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# Ace BANKING & STATIC AWARENESS

A Compete Guide on General Awareness for Banking Examinations

**Useful for SBI, IBPS, RBI, NABARD and Other Exams**

## THIS EDITION INCLUDES:

- Financial/Banking Concepts
- Digital Banking
- Static GK
- Memory Based Questions of SBI PO/Clerk Mains

**SECOND EDITION**

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# A Complete Book on
# Banking Awareness &
# Static Awareness

# PREFACE

The knowledge Banking and Static General Awareness is important if you are preparing for banking and insurance examinations to ace and score in the GA section. Banking and Static GK are not only a part of the General Awareness section but are is also important from interview's point of view where the panel will expect you to be aware of the whereabouts of facts and figures related to banking industry.

With the changes in exam pattern Adda247 has evolved its study and practice material to provide its readers with the latest pattern based content for banking, insurance, and other exams. To help you prepare the Banking and Static GK, Adda247 Publications bring to you ***"A Complete Book on Banking and Static General Awareness"*** which is useful for SBI PO, SBI Clerk, IBPS PO, IBPS Clerk, IBPS RRB, NIACL, NICL, RBI Grade B Officer and Assistant and other Banking and Insurance examinations.

This book covers it all from the basics of Banking and its History, RBI and its Functions to Monetary Policy Committee, NPAs, Economic Survey and Union Budget. For preparation of Static GK you'll get carefully divided chapters of lists of Government Schemes, National Parks, Folk Dances, Cities on River Banks, Dams, Important Awards, Power Plants and a lot more. As a special add on for practice, this book also includes memory based questions asked in SBI Clerk and SBI PO Mains 2018.

We hope that our readers will appreciate our efforts and this book. Any comments or suggestion for further improvements are welcome wholeheartedly.

**Team Adda247**

# CONTENTS

## Banking Awareness

## Static Awareness

## General Awareness Questions Asked in SBI PO/Clerk Mains 2018

# Banking Awareness

# Chapter 1 What is Banking and Its History?

- Banking can be defined as the activity of accepting the deposits from the general public & the entities, and then lending that money to earn profits.
- But now the banking is not only including deposits and loans but also includes providing services like issuance of debit and credit cards, providing safe custody of valuable items, lockers, ATM services and online transfer of funds across the country / world.
- Bank is a financial institution that performs the banking activity ie.it accepts deposits and lending of funds to earn profits.
- Any company, which transacts the business of banking defined above is termed as Banking company

## Introduction

- As per the Reserve Bank of India (RBI), India's banking sector is sufficiently capitalised and well-regulated.
- Indian banking industry has recently witnessed the roll out of innovative banking models like payments and small finance banks. RBI's new measures may go a long way in helping the restructuring of the domestic banking industry.
- The digital payments system in India has evolved the most among 25 countries with India's Immediate Payment Service (IMPS) being the only system at level 5 in the Faster Payments Innovation Index (FPII).

## Market Size

- Public-sector banks control more than 70 per cent of the banking system assets, thereby leaving a comparatively smaller share for its private peers. Banks are also encouraging their customers to manage their finances using mobile phones.
- As the Reserve Bank of India (RBI) allows more features such as unlimited fund transfers between wallets and bank accounts, mobile wallets are expected to become strong players in the financial ecosystem.

## History of Banking Sector in India

- The first bank of a joint stock variety was Bank of Bombay, established in 1720 in Bombay. This was followed by Bank of Hindustan in Calcutta, which was established in 1770 by an agency house.
- The General Bank of Bengal and Bihar, which came into existence in 1773, after a proposal by Governor (later Governor General) Warren Hastings, proved to be a short-lived experiment.
- The first 'Presidency bank' was the Bank of Bengal established in Calcutta on June 2, 1806 with a capital of Rs.50 lakh. The bank was given powers to issue notes in 1823.
- Bank of Bombay was the second Presidency bank set up in 1840 with a capital of Rs.52 lakh, and the Bank of Madras the third Presidency bank established in July 1843 with a capital of Rs.30 lakh.
- With the collapse of the Bank of Bombay, the New Bank of Bombay was established in January 1868.
- The Presidency Bank Act, which came into existence in 1876, brought the three Presidency banks under a common statute and imposed some restrictions on their business.
- The first Indian owned bank was the Allahabad Bank set up in Allahabad in 1865, the second, Punjab National Bank was set up in 1895 in Lahore, and the third, Bank of India was set up in 1906 in Mumbai. All these banks were founded under private ownership.

- Swadeshi Movement of 1906 provided a great impetus to joint stock banks of Indian ownership and many more Indian commercial banks such as Central Bank of India, Bank of Baroda, Canara Bank, Indian Bank, and Bank of Mysore were established between 1906 and 1913.
- The late Shri Vithal L Kavthekar pioneered the urban co-operative credit movement in the year 1889 in the then princely State of Baroda.
- The first registered urban co-operative credit society was the Conjeevaram Urban Co-operative Bank, organised in Conjeevaram, in the then Madras Presidency.

  **Note:** They were known as Presidency banks as they were set up in the three Presidencies that were the units of administrative jurisdiction in the country for the East India Company. The Presidency banks were governed by Royal Charters. The Presidency banks issued currency notes until the enactment of the Paper Currency Act, 1861, when this right to issue currency notes by the Presidency banks was abolished and that function was entrusted to the Government.

- The presidency banks were amalgamated into a single bank, the Imperial Bank of India, in 1921. It also functioned as a central bank prior to the establishment RBI. The Imperial Bank of India performed three set of functions, viz., commercial banking, central banking and the banker to the government.
- By 1930, the number of commercial banks increased to 107 with the Imperial Bank of India still dominating the Indian banking sector.
- Indian Central Banking Enquiry Committee was set up in 1929 to survey extensively the problems of Indian banking, observed that a central bank be established for the country.
- Reserve Bank of India Act 1934 was enacted paving the way for the setting up of the Reserve Bank of India. The issue of bank failures and the need for catering to the requirements of agriculture were the two prime reasons for the establishment of the Reserve Bank. The banking sector came under the purview of the Reserve Bank in 1935.

