

BANKING AND INSURANCE

UNIT 3

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BANK CAPITAL

Bank capital is the difference between a bank's assets and its liabilities, and it represents the net worth of the bank or its equity value to investors. The asset portion of a bank's capital includes cash, government securities, and interest-earning loans (e.g., mortgages, letters of credit, and inter-bank loans). The liabilities section of a bank's capital includes loan-loss reserves and any debt it owes. A bank's capital can be thought of as the margin to which creditors are covered if the bank would liquidate its assets.

How Bank Capital Works

Bank capital represents the value of a bank's equity instruments that can absorb losses and have the lowest priority in payments if the bank liquidates. While bank capital can be defined as the difference between a bank's assets and liabilities, national authorities have their own definition of regulatory capital. The main banking regulatory framework consists of international standards enacted by the Basel Committee on Banking Supervision through international accords of Basel I, Basel II, and Basel III. These standards provide a definition of the regulatory bank capital that market and banking regulators closely monitor. Because banks serve an important role in the economy by collecting savings and channelling them to productive uses through loans, the banking industry and the definition of bank capital are heavily regulated. While each country can have its own requirements, the most recent international banking regulatory accord of Basel III provides a framework for defining regulatory bank capital.

Regulatory Capital Classifications

According to Basel III, regulatory bank capital is divided into tiers. These are based on subordination and a bank's ability to absorb losses with a sharp distinction of capital instruments when it is still solvent versus after it goes bankrupt. Common equity tier 1 (CET1) includes the book value of common shares, paid-in capital, and retained earnings less goodwill and any other intangibles. Instruments within CET1 must have the highest subordination and no maturity.

Tier 1 Capital

Tier 1 capital includes CET1 plus other instruments that are subordinated to subordinated debt, and have no fixed maturity, no embedded incentive for redemption, and for which a bank can cancel dividends or coupons at any time. Tier 1 capital consists of shareholders' equity and retained earnings. Tier 1 capital is intended to measure a bank's financial health and is used when a bank must absorb losses without ceasing business operations. Tier 1 capital is the primary funding source of the bank. Typically, it holds nearly all of the bank's accumulated funds. These funds are generated specifically to support banks when losses are absorbed so that regular business functions do not have to be shut down. Under Basel III, the minimum tier 1 capital ratio is 8.5%, which is calculated by dividing the bank's tier 1 capital by its total risk-based assets. For example, assume there is a bank with tier 1 capital of \$176.263 billion and risk-weighted assets worth \$1.243 trillion. The bank's tier 1 capital ratio for the period was $\$176.263 \text{ billion} / \$1.243 \text{ trillion} = 14.18\%$, which meets the minimum Basel III requirement of tier 1 capital of 8.5% and the total capital ratio of 10.5%.

Tier 2 Capital

Tier 2 capital consists of unsecured subordinated debt and its stock surplus with an original maturity of fewer than five years minus investments in non-consolidated financial institution subsidiaries under certain circumstances. The total regulatory capital is equal to the sum of Tier 1 and Tier 2 capital. Tier 2 capital includes revaluation reserves, hybrid capital instruments, subordinated term debt, general loan-loss reserves, and undisclosed reserves. Tier 2 capital is supplementary capital because it is less reliable than tier 1 capital. Tier 2 capital is considered less reliable than Tier 1 capital because it is more difficult to accurately calculate and is composed of assets that are more difficult to liquidate. Under Basel III, the minimum total capital ratio is 10.5%, there is not a specified requirement for tier 2 capital.

CONCEPT OF ECONOMIC MODEL

An economic model is a simplified description of reality, designed to yield hypotheses about economic behaviour that can be tested. An important feature of an economic model is that it is necessarily subjective in design because there are no objective measures of economic outcomes. Different economists will make different judgments about what is needed to explain their interpretations of reality. There are two broad classes of economic models—theoretical and empirical. Theoretical models seek to derive verifiable implications about economic behaviour under the assumption that agents maximize specific objectives subject to constraints that are well defined in the model (for example, an agent's budget). They provide qualitative

answers to specific questions such as the implications of asymmetric information (when one side to a transaction knows more than the other) or how best to handle market failures.

