MONEY SUPPLY, BANKING AND FINANCIAL INSTITUTIONS BASED INDIAN ECONOMY MCQ PRACTICE QUESTIONS AND ANSWERS PDF WITH EXPLANATION

For All Competitive SSC, Bank, IBPS, UPSC, Railway, IT & Other Govt. Exams

Created By Careericons Team

Q1. What is the purpose of setting up of Small Finance Banks (SFBs) in India?

i. To supply credit to small business units
ii. To supply credit to small and marginal farmers
iii. To encourage young entrepreneurs to set up business particularly in rural areas.

Select the **correct** answer using the code given below:
a) (ii) & (iii) only

b) (i) & (iii) only

c) (i) & (ii) only

d) (i), (ii) & (iii)

Q2. Which one of the following is **not** the function of Regional Rural Banks?

a) To provide credit to common people in rural area

b) To take over the functions of Agricultural Refinance Corporation of India

c) To supplement Scheduled Commercial Banks

d) To provide credit to small and marginal farmers

Q3. Consider the following statements.

- Gorewal Committee recommendation led to the establishment of State Bank of India.
- 14 banks were nationalised on July 19, 1969.

Which of the statement(s) given above is/are **correct**?
a) Only 2

b) Neither 1 nor 2

c) Both 1 and 2

d) Only 1

Q4. Which of the following markets are independently regulated by Forward Market Commission?

a) Mutual Funds

b) Stock Market

c) Commodity Futures Market

d) Foreign Exchange Markets

Q5. The "**Consumer Confidence Survey**" in India is conducted by which of the following:

a) National Statistical Office (NSO)

b) Department of Consumer Affairs

c) Reserve Bank of India

d) Ministry of Labour & Employment

Q6. Which of the following could be a cause of demand inflation?

a) An increase in the cost of labour

b) An increase in the level of consumer spending

c) An increase in domestic interest rates

d) An increase in import prices, resulting from a depreciating dollar

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Q7. The accounting year of the Reserve Bank of India is

a) July - June

b) January – December

c) October - September

d) April - March

Q8. Which one of the following does **not** implement the Self-Help Groups (SHGs) - Bank Linkage Programme?

a) Commercial Banks

b) Co-operative Banks

c) RRBs

d) NABARD

Q9. Consider the following statements regarding the “**spread**” charged over the external benchmark rate by the banks:

i. The spread will be decided by the banks
ii. The spread will change with the change of external benchmark rate
iii. The spread may be different for different categories of loans

Select the **correct** answer using the code given below:
a) (ii) & (iii) only

b) (i) & (iii) only

c) (i) & (ii) only

d) All of the above

Q10. In order to control credit, Reserve Bank of India should

a) decrease CRR and reduce Bank rate

b) reduce CRR and increase Bank rate

c) increase CRR and increase Bank rate

d) increase CRR and decrease Bank rate

Q11. The term "SWIFT" is sometimes seen in the news, is related to:

a) It is used to securely transmit information and instructions by financial institutions

b) It is used for messaging in secret defence communication

c) It is used in space technology

d) It is used for faster transmission of data

Q12. The export competitiveness of a country with its trading partners can be best measured through which of the following exchange rates:

a) Real Exchange Rate

b) Nominal Effective Exchange Rate

c) Nominal Exchange Rate

d) Real Effective Exchange Rate

Q13. An increase in CRR by the Reserve Bank of India results in

a) reduction in liquidity in the economy

b) more flow of credit to desired sector

c) attracting more FDI in the country

d) decrease in debt of the government

Q14. Which of the following are **instrument/s of the money market**?

i. Cash management bills
ii. Treasury bills
iii. Certificate of Deposits
iv. State Development Loans

Select the **correct** answer using the code given below:
a) (ii) & (iii) only

b) (i) & (iv) only

c) (i) & (ii) only

d) (i), (ii) & (iii) only

Q15. RBI is keeping the policy rate at a higher level for quite some time. Which of the following conditions may have led to such behaviour?

i. Inflation in the economy is high
ii. Inflation expectation in the economy is high

Select the **correct** answer using the code given below:
a) (ii) only

b) Both (i) & (ii)

c) (i) only

d) Neither (i) nor (ii)

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Answers to the above questions :

Q1. Answer: (c)

The objectives of setting up small finance banks are

1. to promote financial inclusion by providing provision of savings vehicles and supply of credit to small business units;
2. small and marginal farmers; micro and small industries; and other unorganized sector entities, through high technology-low cost operations.
3. They are required to extend 75% of their loans to priority sectors and 50% of their loan portfolio shall constitute loans of up to 25 lacs.

The scope of activities for small finance banks will be,

Basic banking activities of acceptance of deposits and lending to unserved and underserved sections including small business units, small and marginal farmers, micro and small industries and unorganized sector entities and there will not be any restriction in the area of operations.

They will be required to maintain CRR and SLR. They will be set up as differentiated banks for serving niche interests

Small Finance Banks are not particularly for rural areas.

