Functions of Central Bank

The Central Bank is the apex bank that controls the entire banking system of a country. It is the sole agency of note issuing in a country. It serves as a banker to the government and controls the supply of money in the country

In India Reserve Bank, in England, Bank of England and in America Federal Reserve System operate as central banks. (Although, the first central bank in the world was set up in 1668 in Sweden.

India's central bank is known as the Reserve Bank of India. Its role is to foster financial stability and regulate India's currency and credit. Founded in 1935, the bank sets monetary policy for the country. It is fully owned by the government of India and is run by a government-appointed board of directors. The central Bank of India plays a major role in India's banking system and economy.

There is no standard definition of a central bank. The definition depends on the function it discharges. However a common function that the central bank performs in all economies of the world is that it controls and manages the flow of credit and supply of money in the economy. According to Samuelson - "Every central bank has one function. It operates to control economy, supply of money and credit."

The main functions of the central bank are as follows:—

① Issuing Notes:— Central Bank of a country has the exclusive right of issuing notes.

This is called currency Authority function of the central bank. Actually, till the beginning of 20th century, the central bank was known as Bank of Issue. The notes issued by the central bank are an unlimited legal tender througout the country. The central bank has to keep gold, silver or other securities against the notes issued. The system of note-issue diffess from country to country.

It may be noted that RBI issues all currency notes in India except one rupee note. One rupee notes and small coins are issued by government

(2) Banker to the Government:- Central Bank is a banker, agent and financial advisor to the government. As a banker to the government, it manages account of the government. As an agent, it buys and sells securities on behalf of the government. As an advisor, it helps the government in framing policies to regulate the money market.

(3) Bankers' Bank:- As a Banker's Bank, the central bank has almost the same relation with other banks in the country as a commercial bank has with its customers. It accepts deposits from the commercial banks and offers them loans.

The rate at which the central bank offers loans to the commercial banks is called "Repo Rate." It is also called Bank's policy Rate.

The rate at which commercial banks are allowed to park their surplus funds with the RBI is called Reverse Repo Rate.

Commercial Banks are required under the law to keep a certain percentage of their total deposits with the Central Bank

in the form of cash Reserves. ~~This is~~
Called "Cash Reserve Ratio" (CRR).

(4) Lender of the Last Resort:— Central Bank act as a lender of last resort when a commercial bank suffers the crises of confidence and people go crazy to withdraw their deposits. In this situation, central bank offers loans to the bank against their securities. This saves bank from possible failure. On the other hand, Central Bank, by providing temporary financial accommodation, saves the financial structure of the country from collapse.

(5) Custodian of Foreign Exchange:— Central Bank is the custodian of nation's foreign exchange reserves.

(6) Clearing House Function:— Central Bank also performs the function of a clearing house. The cheques of different banks are cleared through their specified accounts with the central bank.

(7) Control of Credit:— The most important function of the central bank is to control the supply of ~~money~~ credit in the economy. The central bank needs to control the supply of money during the situations of inflation and deflation. During inflation, the supply of money is restricted and during deflation, the supply of money is liberalised.

Performing all these functions, the Central Bank ~~plays~~ a central role in stabilising the economy by minimising the impact of inflationary and deflationary cycles in the economy.