



NBFC — Certificate Course on Non-Banking Financial Companies

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CH-1 Indian Financial System

Topic 1 — Financial System

- **Meaning** — A **financial system** is an economic arrangement of institutions and practices.
- **Purpose** — Through it, funds and assets move between **borrowers, lenders and investors**.
- **Levels** — It exists at firm-specific, regional and global levels.

It is a mixture of inter-related **intermediaries, markets and instruments**, and its core economic job is to transform **savings into investment**.

Component	Examples
Institutions / intermediaries	Banks, government treasuries, insurance companies, loan companies (NBFCs), mutual funds
Markets	Money market, debt market, forex market, capital (stock) market, insurance market
Instruments	Deposits, T-bills, CDs, CPs, bonds, debentures, shares, MF units, insurance policies

Topic 2 — Regulators of the Financial System

Each segment of the Indian financial system has its own regulator. A single entity may be registered with one regulator and exempt from registration with another for the same activity.

Regulator	Core role	Supervises
RBI (central banking authority)	Monetary control; management of government debt; banker to government; lender of last resort to banks; regulates money markets through CRR, SLR, repo rate, Bank Rate, MSF	Commercial banks, NBFCs (including HFCs), primary dealers, financial institutions, co-operative banks, clearing and settlement systems
SEBI (capital market regulator)	Equity and debt market supervision	Stock exchanges, brokers, equity and debt raisers, merchant bankers, FPIs, mutual funds, listed companies, registrars, custodians, depositories
IRDAI	Rules for running insurance business; regulates pricing, investments and cost structure of insurers; regulates insurance brokers and agencies, including banks acting as agents	All life and general insurers, reinsurers, intermediaries
PFRDA	Regulates covered pension arrangements	NPS, pension fund managers, CRAs, other pension intermediaries

- **Two roles** — The **Reserve Bank of India** acts as **monetary authority** and as **regulator-supervisor**.
- **Coverage** — It regulates banks and specified NBFCs, including **housing finance companies**.
- **HFCs** — HFCs are **not** outside RBI regulation.

Exemption from RBI registration

- **Principle** — Entities already regulated by another regulator may get **exemption from RBI registration** as NBFCs for that activity.
- **See** — Ch 3 (p. 10) for the exempt entities and the conditions of each exemption.

Topic 3 — Commercial Banks and Co-operative Banks

- **Composition** — The commercial banking system comprises **public sector, private sector and foreign banks**.
- **Specialised categories** — Small finance banks, payments banks, RRBs and local area banks are specialised categories.
- **Legal definition** — **Section 5(b) of the Banking Regulation Act, 1949** defines **banking**.
- **Meaning of banking** — It means accepting deposits of money from the public for the purpose of **lending or investment**.
- **Nature of deposits** — Deposits are **repayable on demand or otherwise** and **withdrawable by cheque, draft, order or otherwise**.

Tools of RBI regulation

- **Statutory and prudential** — RBI regulates commercial banks through **statutory and prudential regulations**.
- **Guidelines** — It also issues other regulatory guidelines.
- **Moral suasion** — It uses **moral suasion**: speeches of the Governor and Deputy Governors, periodic meetings and seminars.

The **rural co-operative credit system** is mandated mainly to ensure flow of credit to **agriculture**. It has **short-term** and **long-term** structures.

Tier (short-term structure)	Level
Primary Agricultural Credit Societies (PACS)	Village
Central Co-operative Banks (CCBs)	District
State Co-operative Banks (StCBs)	State

Primary Co-operative Banks, also called **Urban Co-operative Banks (UCBs)**, serve customers in **urban and semi-urban** areas.

Remember this

- Short-term co-operative credit: **PACS (village) → CCB (district) → StCB (state)**.