In contrast, empirical models aim to verify the qualitative predictions of theoretical models and convert these predictions to precise, numerical outcomes. For example, a theoretical model of an agent's consumption behaviour would generally suggest a positive relationship between expenditure and income. The empirical adaptation of the theoretical model would attempt to assign a numerical value to the average amount expenditure increases when income increases. Economic models generally consist of a set of mathematical equations that describe a theory of economic behaviour. The aim of model builders is to include enough equations to provide useful clues about how rational agents behave or how an economy works (see box). The structure of the equations reflects the model builder's attempt to simplify reality—for example, by assuming an infinite number of competitors and market participants with perfect foresight. Economic models can be quite simple in practice: the demand for apples, for example, is inversely related to price if all other influences remain constant. The less expensive the apples, the more are demanded. Or models can be rather complex: some models that seek to predict the real level of output of an economy use thousands of complex formulations that go by such names as “nonlinear, interconnected differential equations.”

Economic models can also be classified in terms of the regularities they are designed to explain or the questions they seek to answer. For example, some models explain the economy's ups and downs around an evolving long-run path, focusing on the demand for goods and services without being too exact about the sources of growth in the long run. Other models are designed to focus on structural issues, such as the impact of trade reforms on long-term production levels, ignoring short-term oscillations. Economists also build models to study “what-if” scenarios, such as the impact on the overall economy of introducing a value-added tax.

CONCEPT OF REGULATORY CAPITAL

A bank's capital is simply the difference between its assets and liabilities, i.e., the value of what the bank owners actually own. Because banks use extensive leverage to augment profits, a small decrease in the value of its assets can wipe out the bank's capital, causing it to fail. To lessen the probability of failure, banks must maintain a minimum of capital, called regulatory capital, because the amount that must be maintained, which varies according to the riskiness of the assets, is stipulated by law. Regulatory capital, which includes equity, preferred stock,

subordinated debt, and general reserves, must be sufficient to repay depositors and senior debtholders in the event of a bankruptcy. In the aftermath of the Great Recession, banks have started to issue a new type of bond called contingent convertible bonds (CoCos), which convert to equity when a bank's common equity tier 1 ratio drops below 7%. Barclays has even issued total-loss bonds, so-called because bondholders lose the entire principal if financially triggered. These 10 year bonds were sold for a 7.625% interest rate. CoCos and total-loss bonds lower risk by eliminating the legal obligation to pay interest when the issuing bank becomes financially stressed.

Bank owners generally want lower capital ratios because they increase the return on assets and the return on equity. Banks earn a profit from the net interest margin, which is the difference between the interest rates received on loans and interest rates paid on deposits and short-term debt, so leverage increases profits for a given investment of bank capital. But that also increases risk. Banks have various means of modifying the capital to assets ratio. Banks can reduce capital to assets by paying a higher dividend; buying back company shares, or increase lending that is financed by issuing CDs, bonds, commercial paper, or by attracting more deposits. Banks can increase the capital to assets by reducing dividends; selling new shares; reducing assets by borrowing less or selling off existing loans; by selling securities; or by reducing costs, such as pay, bonuses, and other costs.

Banks must also maintain a minimum liquidity, as measured by the liquidity coverage ratio. While increased capital helps to protect against insolvency, increased liquidity allows banks to weather runs on the bank, freezes in the short term debt markets, and higher credit demands from existing customers.

Liquidity Coverage Ratio = High-Quality Liquid Assets/Total Net Cash Outflows

Liquidity coverage ratios are required to be 60% by 2015, which will gradually increase to 100% by 2019. Of its liquid assets, 60% must be cash, central bank reserves, and government bonds; 40% may be corporate bonds, residential mortgage-backed securities, and stocks of creditworthy corporations, but RMBSs (Residential mortgage-backed securities) and stocks cannot compose more than 15% of liquid assets.

BASEL ACCORDS

Global standards are generally set by the Basel Committee on Banking Supervision. A set of 3 standards have been developed since the 1990s. Basel I was enacted in 1992. The Basel II rules

were published in 2004 and enacted in 2008. The current recommended regulations, Basel III, enacted as a response to the Great Recession, will be implemented over a 6-year period, from 2013 to 2019. The minimum capital required by Basel III for assets with some risk is 10.5%, from the previous minimum of 8%.

The Basel rules were developed as a means to facilitate international banking, which greatly increased since 1988. Regulatory authorities from the major G-10 countries got together in 1988 in Basel, Switzerland to develop new rules to facilitate international banking and to set standards for controlling risk. The Basel rules are administered by the Bank for International Settlements (BIS). They do not have regulatory force, but they do set the global standards that most countries follow to facilitate international banking and to prevent the spread of risk. Domestic regulations plus cross-border regulations, such as that by the European Union's Capital Adequacy Directive, are based on the Basel accords. The primary protection against risk and a major focus of the Basel accords is the primary requirement that banks have adequate capital.

