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THE ROLE OF RESERVE BANK OF INDIA IN THE BANKING SECTOR

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ABSTRACT

This research paper analysis the role of Reserve Bank of India in regulating the Indian banking sector and stabilizing the Indian financial market. RBI was established in 1935 as the legal guardian of all Indian banks. It evolved from colonial rule period to present day central bank which oversee overall development and financial and monetary status in the country. During the evolution, many acts were introduced for advancement and efficiency of the sector. This research paper discusses about the monetary policy tools for the issuance of currency in the country, the core functions of the guardian of all the banks and the regulatory bodies which governs the Reserve Bank of India and ensures its stability, functioning and international standards. Further, it discusses about how the RBI supports Indian banking sector in their transformation through digital payments and how RBI regulates loans and deposits in the banking sector. Reading further, the readers come to know about the impact of Monetary Policy Committee in banking sector. At last, the paper provides the analysis on the challenges currently facing by the RBI in performing its roles in the banking sector and the future outreach to overcome the challenges.

INTRODUCTION

How the Indian digital payments are made? Who gives directions to banks to provide loans, deposit money, implement rules on customers, keeping a particular fixed amount of reserves to themselves? A question rises that who directs the Indian banks on their functioning and

execution tasks? The President? The Financial Minister? The Prime Minister? The Cabinet? The Parliament? Who? Who is the authoritative power to manage all the banks?

At this juncture, the supreme authoritative body emerges in the name of Reserve Bank of India which not only the legal guardian of all the Indian banks but perhaps the main authoritative body to regulate the monetary policies, providing supervision to banks, ensuring the financial stability in the nation, providing protection to the depositor and promotes the economic growth.

The Reserve Bank of India established in the year 1935 to concentrated centralize control over the financial and monetary system of India. RBI issues bank licenses and looks after the bank's performance and their expansion. The Reserve Bank of India was set up on the basis of the recommendations of the Hilton Young Commission. The Reserve Bank of India Act, 1934 (II of 1934) provides the statutory basis of the functioning of the Bank, which commenced operations on April 1, 1935.

The Bank was constituted to:

- * Regulate the issue of banknotes
- * Maintain reserves with a view to securing monetary stability and
- * To operate the credit and currency system of the country to its advantage¹.

The issuance of banknotes in India is done by RBI through monetary policy tools like:

1. REPO RATE

It is a rate for short-term need on which RBI lends money to commercial banks to control inflation and maintain stability. For instance, higher the repo rate = heavier the borrowing cost which results in reduction of money supply and vice versa.

2. REVERSE REPO RATE

It's a rate on which money is borrowed by RBI from commercial banks and its purpose is to absorb liquidity from the system of banking which is excess in system.

3. CRR (CASH REVERSE RATIO)

Commercial banks must maintain a particular total deposit percentage in cash form with the RBI.

¹ Reserve Bank of India, Brief History, RESERVE BANK OF INDIA, https://www.rbi.org.in/History/Brief_History.html (last visited July 30, 2026).

4. SLR (STATUTORY LIQUIDITY RATIO)

A particular net demand and time liability (NDTL) of commercial bank's percentage which is mandatory to be maintained in the form of liquid assets (approved government securities, gold etc.) before the credit's offering.

HISTORICAL BACKGROUND AND FUNCTIONING OF RBI

The Reserve Bank of India established on 1st of April, 1935 on the recommendations of the Hilton Young Commission as the central and supreme authority. The statutory foundation of RBI lies under the Reserve Bank of India Act, 1934 ²which empowered credit, currency regulation and other banking operation. Initially, the RBI had headquartered in Calcutta (present day Kolkata) and in 1937, after two years of RBI establishment, the headquarter of RBI were shifted to Bombay (present day Mumbai). The Reserve Bank of India was nationalized on January 1 of 1949 after the India got independence which transferred the ownership of RBI to the Government of India from the private ownership under Reserve Bank of India (Transfer to Public Ownership) Act, 1948³. The Reserve Bank of India during its formative years, focused on credit, currency regulation, managing foreign exchange, other banking operation and acting as the banker to the government. Post-Independence, The Reserve Bank of India professionally managed the shift to convert British currency into the Indian currency. The RBI become more powerful in monetary regulation and nationalization of commercial banks. Over the decades, RBI's mandatory powers expanded to oversee the banks and non-banking financial companies (NBFCs), promoting financial stability, facilitating the digital payments. The Monetary Policy Committee (MPC), 2016 ⁴introduced the targeting of the formal inflation and enhanced monetary policy's transparency.