- The Government, therefore, first implemented the exercise of nationalisation of the Imperial Bank of India with the objective of "extension of banking facilities on a large scale, more particularly in the rural and semi-urban areas, and for diverse other public purposes". The Imperial Bank of India was converted into the State Bank of India in 1955 with the enactment of the State Bank of India Act, 1955.

# Chapter 2 Types of Banking in India

**The different types of Banking are as follows:**

1. *Para Banking*
2. *Narrow Banking*
3. *Offshore Banking*
4. *Green banking*
5. *Retail Banking*
6. *Wholesale banking*
7. *Universal Banking*
8. *Islamic Banking*
9. *Merchant Banking*

## Para Banking

Banks can undertake certain eligible financial services i.e. the para-banking activities either departmentally or by setting up subsidiaries. The banks can form a subsidiary company for undertaking the types of business which a banking company is otherwise permitted to undertake, with prior approval of RBI.

**Subsidiary Companies/Different Para-Banking Activities**

Under the provisions of Section 19(1) of the Banking Regulation Act, 1949, banks may form subsidiary companies for undertaking types of banking business. Prior approval of the RBI should be taken by a bank, to set up a subsidiary company.

- Banks can form subsidiary companies for undertaking equipment leasing, hire purchase business and factoring services.
- Banks can also undertake equipment leasing, hire purchase and factoring services departmentally.
- Mutual Fund business.
- Credit Card and Smart/Debit Card Business.
- Money Market Mutual Funds (MMMFs): Banks can set up this after the approval from RBI.
- Entry of banks into Insurance business.
- Underwriting of Corporate Shares and Debentures.
- Underwriting of bonds of Public Sector Undertakings.
- RBI observed that some banks/their subsidiaries were providing buy-back facilities under the name of 'Safety Net' Schemes. Under such schemes, large exposures are assumed by way of commitments to buy the relative securities from the original investors at any time during a stipulated period at a price determined at the time of issue, irrespective of the prevailing market price.

## Narrow Banking

- Narrow banks are safe banks. By not lending, and using their deposits to buy government bonds, they carry virtually no credit risk. There is no danger of non-performing loans and frequent injections of equity capital that has to be funded by taxpayers.
- Narrow Banking; i.e. the banks that place funds only in riskless securities. The main thinking that goes behind for this is that since their investment is mainly in riskless securities they will not fail.

- The Tarpore Committee gave the recommendation to convert weak banks into narrow banks. The committee has proposed that the incremental resources of these narrow banks should be restricted only to investments in government securities.

## Offshore Banking

- 'Offshore Banking Unit' means a branch of a bank in India located in the Special Economic Zone and holds an authorisation issued under clause (a) of sub-section (1) of section 23 of the Banking Regulation Act, 1949 (10 of 1949).
- An offshore banking unit (OBU) is a financial service unit (normally a branch or subsidiary of a non-resident bank), which plays an intermediary role between non-resident borrowers and lenders. In Indi, these are found in Special Economic Zones.
- Offshore banking units are allowed to accept deposits from foreign banks, from some onshore banks that permit deposits and other offshore banking units, and the OBU may make loans to non-resident companies as well.
- They do not carry retail business, but generally provide wholesale banking services — project financing, syndicated loans, issue of short-term and medium-term instruments, etc.

## Green Banking

- The concept of green banking has emerged and is recognized as an important strategy to address sustainable development concerns and creating awareness among people about environmental responsibility.
- Green banking has two dimensions. First, the way the banking business is being done – is it paperless or not. The second dimension relates to where the bank puts its money. Green Banking entails banks to encourage environment friendly investments and give lending priority to those industries which have already turned green or are trying to go green and, thereby, help to restore the natural environment.
- Green banking generally refers to how environmentally friendly the bank is, and how committed to green and ethical policies the banks are.
  **Note:** "Green Banking" can be called as the method of finance by the banks to make the industries grow green and in the process restore the natural environment. This concept of "Green Banking" will be mutually beneficial to the banks, industries and the economy.

## Retail Banking

- Retail banking refers to the dealing of commercial banks with individual customers, both on liabilities and assets sides of the balance sheet.
- Fixed, current / savings accounts on the liabilities side; and mortgages, loans (e.g., personal, housing, auto, and educational) on the assets side, are the more important of the products offered by banks.
- Related ancillary services include credit cards, or depository services.
- Retail banking sector is characterized by three basic characteristics:
  **(a)** multiple products (deposits, credit cards, insurance, investments and securities);
  **(b)** multiple channels of distribution (call centre, branch, Internet and kiosk); and
  **(c)** multiple customer groups (consumer, small business, and corporate).

## Wholesale Banking

- Wholesale banking refers to banking services between merchant banks and other financial institutions. In this the banks deals with larger clients, such as large corporations and other banks.
- It refers to doing banking business with industrial and business entities mostly corporates and trading houses, including multinationals, domestic business houses and prime-public sector.

- It is also called corporate banking.
- It is the borrowing and lending of funds to other banks, large multinationals and even government agencies.
- It focuses on corporate, i.e. Companies, firms, proprietorship concerns, Public Sector, Institutions, societies, Trusts and clubs.

## Universal Banking

- Universal Banking is a multi-purpose and multi-functional financial supermarket (a company offering a wide range of financial services e.g. stock, insurance and real-estate brokerage) providing both banking and financial services through a single window.
- As per the World Bank, "In Universal Banking, large banks operate extensive network of branches, provide many different services, hold several claims on firms(including equity and debt) and participate directly in the Corporate Governance of firms that rely on the banks for funding or as insurance underwriters".
- Universal banking, popular in developed countries, offers one-stop shopping for all financial products and services. A wide range of financial services such as commercial banking investment banking, development banking and insurance are available to the customer under one roof. Investment products like savings accounts, certificates of deposits, mutual funds, credit cards and loans are within the reach of the customer.

## Islamic Banking

- Islamic or Sharia banking is a finance system based on the principles of not charging interest, which is prohibited under Islam.
- Islamic banking is a banking system in accordance with the Shariat. In Islam, money has no intrinsic value – money, therefore, cannot be sold at a profit and is permitted to be used as per shariat only.
- The Islamic Law or Shariat prohibits paying any fee for renting of money (called riba) for specific periods of time.