Topic 4 — Securities and Exchange Board of India (SEBI)

- **Origin** — SEBI was first set up as a **non-statutory body**.
- **Statutory status** — Statutory powers came with the **SEBI Act, 1992**.
- **Mandate** — It must **protect investors** in securities.
- **Market role** — It must **promote the development of and regulate** the securities market.

Function	Activities
Protective	Protect investor interests; check price rigging , fraud and cheating; prohibit insider trading (dealing on unpublished price-sensitive information, UPSI); issue investor-protection guidelines
Developmental	Train market intermediaries; facilitate internet trading through registered intermediaries; underwriting requirements depend on the issue and SEBI rules (not universally optional)

Function	Activities
Regulatory	Codes of conduct for intermediaries. Register and regulate stock brokers, share transfer agents, trustees, merchant bankers, underwriters, mutual funds, depositories, custodians, FPIs and credit rating agencies.
Regulatory (contd.)	Inquiries and audit of stock exchanges. Approve exchange by-laws . Inspect books and call for periodical returns from recognised exchanges.

Topic 5 — National Housing Bank (NHB)

- **Law** — NHB was set up under the **National Housing Bank Act, 1987**.
- **Role** — It is the principal agency to promote **housing finance institutions** at local and regional levels.
- **Support** — It provides them financial and other support.
- **Ownership** — It is **wholly owned by the Government of India** after RBI's shareholding was transferred to the Government.
- **Shift to RBI** — Registration and regulation of **HFCs** moved from NHB to **RBI** from **9 August 2019**.
- **Legal basis** — RBI now administers HFC registration under **Section 29A of the NHB Act**.
- **NHB's role** — NHB retains **supervision** (on-site and off-site surveillance) and development and refinance roles.
- **Old directions** — Older NHB directions, including ALM instructions, must be read with current RBI rules.

Function	Activities
Supervision	On-site and off-site surveillance of the housing finance sector
Financial support	Refinance to primary lenders for eligible individual housing loans. Refinance for project loans to implementing agencies. Direct finance to public housing agencies for housing and related infrastructure.
Financial support (contd.)	Guarantee of principal and interest on HFC bonds. Acts as SPV for securitising housing loan receivables.
Promotion and development	Facilitator for new HFCs. Model Memorandum and Articles of Association. Guidelines for equity participation in HFCs. Refinance to eligible registered HFCs and approved lenders. Bond-guarantee scheme. Training programmes for the sector.

Topic 6 — Insurance Regulatory and Development Authority of India (IRDAI)

- **Status** — IRDAI is an **autonomous statutory body** under the **IRDA Act, 1999**.
- **Origin** — It was set up on the recommendations of the **Malhotra Committee**.
- **Purpose** — It regulates and develops the business of **insurance and reinsurance**.
- **Objectives** — Its two objectives are **policyholder protection** and **healthy growth** of the insurance market.

Malhotra Committee area	Key proposals (historical reform agenda)
Structure	Government stake in insurers to come down to 50% ; Government to take over GIC's holdings so subsidiaries act independently; greater operating freedom for all insurers

Malhotra Committee area	Key proposals (historical reform agenda)
Competition	Private insurers with minimum paid-up capital ₹100 crore . No single entity to do both life and general business. Foreign insurers with domestic partners.
Competition (contd.)	Postal Life Insurance in rural markets. One state-level life insurer per state. An insurance regulator to be set up.
Investment	Mandatory investment of LIC life funds in government securities to be cut from 75% to 50% ; GIC and subsidiaries not to hold more than 5% in any company
Customer service	LIC to pay interest on payment delays beyond 30 days ; unit-linked pension plans; computerisation and technology upgrades

Current position

- **Capital** — Minimum paid-up capital remains **₹100 crore** for life and general insurers.
- **Reinsurers** — Reinsurers need **₹200 crore**.
- **No composite licence** — A single insurer still cannot write both life and non-life business.
- **2025 Act** — The **Sabka Bima Sabki Raksha (Amendment of Insurance Laws) Act, 2025** permits up to **100% FDI** in insurers.
- **New power** — The same Act empowers IRDAI to **disgorge wrongful gains**.
- **Head** — IRDAI is headed by a full-time **Chairperson**.
- **Members** — It has up to **five whole-time** and **four part-time members**.
- **Appointment** — All are appointed by the Government.
- **Duty** — Under Section 14 of the IRDA Act, it regulates, promotes and ensures orderly growth of insurance and reinsurance business.

