

SFB — Certificate Course for Small Finance Banks

Complete Book | Table of Contents | 30 chapters + 9 sections

Module A — Financial System, Regulation and SFB Framework

CH-1	Financial System	2
CH-2	Banking Regulations	5
CH-3	Setting Up of a Small Finance Bank	9
CH-4	Financial Inclusion and Financial Literacy	13
CH-5	Government Sponsored Credit-Linked Schemes	16
CH-6	Risk Management	20

Module B — Operational Aspects of Banking

CH-7	Operations of Banks	23
CH-8	Maintenance of Accounts	27
CH-9	Know Your Customer and Anti-Money Laundering	32
CH-10	Banker Special Relationship	36
CH-11	Negotiable Instrument	40

Module C — Credit Management

CH-12	Principles of Lending, Working Capital Assessment and Credit Monitoring	44
CH-13	Documentation	48
CH-14	Different Modes of Charges	51
CH-15	Priority Sector Advances	55
CH-16	Non-Performing Assets	59
CH-17	Agricultural Advances	62
CH-18	Recovery of Loans	65
CH-19	Credit Guarantee Schemes	69
CH-20	Foreign Exchange	73

Module D — Marketing and Customer Relationship Management

CH-21	Marketing	76
CH-22	Consumer Behaviour	81
CH-23	Pricing and Distribution	85
CH-24	Channel Management	89
CH-25	Para Banking Activities	92
CH-26	Data Communication	96
CH-27	Customer Service	100
CH-28	Payment Systems and Electronic Banking	103
CH-29	Consumer Protection	107
CH-30	Soft Skills and Leadership Skills	111

Additional Resources

—	Case Studies — Module A: Financial System, Regulation and SFB Framework	116
—	Case Studies — Module B: Operational Aspects of Banking	119
—	Case Studies — Module C: Credit Management	121
—	Case Studies — Module D: Marketing and Customer Relationship Management	125
—	Mega Tests — Mega Test 1 — 100 Questions (Full Syllabus)	130
—	Mega Tests — Mega Test 2 — 100 Questions (Full Syllabus)	137
—	Mega Tests — Mega Test 3 — 100 Questions (Full Syllabus)	144
—	Mega Tests — Mega Test 4 — 100 Questions (Full Syllabus)	150
—	Mega Tests — Mega Test 5 — 100 Questions (Full Syllabus)	157

CH-1 Financial System

Topic 1 — Financial System

- **Meaning** — A **financial system** is the set of **institutions, markets, instruments and practices** that moves funds.
- **Direction** — Funds flow from **surplus sectors** (savers, lenders, investors) to **deficit sectors** (borrowers, spenders).
- **Levels** — It exists at firm-specific, regional and global levels.
- **Role** — It transforms **savings into investment and consumption**.
- **Intermediaries** — **Financial intermediaries** (banks, financial institutions, mutual funds) stand between investors and spenders.
- **Assets** — They offer financial assets that suit both sides.
- **Market** — The place where these transactions happen is the **financial market**.

Component	Role	Examples
Institutions / intermediaries	Mobilise savings and allocate them to needy sectors	Banks, government treasuries, insurance companies, loan companies, mutual funds
Markets	Place where financial assets are traded and priced	Money, debt, forex and capital markets; stock exchanges
Instruments	Claims that carry funds from savers to users	Deposits, T-bills, CDs, CPs, G-secs, bonds, shares, units
Regulators	Set rules and supervise each segment	RBI, SEBI, IRDAI, PFRDA

Topic 2 — Segments of the Financial Market

The financial market has four segments: **money market** (short term, up to 1 year), **debt market**, **forex market** and **capital market** (long term).

Segment	Instruments / participants
Money market	Call/notice money, Treasury Bills , term money, Certificates of Deposit , Inter-Corporate Deposits (ICD), Commercial Paper , repo, commercial bills
Debt market	Government securities — Central Government and State Governments; Bonds — FI bonds, PSU bonds, corporate securities
Forex market	Purchase and sale of foreign currencies by Authorised Dealers and their customers
Capital market	Equity and long-term debt; stock exchanges, brokers, depositories, mutual funds

Remember this

- Call money = **overnight**; notice money = **2 to 14 days**; term money = **15 days to 1 year**.

