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Topic:- Central Bank

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B.A. Part - I (Hons.)

C.B. Meaning :- An apex body that controls, operates ,regulates and directs the entire banking and directs the entire banking and monetary structure of the country.

Functions of central bank :-.

1 Currency authority of bank of issues : Central bank is a sole authority to issue currency in the country. Central Bar obliged to back the currency with assets of equal value (usually gold coins, gold bullions ,foreign securities etc)

Advantages of sole authority of note issue :

a) Uniformity in note circulation
b) Better supervision and control
c) It is easy to control credit
d) Ensures public faith
e) Stabilization of internal and external value of Currency

2. Banker to the government : As a banker is carries out all banking business of the Government and maintains cur account for keeping cash balances of the government. Accepts receipts and makes payments for the government . I also gives loans and Advance to the government.

3. Banker's bank and supervisor :- Acts as a Banker to other banks in the country__

a) Custodian of cash reserves :-. Commercial banks must keep a certain proportion of cash reserves with the central bank (CRR)

b) Lender of last resort :- when commercial banks fail to need their financial requirements from other sources, they approach Central Bank which gives loans and advances.

c) Clearing house :- Since the central bank holds the cash reserves of commercial banks it is easier and more convenient to act as clearing house of commercial banks.

4. Controller of money supply and credit :- Central Bank for RBI please an important role during the times of . economic fluctuations. It influences the money supply through quantitative and qualitative instruments . . Former refers to the volume of credit and the letter refers to regulate the direction of credit.

5. Lender of the resort :- It means that if a commercial bank fails to get financial accommodation from anywhere , it approaches the central bank as a last resort.

Central bank advances loans to such Bank against approved securities.

By offering loans to Commercial Bank in situation of emergency the central ensures that the banking system of the country does not suffer any setback and money market remains stable.

QUANTITATIVE INSTRUMENTS :-

i) **Bank Rate Policy :-** it refers to the rate at which the central bank lends money to commercial banks as a lender of The last resort.

Central Bank increases the bank rate during inflation(excess demand)and reduces the same in times of deflation (defective demand).

ii) **Open Market Operations :-** it refers to the buying and selling of securities by the central bank from\. to the Public and commercial banks.

It sales government securities during inflation / excess demand and by the securities during deflation \ deficient demand.

iii) **Legal Reserve Ratio :-** R. B. I. can influence the credit creation power of commercial banks by making Change in CRR and SLR.

Cash Reserve Ratio(CRR) :- It refers to the minimum percentage of net demand and time liabilities to be kept by commercial banks with central bank.

Reserve Bank increases CRR during inflation and decrease the same during deflation.

Statutory Liquidity Ratio (SLR) :- It refers to minimum percentage of net demand and time liabilities which Commercial banks are required to maintain with themselves SLR is increased during inflation or excess demand and decrease during deflation or deficit demand.

iv) **Repo Rate :-** The rate at which RBI offer shot near loan to Commercial Bank by buying government securities. In fact it is repurchase rate.

During inflation the cost of capital is increased by increasing the repo rate.

This lowest the demand for credit the supply of money decreases.

On the other hand during depletion the cost of capital is reduced by reducing the repo rate. This increases the demand for credit and supply of money also increases.

v) **Reverse Repo Rate :-** The rate at which the RBI accepts deposit from the commercial bank. It is also called reverse repo rate.

When reverse repo rate is lowered, banks are discourage to park their surplus fund with the RBI .This leads to rise in credit supply by the commercial bank. Accordingly the supply of money enhanced as Desire to control deflation.

On the other hand rise in reserve repo rate may induce the commercial bank to park more funds with the RBI to generate interest income. This lowers the capacity of offer CRR fund to RBI for creation of credit. Accordingly Supply of money will reduce in economy.

QUALITATIVE INSTRUMENTS :-

Margin Requirements : it is the difference between the amount of loan and market value of the security Offered by the borrower against the loan.

margin requirements are increased during inflation and decrease during deflation.

Moral Suasion : It is a combination of persuasion and pressure that Central Bank applies on other banks in order to get them act in a manner in line with its policy.It is done through letters, speeches etc.

Selective credit controls : central bank gives direction to other banks to give or not to give credit for certain purposes to particular sectors.

This can be applied in both a positive as well as negative manner

In positive manner, the credit will be channelised to particular priority sectors.

In negative manner, the flow of credit will be restricted to a particular sector.

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