Powers and functions	Entities regulated
Grant, renew, modify, withdraw, suspend or cancel registration . Protect policyholders. Prescribe qualifications, code of conduct and training for intermediaries and agents. Promote professional bodies.	Life insurers (public and private); general insurers (public and private); reinsurers; agency channels; insurance intermediaries (brokers, corporate agents, surveyors, TPAs)
Inspect, investigate and audit insurers and intermediaries. Prescribe form of books of account. Regulate investment of funds . Adjudicate disputes between insurers and intermediaries.	

Topic 7 — Pension Fund Regulatory and Development Authority (PFRDA)

- **Origin** — PFRDA began as an **interim** body.
- **Statutory status** — It became statutory under the **PFRDA Act, 2013**, effective **1 February 2014**.
- **Role** — It promotes, regulates and develops the **pension sector**.
- **Ministry** — It works under the **Ministry of Finance**.
- **NPS** — The **National Pension System (NPS)** is governed by PFRDA.
- Protect pension subscribers' interests; promote, regulate and develop pension funds

- Promote pension products for old-age financial needs and educate citizens on pensions
- Appoint intermediaries such as **Pension Fund Managers** and the **Central Recordkeeping Agency (CRA)**; train and inform intermediaries
- Address grievances of subscribers and resolve disputes between intermediaries

Topic 8 — Referral Services by Banks

Banks may offer **referral services** for third-party financial products to their customers, subject to conditions in RBI's directions on para-banking activities.

Condition	Requirement
KYC/AML	Bank and third-party issuer strictly follow KYC/AML norms for referred customers
Issuer selection	Choose third-party issuers so as to manage the bank's reputational risk
Disclosure	Tell the customer upfront that it is purely a referral, on a non-risk participation basis
Issuer compliance	Third-party issuers follow regulations applicable to them
Bank compliance	Bank follows relevant RBI guidelines while offering referral

Topic 9 — National Bank for Agriculture and Rural Development (NABARD)

- **Origin** — NABARD was formed on the recommendation of the **CRAFICARD** committee, chaired by **B. Sivaraman**.
- **Functions taken over** — It took over RBI's agricultural credit functions.
- **ARDC** — It also took over the refinance functions of the **Agricultural Refinance and Development Corporation (ARDC)**.
- **Status** — It is the **apex institution** for policy, planning and operations in agriculture and other rural economic activities.

Function	Activities
Financial / credit	Frame policy for rural financial institutions; provide credit to them; monitor rural credit flow; finalise annual district credit plans; refinance to StCBs, Land Development Banks, RRBs and other approved institutions
Developmental	Monitor banks' development action plans; fund training institutes of co-operative banks, commercial banks and RRBs; support MIS, computerisation and HR development of co-operative banks
Supervisory	Inspect RRBs and co-operative banks other than UCBs under the BR Act, 1949. Voluntary inspection of SCARDBs and apex non-credit co-operatives.
Supervisory (contd.)	Recommend to RBI on licences to co-operative banks and branches of StCBs and RRBs. Portfolio inspections and off-site surveillance.

Remember this

- NABARD supervises **RRBs, StCBs and DCCBs**; **UCBs** are supervised by **RBI**.

Topic 10 — Non-Banking Financial Companies (NBFCs)

- **Meaning** — An **NBFC** is a company registered under the Companies Act.