At present, the RBI is governed by Central Board of Directors consists of 21 members which includes one governor, four deputy governors, two government representatives, four directors representing local boards in Mumbai, Kolkata, Chennai and Delhi and ten directors appointed

² Reserve Bank of India Act, No. 2 of 1934, INDIA CODE.

³ Reserve Bank of India (Transfer to Public Ownership) Act, No. 57 of 1948, INDIA CODE.

⁴ Finance Act, No. 28 of 2016, § 45ZB, INDIA CODE.

by the government of India. This structure is highly focused on central oversight and regional representation.

The journey from historical to the present day evolution of RBI reflects the economic and financial evolution of India, evolution to modern central bank from the colonial-era highlights the pivotal role of RBI in monetary, economic development and financial regulation.

FUNCTIONS AND THE GOVERNANCE OF RBI

The RBI's functionary is as an India's central bank, financial stability, currency regulation and bank's supervisor and all this functionary of governance is managed by the Central Board of Directors which is appointed by the Indian government.

- **THE CORE FUNCTIONS OF THE RBI ARE :**

1. ISSUANCE OF CURRENCY AND MONETARY FUNCTIONS

Money supply in the country is managed by the Reserve Bank of India and it also manages the credit system to promote the economic growth and the price stability. It issues the banknotes in the country. Except the 1 rupee note which is issued by the government, all the currency notes are issued by the RBI. Liquidity, inflation and credit flow in economy is controlled by RBI through instruments like reverse repo, repo rate, CRR (Cash Reverse Ratio), SLR (Statutory Liquidity Ratio).

2. SUPERVISORY FUNCTION

RBI supervises the non-banking financial companies, financial institutions and commercial banks both. The Board of Financial Supervision (BFS) strengthens surveillance and implements integrated supervision over the financial system ⁵.

RBI issues licenses to the banks, ensures compliance, makes systems stable, maintain public confidence and ensures cost-effective system.

3. FOREIGN EXCHANGE MANAGEMENT

⁵ Reserve Bank of India, Governance and Functions of RBI, <https://www.rbi.org.in/Scripts/AboutusDisplay.aspx> (last visited July 30, 2026).

It regulates the Indian rupee's external value and keep manage the foreign exchange reserves of India which facilitates the smooths the exports and imports practices, under the Foreign Exchange Management Act, 1999.⁶

4. LENDER OF LAST RESORT

The emergency funds which the banks needs during their liquidity crisis are provided by the RBI.

5. FUNCTION OF DEVELOPMENT

The Reserve Bank of India supports rural creditability, promotes financial inclusion and digital payments, encourages the technologies which innovates in the banking sector including the specialized departments for rural and agricultural finance.

• THE GOVERNANCE OF THIS AUTHORITATIVE BODY ENSURED BY:

1. CENTRAL BOARD OF DIRECTORS

Governed by 21 members which includes one governor, four deputy governors, two government representatives, four directors representing local boards in Mumbai, Kolkata, Chennai and Delhi and ten directors appointed by the government of India under RBI Act, 1934 which serves 4 years of tenure that oversees operations, serves accountability and formulates the policies.

2. LOCAL BOARDS

Four local boards located in Mumbai, Kolkata, Chennai and Delhi which represents the Northern, Eastern, Southern and Western regions of India, each board consists of five members on whose advice the Central Board on regional matters works for promoting the better governance and represents the local banks.

3. DEPARTMENTS AND SUBSIDIARIES

The subsidiary like Bhartiya Reserve Bank Note Mudran Private Limited (BRBNMPL) for the printing of currency and Deposit Insurance and Credit Guarantee Cooperation (DICGC). Many other departments are for handling the rural credit, monetary supply and technologies related to finance.

