1. “A Financial Institution is an organization that facilitates financial transactions and is a key player in financial intermediation”.Explain the statement in light of the Importance of Financial Institutions.

Importance of Financial Institutions:

- **Provide funds:** Financial institutions provide funds for investment and industrial activities. Active sources offer an appropriate source of funds for the requirement of institutions and individuals.
- **Infrastructural facilities:** Financial institutions also offer basic infrastructural facilities needed for the development and promotion of lucrative ventures. Infrastructural facilities involve the development of industrial estates, tech parks, roads, water, etc.
- **Promotional activities:** To mobilize the funds, reduce the risk of selling financial securities, arrangement of working and long-term capital of the business.
- **Development of Backward Areas:** Financial institutions also take social responsibility for developing the backward areas at a free cost by offering credit facilities, free education, employment creation, etc.
- **Planned development:** Financial institutions initiate all planned developments in the view of economic growth of the state and are coordinated with the government plan and social welfare.
- **Accelerating industrialization:** As financial institutions are established to earn the profit and safeguard the interests of their members, they accelerate industrialization to contribute to industrial growth. They support the industries by granting finance, project development, and consultancy.
- **Employment generation:** Channelizing the funds for investment, building industrial facilities and acceleration of industries generates employment for the educated and qualified people of the state.

2. What are the types of Financial Institutions?

Types of financial institutions

I. Banking Institutions

II. Non Banking Financial Institutions

I. **Banking Institutions:** They are governed by RBI, and come under Banking Regulations Act 1949.

A. **Commercial Banks:** are established with a objective to create saving habit among the people , provide banking services like accepting deposits and lending money.

a) Scheduled bank- Banks which are registered in the second schedule of RBI.

Features of scheduled bank

- The scheduled bank must be in business of banking in India .
- It is either a company under companies act or an institution notifies by the central government.
- It must have paid up capital and reserve of an aggregate of 5 lakhs rupees.
- It must be working as per RBI rules and regulation.

- **Public sector banks-** Include all banks in which government has major share holdings. SBI & it s & subsidiaries and all nationalized banks belongs to this category e.g. SBI , Indian bank, Bank Of India, Canara Bank.
- **Private sector-banks** in which owned by shareholders. At present there are 30 private sector banking south Indian bank.
- **Foreign banks-banks** belong to foreign country and started their branches in india.eg; standard chartered bank, Citi bank.

c) **Non scheduled bank**-banks which are not under the scheduled of RBI. At present in India there are no non scheduled bank.

2. **RRBs:** Regional Rural Bank s are to be set-up mainly with a view to develop rural economy by providing credit facilities for the purpose of development of agriculture, trade, commerce, industry and other productive activities in the rural areas. Such facility is provided particularly to the small and marginal farmers, agricultural labourers, artisans, and small entrepreneurs and for other related matters.

3. **Co-operative banks:** are registered under Cooperative societies Act in 1912, give credit facilities to small farmers, SSI etc.

- **Unorganized Financial Institutions:** These are comprised with private money lenders, pawn brokers, indigenous bankers, traders etc. they lend money to the public from their own fund.(Operations and activities are not regulated by RBI).

2. **Non Banking Financial Institutions:** These are institutions which do not have full license or is not supervised by a National or International Banking Regulatory Agency. They facilitate bank related financial services such as

   - Provident and Pension Fund
   - Small Saving Organization
   - Life Insurance Corporation(LIC)
   - General Insurance Corporation(GIC)
   - Unit Trust of India(UTI)
   - Mutual Funds
   - Investment Trust etc.

3. What are the functions of RBI?

Note Issuing Authority: The RBI has, since its inception, the sole right or authority or monopoly of issuing currency notes other than one rupee notes and coins, and coins of smaller denominations. At present, the Bank issues notes in the following denominations: Rs 5, 10, 20, 50, 100, 500 and 2000

Government Banker: The RBI is the banker to the Central and state governments. It provides to the government all banking services such as acceptance of deposits, withdrawal of funds by cheque, making payments as well as receipts and collection of payments on behalf of the government, transfer of funds, and management of public debt

Management of Public Debt: The Reserve Bank manages the public debt and issues new loans on behalf of the Central and State Governments. It involves the issue and retirement of rupee loans, interest payments on the loan, and operational matters about debt certificates and their registration.