- **Principal business** — It is engaged **principally** in financial activities.
- **Activities** — These include **loans and advances, acquisition of securities, leasing and hire-purchase**.
- **Deposits** — Only **authorised deposit-taking** NBFCs may accept permitted public deposits.
- **Not banks** — Even deposit-taking NBFCs are **not banks**.
- **See** — Ch 3 (p. 10) for the statutory definition of an NBFC and the activities excluded from NBFC business.

Principal business test (both conditions must be met):

Test	Condition
Asset test	Financial assets > 50% of total assets (netted off by intangible assets)
Income test	Income from financial assets > 50% of gross income

$$\frac{\text{Financial assets}}{\text{Total assets} - \text{Intangible assets}} > 50\%$$

$$\frac{\text{Income from financial assets}}{\text{Gross income}} > 50\%$$

Example: Total assets ₹500 crore (intangibles ₹20 crore), financial assets ₹260 crore → $260/480 = 54.2\%$ (passes). Gross income ₹80 crore, financial income ₹38 crore → 47.5% (fails). The company is **not** an NBFC by principal business.

- **Not banks** — NBFCs cannot accept demand deposits, are not part of the payment and settlement system and cannot issue cheques drawn on themselves; their deposits have no DICGC cover (bank deposits are covered up to ₹5 lakh).
- **See** — Ch 11 (p. 43) for NBFC deposits compared with bank deposits.

Topic 11 — Primary Dealers

- **Introduction** — RBI introduced **Primary Dealers (PDs)** in the Government Securities (G-sec) market.
- **Meaning** — PDs are RBI-registered entities authorised to buy and sell government securities.
- **Infrastructure** — The PD system aims to **strengthen G-sec market infrastructure**.
- **Capability** — It builds **underwriting and market-making** capability.
- **Liquidity** — It improves **secondary market trading**.
- **OMO** — It makes PDs an effective conduit for **Open Market Operations (OMO)**.

PDs are of two kinds: **standalone PDs** (NBFCs, e.g. SBI DFHI, PNB Gilts, ICICI Securities PD, STCI PD) and **bank PDs** — scheduled commercial banks (**except RRBs**) doing PD business **departmentally**.

Facility (subject to PD category, eligibility and current RBI directions)
Current account and Subsidiary General Ledger (SGL) account with RBI
e-Kuber access for primary auctions
Borrow and lend in the money market, including call money , and trade all money market instruments
Membership of NDS platforms, INFINET, RTGS and CCIL
Access to RBI's Liquidity Adjustment Facility (LAF) and to OMOs
Separately notified liquidity support scheme for standalone PDs

Topic 12 — Foreign Investment in India

- **Need** — Capital is a key input for growth.
- **Gap** — Domestic resources alone cannot meet the requirement, so countries attract **foreign investors**.
- **Uses** — Foreign capital funds **infrastructure**, manufacturing facilities, service hubs and productive assets such as machinery.
- **Result** — It stimulates **growth and employment**.

Topic 13 — All India Financial Institutions

There are **five All India Financial Institutions (AIFIs)** regulated by RBI, each with a distinct mandate. IFCI and MUDRA are **not** in this category.

AIFI	Mandate
EXIM Bank	Export and import finance
NABARD	Agriculture and rural development
NaBFID	Long-term infrastructure finance
NHB	Housing finance support and refinance
SIDBI	Finance for small (MSME) industry

Older institution charts carry legacy names. For example, **Capital Local Area Bank** became **Capital Small Finance Bank**; always use the entity's current RBI category.

Remember this

- Five AIFIs: EXIM, NABARD, NaBFID, NHB, SIDBI.