Topic 3 — Regulators of the Financial System

Each segment has its own regulator. RBI is the **central banking authority**; SEBI regulates the **capital market**; IRDAI and PFRDA regulate **insurance and pensions**.

Regulator	Functions and entities supervised
RBI (central banking authority)	Monetary control (CRR, SLR, repo, Bank Rate, MSF). Supervises banks, NBFCs, primary dealers, FIs, co-op banks, clearing and settlement . Manages government debt. Banker to Government. Lender of last resort . Regulates money markets.

Regulator	Functions and entities supervised
SEBI (capital market regulator)	Supervises equity and debt markets: stock exchanges, brokers , equity and debt raisers, merchant bankers, Foreign Portfolio Investors , custodians, depositories, mutual funds , listed companies, registrars, other service providers.
IRDAI (insurance)	Rules for running insurance business; supervision of life and general insurers; regulating pricing, investments and cost structure; regulating insurance brokers and agents
PFRDA (pension)	Regulates pension arrangements, including NPS

Topic 4 — RBI as the Central Banking

Authority

- **RBI** — RBI is constituted under **Section 3 of the RBI Act, 1934**.
- **Banks** — Banks are separately regulated under the **Banking Regulation Act, 1949**.
- **Others** — Banks, NBFCs and development financial institutions each have their own legal mandate.
- **Core roles** — RBI has two core roles: **monetary control** (including inflation control) and **bank supervision**.
- **Currency** — With the Government, RBI designs, produces and manages the currency.
- **Aim** — This ensures an adequate supply of **clean and genuine notes**.

Function	What RBI does
Payment and settlement	Runs an efficient payment and settlement system — clearing houses, currency chests across regions and electronic funds transfer
Management of government debt	Manages issue and servicing of government debt: price discovery, volume, tenure, matching with cash management
Banker to Government	Holds the Government's cash balances, gives temporary loans to Central and State Governments, manages Central Government debt; acts for State Governments by agreement
Lender of last resort	Provides liquidity to banks in crisis that cannot raise funds elsewhere, under its statutory powers and terms; it is not a guarantee against every bank failure
Inflation control	Through CRR and SLR and policy rates
Financial inclusion and development	Financial inclusion, financial education and literacy, credit to productive sectors including rural and MSME

- **CRR** — The prescribed percentage of **net demand and time liabilities (NDTL)** kept as cash balance with RBI; currently **3% of NDTL**.
- **SLR** — Kept in eligible **cash, gold and approved securities**; currently **18% of NDTL**.
- **Effect** — A higher CRR or SLR, other things equal, reduces banks' freely lendable funds.
- **Caution** — The actual effect on money supply also depends on credit demand and policy conditions.
- **Risk** — SLR assets are not all risk-free.

Topic 5 — Constituents of the Indian Banking System

Category	Constituents
Public sector banks	State Bank of India; nationalised banks
Private sector banks	Old private sector banks; new private sector banks; foreign banks; Payments Banks ; Small Finance Banks ; Local Area Banks
Regional Rural Banks	RRBs
Rural co-operatives	State Co-operative Banks and District Central Co-operative Banks
Urban co-operatives	Urban Co-operative Banks

- **IDBI Bank** is classified as a **private sector bank**; **Bharatiya Mahila Bank** has merged with SBI.
- **Capital Local Area Bank** became **Capital Small Finance Bank**.
- The **Banking Regulation Act, 1949** is the framework for supervising and regulating commercial banking; co-operative banks were brought under it by adding **Section 56**.
- Names, status and counts in older diagrams are dated illustrations; SFBs and Payments Banks hold **distinct licences** with defined permitted activities.

Differentiated bank	Objective
Small Finance Bank	Further financial inclusion. Give savings vehicles and credit to small units, small and marginal farmers , micro and small industries and other unorganised entities. Use high-technology , low-cost operations .
Payments Bank	Further financial inclusion. Give small savings accounts and payment/remittance services to migrant labour, low-income households, small businesses and other unorganised users. End-of-day cap ₹2 lakh per customer. No lending .

