a precondition of the rapid economic development of the nation. The RBI has encouraged establishment of banking and non-banking institutions to cater to the credit requirements of diverse sectors of the economy.
Functions of RBI

**Developmental Functions:**

- **Development of Agriculture**
  
  In an agrarian economy like ours, the RBI must provide special attention for the credit need of agriculture and allied activities. It has successfully rendered service in this direction by increasing the flow of credit to this sector.

  - It has earlier the Agriculture Refinance and Development Corporation (ARDC) to look after the credit, National Bank for Agriculture and Rural Development (NABARD) and Regional Rural Banks (RRBs).

- **Provision of Industrial Finance**

  Rapid industrial growth is the key to faster economic development. In this regard, the adequate and timely availability of credit to small, medium and large industry is very significant. In this regard the RBI has always been instrumental in setting up special financial institutions such as ICICI Ltd. IDBI, SIDBI and EXIM BANK etc.
Functions of RBI

**Developmental Functions:**

- **Provisions of Training**

The RBI has always tried to provide essential training to the staff of the banking industry. The RBI has set up the bankers' training colleges at several places. National Institute of Bank Management i.e. NIBM, Bankers Staff College i.e BSC and College of Agriculture Banking i.e CAB are few to mention.

- **Collection of Data**

Being the apex monetary authority of the country, the RBI collects process and disseminates statistical data on several topics. It includes interest rate, inflation, savings and investments etc. This data proves to be quite useful for researchers and policy makers.
Functions of RBI

Developmental Functions:

- **Publication of the Reports**
  The Reserve Bank has its separate publication division. This division collects and publishes data on several sectors of the economy. The reports and bulletins are regularly published by the RBI. It includes RBI weekly reports, RBI Annual Report, Report on Trend and Progress of Commercial Banks India., etc. This information is made available to the public also at cheaper rates.

- **Promotion of Banking Habits**
  As an apex organization, the RBI always tries to promote the banking habits in the country. It institutionalizes savings and takes measures for an expansion of the banking network. It has set up many institutions such as the Deposit Insurance Corporation-1962, UTI-1964, IDBI-1964, NABARD- 1982, NHB -1988, etc. These organizations develop and promote banking habits among the people. During economic reforms it has taken many initiatives for encouraging and promoting banking in India.

- One of the Important Functions of RBI is to Promote & License New Banks
Functions of RBI

Developmental Functions:

- **Promotion of Export through Refinance**

The RBI always tries to encourage the facilities for providing finance for foreign trade especially exports from India.

- The Export-Import Bank of India (EXIM Bank India) and the Export Credit Guarantee Corporation of India (ECGC) are supported by refinancing their lending for export purpose.
THANK YOU