⁶ Foreign Exchange Management Act, No. 42 of 1999, INDIA CODE.

4. LEGAL FRAMEWORK

Reserve Bank of India operates under the RBI Act, 1934 which states the objectives, structure of governance and the powers of RBI. RBI facilitates the economic development while maintaining the monetary stability.

RBI AND THE TRANSFORMATION OF BANKING THROUGH DIGITAL PAYMENTS

The Reserve Bank of India prioritizes the involvement of advanced technologies in the Indian banking sector since its origin. It supports the banks to adapt new and advanced technologies in their systems to enhance bank performance and gives better output which results in promotion of the economic growth of the country and financial stability.

• EVOLUTION OF DIGITAL PAYMENTS IN INDIA

Over the last decade, India has witnessed an unprecedented surge in digital payments. From 222 crore transactions valued at ₹772 lakh crore in 2013, digital payments grew to over 20,787 crore transactions worth ₹2,758 lakh crore by 2024, reflecting a five-year CAGR of 45.9% in volume and 10.2% in value. This growth has been driven by the adoption of platforms like Unified Payments Interface (UPI), launched in 2016, which consolidates multiple bank accounts into a single mobile interface, enabling instant, interoperable payments across banks and apps.⁷ There are several UPI platforms like GooglePay, Paytm, digital wallet etc. which provides different users the different platforms for using the digital payment method.

This digital payment system also helped government to monitor the digital transactions which prevents the black money and soothes the economy functioning.

• REGULATORY AND SECURITY FRAMEWORK

Reserve Bank of India regulates all payments in India under the Payment and Settlement System Act, 2007 which set a bar for authentication, security, efficiency and the redressal

⁷ Reserve Bank of India, Evolution of Digital Payments in India,
<https://www.rbi.org.in/Scripts/PublicationsView.aspx?Id=23127> (last visited July 31, 2026).

adapting measures such as tokenization of cards and guidelines for cyber security. The Payments Regulatory Board (PRB), replacing the earlier BPSS, now oversees all payment systems, ensuring regulatory compliance and fostering innovation.⁸ Additionally, the Digital Banking Channels Authorisation Directions, 2025 provide a uniform framework for banks to offer view-only and transactional digital banking services, emphasizing customer consent, cybersecurity, and operational readiness⁹.

• FINANCIAL INCLUSION AND IMPACT ON BANKING SECTOR

With the efforts of RBI and its supervisor functionary, the rural and semi-urban areas have the access to the digital payments which transformed the banking sector providing them the faster, efficient, more accessible and cheaper services. At present day, consumer can access their banking details through their mobile phones, laptops etc. which also have the record digitally that prevents to cause unnecessary burden on the banks and allows banks to focus on more important tasks. Such modernization in the banking sector of India directed by the Reserve Bank of India established India as a global leader in digital payments. As we see nowadays, even a vegetable hawker is able to make digital payments, this signifies that RBI directions are not only legislative but their execution is executed well at present day.

RBI encouraged the innovation and transparency via open-loop systems such as UPI through multiple banks and apps to make seamless transactions. The Payments Vision 2028 further emphasizes AI-driven supervision, interoperability, and MSME support, aiming to make India's payments ecosystem more secure, accountable, and globally influential ¹⁰.

• STRATEGIC AND FUTURE VISION

⁸ ET Edge Insights, India's Digital Payment Story 2025, <https://www.etedge-insights.com/industry/bfsi/indias-digital-payment-story-2025> (last visited July 31, 2026).

⁹ Economic Times India Times, RBI's 2025 Digital Banking Framework, <https://bfsi.economictimes.indiatimes.com/articles/rbis-2025-digital-banking-framework-revolutionizing-online-banking-for-indian-banks/125640014> (last visited July 31, 2026).

¹⁰ EY India, How RBI's Payments Vision 2028 Could Reshape India's Digital Payments, https://www.ey.com/en_in/insights/payments/how-rbis-payments-vision-2028-could-reshape-india-s-digital-payments (last visited July 31, 2026).