## Merchant Banking

- Merchant Banking is a combination of Banking and consultancy services.
- It provides consultancy to its clients for financial, marketing, managerial and legal matters. Consultancy means to provide advice, guidance and service for a fee.
- Ministry Of Finance in India defines Merchant Banker as “any person who is engaged in the business of issue management either by making arrangements regarding selling, buying, or subscribing to the securities as manager, consultant, adviser in relation to such an issue management”.
- In general the merchant banks are the financial institution which provides financial services, solutions, & advice to corporate houses.

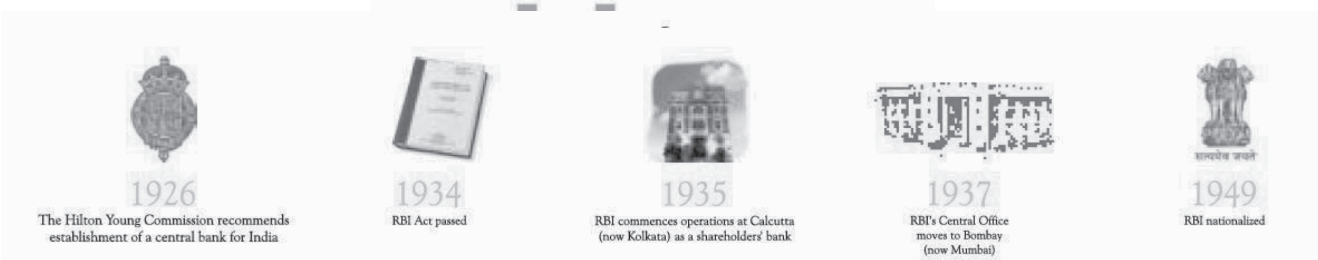
# Chapter 3

# RBI and Its Functions

## All about the Formation of RBI

- RBI is the central bank of India. It is also known as the banker's Bank.
- The origins of RBI can be traced to 1926, when the Royal Commission on Indian Currency and Finance – also known as the Hilton-Young Commission – recommended the creation of a central bank for India to separate the control of currency and credit from the Government and to augment banking facilities throughout the country.
- RBI Act of 1934 established the Reserve Bank and it started its operations in 1935.
- The Central Office of the Reserve Bank was initially established in Calcutta but was permanently moved to Mumbai in 1937.
- Starting as a private shareholders' bank, the Reserve Bank was nationalised in 1949. It aimed at achieving coordination between the policies of the government and those of the central bank.

## Origins of the Reserve Bank of India




- **1926:** The Royal Commission on Indian Currency and Finance recommended creation of a central bank for India.
- **1927:** A bill to give effect to the above recommendation was introduced in the Legislative Assembly, but was later withdrawn due to lack of agreement among various sections of people.
- **1933:** The White Paper on Indian Constitutional Reforms recommended the creation of a Reserve Bank. A fresh bill was introduced in the Legislative Assembly.
- **1934:** The Bill was passed and received the Governor General's assent
- **1935:** The Reserve Bank commenced operations as India's central bank on April 1 as a private shareholders' bank with a paid up capital of rupees five crore (rupees fifty million).
- **1942:** The Reserve Bank ceased to be the currency issuing authority of Burma (now Myanmar).
- **1947:** The Reserve Bank stopped acting as banker to the Government of Burma.
- **1948:** The Reserve Bank stopped rendering central banking services to Pakistan.
- **1949:** The Government of India nationalised the Reserve Bank under the Reserve Bank (Transfer of Public Ownership) Act, 1948.

## RBI as on Organisation

- The Central Board of Directors is at the top of the Reserve Bank's organisational structure. These are appointed by the Government under the provisions of the Reserve Bank of India Act, 1934.
- The Governor is the Reserve Bank's chief executive. It supervises and directs the affairs and business of the RBI. The management team also includes Deputy Governors and Executive Directors.
- The Central Government nominates fourteen Directors on the Central Board, including one Director each from the four Local Boards. The other ten Directors represent different sectors of the economy.
- All these appointments are made for a period of four years.
- Govt. also nominates one Government official as a Director representing the Government, who is usually the Finance Secretary to the Government of India and remains on the Board 'during the pleasure of the Central Government'.
- The Reserve Bank Governor and a maximum of four Deputy Governors are also ex officio Directors on the Central Board.

## Subsidiaries of the RBI

The fully owned subsidiaries of RBI are as follows:

a) **Deposit Insurance and Credit Guarantee Corporation of India (DICGC)**
b) **Bharatiya Reserve Bank Note Mudran Private Limited (BRBNMPL)**
**c)** **National Housing Bank (NHB)**

## A Brief on Deposit Insurance and Credit Guarantee Corporation of India (DICGC)

- With a view to integrating the functions of deposit insurance and credit guarantee, the Deposit Insurance Corporation and Credit Guarantee Corporation of India were merged and the present Deposit Insurance and Credit Guarantee Corporation (DICGC) came into existence on July 15, 1978.
- It was established under the DICGC Act 196.
- It insures all deposits (such as savings, fixed, current,
- and recurring deposits) with eligible banks except some deposits that we will study in the chapter related to DICGC.

## National Housing Bank (NHB)

NHB was set up on July 9, 1988 under the National Housing Bank Act, 1987 as a wholly-owned subsidiary of the Reserve Bank to act as an apex level institution for housing.

### Bharatiya Reserve Bank Note Mudran Private Limited (BRBNMPL)

- RBI established BRBNMPL in February 1995 as a wholly-owned subsidiary to augment the production of bank notes in India and to enable bridging of the gap between supply and demand for bank notes in the country.
- It has been registered as a Public Limited Company under the Companies Act, 1956 with its Registered and Corporate Office situated at Bengaluru.

### The Current Office Holders

**Dr. Urjit R. Patel | Governor**
**Shri N. S. Vishwanathan | Deputy Governor**
**Dr. Viral V. Acharya | Deputy Governor**
**Shri B.P. Kanungo | Deputy Governor**
**Mahesh Kumar Jain | Deputy Governor**

## Functions of the RBI

**Monetary Authority**

- Formulates, implements and monitors the monetary policy.
- Objective: maintaining price stability while keeping in mind the objective of growth.

**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 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.

**Other Functions of RBI**

- **Also, RBI** performs a wide range of promotional functions to support national objectives.
- **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.