Bankers' Bank: The Reserve Bank controls the volume of reserves of commercial banks and determines their deposits/credit-creating ability. It opens current accounts with banks, allowing them to maintain cash reserves and carry out inter-bank transactions. In times of need, banks borrow funds from the RBI.

Supervising Authority: The Reserve Bank of India issues licenses for the establishment of new banks, prescribes minimum requirements for paid-up capital and reserves transfer, inspects the working of banks, conducts investigations into complaints, irregularities, and frauds, controls appointment, re-appointment, and termination of appointments of Chairman and chief executive officers, and approves or forces amalgamations.

Exchange Control (EC) Authority: Administers foreign exchange control, chooses exchange rate system, manages exchange reserves, interacts with monetary authorities, and negotiates with international financial institutions.

Formulating Prudential Norms: RBI formulates various prudential norms to create and maintain a stable, efficient, and well-functioning financial system in India.

Promoter of the Financial System: RBI has strengthened the country's banking and financial structure by mobilizing savings, providing concessional loans, and setting up institutions to develop the agricultural sector.

Regulation and Supervision of Payment System: The Central Board created the Negotiated Dealing System, a screen-based trading platform, a Board for Regulation and Supervision of Payment and Settlement Systems (BPSS), and a Department of Payment and Settlement Systems (DPSS) to assist the BPSS in performing its functions.

Regulator of Money and Credit: The function of formulating and conducting monetary policy is of paramount importance for any Central Bank.

4. What are the Advantages & Disadvantages of Over the Counter Market?

5. Distinguish between over–the–counter (OTC) markets and exchange markets.

BASIS FOR COMPARISON	OTC (OVER THE COUNTER)	EXCHANGE
Meaning	Over the Counter or OTC is a decentralized dealer market wherein brokers and dealers transact directly via computer networks and phone.	Exchange is an organized and regulated market, wherein trading of stocks takes place between buyers and sellers in a safe, transparent and systematic manner.
Market maker	Dealer	Exchange itself
Used by	Small companies	Well established companies
Physical Location	No	Yes
Trading hours	24×7	Exchange hours
Stocks	Unlisted Stocks	Listed Stocks
Transparency	Low	Comparatively high
Contracts	Customized	Standardized

6. What are the Advantages & Disadvantages of Spot Markets

Advantages:

- Spot markets facilitate trading in a transparent environment, where transactions occur at prevailing prices that are public information and known to all parties. Basically, it is easier to execute spot market contracts.
- Traders in spot markets can hold and find a better deal if they are not satisfied with current prices and terms.
- Trades are done and completed on the spot.
- There may be no minimum capital requirements in spot market transactions compared to some contracts on the futures market that have minimum investment amounts for a single contract.

Disadvantages:

- Due to the volatility of some financial instruments and commodities, investors can buy on the spot at inflated prices before assets find their "true price." Hence, trading on the spot market can present significant risks, especially for volatile assets.
- There may be no recourse if a party notices some irregularities in the trade after the spot market transaction is concluded.
- There is usually a lack of planning in spot trades, as opposed to forwards and futures trading where parties agree on settlement and delivery at a future date.
- The spot market is not flexible in terms of timing, as parties will have to handle physical delivery on the spot.
- The interest rate spot market is affected by counterparty default risk.
- Currency trading in spot markets is prone to counterparty risk due to the solvency of the market maker.

7. Explain the Features of the Foreign Exchange Market.

High liquidity: The foreign exchange market is highly liquid due to its size and geographical spread. It processes US$5.1 trillion worth of transactions per day and is extremely active, meaning trades can be executed at any time. This also provides ease of entry and exit, which traders find important.

Market transparency: The foreign exchange market is highly efficient and transparent, with transactions recorded electronically and information updated quickly. It is too large and spread out to be manipulated by one individual or group, and transactions cannot be concealed. A transparent market means all known information is displayed in the prices, and there are no opportunities for manipulation of other participants.