Topic 6 — Non-Banking Financial Companies

- **Meaning** — **NBFCs** provide bank-like financial services **without a banking licence**.
- **Services** — These include lending, investment, leasing and related services.
- **Registration** — RBI registration is generally required.
- **Check** — Activity-specific exemptions and other regulators' jurisdiction must be checked.

A company is in the business of a financial institution only if it passes the **principal business test** — **both** conditions must be met:

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

$$\frac{\text{Financial income}}{\text{Gross income}} > 50\%$$

Example: Total assets ₹1,000 crore, intangibles ₹50 crore, financial assets ₹520 crore → $520 \div 950 = 54.7\%$. Gross income ₹200 crore, financial income ₹110 crore → 55% . Both exceed 50%, so the company must register as an NBFC.

Point	Position
Public deposits	Registration alone does not permit public deposits; only authorised deposit-taking NBFCs may accept permitted deposits
Demand deposits	NBFCs cannot accept demand deposits
Cheques	NBFCs cannot issue cheques drawn on themselves

Point	Position
Deposit insurance	No DICGC cover for NBFC deposits
Public funds	Include more than public deposits; borrowing does not amount to a bank licence

Topic 7 — Primary Dealers and Financial Institutions

Primary Dealers (PDs) deal in **government securities** in both the **primary and secondary markets**. They act as **market makers** and strengthen the G-sec market.

- **FIs — Financial Institutions (FIs)** deal in investments, loans and deposits.
- **DFIs — Development financial institutions** provide **long-term funds** for industry and agriculture.
- **Regulation** — RBI regulates the specified **All India Financial Institutions (AIFIs)**.
- **Others** — Other development institutions have their own mandates and oversight.

AIFI	Focus
EXIM Bank	Exports
NABARD	Agriculture and rural development
NHB	Housing finance
SIDBI	Micro, small and medium enterprises
NaBFID	Infrastructure financing

Remember this

- RBI-regulated AIFIs = **5**: EXIM Bank, NABARD, NHB, SIDBI, NaBFID.

Topic 8 — Equity and Debt Market Intermediaries

Financial markets are where financial assets are traded. The **equity market** deals in equity-related securities and the **debt market** in debt securities.

Intermediary	Role
Stock exchange	Secure, rule-based place for trading listed shares and debentures of public companies and bonds of government, municipal and public bodies
Brokers	Only SEBI-approved brokers trade on exchanges; they intermediate between buyers and sellers, build the order book, aid price discovery, honour contracts and earn brokerage
Equity and debt raisers	Issuers must comply with SEBI disclosure, issue and listing rules; filing or SEBI observations do not guarantee merit, returns or repayment
Merchant bankers	Manage issues, fund raising, advise on mergers and acquisitions ; licensed by SEBI
Foreign Portfolio Investors (FPIs)	Registered under SEBI's FPI framework and FEMA rules; invest in permitted Indian securities within investment limits (FII is a legacy term)
Depositories	Hold securities in dematerialised form through depository participants , who keep sub-accounts of customers
Mutual funds	Collective investment pooling money into stocks, debt and other securities; risk depends on the scheme; trustees approve schemes and SEBI gives observations on offer documents — no assured returns
Registrars	Maintain registers of share and debenture holders and process allotment; need regulator's approval

- **Settlement** — Securities move from **sellers to buyers** through depository and clearing arrangements.
- **Payment** — Buyers pay funds.



- **Demat** — Dematerialisation changes only the **form** of holding, not this direction.

Topic 9 — Insurance Regulatory and Development Authority of India

- **Status** — IRDAI is the apex **statutory, autonomous** body for the insurance industry.
- **Role** — It regulates and develops the insurance industry.
- **Law** — It was set up under the **IRDA Act, 1999**.
- **Scope** — It regulates both **life and general** insurance.
- Regulates insurers, insurance conduct and products; product filing and approval routes depend on the current regulations — not every product needs identical prior approval.
- Mission: **protect policyholders' interests**, regulate, promote and ensure **orderly growth** of the insurance industry.

Topic 10 — Multi Commodity Exchange of India

MCX is India's **first listed exchange** — a commodity futures exchange offering online trading, clearing and settlement of commodity futures, giving a platform for **risk management**.