**What is Financial Supervision by RBI with the help of BFS?**

RBI performs the function of Financial supervision under the guidance of the Board for Financial Supervision (BFS). This was constituted in November 1994 as a committee of the Central Board of Directors of the Reserve Bank of India. The objective is to undertake consolidated supervision of the financial sector comprising commercial banks, financial institutions and non-banking finance companies.

The Board is constituted by co-opting four Directors from the Central Board as members for a term of two years and is chaired by the Governor.

## Other important points related to RBI

- It has 27 regional offices, most of them in state capitals and 04 Sub-offices.
- It has five training establishments
  - **a)** Two, namely, College of Agricultural Banking and Reserve Bank of India Staff College are part of the Reserve Bank.
  - **b)** Others are autonomous, such as, National Institute for Bank Management, Indira Gandhi Institute for Development Research (IGIDR), Institute for Development and Research in Banking Technology (IDRBT) etc.

**The acts administered by Reserve Bank of India**

- Reserve Bank of India Act, 1934
- Public Debt Act, 1944/Government Securities Act, 2006
- Government Securities Regulations, 2007
- Banking Regulation Act, 1949
- Foreign Exchange Management Act, 1999
- Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (Chapter II)
- Credit Information Companies (Regulation) Act, 2005
- Payment and Settlement Systems Act, 2007
- Payment and Settlement Systems Regulations, 2008 and Amended up to 2011 and BPSS Regulations, 2008
- The Payment and Settlement Systems (Amendment) Act, 2015 - No. 18 of 2015
- Factoring Regulation Act, 2011

# Chapter 4 Monetary Policy of RBI

Monetary policy refers to the policy of the RBI with regard to the use of monetary instruments under its control to achieve the goals specified in the RBI Act,1934.

## What are the goals of the Monetary Policy of RBI?

- Primary objective is to maintain price stability while keeping in mind the objective of growth.
- In May 2016, RBI Act, 1934 was amended to provide a statutory basis for the implementation of the flexible inflation targeting framework.
- The Act also provides for the inflation target to be set by the Government of India, in consultation with the Reserve Bank, once in every five years.

## What is the Monetary Policy Framework?

- Monetary Policy framework aims at setting the policy (repo) rate based on an assessment of the current and evolving macroeconomic situation; and modulation of liquidity conditions to anchor money market rates at or around the repo rate.
- Repo rate changes transmit through the money market to the entire the financial system, which, in turn, influences aggregate demand – a key determinant of inflation and growth.

## The Monetary Policy Process

- Section 45ZB of the amended RBI Act, 1934 also provides for an empowered six-member monetary policy committee (MPC) to be constituted by the Central Government by notification in the Official Gazette.
- Accordingly, the Central Government in September 2016 constituted the MPC as under:
  1. Governor of the Reserve Bank of India – Chairperson, ex officio;
  2. Deputy Governor of the Reserve Bank of India, in charge of Monetary Policy – Member, ex officio;
  3. One officer of the Reserve Bank of India to be nominated by the Central Board – Member, ex officio;
  4. Shri Chetan Ghate, Professor, Indian Statistical Institute (ISI) – Member;
  5. Professor Pami Dua, Director, Delhi School of Economics – Member; and
  6. Dr. Ravindra H. Dholakia, Professor, Indian Institute of Management, Ahmedabad – Member.

**Note:**

- Members referred to at 4 to 6 above, will hold office for a period of four years or until further orders, whichever is earlier.
- The MPC determines the policy interest rate required to achieve the inflation target.
- Reserve Bank's Monetary Policy Department (MPD) assists the MPC in formulating the monetary policy.
- Financial Markets Operations Department (FMOD) operationalises the monetary policy, mainly through day-to-day liquidity management operations.

## Important Points related to Monetary Policy Making

Under the amended RBI Act, the monetary policy making is as under:

- The MPC is required to meet at least four times in a year.
- The quorum for the meeting of the MPC is four members.
- Each member of the MPC has one vote, and in the event of an equality of votes, the Governor has a second or casting vote.

## What are the Instruments of Monetary Policy?

- There are several direct and indirect instruments that are used for implementing monetary policy.

**Repo Rate**

- The (fixed) interest rate at which the Reserve Bank provides overnight liquidity to banks against the collateral of government & other approved securities under the liquidity adjustment facility (LAF).

**Reverse Repo Rate**

The (fixed) interest rate at which the Reserve Bank absorbs liquidity, on an overnight basis, from banks against the collateral of eligible government securities under the LAF.

**Liquidity Adjustment Facility (LAF):**

- RBI's liquidity adjustment facility/LAF helps banks to adjust their daily liquidity mismatches.
- It has two components which are repo (repurchase agreement) and reverse repo.
- When banks need liquidity to meet its daily requirement, they borrow from RBI through repo. The rate at which they borrow fund is called the repo rate. When banks are flush with fund, they park with RBI through the reverse repo mechanism at reverse repo rate.

**Marginal Standing Facility (MSF)**

- A facility under which scheduled commercial banks can borrow additional amount of overnight money from the Reserve Bank by dipping into their Statutory Liquidity Ratio (SLR) portfolio up to a limit at a penal rate of interest.
- This provides a safety valve against unanticipated liquidity shocks to the banking system.

**Corridor**

- The MSF rate and reverse repo rate determine the corridor for the daily movement in the weighted average call money rate.

**Bank Rate**

- It is the rate at which the Reserve Bank is ready to buy or rediscount bills of exchange or other commercial papers for long terms. The Bank Rate is published under Section 49 of the Reserve Bank of India Act, 1934.
- This rate has been aligned to the MSF rate and, therefore, changes automatically as and when the MSF rate changes alongside policy repo rate changes.

**Cash Reserve Ratio (CRR)**

- The average daily balance that a bank is required to maintain with the Reserve Bank as a share of such per cent of its Net demand and time liabilities (NDTL) that the Reserve Bank may notify from time to time in the Gazette of India.

**Statutory Liquidity Ratio (SLR)**

- The share of NDTL that a bank is required to maintain in safe and liquid assets, such as, unencumbered government securities, cash and gold.
- Changes in SLR often influence the availability of resources in the banking system for lending to the private sector.