The Basel Accords refers to a set of banking supervision regulations set by the Basel Committee on Banking Supervision (BCBS). They were developed over several years between 1980 and 2011, undergoing several modifications over the years. The Basel Accords were formed with the goal of creating an international regulatory framework for managing credit risk and market risk. Their key function is to ensure that banks hold enough cash reserves to meet their financial obligations and survive in financial and economic distress. They also aim to strengthen corporate governance, risk management, and transparency. The regulations are considered to be the most comprehensive set of regulations governing the international banking system. The Basel Accords can be broken down into Basel I, Basel II, and Basel III.

Basel I

Basel I, also known as the Basel Capital Accord, was formed in 1988. It was created in response to the growing number of international banks and the increasing integration and interdependence of financial markets. Regulators in several countries were concerned that international banks were not carrying enough cash reserves. Since international financial markets were deeply integrated at that time, the failure of one large bank could cause a crisis in multiple countries. Basel I was enforced by law in G10 countries in 1992, but more than 100 countries implemented the regulations with minor customizations. The regulations aimed to

improve the stability of the financial system by setting minimum reserve requirements for international banks. It also provided a framework for managing credit risk through the risk-weighting of different assets. According to Basel I, assets were classified into four categories based on risk weights:

- 0% for risk-free assets (cash, treasury bonds)
- 20% for loans to other banks or securities with the highest credit rating
- 50% for residential mortgages
- 100% for corporate debt

Banks with a significant international presence were required to hold 8% of their risk-weighted assets as cash reserves. International banks were guided to allocate capital to lower-risk investments. Banks were also given incentives for investing in sovereign debt and residential mortgages in preference to corporate debt.

Basel II

Basel II, an extension of Basel I, was introduced in 2004. Basel II included new regulatory additions and was centered on improving three key issues – minimum capital requirements, supervisory mechanisms and transparency, and market discipline. Basel II created a more comprehensive risk management framework. It did so by creating standardized measures for credit, operational, and market risk. It was mandatory for banks to use these measures to determine their minimum capital requirements. A key limitation of Basel I was that the minimum capital requirements were determined by looking at credit risk only. It provided a partial risk management system, as both operational and market risks were ignored. Basel II created standardized measures for measuring operational risk. It also focused on market values, instead of book values, when looking at credit exposure. Additionally, it strengthened supervisory mechanisms and market transparency by developing disclosure requirements to oversee regulations. Finally, it ensured that market participants obtained better access to information.

Basel III

The Global Financial Crisis of 2008 exposed the weaknesses of the international financial system and led to the creation of Basel III. The Basel III regulations were created in November 2010 after the financial crisis; however, they are yet to be implemented. Their implementation's constantly been delayed in recent years and is expected to occur in January 2022. Basel III

identified the key reasons that caused the financial crisis. They include poor corporate governance and liquidity management, over-levered capital structures due to lack of regulatory restrictions, and misaligned incentives in Basel I and II. Basel III strengthened the minimum capital requirements outlined in Basel I and II. In addition, it introduced various capital, leverage, and liquidity ratio requirements. According to regulations in Basel III, banks were required to maintain the following financial ratios:

Tier 1 Capital Ratio

$$= \frac{\text{Equity Capital}}{\text{Risk Weighted Assets}} \geq 4.5\%$$

Leverage Ratio

$$= \frac{\text{Tier 1 Capital}}{\text{Average Total Assets}} \geq 3\%$$

Liquidity Coverage Ratio

$$= \frac{\text{Liquid Assets}}{\text{Total Outflows Over Next 30 Days}} \geq 100\%$$

Also, Basel III included new capital reserve requirements and countercyclical measures to increase reserves in periods of credit expansion and to relax requirements during periods of reduced lending. Under the new guideline, banks were categorized into different groups based on their size and overall importance to the economy. Larger banks were subjected to higher

reserve requirements due to their greater importance to the economy. The Basel Accords are extremely important for the functioning of international financial markets. They can never be constant and need to continuously be updated based on present market conditions and lessons learned from the past.

BANKING INNOVATIONS

The term “Innovation” means ‘to make something new’. Banks no longer restricted themselves to traditional banking activities, but explored newer avenues to increase business and capture new market. Today, there is fairly well developed banking system with different classes of banks. Some of them have engaged in the areas of consumer credit, credit cards, merchant banking, internet and phone banking, leasing, mutual funds etc. A few banks have already set up subsidiaries for merchant banking, leasing and mutual funds and many more are in the process of doing so.