RBI released guidelines for 'on-tap' licensing of Small Finance Banks. Urban Cooperative Banks and Payment Banks can apply for conversion into SFB.

‘On-tap’ means any time they can apply for conversion into SFB and they don’t need to wait for a time window when RBI will grant licenses.

Q2. Answer: (b)

Q3. Answer: (c)

Q4. Answer: (c)

Q5. Answer: (c)

The Reserve Bank has been conducting Consumer Confidence Survey (CCS) since June 2010.

The survey captures qualitative responses on questions pertaining to economic conditions, household circumstances, income, spending, prices and employment prospects.

The survey results are based on the views of the respondents and are not necessarily shared by the Reserve Bank of India. It is conducted in 6 rounds in a year.

Q6. Answer: (b)

Q7. Answer: (a)

Q8. Answer: (a)

Q9. Answer: (b)

Every Bank calculates its own MCLR Rate based on marginal cost of deposits, operational costs, reserve requirements and tenor premium. So MCLR (or Base Rate) is an “internal benchmark” that varies from bank to bank. Banks link their lending rate with MCLR.

But, the transmission of policy (repo) rate changes to the lending rate of banks under the MCLR framework has not been satisfactory due to various reasons like:

1. Banks feared that they will lose the depositors/customers if they will reduce the deposit rate first, and since the deposit rate was not reduced, MCLR (or base rate) was also not coming down.
2. Government offering higher interest rates on its own small savings schemes like Kisan Vikas Patra, Sukanya Samriddhi Scheme, PPF etc.

Hence, RBI has made it mandatory for banks to link all new floating rate personal or retail loans and floating rate loans to MSMEs to an external benchmark effective October 1, 2019.

Banks can choose one of the four external benchmarks –

1. repo rate,
2. three-month Treasury bill yield,
3. six-month treasury bill yield or
4. any other benchmark interest rate published by Financial Benchmarks India Pvt. Ltd.

Banks are not mandated to link their deposit rates with an external benchmark rate.

Now, suppose Axis Bank links its loan rates as per following: Home Loan = repo rate + 3% (3% is called the Spread) Education Loan = repo rate + 4% Personal Loan = repo rate + 5%

Here, all the loans are linked to the repo rate, which is an external benchmark, on which Axis Bank does not have any control. So, the moment RBI changes the repo rate, it will automatically be transmitted to all the lending rates at the same moment for the new loans (Even if the bank links the lending rate with Treasury bill yield; when RBI changes repo rate, the T-bill yield also changes in the market immediately).

The purpose of linking the lending rate with an external benchmark is the faster transmission of repo rate into the lending rate and this mechanism is more transparent also. Adopting multiple benchmarks by the same bank is not allowed within a loan category

Banks are free to decide the components of spread and the amount of spread. But in general, the spread consists of credit risk premium, business strategy, operational costs of banks etc. While the banks will be free to decide on the spread over the external benchmark, credit risk premium can change only when the borrower’s credit assessment undergoes a substantial change. The other components of the spread like operating cost can be altered once in three years.

The interest rate under the external benchmark shall be reset at least once in three months. This means that if a borrower has taken a loan on 1st Jan 2020 and RBI changes the repo rate on 1st Feb 2020, then the borrower may not get the immediate benefit of the rate cut as the interest rate on his loan will only get revised at the latest by 1st April 2020 (within three months of the loan taken).

RBI has mandated banks to link the lending rate with an “anchor rate” like MCLR or repo rate (while MCLR was the internal rate of banks, but the repo is an external rate). But there is no mandate for NBFCs to link their lending rates.

Q10. Answer: (c)

Q11. Answer: (a)

SWIFT stands for the ‘Society for Worldwide Interbank Financial Telecommunications’. It is a messaging network that financial institutions use to securely transmit information and instructions through a standardized system of codes.

SWIFT code is an 8 digit or 11- digit code and is interchangeably also called Bank Identifier Code (BIC). (It was in the news in the context of Punjab National Bank fraud of Rs. 11,000 crore)

Q12. Answer: (d)

Q13. Answer: (a)

Q14. Answer: (d)

In money market, short term (less than one-year maturity), highly liquid and debt instruments are traded. State Development Loans (SDL) have a maturity of more than a year.

Cash management bills, Treasury bills and Certificate of deposits are debt instruments with less than one year maturity.

Certificate of Deposit (CD) is a negotiable/tradable money market instrument (a kind of Promissory Note) and issued in dematerialised form against funds deposited at a bank or other eligible financial institution for a specified time period.

(It is different from the Deposit certificates that individuals get when they deposit money in a bank that is non-tradable).

Q15. Answer: (b)

RBI keeps the repo rate high or increases it when the inflation in the economy increases.

When "inflation expectation" of the people is high, i.e. they are expecting that in future inflation will increase, then such a behaviour of the people ultimately leads to higher inflation in the economy due to which RBI increases the repo rate.

So, both the statements are true.