**Open Market Operations (OMOs)**

- These include both, outright purchase and sale of government securities, for injection and absorption of durable liquidity, respectively.

**Market Stabilisation Scheme (MSS)**

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

# Chapter 5 — Different Stages of Development of Indian Banking

- Indian Banking System starts with **the Indigenous Banking System** which was mainly carried by the businessmen called Sharoffs, Seths, Sahukars, Mahajans, Chettis, etc. It couldn't be developed because they were not able to obtain deposits from the public.
- **Modern banking** in India originated in the last decades of the 18th century. The first banks were The **General Bank of India which started in 1786, and the Bank of Hindustan.**
- Thereafter, **three presidency banks namely the Bank of Bengal** (this bank was originally started in the year 1806 as Bank of Calcutta and then in the year 1809 became the Bank of Bengal), the Bank of Bombay and the Bank of Madras, were set up. These three banks were merged in 1925 to form the Imperial Bank of India.
- **The Allahabad Bank,** established in 1865, is the oldest survived Joint Stock bank in India.
- **Punjab National Bank,** established in Lahore in 1895, which is now one of the largest banks in India.
- A major landmark in Indian banking history took place in **1934 when a decision was taken to establish 'Reserve Bank of India'** which started functioning in 1935. Since then, RBI, as a central bank of the country, has been regulating banking system.
- In 1949, to have close integration between policies of the Reserve Bank and those of the Government, it was decided to **nationalize the Reserve Bank immediately after the independence of the country.**
- To streamline the functioning of commercial banks, the **Government of India enacted the Banking Companies Act,1949 which was later changed as the Banking Regulation Act 1949.** RBI acts as a regulator of banks, banker to the Government and banker's bank.
- To serve the economy in general and the rural sector in particular, **the All India Rural Credit Survey Committee recommended the creation of a state-partnered and state-sponsored bank by taking over the Imperial Bank of India, and integrating with it, the former state-owned or state-associate banks. An act was accordingly passed in Parliament in May 1955 and the State Bank of India was constituted on 1 July 1955.** Later, the State Bank of India (Subsidiary Banks) Act was passed in 1959, enabling the State Bank of India to take over eight former State-associated banks as its subsidiaries (later named Associates).
- Indian Banking System witnessed a major revolution in the year **1969 when 14 major commercial banks in the private sector were nationalized on 19th July,1969.** Most of these banks having deposits of above Rs. 50 crores.
- In **1980, another six more commercial banks with deposits of above Rs. 200 crores were nationalized.**

## Regional Rural Banks

- In 1975, a new set of banks **called the Regional Rural Banks, were setup based on the recommendations of a working group headed by Shri Narasimham,** to serve the rural population in addition to the banking services offered by the co-operative banks and commercial banks in rural areas.

## New Private Sector Banks

- In 1991, the Narasimham committee recommended that banks should increase operational efficiency, strengthen the supervisory control over banks and the new players should be allowed to create a competitive environment. Based on the recommendations, **new private banks were allowed to start functioning.**

## History of Banking Sector in India

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- By 1930, the number of commercial banks increased to 107 with the Imperial Bank of India still dominating the Indian banking sector.
- Indian Central Banking Enquiry Committee was set up in 1929 to survey extensively the problems of Indian banking, observed that a central bank be established for the country.
- Reserve Bank of India Act 1934 was enacted paving the way for the setting up of the Reserve Bank of India. The issue of bank failures and the need for catering to the requirements of agriculture were the two prime reasons for the establishment of the Reserve Bank. The banking sector came under the purview of the Reserve Bank in 1935.
- The Government, therefore, first implemented the exercise of nationalisation of the Imperial Bank of India with the objective of "extension of banking facilities on a large scale, more particularly in the rural and semi-urban areas, and for diverse other public purposes". The Imperial Bank of India was converted into the State Bank of India in 1955 with the enactment of the State Bank of India Act, 1955.

## Major Controls/Schemes introduced in Banking Sector from 1968

| Year | Reform Introduced |
|---|---|
| **1962** | In order to ensure the safety of deposits of small depositors in banks in India, Deposit Insurance Corporation Act, 1961 was enacted. Deposit Insurance Corporation of India was established in January 1962. |
| **1963** | Agricultural Refinance Corporation (ARC) was set up by the Act of July 1, 1963. Its objective was to refinance central land mortgage banks, State cooperative banks and scheduled commercial banks. |
| **1965** | Credit Authorisation Scheme(CAS) was introduced, under which the commercial banks were required to obtain prior permission of RBI for sanctioning any fresh working capital limits above the prescribed norm which was revised from time to time. |
| **1968** | National Credit Council (NCC) set up in Feb. 1968 to assist RBI & Govt. to allocate credit according to plan priorities. |
| **1969** | Fourteen banks with deposits of over Rs.50 crores were nationalised. |
| **1969** | Lead Bank Scheme was introduced to mobilise deposits on a massive scale throughout the country and also for stepping up lending to the weaker sections. |
| **1972** | Concept of Priority Sector was formalised. Specific targets were set out in Nov 1974 for public sector banks & in Nov. 1978 for private sector banks. |
| **1972** | Differential Rate of Interest (DRI) Scheme was instituted to cater to the needs of the weaker sections of the society and for their upliftment. |
| **1980** | Six Banks with demand and time liabilities greater than Rs.200 crore as on March 14, 1980, were nationalised on April 15, 1980. |
| **1994** | Board for Financial Supervision (BFS) was set up within RBI to attend exclusively to supervisory functions & provide effective supervision in an integrated manner over the banking system, financial institutions, NBFCs & other para-banking financial institutions. |
| **1995** | Banking Ombudsman Scheme was introduced under the provisions of the BR Act, 1949. |
| **2006** | Banking Codes and Standards Board of India (BCSBI) was set up by Reserve Bank in order to provide for voluntary registration of banks committing to provide customer services as per the agreed standards and codes. |

The roadmap for the presence of foreign banks in India was drawn up in **February 2005.**

Banks were advised to introduce a facility of 'no frills' account with nil or low minimum balances **in November 2005.**

Recovery of Debts Due to Banks and Financial Institutions Act **was enacted in 1993,** which provided for the establishment of tribunals for expeditious adjudication and recovery of non-performing loans.

Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act**, 2002 was enacted in March, 2002.**

# Chapter 6 Nationalization of Banks

- Before 1949, all the commercial banks in India were exclusively owned, controlled and managed by private entrepreneurs. The process of **nationalisation of banks began** with the nationalization of RBI on 1st Jan 1949, with the passing of Reserve Bank (Transfer of Public Ownership) Act, 1948.
- RBI was nationalized to ensure greater coordination of monetary, economic and fiscal policies in independent India.

## Nationalization of SBI

- The first step towards the nationalisation of commercial banks started with **the nationalisation of the Imperial Bank of India as the State Bank of India on 1 July 1955.**
- After this the 7 State-associated banks were nationalised as subsidiaries of the State Bank of India in 1959.
- The 7 associate banks were– the State Bank of Hyderabad, the State Bank of Jaipur and Bikaner, the State Bank of Travancore, the State Bank of Mysore, the State Bank of Patiala, the State Bank of Indore, and the State Bank of Saurashtra.

## Nationalization of Banks in 1969

On 19th July 1969, 14 major commercial banks with deposits exceeding Rs. 50 crores were nationalized.

1. Allahabad Bank
2. Bank of Baroda
3. Bank of India
4. Bank of Maharashtra
5. Canara Bank
6. Central Bank of India
7. Dena Bank
8. Indian Bank
9. Indian Overseas Bank
10. Punjab National Bank
11. Syndicate Bank
12. Union Bank of India
13. United Bank of India
14. United Commercial Bank (now known as UCO bank)

## Nationalization of Banks in 1980

On 15th April 1980, 6 more commercial banks were nationalized which were having the deposits above Rs.200 crores. The banks were:

1. Andhra Bank
2. Corporation Bank
3. New Bank of India
4. Punjab and Sind Bank
5. Oriental Bank of Commerce
6. Vijaya Bank

**Note:** New Bank of India was merged with Punjab National Bank in 1993.

## An Important Point

- Because of the nationalization, the major segment of the banking sector came under the control of the Government.
- The nationalization of banks imparted major impetus to branch expansion in unbanked, rural and semi-urban areas, which in turn resulted in huge deposit mobilization, thereby giving boost to the overall savings rate of the economy.
- It also resulted in scaling up of lending to agriculture and its allied sectors.

## What were the possible OBJECTIVES of Nationalization?

- **The Banking Companies (Acquisition and Transfer of Undertakings) Act, 1970 under which 14 banks were nationalised with effect from 19 July 1969** spelt the main objective as "to serve better the needs of development of the economy in conformity with national policy and objectives and for matters connected therewith or incidental thereto".
- These objectives included:
- To mobilise the savings of the people to the largest possible extent and to utilise them for productive purposes.
- To ensure the operations of the banking system for a larger social purpose and to subject them to close public regulation.
- To meet the legitimate credit needs of private sector industry and trade, big or small.
- To meet in an increasing manner the needs of productive sectors of the economy and in particular those of farmers, small scale industrialists and self-employed professional groups.
- To actively foster the growth of the new and progressive entrepreneurs and credit fresh opportunities for hitherto neglected and backward areas in different parts of the country
- To curb the use of bank credit for speculative and other unproductive purposes;
- To provide adequate training and reasonable terms of service to bank staff
- To considerably expand the branch network 0f bank in all parts of the country, and
- To reduce regional and sectoral imbalance in banking and through that in economic development.

## SBI Merger with its Associates

- Five associates & the Bharatiya Mahila Bank became part of the State Bank of India (SBI) on 1st April 2017, catapulting the country's largest lender to among the top 50 banks in the world.
- State Bank of Bikaner and Jaipur (SBBJ), State Bank of Hyderabad (SBH), State Bank of Mysore (SBM), State Bank of Patiala (SBP) and State Bank of Travancore (SBT), besides Bharatiya Mahila Bank (BMB), merged with SBI with effect from April 1,2017.
- The merged entity resulted in the deposit base of more than Rs 26 lakh crore and advances level of □18.50 lakh crore.
- Post-merger, the bank will rationalise its branch network by relocating some of the branches to maximise reach. This will help the bank optimise its operations and improve profitability, she said.

# Chapter 7 Financial Markets in India

- Financial System in a country comprises of various intermediaries who plays crucial roles in sourcing out the funds from the surplus segment & deploying such funds to needy segment.
- The intermediaries are banks, financial institutions, mutual funds, etc.

## Money Market

- Money market is a market for short-term financial assets that are close substitutes of money.
- The most important feature of a money market instrument is that it is liquid and can be turned into money quickly at low cost.
- The call/notice/Term money market forms an important segment of the Indian Money Market.
- **Under call money market,** funds are transacted on an overnight basis and **under notice money market,** funds are transacted for a period between 2 days and 14 days & **under the Term Money Market,** funds are funds are transacted for a period between 15 days and 365 days.
- Scheduled commercial banks (excluding RRBs), co-operative banks (other than Land Development Banks) and Primary Dealers (PDs), **are permitted to participate in call/notice money market both as borrowers and lenders.**

## What are the Money Market Instruments?

**Commercial Paper**

- Commercial Paper (CP) is an unsecured money market instrument issued in the form of a promissory note.
- CP, as a privately placed instrument, was introduced in India in 1990 with a view to enable highly rated corporate borrowers to diversify their sources of short-term borrowings and to provide an additional instrument to investors.
- Primary Dealers (PDs) and all-India financial institutions (FIs) were also permitted to issue CP to enable them to meet their short-term funding requirements.

**Wo can issue CP?**

- Companies, PDs and FIs are permitted to raise short term resources through CP.
- A company would be eligible to issue CP provided:
  - **a)** the tangible net worth of the company, as per the latest audited balance sheet, is not less than Rs.4 crore;
  - **b)** the company has been sanctioned working capital limit by bank/s or FIs; and
  - **c)** the borrowal account of the company is classified as a Standard Asset by the financing bank/institution.

**Important Key Points related to CP**

- CP shall be issued in the form of a promissory note.
- CP shall be issued in denominations of Rs. 5 lakh and multiples thereof.
- CP shall be issued at a discount to face value as may be determined by the issuer.
- CP shall be issued for maturities between a minimum of 7 days and a maximum of up to one year from the date of issue.