CORE BANKING SOLUTION (CBS)

Today Banking as a business has grown tremendously and transformed itself from only a deposits taking and loan providing system to an institution which provides an entire gamut of products and services under a wide umbrella. All such activities commenced by a bank is called Core Banking. Core banking refers to a centralized system established by a bank which allows its customers to conduct their business irrespective of the bank’s branch. Thus, it removes the impediments of geo-specific transactions. In fact, CORE is an acronym for "Centralized Online Real-time Exchange", thus the bank’s branches can access applications from centralized data centers. Core banking solutions offer the following advantages to the bank:

- Improved operations which address customer demands and industry consolidation
- Errors due to multiple entries eradicated
- Easy ability to introduce new financial products and manage changes in existing
- Seamless merging of back office data and self-service operations.
- Minimum features of Core Banking Solution:
 - Customer-On Boarding.
 - Managing deposits and withdrawals.
 - Transactions management
 - Interest. Calculation and management.
 - Payments processing (cash, cheques /checks, mandates, NEFT, RTGS etc.).

RETAIL BANKING

Retail banking is a banking facility that offers financial services to the general population rather than companies. It certainly helps retail customers conduct their daily financial dealings more effectively and safely. Also labelled as “consumer banking,” it occurs between consumers and their banks. Retail banking services are provided both on online portals and offline branches. Moreover, it incorporates savings and checking account, credit cards, consumer loans, debit cards, internet banking services, and mortgages. Simply put, it is a consumer-oriented banking approach. Retail banking assists consumers in directly connecting with the bank to manage their everyday requirements, for example, personal loans and mortgages. Moreover, they must approach the bank portal or branch to examine its menu of retail banking services. It helps customers certainly get the desired services at the concerned portal or branch. In recent years, the growth of retail banking jobs has certainly attained a high level owing to the demand for digital banking services. Also termed “personal banking,” it facilitates management of the money for individual consumers.

Types of Retail Banks

1 – Small Banks

They function in a small range via branch banking with nearly all facilities offered by the large banks and hence are quite known among the populace. Nevertheless, they possess lower market shares and lesser deposits compared to them.

2 – Large Banks

These prominent banks operate in big cities with numerous branches and certainly have more personnel than small banks. Also, several retail clients choose them because of their huge popularity.

3 – Online Banks

As the name suggests, online banks work electronically with no tangible offices. Moreover, they operate through an official website accessible from even the remotest parts of the world. Now that a majority of people prefer to avail banking services from the comfort of their homes.

Retail Banking Products

1 – Savings Accounts: Also known as “interest-bearing accounts”, it is a relevant retail banking example referring to basic deposit accounts to safeguard cash with a decent interest rate. They stash away the amount for short-term requirements and generally apply cash transferral and withdrawal limits.

2 – Checking Accounts: These deposit accounts permit easily accessible (and usually unlimited) cash withdrawals and deposits for regular payments. Also known as “Transactional accounts,” they offer debit cards for purchases and online bill payments.

3 – Debit Cards: Also called ATM Cards, they are bank-issued payment cards for cashless transactions through money deduction directly from the checking account. Furthermore, they link straight to the bank account, and consumers can utilize them at Automated Teller Machines (ATMs).

4 – Certificates Of Deposit (CDs): This savings account holds a set capital amount for a predetermined duration and the issuing bank grants interest in exchange. When cashed in, consumers collect the actual amount and the interest amount.

5 – Credit Cards: Credit cards are financial tools released by banks to borrow money for digital transactions with a fixed line of credit. Cardholders must repay the entire amount with any levied interest either until the payment date or with time to avoid credit risk.

6 – Home Loans: They denote a capital amount consumers lent from banks or financial institutions to buy a home. Moreover, second mortgages infer the usage of home equity as collateral to borrow funds.

7 – Personal Loans: These loans certainly entail money borrowed from banks, online lenders, or credit unions to meet financial obligations. Moreover, the multi-purpose unsecured loan is compensated in monthly payments within a few months or years.

Services Offered by Retail Bank

- **Bank Accounts:** Bank accounts include things like checking accounts, savings accounts, and retirement accounts, to name a few examples.
- **Safe Lockers:** In order to prevent your valuables from being stolen or damaged while you are away from home, little value safes are housed in Safes inside the bank’s walls.
- **Deposits;** The interest rates on Certificates of Deposit (CDs) are greater than those on savings accounts, but you must normally leave your money in the account for at least several months in order to avoid being charged an early withdrawal fee.
- **Personal Loan:** Unsecured personal loans may be used to pay a number of costs without the need to put up any kind of collateral as a form of security.
- **Auto Loans:** Individuals may get auto loans to aid them in the purchase of a car. Auto loans can also be refinanced.

