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Faculty of Economics, Commerce and Management Sciences

Commerce Department

Module: English
Branch: Finance and International Trade
Level: Third year Bachelor

Lecture 05: An overview of Bank Sector

This Lecture is To enable the Student to:
– Understand the features of Banking Sector
– Know the significant contribution of different types of banks
– Appreciate how important banking services for the economy

1-Origin of Bank:

According to some writer the word „Bank" was derived from „Banco", „Bancus", „Banque" or „Banc" all of which mean a bench upon which the mediaeval European Money-lenders and Money – Changers used to display their coins. In the Mediaeval age Italian states were sound and solvent economically and commercially. At that time a group of people used to conduct business of transaction of money sitting on a stool or bench which was replaced by „Banco," „Banko" „Banca", „Bangk", „Bancus", „Banc" etc.It is assumed that the word „Bank" was originated from these words.

2-Definition and Characteristics

Banks are the important segment in any economy, especially Financial System. An efficient banking sector helps the nation's economic development. Various categories of stakeholders of the Society use the banks for their different requirements. Banks are financial intermediaries between the depositors and the borrowers. Apart from accepting deposits and lending money, banks in today's changed global business environment offer many more value added services to their clients. The Central Bank of the country plays different roles like the regulator, supervisor and facilitator of the economy's Banking System. In general terms, banks make profits by selling liabilities with one set of characteristics (a particular combination of liquidity, risk, size, and return) and using the proceeds to buy assets with a different set of characteristics. This process is often referred to as *asset transformation.* For example, a savings deposit held by one person can provide the funds that enable the bank to make a mortgage loan to another person. The bank has, in effect, transformed the savings deposit (an asset held by the depositor) into a mortgage loan (an asset held by the bank). Another way

this process of asset transformation is described is to say that the bank "borrows short and lends long" because it makes long-term loans and funds them by issuing short-dated deposits. The process of transforming assets and providing a set of services (check clearing, record keeping, credit analysis, and so forth) is like any other production process in a firm. If the bank produces desirable services at low cost and earns substantial income on its assets, it earns profits; if not, the bank suffers losses.

3- Functions of Commercial Banks

These functions can be divided into two parts:

(a) Major functions

(b) Other functions/ancillary services

(a) Major functions:

(i) Accepting Deposits

(ii) Granting Advances

(b)Other functions:

(i) Discounting of bills and cheques

(ii) Collection of bills and cheques

(iii) Remittances

(iv) Safe custody of articles

(v) Safe Deposit Lockers

(vi) Issue of Letter of Credit

Besides the above functions, Banks now-a-days associate themselves in the following activities also either by

opening separate departments or through separately floated independent subsidiaries:

(i) Investment Counseling

(ii) Investment Banking

(iii) Mutual Fund

(iv) Project Appraisal

(vii) Issue of Guarantees

(v) Merchant Banking Services

(vi) Taxation Advisory Services

(vii) Executor Trustee Services

(viii) Credit Card Services

(ix) Forex Consultancy

(x) Transactions of Government Business

(xi) Securities Trading

(xii) Factoring

(xiii) Gold/Silver/Platinum Trading

(xiv) Venture Capital Financing

(xv) Bankassurance - Selling of Life and General Insurance policies as Corporate Agent

4-Distinguish between Central Bank and Commercial Bank:

The following points of distinction between central bank and commercial bank:

Sl.	**Points of distinction**	**Central Bank**	**Commercial Bank**
01.	**Formation**	Central Bank is the sole banking Institution which is established through ordinance or special law of the Government.	Commercial Bank is formed on the basis of Banking Company Laws.
02.	**Ownership**	Central Bank is established under Government ownership.	Commercial Bank is established under both govt. and private Ownership.
03.	**Purpose**	To earn profit is not the main purpose of central bank. Its main purpose is to control credit system and money market.	The main purpose of commercial bank is to earn profit. Recovery of loan is the main stay for generation of profit.
04.	**Number**	In a country there is only one Central Bank.	In a country there may be more number of commercial banks.
05.	**Control**	Central bank is conducted exclusively under Government control.	Commercial Bank is conducted under central bank‟s control.
06.	**Government Influence**	Government has direct influence on Central Bank.	Government has indirect influence On Commercial Bank through Central Bank.
07.	**Currency Market**	Central Bank organizes, controls and administers currency market.	Commercial Banks are the members of the currency market.
08.	**Competition**	Central Bank does not compete with other banks.	Commercial Bank has to face to face lot of competition.
09.	**Representative**	Central Bank represents the country or state.	Commercial Bank represents the Customers.
	Foreign Branch	Central Bank has no branch abroad.	Commercial Bank may have many Branches abroad.
	Note issue	Note issue is the primary function of central bank.	Commercial Bank cannot issue notes.
	Credit control	Central Bank controls credit.	Commercial Bank assists central bank In controlling credit.
	Clearing House	Central Bank acts as a clearing house for settlement of inter-bank	Commercial banks are the members of the clearing house. They settle transactions

		transactions.	through clearing house.
	Lender of	In case of any crisis, central bank Last resort lends commercial bank as a last resort.	Commercial Bank gets assistance from central bank in case of need.
	Nature Of work	Central bank is not engaged in general banking activities i.e. to receive deposits, to lend, to create loan etc.	Commercial bank is engaged in receiving deposits, paying money, creating loan etc.
	Foreign Exchange	Central Bank controls foreign exchange.	Commercial bank helps central bank in controlling foreign exchange.
	Investments	Central bank does not Make any investment for profitability purpose.	Commercial bank makes investments in various sectors for the purpose of profitability.
	Refinance Facility	Central bank refinances commercial bank against first class securities, bill of exchange.	Commercial bank takes refinance facility from the central bank.
	Development work	Central Bank formulates policy on development Work.	Commercial bank participates in the development program Initiated by the central bank.