Dynamic market: The foreign exchange market is dynamic because it provides opportunities to earn a profit based on the market value of a particular currency. This feature is one of the key reasons the market is so large, as it opens it up to many more market participants, such as people who need foreign currency for transacting purposes, hedging purposes, and speculators.

Operates 24 hours: Japan is the first country to operate a foreign currency market based on time zone. As other countries start and end their days, the market moves to the next time zone, with the Americas being the last to operate on a given day. There is still trading in the foreign currency market at any given time.

Lower trading Cost: The foreign exchange market offers low trading costs due to its lack of restrictive barriers to entry and high fees. Small percentages are charged for transactions, making it favorable for small participants and widening the market. In other markets, brokers require large sums to participate and charge large transaction fees.

8. What is a Bond? Explain the Characteristics of Bonds.

Bonds refer to high-security debt instruments that enable an entity to raise funds and fulfill capital requirements. It is a category of debt that borrowers avail from individual investors for a specified tenure.

- **Face Value:** Face value implies the price of a single unit of a bond issued by an enterprise. Principal, nominal, or par value is used alternatively to refer to the price of bonds. Issuers are under a legal obligation to return this value to the investor after a stipulated period.
  Bond example - an investor chooses to purchase a corporate bond at a face value of Rs. 6,500. The company issuing the bond is thus obliged to return Rs. 6,500 plus interest to the investor after the maturity of the tenor. Note that the face value of a bond is different from its market value as market operations influence the latter.

- **Interest or Coupon Rate:** Bonds accrue fixed or floating rates of interest, known as coupon rates, payable periodically to creditors. Interest earned depends on tenure and the issuer's reputation in the public debt market.

- **Tenure of Bonds:** Tenure is the period after which bonds mature. Short-term bonds have a tenure of less than 5 years, while intermediate-term bonds have a tenure of 5-12 years and long-term bonds have a tenure of more than 12 years. Longer tenures suggest participation in prevailing businesses in the trade market.

- **Credit Quality:** The credit quality of a bond is determined by the degree of confidence investors have in an organization's bonds. Credit rating agencies classify bonds based on the risk of default and categorize them into investment-grade and non-investment-grade debt instruments. Investment-grade securities are susceptible to lower yields, while non-investment-grade securities offer high returns at considerable risks.

- **Tradable Bonds:** Bonds are tradable in the secondary market. The ownership can thus shift among various investors within a given tenure. These creditors often sell their bonds to other entities when market prices exceed the nominal values as they have an option to secure bonds with high yield and appropriate credit ratings.

9. What are the Pros and cons of Mortgage-Backed Security (MBS)?

MBS Pros and Cons

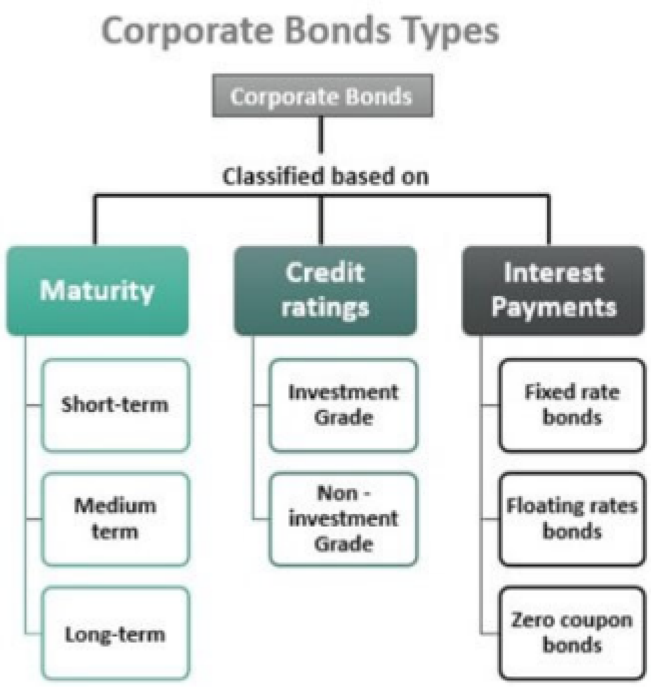
Pros

- Fixed interest rate and monthly payouts.
- More diversification than single loans.
- Relatively low correlation with corporate bonds or the stock market.