NBFC | Module A | CH-1 | MCQs

Q1. An entity accepts deposits from the public for lending, repayable on demand and withdrawable by cheque. Under the Banking Regulation Act, this activity is: [Ref: Topic 3, p. 2]

- (a) Banking under Section 5(b)
(b) Non-banking financial business
(c) Para-banking
(d) Merchant banking

Q2. Which institution is the regulator of housing finance companies today? [Ref: Topic 5, p. 3]

- (a) National Housing Bank
(b) Reserve Bank of India
(c) SEBI
(d) Ministry of Housing

Q3. A company has financial assets of 55% of total assets (net of intangibles) and financial income of 48% of gross income. It is: [Ref: Topic 10, p. 4]

- (a) An NBFC, since one test is met
(b) An NBFC, since asset test prevails
(c) Not an NBFC by principal business
(d) A deposit-taking NBFC

Q4. A customer asks whether his fixed deposit with an authorised deposit-taking NBFC is insured. The correct reply is: [Ref: Topic 10, p. 4]

- (a) Insured up to ₹5 lakh by DICGC
(b) Insured up to ₹1 lakh by DICGC
(c) Insured by RBI
(d) Not covered by DICGC insurance

Q5. In the short-term rural co-operative credit structure, the institution operating at district level is the: [Ref: Topic 3, p. 2]

- (a) PACS
(b) Central Co-operative Bank
(c) State Co-operative Bank
(d) Urban Co-operative Bank

Q6. Which entity is NOT supervised by NABARD? [Ref: Topic 9, p. 4]

- (a) Regional Rural Banks
(b) State Co-operative Banks
(c) Urban Co-operative Banks
(d) District Central Co-operative Banks

Q7. A bank refers its customers to a mutual fund. Which condition must it satisfy? [Ref: Topic 8, p. 4]

- (a) Share the risk of the product
(b) Guarantee the returns
(c) Avoid KYC to speed up referral
(d) Disclose that it is purely a referral on non-risk participation basis

Q8. Checking price rigging and prohibiting insider trading fall under which category of SEBI functions? [Ref: Topic 4, p. 2]

- (a) Protective
(b) Developmental
(c) Regulatory
(d) Supervisory of banks

Q9. Which of the following is one of the five All India Financial Institutions regulated by RBI? [Ref: Topic 13, p. 5]

- (a) IFCI
(b) NaBFID
(c) MUDRA
(d) SBI DFHI

Q10. Which function of NHB involves acting as an SPV for securitising housing loan receivables? [Ref: Topic 5, p. 3]

- (a) Supervision
(b) Regulation
(c) Financial support
(d) Registration

Q11. Under current insurance law, a new life insurer wishes to also sell motor insurance from the same company. The position is: [Ref: Topic 6, p. 3]

- (a) Permitted with IRDAI approval
(b) Permitted if capital is ₹200 crore
(c) Permitted only for foreign insurers
(d) Not permitted, as composite licences are not allowed

Q12. The minimum paid-up capital required to start a reinsurance company in India is: [Ref: Topic 6, p. 3]

- (a) ₹200 crore
(b) ₹100 crore
(c) ₹50 crore
(d) ₹500 crore

Q13. Which bank is NOT permitted to undertake primary dealer business departmentally? [Ref: Topic 11, p. 4]

- (a) A private sector bank
(b) A Regional Rural Bank
(c) A public sector bank
(d) A foreign bank

Q14. Appointment of Pension Fund Managers and the Central Recordkeeping Agency is done by: [Ref: Topic 7, p. 3]

- (a) IRDAI
(b) SEBI
(c) PFRDA
(d) RBI

Q15. Which tool lets RBI influence banks without issuing a binding direction? [Ref: Topic 3, p. 2]

- (a) CRR
(b) SLR
(c) Repo rate
(d) Moral suasion

Answer key

Q	Ans	Q	Ans	Q	Ans	Q	Ans	Q	Ans
1	a	4	d	7	d	10	c	13	b
2	b	5	b	8	a	11	d	14	c
3	c	6	c	9	b	12	a	15	d

CH-2 Markets

Topic 1 — Financial Markets and Sub-markets

- **Meaning** — A **financial market** is any place or system where buyers and sellers trade financial instruments.
- **Instruments** — These include **bonds, equities, currencies and derivatives**.
- **Role** — It connects those who **need capital** with those who **have capital** to invest.