Payment vision of 2028 of RBI address to build an ecosystem on trust, future-ready payments, fraud prevention and cybersecurity. Key priorities include cross-border efficiency, fraud accountability, interoperability, and MSME support, positioning India not only as a leader in payment volumes but also in payment system design and global innovation¹¹. This ensures balance between the advanced technology with the regulation while enforcing the credibility of banking sector.

REGULATION OF RBI FOR LOANS AND DEPOSITS IN THE BANKING SECTOR

RBI plays a crucial role in safeguarding the trust of depositors and gives ensures the stability through regulating loans and deposits. Several amendments are issued by RBI on its regulations for banking sector which come into force from 2st October 2025 and its aim is to provide banks the flexibility for enhancing borrower's benefits. These amendments included:

1. INTEREST RATE ON ADVANCES

Banks can now reduce certain components of the spread on floating-rate loans to benefit borrowers sooner than the previous three-year limit. Lenders may also offer the option to switch from floating to fixed rates during interest rate resets at their discretion.

2. LENDING AGAINST GOLD AND SILVER COLLATERAL

The amendments expand the scope of working capital loans for borrowers using gold as raw material in manufacturing or industrial processing.

3. BASEL III CAPITAL REGULATIONS

The RBI has revised the eligible limits for PDIs denominated in foreign currency or rupee-denominated bonds overseas.

¹¹ EY India, How RBI's Payments Vision 2028 Could Reshape India's Digital Payments, https://www.ey.com/en_in/insights/payments/how-rbis-payments-vision-2028-could-reshape-india-s-digital-payments (last visited July 31, 2026).

These changes are part of the RBI's broader strategy to strengthen the banking sector and ensure a more stable financial system. The amendments are expected to benefit both banks and borrowers by providing greater flexibility and improving the overall banking experience.¹²

MONETARY POLICY COMMITTEE AND ITS IMPACT ON BANKING OPERATIONS

Monetary Policy Committee meets four times a year. It is a crucial institution of RBI which directly effects the banking sector's functioning. It is established under the RBI Act, 1934 (amended in the year 2016). The MNC determined repo rate has direct coast on bank's funds in deposit rates, loan pricing, and the management of the liquidity of the Indian banks. The MonetaryPolicyCommittee's recent meetings have focused on adjusting key lending rates and implementing measures to enhance the banking sector's resilience and credit flow. These decisions are influenced by the evolving macroeconomic and financial developments, aiming to achieve price stability, promote economic growth, and ensure financial stability. The MPC's stance on the neutral monetary policy is expected to support medium term target for consumer price index (CPI) inflation of 4% within a band of +/- 2%. The RBI's recent updates reflect a wait-and-watch approach amidst global uncertainties, with a focus on maintaining the status quo on key lending rates and taking a neutral stance.¹³ MNC consists of three members from RBI and three external experts which are appointed by Indian government.

ANALYSIS ON RESERVE BANK OF INDIA IN THE BANKING SECTOR

• CHALLENGES:

1. PRIVACY BREACH AND DATA LEAK

The method of digital payments made the system easier for both customers and banks which not only enhanced the performances of the banks but at the same time, it also encouraged the modernization in the Indian banking sector as well. Adaption to advanced technologies in banking sector made India reach the global standard but with this the risk of data leak and

¹² Reserve Bank of India, Master Directions – Banking Regulations,

https://www.rbi.org.in/SCRIPTS/BS_ViewMasterDirections.aspx (last visited July 31, 2026).

¹³ Reserve Bank of India, Master Directions – Banking Regulations,

https://www.rbi.org.in/SCRIPTS/BS_ViewMasterDirections.aspx (last visited July 31, 2026).

privacy breach also rise. In July, 2026, a critical data leak of around 1TB in Bank of Baroda occurred which put risk on KYC documents (with names, photos, Aadhaar numbers), Account opening forms & customer statements, Savings and current account records, Loan appraisal, documents & loan records, Internal audit reports & vigilance investigations, bobWorld audit files, NetBanking user information, NRI and corporate banking records, Branch-level operational files and ATM-related records¹⁴. Other leaks as ‘NuPay Fintech Cloud Data Leak (Aug–Sep 2025)’, ‘Coordinated UPI Data Breach (June 2025)’ and many other recent leaks are the consistent challenge to the RBI in banking sector.