- Commodity derivatives are regulated by **SEBI** under the **Securities Contracts (Regulation) Act**; the **Forward Contracts (Regulation) Act, 1952** has been repealed.
- Segments: **bullion, ferrous and non-ferrous metals, energy and agricultural commodities**.
- Provides neutral, secure, transparent trading and sets quality parameters and trade rules within the regulatory framework.

Topic 11 — Development Banks

Development banks provide long-term and developmental finance to specific sectors, including rural economic development. Their mandate must be distinguished from their statutory regulator.

NABARD

- **Set up** — NABARD was set up by a special Act of Parliament (**Act 61 of 1981**).
- **Origin** — It was set up on the recommendation of **CRAFICARD** and started on **12 July 1982**.
- **Role** — It is the **apex institution** for policy, planning and operations in agriculture and other rural economic activities.

Function area	Activities
Financial	Finance for rural infrastructure ; refinance for agriculture and rural non-farm sector
Developmental	District-level credit plans to guide banks; training and marketing platforms for handicraft artisans ; advisory and financial support with global partners
Supervision	Supervises RRBs and co-operative banks ; develops their practices and integration with Core Banking Solution

SIDBI

- **Status** — SIDBI is a statutory body that started on **2 April 1990**.
- **Role** — It is the **principal institution** for the promotion, financing and development of **MSMEs**.
- **Coordination** — It also coordinates institutions doing similar work.
- **Aim** — It aims to be a **single window** for MSME financial and developmental needs.
- **Nodal agency** — It acts as **nodal/implementing agency** for ministries such as MSME, Textiles, Commerce and Industry and Food Processing Industries.

SIDBI support	Form
Indirect	Refinance to banks and financial institutions for onward lending to MSMEs
Direct	Service-sector finance, receivable finance , risk capital, sustainable finance

NHB

- **Set up** — NHB was set up in **July 1988** as the apex financing institution for **housing**.
- **Role** — It promotes sound **Housing Finance Companies (HFCs)** and gives refinance.
- **Ownership** — It is **wholly owned by the Government of India**; RBI's entire shareholding was transferred on **19 March 2019**.
- **Regulation** — **Regulation of HFCs** moved to RBI from **9 August 2019**.
- **Retained** — NHB keeps supervision and development functions.

EXIM Bank

- **Status** — EXIM Bank is India's leading **export financing institution, wholly owned by the Government of India**.
- **Aim** — It integrates foreign trade and investment with economic growth.
- **LOCs** — It extends **Lines of Credit (LOCs)** to overseas governments, institutions and banks.
- **Export credit** — It gives **buyer's credit** and **supplier's credit** to promote exports.

SFB | Module A | CH-1 | MCQs

Q1. A company has financial assets of ₹480 crore, total assets of ₹1,000 crore including ₹60 crore intangibles, and financial income of 58% of gross income. Under the principal business test it:

- Must register as an NBFC, as both ratios exceed 50%
- Need not register, as financial assets are below 50% of total assets
- Must register only as a deposit-taking NBFC
- Need not register, as only the income test applies

Q2. Which is a money market instrument?

- State Government security
- PSU bond
- Commercial Paper
- Corporate debenture

Q3. A broker wants to operate on a stock exchange. Its approval must come from:

- RBI
- SEBI
- IRDAI
- Ministry of Corporate Affairs

Q4. Which entity is supervised by RBI and not by SEBI?

- Merchant banker
- Depository
- Primary Dealer
- Registrar to an issue

Q5. An NBFC holding a certificate of registration (non-deposit-taking) is approached by customers wanting to open a savings-type account with cheque facility. The NBFC:

- Can accept demand deposits up to ₹2 lakh
- Can accept them if covered by DICGC
- Can accept them with Board approval
- Cannot accept demand deposits or issue cheques drawn on itself

Q6. A migrant worker's Payments Bank account reaches ₹2.3 lakh at end of day. This breaches the:

- SLR requirement
- End-of-day balance cap of ₹2 lakh per customer
- Lending limit of the payments bank
- DICGC cover limit

Q7. Which institution supervises Regional Rural Banks and co-operative banks and prepares district-level credit plans?