- **Home / Mortgage Loans:** Homes are purchased with the help of mortgage loans, and second mortgages allow borrowers to refinance current debts or withdraw cash from the value of their property.

PLASTIC MONEY

A plastic money card is a thin card that contains identification information such as a signature or picture, and authorizes the card holder to charge purchases or services to the card holder's account. Today, the information on the card is read by automated teller machines (ATMs), banks, and the internet. It all started in the 1920s, when individual companies (such as oil companies and hotels) issued these "plastic money cards" for purchases made at their businesses. However, these cards could not be used outside of the company. In the 1950s a "universal card" was introduced by Diners Club, INC. This was when credit cards were made.

These cards allowed the card holders to use the cards in various locations and businesses. The way the cards worked was that there were annual fees, and depending on the plan, the card holders were billed either monthly or yearly. Later on the "bank credit card system" was introduced. Under this system, the bank credits the account of the merchant at each sale and bills to the card holder at the end of the billing period to account for the sale. The card holder, in turn, pays the bank either the entire balance or in monthly instalments with interest. This is the system that all credit cards are under today. Now there are three different types of cards: credit cards, debit cards, and prepaid cards.

NATIONAL ELECTRONIC FUND TRANSFER (NEFT)

National Electronic Fund Transfer (NEFT) is a nation-wide payments system that allows the transfer of funds from one bank's account to another. With an increased focus on online banking, NEFT has become one of the most popular ways of transferring funds. Since it can electronically transfer funds from any bank branch to any individual, it has eliminated the need to visit a bank branch for transfer of funds.

NEFT Process

- Stated simply, if an individual wish to transfer a sum of money from his bank account to another person's bank account, he can do so through the process of NEFT, instead of withdrawing money and then paying it in cash or by writing out a cheque.

- The main benefit offered by NEFT is that it can transfer funds from any account of any branch to any other bank account located at any place
- The only condition is that both the sender and receiver branches should be NEFT-enabled
- You can check the list of NEFT-enabled bank branches on RBI's website or just call your bank's customer service to confirm the same
- NEFT system also facilitates the one-way cross-border transfer of funds from India to Nepal under the Indo-Nepal Remittance Facility Scheme

How to Transfer Funds through NEFT

One needs to follow the procedure given below to transfer funds using NEFT-

Step 1- Login to your online banking account using your login ID and password.

Step 2- Go to the NEFT Fund Transfer Section.

Step 3- Add beneficiary by entering his/her name, bank account number and IFSC Code.

Step 4- Once the beneficiary is successfully added, you can initiate an NEFT transfer. Just enter the amount to be remitted and send.

AUTOMATED TELLER MACHINE (ATM)

An automated teller machine (ATM) is an electronic banking outlet that allows customers to complete basic transactions without the aid of a branch representative or teller. Anyone with a credit card or debit card can access cash at most ATMs. ATMs are convenient, allowing consumers to perform quick self-service transactions such as deposits, cash withdrawals, bill payments, and transfers between accounts. Fees are commonly charged for cash withdrawals by the bank where the account is located, by the operator of the ATM, or by both. Some or all of these fees can be avoided by using an ATM operated directly by the bank that holds the account. ATMs are known in different parts of the world as automated bank machines (ABM) or cash machines.

Types of ATMs

There are two primary types of ATMs. Basic units only allow customers to withdraw cash and receive updated account balances. The more complex machines accept deposits, facilitate line-of-credit payments and transfers, and access account information. To access the advanced features of the complex units, a user often must be an account holder at the bank that operates the machine. Analysts anticipate ATMs will become even more popular and forecast an

increase in the number of ATM withdrawals. ATMs of the future are likely to be full-service terminals instead of or in addition to traditional bank tellers.

MOBILE BANKING

Mobile banking refers to the use of a mobile device to carry out financial transactions. The service is provided by some financial institutions, especially banks. Mobile banking enables clients and users to carry out various transactions, which may vary depending on the institution. Currently, mobile banking's become easier with the development of cellular mobile applications. Clients are now able to check their balances, view their bank statements online, make transfers, and even carry out prepaid service purchases.