**Certificates of Deposit**

- Certificate of Deposit (CD) is a negotiable money market instrument and issued in dematerialised form or as a Usance Promissory Note against funds deposited at a bank or other eligible financial institution for a specified time period.

**Who can issue CDs?**

- CDs can be issued by
  - **a)** scheduled commercial banks {excluding Regional Rural Banks and Local Area Banks}
  - **b)** select All-India Financial Institutions (FIs) that have been permitted by RBI to raise short-term resources within the umbrella limit fixed by RBI.

**Important Key Points related to CDs**

- Minimum amount of a CD should be Rs.1 lakh, and in multiples of Rs. 1 lakh thereafter.
- Maturity period of CDs issued by banks should not be less than 7 days and not more than one year, from the date of issue.
- FIs can issue CDs for a period not less than 1 year and not exceeding 3 years from the date of issue.
- CDs may be issued at a discount on face value.
- Banks / FIs should issue CDs only in dematerialised form.

**Non-Convertible Debentures (NCDs) of original or initial maturity up to one year**

- Non-Convertible Debenture (NCD) means a debt instrument issued by a corporate (including NBFCs) with original or initial maturity up to one year and issued by way of private placement.
- "Corporate" means a company as defined in the Companies Act, 2013 (including NBFCs) and a corporation established by an act of any Legislature.

**Eligibility to issue NCDs**

A corporate shall be eligible to issue NCDs if it fulfills the following criteria, namely,

- the corporate has a tangible net worth of not less than Rs.4 crore, as per the latest audited balance sheet;
- the corporate has been sanctioned working capital limit or term loan by bank/s or all-India financial institution/s; and
- the borrowal account of the corporate is classified as a Standard Asset by the financing bank/s or institution/s.
- NCDs shall not be issued for maturities of less than 90 days from the date of issue.
- NCDs may be issued in denominations with a minimum of Rs.5 lakh (face value) and in multiples of Rs.1 lakh.

**Important Definitions in One Line**

- "**Call Money"** means deals in overnight funds.
- **"Notice Money"** means deals in funds for 2 – 14 days.
- **"Term Money"** means deals in funds for 15 days-1 year.
- **"Primary Dealer (PD)"** means a financial institution which holds a valid letter of authorisation as a PD issued by the Reserve Bank.
- **'Issuing and Paying Agent (IPA)'** means a Scheduled Bank acting as an IPA.
- **'CRA'** means a Credit Rating Agency registered with Securities and Exchange Board of India.

## What is a Government Security (G-Sec)?

- It is a tradeable instrument issued by the Central Government or the State Governments.
- It acknowledges the Government's debt obligation.
- These securities can be short term (usually called treasury bills, with original maturities of less than one year) or long term (usually called Government bonds or dated securities with original maturity of one year or more).
- G-Secs carry practically no risk of default and, hence, **are called risk-free gilt-edged instruments.**
- **Note:** In India, the Central Government issues both, treasury bills and bonds or dated securities while the State Governments issue only bonds or dated securities, which are called the State Development Loans (SDLs).

**Treasury Bills (T-bills)**

- Treasury bills or T-bills, which are money market instruments, are short term debt instruments issued by the Government of India and are presently issued in three tenors, namely, 91 day, 182 day and 364 day.
- These are zero coupon securities and pay no interest.
- They are issued at a discount and redeemed at the face value at maturity.

**Cash Management Bills (CMBs)**

- In 2010, Government of India, in consultation with RBI introduced a new short-term instrument, known as Cash Management Bills (CMBs), to meet the temporary mismatches in the cash flow of the Government of India.
- The CMBs have the generic character of T-bills but are issued for maturities less than 91 days.

**Dated G-Secs**

- Dated G-Secs are securities which carry a fixed or floating coupon (interest rate) which is paid on the face value, on half-yearly basis.
- Generally, the tenor of dated securities ranges from 5 years to 40 years.

**Note:**

- The Public Debt Office (PDO) of the Reserve Bank of India acts as the registry / depository of G-Secs and deals with the issue, interest payment and repayment of principal at maturity.

**What are the Types of Government Bonds?**

- **Fixed Rate Bonds:** These are bonds on which the coupon rate is fixed for the entire life (i.e. till maturity) of the bond.
- **Floating Rate Bonds (FRB):** FRBs are securities which do not have a fixed coupon rate. FRBs were first issued in September 1995 in India.
- **Zero Coupon Bonds:** Zero coupon bonds are bonds with no coupon payments.
- **Capital Indexed Bonds:** These are bonds, the principal of which is linked to an accepted index of inflation with a view to protecting the Principal amount of the investors from inflation.
- **Inflation Indexed Bonds (IIBs):** IIBs are bonds wherein both coupon flows and Principal amounts are protected against inflation. The inflation index used in IIBs may be Whole Sale Price Index (WPI) or Consumer Price Index (CPI).
- **STRIPS (Separate Trading of Registered Interest and Principal of Securities):** STRIPS are the securities created by way of separating the cash flows associated with a regular G-Sec i.e. each semi-annual coupon payment and the final principal payment to be received from the issuer, into separate securities. They are essentially Zero-Coupon Bonds (ZCBs).

**Sovereign Gold Bond (SGB)**

- SGBs are unique instruments, prices of which are linked to commodity price viz Gold.
- SGBs are denominated in multiples of gram(s) of gold with a basic unit of 1 gram.
- The tenor of the SGB is for a period of 8 years with exit option from 5th year to be exercised on the interest payment dates.

## Other Important Points related to Government Securities

**What are the State Development Loans (SDLs)?**

- State Governments also raise loans from the market which are called SDLs.
- SDLs are dated securities issued through normal auction similar to the auctions conducted for dated securities issued by the Central Government.
- Interest is serviced at half-yearly intervals and the principal is repaid on the maturity date.

**What are Open Market Operations (OMOs)?**

- OMOs are the market operations conducted by the RBI by way of sale/ purchase of G-Secs to/ from the market with an objective to adjust the rupee liquidity conditions in the market on a durable basis.
- When the RBI feels that there is excess liquidity in the market, it resorts to sale of securities thereby sucking out the rupee liquidity.
- Similarly, when the liquidity conditions are tight, RBI may buy securities from the market, thereby releasing liquidity into the market.