2. INFLATION VS. GROWTH

Inflation and growth are inversely proportional to each other. When the inflation is moderate in a country that keep the growth at the moderate level or supports the growth of a country. Just like this, when inflation is high that results in backstabbing the country’s growth which results in slower growth. RBI prioritizes control over inflation by measures like tightening the monetary policy, slower credit growth and reduction in liquidity.

Inflation rises when the demand for goods and services exceeds the supply, that results in lowering the purchasing power of money. The inflation occurs when the price of raw material exceeds the production cost or if there is increase in wages. while on the other side, the economic growth measured by the Gross Domestic Product (GDP) of the country. This growth can be driven by the aggregate demand and the aggregate supply of goods and services.

Positive results can be get out of the lower level inflation when the growth remains at the supportively level but high inflation cause the economic growth negatively by reducing the supply and raising the demand which cause lowering the GDP of the country. Perhaps, the monetary policies and fiscal policies the issue can be over come easily.

3. INEVITABLE GLOBAL CIRCUMSTANCES

Global economy develops inevitable circumstances that inevitably effects the Indian monetary policies and country’s financial stability. The geopolitical tensions like Russia-Ukraine war, USA-Israel war, such disturbance globally, creates stress in Indian economy as we see the LPG crisis and raising oil prices effect the domestic economic stability. The World Economic

¹⁴ Outlook Business, Bank of Baroda 1TB Data Leak: Branch Audits, Loan Appraisal Documents, Passwords Exposed on Dark Web, <https://www.outlookbusiness.com/corporate/bank-of-baroda-1tb-data-leak-branch-audits-loan-appraisal-documents-passwords-exposed-dark-web> (last visited Aug. 1, 2026).

Forum's Global Risk Report 2024 highlights the risk of global insecurity and extreme weather events, which are critically for the banking industry.¹⁵ Some other inevitable global circumstances which effects the Indian banking are:

- Disruption in the supply chain
- Climate change and natural disasters
- Shift in the global technology

These global circumstances are still the most challenging issue that disturbs the entire economy and effects can be seen in inflation, depression, unstable economy and reduced economic growth.

4. RURAL OUTREACH

RBI provides the rural people, facility that they have the right to open their bank accounts and there the zero-balance accounts are introduced for their betterment, development and modernization. Despite achieving progress in advanced technologies, digital payment system and financial inclusion, the challenge is persistent in the rural outreach due to the social-economic barriers, infrastructure and geography. Rural people facing these issues often get trapped in informal credit sources like chit funds and moneylenders because of their lack of trust on formal institutions and this lack of trust was rooted as in rural areas there is no adequate infrastructure for ATMs , banks or internet connectivity, and also due to low digital literacy, irregularity in employment, income levels are lower, restricts rural to limited services of formal financial.

• FUTURE OUTREACH:

1. STRENGTHENING AI DRIVEN TECHNOLOGY AND DIGITAL BANKING

The issues related to privacy breach, data leak and putting the personal details of customers on risk can be prevented by strengthening the digital banking of India. The Indian banking sector is developing on direction given by Reserve Bank of India. Its technological advancements, increasing penetration of mobiles, initiatives taken by government, all helping in driving the banking technology on the next level. RBI must enforce end-to-end encryption, real-time

¹⁵ World Economic Forum, Global Risks Report 2024,

<https://www.nibmindia.org/staticfile/pdf/India%20Banking%20and%20Finance%20Report%202024%20for%20author.pdf> (last visited Aug. 1, 2026).

monitoring of payments made digitally and fraud driven by artificial intelligence. With this, it should implement stronger compliance frameworks and steps like 2028 payments vision aims to set benchmark globally.