Types of Mobile Banking Services

- 1. Account information access:** Account information access allows clients to view their account balances and statements by requesting a mini account statement, review transactional and account history, keep track of their term deposits, review and view loan or card statements, access investment statements, and for some institutions, management of insurance policies.
- 2. Transactions:** Transactional services enable clients to transfer funds to accounts at the same institution or other institutions, perform self-account transfers, pay third parties, and make purchases in collaboration with other applications or prepaid service providers.
- 3. Investments:** Investment management services enable clients to manage their portfolios or get a real-time view of their investment portfolios (term-deposits, etc.)
- 4. Support services:** Support services enable clients to check on the status of their requests for loan or credit facilities, follow up on their card requests, and locate ATMs.
- 5. Content and news:** Content services provide news related to finance and the latest offers by the bank or institution.

Challenges Associated With Mobile Banking

Some of the challenges associated with mobile banking include (but are not limited to):

- Accessibility based on the type of handset being used
- Security concerns
- Reliability and scalability
- Personalization ability
- Application distribution
- Upgrade synchronization abilities

M WALLET

Mobile Wallet is also known as mWallet, digital wallet, or eWallet. It is basically referred to a mobile technology that is used the same as a real wallet. A mobile wallet is a virtual wallet that stores payment card information on a mobile device. Mobile wallets are a convenient way for a user to make in-store payments and can be used at merchants listed with the mobile wallet service provider. Mobile Wallet is a type of payment service through which individuals can receive and send money by mobile devices. It is a form of an e-commerce model designed for the mobile devices for the convenience and ease of access.

The information stored in a mobile wallet is encrypted, making it difficult for cybercriminals to execute fraudulent activities with them. While physical credit and debit cards can be stolen or duplicated, mobile wallets are difficult to steal since they come with encrypted keys that may not reveal any useful information. Once a customer installs a mobile wallet on their mobile device, they are required to provide their credit card details, reward cards, and coupons. The information is then linked to an accepted personal identification format, such as a key or a scannable QR code. When a customer makes an in-store payment, the mobile app uses near-field communication (NFC) technology to communicate between devices. The NFC uses a QR code, key, or another personal identification format to process the payment at the payment terminal. The action is triggered when the user taps or waves the NPC-enabled device at the merchant's point-of-service terminal.

Types of Mobile Wallets

- 1. Open wallets:** An open wallet is used directly by a bank or through a third party. Open wallets allow customers to use the funds in the mobile wallet for making payments for transactions or withdrawing the funds deposited to the account in cash. An example of an open mobile wallet is PayPal, which allows users to make payments for in-store and online purchases and still withdraw the funds in cash.
- 2. Closed wallets:** Closed wallets are linked to specific merchants, and users can only use the funds to make payments for transactions initiated with the specific merchant. Users cannot use the money to make payments for transactions with other merchants and third-party service providers or withdraw the funds in cash. An example of a closed wallet is Amazon Pay.
- 3. Semi-closed wallets:** Semi-closed mobile wallets allow users to use the funds in the wallet to make payments for transactions with multiple merchants, as long as there is an existing contract between the merchant and the mobile wallet company. Users can also withdraw the

funds into a bank account. However, semi-closed wallets do not allow users to withdraw funds in cash.

NET-BANKING

Net-banking, also known as internet banking, is an electronic system or service offered by banks which enables customers to access financial as well as non-financial banking products online. Earlier, customers had to visit the banks even for a small service. However, after the arrival of internet banking, almost all the banking services and products can be accessed online. From fund transfer to requesting demand draft, net-banking facilitates all banking essentials. It is not just convenient but also a secure method of banking.

- To benefit from net-banking, customers are required to register for internet banking at the bank.
- Individuals having an operating account at any bank or financial institution can register for internet banking
- For net-banking to work properly, you need a personal computer, laptop or mobile phone, and good internet connection
- After registering, a unique customer ID and password is issued by the bank using which one can log-in to the net-banking portal

Features of Net Banking

- A secure and convenient method of banking
- Password-protected banking system
- Easy access to financial and non-financial banking products/services
- Access your bank account anytime anywhere
- Track and manage bank balance, last transactions, statements, etc.
- Transfer funds online via NEFT, RTGS, IMPS anytime
- Process bill payments quickly
- Keep a track of mortgage payments, loans, savings a/c, etc.
- Channelize or cancel automatic payments

BANCASSURANCE

Bancassurance is a relatively new idea in the financial sector. The belief behind Bancassurance is to combine the marketing capabilities and selling-culture of insurance companies with the

distribution network and sizeable customer base of banks. Bancassurance means selling insurance through banks. Banks and insurance companies collaborate in a partnership, where the bank sells the partner insurance company's products to its customers. Banks and insurance companies collaborate to form a partnership in which the bank sells the insurance firm's products to its customers. This arrangement profits both the bank and the insurance company, as the bank earns a commission amount from the insurance company while the insurance firm broadens its market share and customers. In India, the first three models are practised, but the laws do not permit either banks or insurers to own an insurance company or bank wholly. The insurance sector in India is expanding rapidly. Both banks and insurance companies perceive bancassurance as an opportunity to increase the Indian financial industry's future income and footprint. Non-life insurance products are featured to a lesser extent as compared to life insurance products. The banks have a customer base of more than 100 million and therefore are in a perfect situation for taking bancassurance forward.