**What is meant by repurchase (buyback) of G-Secs?**

- Repurchase (buyback) of G-Secs is a process whereby the Government of India and State Governments buy back their existing securities, by redeeming them prematurely, from the holders.
- The objectives of buyback can be reduction of cost (by buying back high coupon securities), reduction in the number of outstanding securities and improving liquidity in the G-Secs market (by buying back illiquid securities) and infusion of liquidity in the system.

**What is Liquidity Adjustment Facility (LAF)?**

- LAF is a facility extended by RBI to the scheduled commercial banks (excluding RRBs) and PDs to avail of liquidity in case of requirement or park excess funds with RBI in case of excess liquidity on an overnight basis against the collateral of G-Secs including SDLs.
- Basically, LAF enables liquidity management on a day to day basis.

**How does Trading in G-Secs take place?**

The securities can be traded in secondary market either through

**(i) Negotiated Dealing System-Order Matching (NDS-OM)**
**(ii) Over the Counter (OTC)**
**(iii) NDS-OM-Web.**

**NDS-OM**

- In August, 2005, RBI introduced an anonymous screen based order matching module called NDS-OM.
- This is an order driven electronic system, where the participants can trade anonymously by placing their orders on the system or accepting the orders already placed by other participants.

**Over the Counter (OTC)/ Telephone Market**

- In this market, a participant, who wants to buy or sell a G-Sec, may contact a bank / PD/financial institution either directly or through a broker & negotiate price and quantity of security.
- Such negotiations are done on telephone and a deal may be struck if both counterparties agree on the amount and rate.

**NDS-OM-Web**

- RBI has launched NDS-OM-Web on June 29, 2012 for facilitating direct participation of gilt account holders (GAH) on NDS-OM through their primary members (PM) (as risk controller only and not having any role in pricing of trade).
- The GAH have access to the same order book of NDS-OM as the PM.
- GAH are in a better position to control their orders (place/modify/cancel/hold/release) and have access to real time live quotes in the market.

## Who are the major players in the G-Secs market?

- Major players in the G-Secs market include commercial banks and PDs besides institutional investors like insurance companies.
- Other participants include co-operative banks, regional rural banks, mutual funds, provident and pension funds.
- Foreign Portfolio Investors (FPIs) are allowed to participate in the G-Secs market within the quantitative limits prescribed from time to time.
- Corporates also buy/ sell the G-Secs to manage their overall portfolio.

## Role of the Clearing Corporation of India Limited (CCIL)

- The CCIL is the clearing agency for G-Secs. It acts as a Central Counter Party (CCP) for all transactions in G-Secs by interposing itself between two counterparties.
- In effect, during settlement, the CCP becomes the seller to the buyer and buyer to the seller of the actual transaction.
- All outright trades undertaken in the OTC market and on the NDS-OM platform are cleared through the CCIL.

## What are the role and functions of FIMMDA?

- The Fixed Income Money Market and Derivatives Association of India (FIMMDA), an association of Scheduled Commercial Banks, Public Financial Institutions, Primary Dealers and Insurance Companies was incorporated as a Company under section 25 of the Companies Act,1956 on June 3, 1998.
- FIMMDA is a voluntary market body for the bond, money and derivatives markets. FIMMDA has members representing all major institutional segments of the market.
- The membership includes Nationalized Banks such as State Bank of India, its associate banks and other nationalized banks; Private sector banks such as ICICI Bank, HDFC Bank; Foreign Banks such as Bank of America, Citibank, Financial institutions such as IDFC, EXIM Bank, NABARD, Insurance Companies like Life Insurance Corporation of India (LIC), ICICI Prudential Life Insurance Company, Birla Sun Life Insurance Company and all Primary Dealers.
- FIMMDA represents market participants and aids the development of the bond, money and derivatives markets.
- It acts as an interface with the regulators on various issues that impact the functioning of these markets.
- It also undertakes developmental activities, such as, introduction of benchmark rates and new derivatives instruments, etc.

## What is the Capital Market?

- It is a market where investors/ buyers, and issuers of securities/ sellers engage in issue/subscription/ trade of financial securities like shares, bonds etc.
- In this market, the long-term securities are traded.
- It consists of two types which are the Primary market and Secondary market.

**Primary Market**

- In this market, securities (shares, debentures, bonds etc) are offered to the public for the first time for subscription with a view to raise capital fund.

- In the primary market, issues are classified into public, rights or preferential issues (also known as private placements).
- The Public issues can be classified into Initial Public Offerings (IPOs) and Further/Follow-on Public Offerings (FPOs).
  **a)** When a company makes either a fresh issue of shares or an offer for sale of its existing shares or both for the first time to the public, it is called IPO.
  **b)** When a company which is already a listed company, either makes a fresh issue of securities to the public or an offer for sale to the public through an offer document, it is known as FPO.
- Rights Issue (RI) is one, when a listed company proposes to issue fresh securities to its existing shareholders as on a record date.
- A private placement is an issue of shares or of convertible securities by a company, to a select group of persons under the provisions of Section 81 of Indian Companies Act, 1956, which is neither a public issue nor a rights issue.

**Secondary Market**

- Once the securities are issued in the primary market and/or listed in the Stock Exchange, these can be traded in a market called the Secondary Market.
- It is a platform for the investors to buy and sell the securities.
- Secondary Market refers to a market where securities are traded after being initially offered to the public in the primary market and/or listed on the Stock Exchange.

## What are the Instruments of Capital Market?

**Equity:** The ownership interest in a company of holders of its common and preferred stock.
**Cumulative Preference Shares:** A type of preference shares on which dividend accumulates if remains unpaid.
**Cumulative Convertible Preference Shares:** A type of preference shares where the dividend payable on the same accumulates, if not paid.
**Debentures:** Bonds issued by a company bearing a fixed rate of interest usually payable on specific dates and principal amount repayable on particular date on redemption of the debentures.

## What is STT?

- Securities Transaction Tax (STT) is a tax being levied on all transactions done on the stock exchanges at rates
- prescribed by the Central Government from time to time.
- The Government of India notified the Securities Transaction Tax Rules, 2004 and STT came into effect from October 1, 2004.