- SIDBI
- NHB
- EXIM Bank
- NABARD

Q8. A bank needs refinance for its MSME loan book. The institution that provides such refinance is:

- (a) NHB (b) SIDBI (c) NaBFID (d) EXIM Bank

Q9. Registration and regulation of Housing Finance Companies currently rest with:

- (a) NHB (b) SEBI
(c) RBI (d) Ministry of Housing

Q10. An Indian exporter's overseas buyer gets a line of credit through its government. This is typically extended by:

- (a) EXIM Bank (b) NABARD (c) SIDBI (d) NHB

Q11. Commodity futures traded on MCX are regulated by:

- (a) Forward Markets Commission
(b) RBI
(c) IRDAI (d) SEBI

Q12. RBI acts as banker to a State Government:

- (a) Automatically under the RBI Act
(b) Only by agreement with that State Government
(c) Only if the State is in deficit
(d) Never; only the Central Government

Q13. A bank's NDTL is ₹10,000 crore. With CRR at 3% and SLR at 18%, the funds it must keep as CRR balance with RBI and in SLR assets are:

- (a) ₹180 crore and ₹300 crore (b) ₹1,800 crore and ₹300 crore
(c) ₹300 crore and ₹1,800 (d) ₹300 crore and ₹180 crore

Q14. Which statement on mutual funds is correct?

- (a) SEBI observations on the offer document assure returns
(b) All mutual funds are low-risk
(c) Units are covered by DICGC
(d) Risk depends on the scheme and its portfolio

Q15. In the delivery of securities sold on an exchange:

- (a) Securities move from seller to buyer through depository and clearing arrangements; buyer pays funds
(b) Buyer delivers securities and seller pays
(c) Depository pays the seller
(d) Dematerialisation reverses the direction of delivery

Answer key

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

CH-2 Banking Regulations

Topic 1 — Constitution and Objectives of RBI

- Constitution** — The Reserve Bank of India was constituted under the RBI Act, 1934.
- Start** — It began functioning on 1 April 1935 in Calcutta.
- Mumbai** — It moved permanently to Mumbai in 1937.
- Ownership** — It was nationalised in 1949; before that it was held by private shareholders.
- Top management** — The Central Government appoints the Governor and up to four Deputy Governors.
- Central Board** — Management vests in the Central Board under Section 8 of the RBI Act.
- Departments** — Internal management is organised by functional departments, with headquarters at Mumbai.

Central Board member	Number
Governor	1
Deputy Governors	Up to 4
Directors nominated from the Local Boards	4
Other directors nominated by the Central Government	10
Government officials	2

RBI's broad aims are to sustain **public confidence** in the system, **protect depositors** and provide cost-effective banking services. Its main objectives are:

Objective	Purpose
Monetary stability	Let business and economic life deliver the welfare gains of a mixed economy
Financial stability	Sound financial institutions so that economic units can transact with confidence
Stable payment systems	Safe and efficient execution of financial transactions
Credit allocation	Credit should reflect national economic priorities and social concerns
Volume of money and credit	Ensure a reasonable degree of price stability
Market development	Develop financial markets and systems so RBI can operate and regulate efficiently

Topic 2 — Role and Functions of RBI

No.	Function
I	Monetary Authority
II	Issuer of Currency
III	Banker and Debt Manager to Government
IV	Banker to Banks
V	Regulator of the Banking System
VI	Manager of Foreign Exchange
VII	Maintaining Financial Stability
VIII	Regulator and Supervisor of Payment and Settlement Systems
IX	Developmental Role

Topic 3 — Monetary Authority

- Meaning** — Monetary policy uses instruments under the central bank's control.
- What it regulates** — It regulates the **availability, cost and use** of money and credit.
- Goals** — It aims at goals such as low and stable inflation and growth.
- MPC** — The Monetary Policy Committee fixes the **policy repo rate**.
- Objectives**: **price stability**; adequate **credit flow to productive sectors** to support growth; **financial stability**.
- RBI monitors interest rates, inflation, money supply, credit, exchange rate, trade, capital flows, fiscal position and output trends.

Policy rate	Current level
Policy repo rate	5.25%
Standing Deposit Facility (SDF)	5.00%
Marginal Standing Facility (MSF)	5.50%
Bank Rate	5.50% (aligned with MSF)

Topic 4 — Direct Instruments — CRR and SLR

- Meaning** — **Cash Reserve Ratio (CRR)** is the reserve a bank keeps with RBI.