Bancassurance in India is gaining ground extremely fast despite being a very new concept. In India, the banking sector is under the control of Reserve Bank of India and insurance sector is managed by the Insurance Regulatory and Development Authority (IRDA). Since Bancassurance contains constituents from both industries, it comes under the influence of both regulators. Each of the regulators (RBI and IRDA) have given out comprehensive regulations for the bank's involvement in the insurance sector. This degree of possible fee-based revenue creation by banks in India from bancassurance is the temptation for banks to get involved.

Importance of Bancassurance

- **Cost-effectiveness:** Insurance companies look to Bancassurance as a cost-effective mode of distribution.
- **Helpful environment:** Given that the customers already trust the bank with their money, they are also generally more willing to consider new products from the same financial institution, thereby creating an enabling environment to sell the products.
- **Commission-based income:** A bank is able to income base and increase its overall productivity by strengthening its branch network, goodwill and client base by presenting itself as a one-stop-shop for its customers, therefore improving customer

Bancassurance companies

- SBI life insurance Company

- LIC is tied up with Vijaya bank, Oriental bank of commerce, Corporation bank
- ICICI Lombard
- Barclays – MetLife India
- Axis bank – MetLife India

Benefits of Bancassurance

- It encourages customers of banks to purchase insurance policies and further helps in building better relationship with the bank.
- The people who are unaware of and/or are not in reach of insurance policies can be benefitted through widely distributed banking networks and better marketing channels of banks.
- Increase in number of providers means increase in competition and hence people can expect better premium rates and better services from bancassurance as compared to traditional insurance companies.
- Bancassurance has a tremendous chance, if appropriately implemented, to be a win-win situation for banks, insurers and the customer.

PAYMENT AND SETTLEMENT SYSTEMS

In India, the payment and settlement systems are regulated by the Payment and Settlement Systems Act, 2007 (PSS Act) which was legislated in December 2007. The PSS Act as well as the Payment and Settlement System Regulations, 2008 framed thereunder came into effect from August 12, 2008. In terms of Section 4 of the PSS Act, no person other than the Reserve Bank of India (RBI) can commence or operate a payment system in India unless authorised by RBI. Reserve Bank has since authorised payment system operators of pre-paid payment instruments, card schemes, cross-border in-bound money transfers, Automated Teller Machine (ATM) networks and centralised clearing arrangements. The Reserve Bank has taken many initiatives towards introducing and upgrading safe and efficient modes of payment systems in the country to meet the requirements of the public at large.

I. Paper-based Payments

Use of paper-based instruments (like cheques, drafts, and the like) accounts for nearly 60% of the volume of total non-cash transactions in the country. In value terms, the share is presently

around 11%. This share has been steadily decreasing over a period of time and electronic mode gained popularity due to the concerted efforts of Reserve Bank of India to popularize the electronic payment products in preference to cash and cheques. Since paper based payments occupy an important place in the country, Reserve Bank had introduced Magnetic Ink Character Recognition (MICR) technology for speeding up and bringing in efficiency in processing of cheques.

II. Electronic Payments

The initiatives taken by RBI in the mid-eighties and early-nineties focused on technology-based solutions for the improvement of the payment and settlement system infrastructure, coupled with the introduction of new payment products by taking advantage of the technological advancements in banks. The continued increase in the volume of cheques added pressure on the existing set-up, thus necessitating a cost-effective alternative system.

Electronic Clearing Service (ECS) Credit

The Bank introduced the ECS (Credit) scheme during the 1990s to handle bulk and repetitive payment requirements (like salary, interest, dividend payments) of corporates and other institutions. ECS (Credit) facilitates customer accounts to be credited on the specified value date and is presently available at all major cities in the country. During September 2008, the Bank launched a new service known as National Electronic Clearing Service (NECS), at National Clearing Cell (NCC), Mumbai. NECS (Credit) facilitates multiple credits to beneficiary accounts with destination branches across the country against a single debit of the account of the sponsor bank.