Cons

- Returns may be affected by borrowers refinancing or paying off their loans early.
- If interest rates increase, the price of an MBS may drop.

10. What are the Types of Corporate Bonds?



11. Distinguish between Corporate Bonds and Government Bonds.

Corporate Bonds	Government Bonds
Corporate bonds are issued by private companies to meet a variety of business needs.	Government bonds are issued by the central/ union or state governments to fund various government projects.
Corporate bonds typically pay interest at different intervals – Monthly, quarterly, semi-annually and annually.	The government pays interest on the face value of the bond annually.
Corporate bonds are risky because they include market risk, credit risk, and interest rate risk.	Government bonds are considered as one of the safest investment options because they carry sovereign guarantees.
The returns will be high because there is a lot of room for growth.	Government bonds give less yield returns than corporate bonds because the risk in these instruments is lower.
Corporate bonds have maturities ranging from 1 to 25 years.	Government bonds are generally issued for terms ranging from 5 to 30 years. Since it is a long tenure, it loses its relevance.

12. Write short notes on:-

a. Spot market

A spot market is a financial market where financial instruments and commodities are traded for instantaneous delivery. Delivery refers to the physical exchange of a financial instrument or commodity with a cash consideration. The spot market is also known as the cash market or physical market because cash payments are processed immediately, and there is a physical exchange of assets.

Characteristics of Spot Markets

- Transactions are settled at the ruling price known as the spot price or spot rate.
- Delivery of the asset takes place immediately or otherwise at T+2.
- Transfer of funds is instantaneous; otherwise, settlement can be at T+2.

b. Corporate Bonds

Corporate bonds are debt securities that public and private companies issue to raise funds and serve their various business purposes. Investors who purchase these bonds become the lending entity for these firms, which pay them interest on the principal amount and return the same once the bond matures.

Features:

High Credit Quality: When individuals or entities invest in corporate bonds, they spend on a high-quality component. Therefore, such bonds ensure a higher return on investment. The bondholders receive the interest on the principal until the firms repay the complete amount after the bond matures.

Highly Liquid: These bonds trade frequently, allowing investors to keep the investment safe for the desired period. It means the investors can invest for two to three years at once and keep enjoying the interest on the same for the desired period and then get the full amount repaid after maturity.

Risk-resistant: Such bonds are less riskier than others. It is because the investors invest after they assess the issuer's creditworthiness. Hence, they know they will surely get back their loan amount. In addition, these bonds become collateral-backed if the bondholders have any doubts relating to timely payment or repayment.

Varied Options: Corporate bonds are classified based on credit quality, interest payments, and maturity periods. As a result, investors get a wide range of alternatives while choosing which bond to invest in as per their convenience and requirements.

c. Functions of RBI

Upar hai

d. Over–the–counter (OTC)market

Upar hai

Question 1: ___________ growth of the country depends on the functions of financial institution.

1. Economic
2. Historical
3. Geographical

Question 2: A financial institution that accepts savings & deposits, gives loans, and with a reasonable rate of interest to its customers is called _____________.

1. Share market
2. Commercial banks
3. Scrap market

Question 3: __________ is one of the financial institution functions which helps investors to find a perfect investment option for investment.

1. Monetary regulation
2. Service
3. Investment consultation

Question 4: Insurance companies accepts risk of uncertain of people with ____________ .

1. Financial assistance
2. Regulation of money
3. Commercial banks

Question 5: Managing assets & investing in the financial market on behalf of the customers the financial institutions act as _____________.

1. Credit unions
2. Helper
3. Trustee

Over the counter market is for

A. selling the share through banker

B. buying /selling of unlisted securities

C. Buying /selling of listed securities

Financial institutions are also known as ______________.

a) Financial organization

b) Financial intermediaries

c) Financial system

d) Any of the above

At which of the following cities is the Head Office of Reserve Bank of India located?

a) Mumbai

b) New Delhi

c) Kolkata

d) Dehradun