2. INCLUSIVE GROWTH

The inclusive growth of banking sector is driven by the technological advancements, fiscal policies, RBI regulations, managing the global crisis, accessible to rural areas, ensuring cybersecurity, monitoring the digital transactions and effective infrastructure. All these factors are equally important for inclusive growth in this sector. The initiatives for financial inclusion involving fiscal initiatives like UPI, Jan Dhan, etc., adopting these initiatives fills the gap and built trust among millions on formal ecosystem. Inclusive growth can be succeed only by developing and making accessible the advancement and facilities to all the groups of society and promoting microfinance and cooperative banking. To balance innovation and achieving inclusive growth, it is must that all the section, marginalized groups must get benefit of financial transformation.

3. GLOBAL COMPETITIVENESS

Indian banking sector has rapid transformation in past decades, via financial inclusion, digitalization, advancement in technologies and regulatory reforms. Shifting to digital payments and introducing UPI, India get position as a global leader. Still, there are domestic distractions due to the global tentions which can be overcome by strongly adopting the artificial intelligence driven technologies for fraud detection and privacy protection, mandates cybersecurity audits among fintech and banks. RBI must manage strong foreign reserves for further shock absorption of rising import bills and for the management of inflationary pressures, RBI must use CRR and repo rate monetary tools. Also, it must support adopting low-energy production methods by MSMEs and industries. For securing stable chains of supply, Reserve Bank of India must coordinate globally and limit the dependency on imports by supporting small industries by providing loans and promoting rural small business by providing formal financial help to them so that it strengthens the economic and financial stability and global competitiveness in finance and Indian banking sector. this can be achieved by two decades as per some report which is like "The Indian banking sector is sufficiently capitalised and well-regulated. The financial and economic conditions in the country are far superior to any other country in the world. Credit, market, and liquidity risk studies suggest

that India's banking sector is well-positioned to meet the financing requirements of infrastructure, MSMEs, and consumption-led segments over the next two decades.”¹⁶

4. SUPERVISORY MECHANISMS

To ensure trust, efficiency and integrity, RBI provides a comprehensive framework for supervisory mechanisms in banking systems. But rural areas are not capable of taking full advantages of all and commercial banks sometimes do fraud with their customers, to prevent this, RBI must have annually inspect focusing on insolvency, banking operations and liquidity and bank's annual financial inspection must also be done. Supervision of technology must be monitored after adapting AI driven technologies and monitor and supervise prompt corrective action and RBI must align with the global standards and must be providing the transparency and accountability.

CONCLUSION

Reserve Bank of India is the India's bank which represents India in the global economy and regulates country's internal economy. RBI issues banknotes by using monetary tools like repo rate, Cash Reverse Ratio, reverse repo rate and Statutory Liquidity Ratio. The establishment of RBI is done on the recommendations of the Hilton Young Commission as the central and supreme authority and now this institution is managing all Indian domestic economy and making India a global leader in finance. It is governed by its 21 members including director and deputy directors and other member elected by government or regional branch representatives, local boards and Departments and Subsidiaries. RBI issues the currency and perform monetary functions, supervises the banking sector, manages foreign reserves.

RBI transformed Indian banking sector when it introduced advanced technologies like digital payments, UPI, artificial intelligence and making its facilities accessible to rural areas. The initiatives like the Payments Vision 2028 gives confidence to citizens to believe in financial institution. The monitoring and supervision of other commercial banks and NBFCs, giving directions to them set RBI as the supreme authority, all other financial institutions are below it and have to follow the directions given by RBI. Despite all this monitoring and supervision, RBI still faces like privacy breach and data leak, high inflation, global circumstances and rural

outreach but all these issues can be overcome if RBI strengthens its AI driven technologies to protect cyber attacks and strengthen digital banking privacy ensuring end-to-end encryption and also to make the technologies and facilities accessible and workshops must be organized for the rural people to fill this gap which will make trust between customers and undoubtedly bridges the gap between rural and urban customers. With this, supervision of the NBFCs and other commercial must be done timely and audits of banks must be supervised to prevent corruption in the system and protect customers, especially the rural people from it. All this caused and managed by internal efforts but the global competitiveness can only be overcome by adopting low-energy production methods by MSMEs and industries to support small business and businesses run by rural people at a small level which can prevent the dependence on imports and support country's GDP and global standards. Final words, RBI is contributing to Indian economy and will be better in this by transforming timely and keeping its focus to developments in competitive market with global and domestic challenges.