Regional ECS (RECS)

Next to NECS, RECS has been launched during the year 2009. RECS, a miniature of the NECS is confined to the bank branches within the jurisdiction of a Regional office of RBI. Under the system, the sponsor bank will upload the validated data through the Secured Web Server of RBI containing credit/debit instructions to the customers of CBS enabled bank branches spread across the Jurisdiction of the Regional office of RBI. The RECS centre will process the data, arrive at the settlement, generate destination bank wise data/reports and make available the data/reports through secured web-server to facilitate the destination bank branches to afford credit/debit to the accounts of beneficiaries. by leveraging the CBS technology put in place by the bank. Presently RECS is available in Ahmedabad, Bengaluru, Chennai and Kolkata

Electronic Clearing Service (ECS) Debit

The ECS (Debit) Scheme was introduced by RBI to provide a faster method of effecting periodic and repetitive collections of utility companies. ECS (Debit) facilitates consumers / subscribers of utility companies to make routine and repetitive payments by 'mandating' bank branches to debit their accounts and pass on the money to the companies. This tremendously minimises use of paper instruments apart from improving process efficiency and customer satisfaction. There is no limit as to the minimum or maximum amount of payment. This is also available across major cities in the country.

Electronic Funds Transfer (EFT)

This retail funds transfer system introduced in the late 1990s enabled an account holder of a bank to electronically transfer funds to another account holder with any other participating bank. Available across 15 major centers in the country, this system is no longer available for use by the general public, for whose benefit a feature-rich and more efficient system is now in place, which is the National Electronic Funds Transfer (NEFT) system.

National Electronic Funds Transfer (NEFT) System

In November 2005, a more secure system was introduced for facilitating one-to-one funds transfer requirements of individuals / corporates. Available across a longer time window, the NEFT system provides for batch settlements at hourly intervals, thus enabling near real-time transfer of funds.

Real Time Gross Settlement (RTGS) System

RTGS is a funds transfer systems where transfer of money takes place from one bank to another on a "real time" and on "gross" basis. Settlement in "real time" means payment transaction is not subjected to any waiting period. "Gross settlement" means the transaction is settled on one to one basis without bunching or netting with any other transaction. Once processed, payments are final and irrevocable. This was introduced in in 2004 and settles all inter-bank payments and customer transactions above ₹2 lakh.

Clearing Corporation of India Limited (CCIL)

CCIL was set up in April 2001 by banks, financial institutions and primary dealers, to function as an industry service organisation for clearing and settlement of trades in money market, government securities and foreign exchange markets. The Clearing Corporation plays the crucial role of a Central Counter Party (CCP) in the government securities, USD –INR forex exchange (both spot and forward segments) and Collateralised Borrowing and Lending Obligation (CBLO) markets.

III. Other Payment Systems

Pre-paid Payment Systems

Pre-paid instruments are payment instruments that facilitate purchase of goods and services against the value stored on these instruments. The value stored on such instruments represents the value paid for by the holders by cash, by debit to a bank account, or by credit card. The pre-paid payment instruments can be issued in the form of smart cards, magnetic stripe cards, internet accounts, internet wallets, mobile accounts, mobile wallets, paper vouchers, etc.

Mobile Banking System

Mobile phones as a medium for providing banking services have been attaining increased importance. Reserve Bank brought out a set of operating guidelines on mobile banking for banks in October 2008, according to which only banks which are licensed and supervised in India and have a physical presence in India are permitted to offer mobile banking after obtaining necessary permission from Reserve Bank. The guidelines focus on systems for security and inter-bank transfer arrangements through Reserve Bank's authorized systems.

ATMs / Point of Sale (POS) Terminals / Online Transactions

Presently, there are over 61,000 ATMs in India. Savings Bank customers can withdraw cash from any bank terminal up to 5 times in a month without being charged for the same. There are over five lakh POS terminals in the country, which enable customers to make payments for purchases of goods and services by means of credit/debit cards. To facilitate customer convenience the Bank has also permitted cash withdrawal using debit cards issued by the banks at PoS terminals.

National Payments Corporation of India

The Reserve Bank encouraged the setting up of National Payments Corporation of India (NPCI) to act as an umbrella organisation for operating various Retail Payment Systems (RPS) in India. NPCI became functional in early 2009. NPCI has taken over National Financial Switch (NFS) from Institute for Development and Research in Banking Technology (IDRBT). NPCI is expected to bring greater efficiency by way of uniformity and standardization in retail payments and expanding and extending the reach of both existing and innovative payment products for greater customer convenience.