Basis	Money market	Capital market
Tenor	Short-term, generally up to one year	Long-term funds through equity and debt
Purpose	Meet liquidity needs; assets are close substitutes of money	Fund investment and capital expenditure
Risk	Liquidity and default risk vary by instrument and issuer; short tenor alone does not remove risk	Market, credit and liquidity risk

Capital market segment	Role
Primary market	Sale of new securities by the issuer to raise funds or discharge obligations
Secondary market	Trading of already-issued securities between investors as their risk-return view changes

The two segments are **interdependent and inseparable**. Indian financial sub-markets are: **money market, debt market, foreign exchange market, capital market, mutual funds and insurance market**.

Topic 2 — Development of the Indian Money Market

- **Segments** — The Indian money market has **organised** and **unorganised** segments.
- **Pre-reform gaps** — Before the reforms it lacked instruments and depth and had micro-structure distortions.
- **Pre-reform instruments** — It consisted mainly of the **uncollateralised call market, treasury bills, commercial bills and participation certificates**.

Committee	Key outcomes
Chakravarty Committee	RBI adopted a monetary targeting framework
Vaghul Committee	DFHI set up to give liquidity and a secondary market to money market instruments; CDs, CPs and IBPCs (with and without risk sharing) introduced; call money rates freed for price discovery
Internal Working Group and Narasimham Committee	Withdrawal of money market interest rate ceilings ; auctions of treasury bills; move from cash credit to a loan-based system

Topic 3 — Participants in the Money Market

Eligible participants in call and notice money

- **Access** — Call and notice money is open only to eligible institutions.

- **Banks** — **Scheduled commercial banks (excluding local area banks), payments banks, small finance banks and RRBs** are eligible.
- **Others** — **Specified co-operative banks and primary dealers** are also eligible.
- **Limits** — Each participant works within RBI's category-wise limits.

Participant	Role
Banks (incl. RRBs)	Act as both lender and borrower ; the link between RBI and the market, through which RBI controls liquidity and transmits monetary policy
SBI DFHI Ltd	Formed by merging DFHI (set up by RBI with public sector banks and AIFIs) with SBI Gilts ; smooths short-term liquidity imbalances through an active secondary market
PSUs	Issue bonds for working capital and capex; invest in CDs and T-bills
Public financial institutions	UTI, LIC, general insurers, ECGC, NABARD — add participants and depth
Money market mutual funds	Invest solely in short-term instruments per scheme mandate; credit, interest-rate and liquidity risks; principal and returns not guaranteed
NBFCs	Invest surplus funds within prudential rules; liquid-asset rules for deposit-taking NBFCs do not require every NBFC to buy bonds
Bank subsidiaries	Merchant banking subsidiaries deal in money market instruments
Primary dealers	Underwriting and market-making in G-secs; conduit for OMO
Corporates	Invest in CDs; issue CPs and debentures; large treasuries trade G-secs
Credit rating agencies	Not direct participants but integral; rate short-term instruments

- **Registered CRAs** — SEBI-registered credit rating agencies include **CRISIL, ICRA, CARE, India Ratings (Fitch group), Acuité (formerly SMERA) and Infomercials**.
- **Brickwork** — **Brickwork Ratings** is **no longer registered**; its SEBI registration was cancelled.

Topic 4 — Features of Money Market Instruments

Feature	Position
Duration	Generally mature within one year ; instrument-specific minimum tenors apply
Liquidity	Trading depth and exit cost vary; conversion to cash at low cost is not guaranteed
Safety	Sovereign bills and bank or corporate paper carry different credit risk; a rating is an opinion , not a repayment guarantee
Interest rates	Market-driven and deregulated
Access	Instrument-specific: call money only for eligible institutions; residents, including individuals, may invest in CDs and CPs