WEEK 3

Subject: ECONOMICS

Topic/Title of lesson: FINANCIAL INSTITUTIONS

Sub-Topic: BANKING INSTITUTIONS

LESSON OBJECTIVES:

By the end of the lesson the learners should be able to:

1. Define banking financial institution
2. Define commercial bank, identify its function
3. Define Central bank, its functions and how it controls commercial bank
4. Identify the roles of commercial and central banks

LESSON NOTES:

BANKING INSTITUTIONS

A banking institution is a financial institution that have full banking license and are supervised by a national or international banking regulatory industry example of banking financial institutes are: commercial banks, central bank etc.

1. **COMMERCIAL BANK:** is a financial institution which accept deposit (money and other valuables) from the public for safe custody and pay it on demand through the use of cheque, passbook or automated teller machine (ATM) card. Commercial banks are just like any business organisation and companies, they are public limited liability companies. They are owned by the shareholders; their main existences are for profit making. Example of such are zenith bank, guaranty trust bank, first bank, union bank, united bank for African (UBA). Access bank equatorial trust bank, diamond bank etc.

FUNCTION OF A COMMERCIAL BANK

1. They act as agent of payments on behalf of their customers.
2. They help in keeping their customers valuable safe e.g. jewelleries, important documents, certificate etc.
3. They accept deposit.
4. They act as lending agents.
5. They give technical advice to their customers in regards of investment.
6. They help in foreign exchange transaction.
7. They help to facilitate business transaction.

   Commercial banks create money through lending of money to people, through giving over draft. However, the creation of money by commercial banks depends on the following:

   a. The amount of collateral available to borrower.

   b. Cash deposit ratio.

   c. restriction imposed on commercial banks by bankers clearing house.

   d. willingness of people to take loan and over draft.

   e. the total amount of money/cash in the economy.

ROLE OF COMMERCIAL BANKS:

1. Commercial banks advice their customers on how to carry out business through financial, technical and management advice.
2. Commercial banks provide both short and long term loans to prospective investors or for business expansion.
3. Commercial banks themselves invest in productive sectors of the economy thereby contributing to economic development.
4. Business and traders find it easier to transact their businesses through the use of cheques, ATMs, etc.

5. Foreign trade and foreign transactions are facilitated by commercial banks, they issue travellers cheques etc.

CENTRAL BANK

This is a bank owned by the government to control and supervise the monetary and financial system of a country. Every country has its own central bank e.g. central bank of Nigeria (CBN), Central Bank of Ghana (CBG) etc.

FUNCTIONS OF CBN

1. It serves as bankers bank that is central bank is the bank of commercial bank.
2. They serve as lenders of last resort to commercial banks.
3. They issue currency to commercial bank as it is the only institution that is allowed to print and issue bank notes.
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7. The central bank carries out external businesses on behalf of the country through the central bank of other countries.
8. They keep government account and make payments on behalf of government.

Central Banks Control Commercial Banks through:

a. **CASH DEPOSITS RATIO:** it is the minimum amount that commercial banks must keep with central banks.
b. **OPEN MARKET OPERATION (OMO):** this is the buying and selling of government securities. If the amount of money in circulation is too low and the central bank wants to increase it, they will buy securities from the public and commercial banks to increase the volume of money in circulation and vice versa.

c. **MORAL SUATION:** This is an appeal from commercial banks by central banks to liberalise or restrict their lending policies.
d. **DIRECTIVES:** The central banks give directives or instructions to commercial banks about their lending policies.
e. **USE OF SPECIAL DEPOSITS:** Apart from the cash deposits that commercial banks keeps central banks, from time to time central banks may give to increase their deposits this is mainly to control inflation.
f. **BANK RATE:** This the rate at which central banks lends money to commercial banks, if there is inflation that will increase bank rate but if there is no inflation, they will reduce bank rate.

ROLES OF CENTRAL BANKS IN ECONOMIC DEVELOPMENT

1. Provision of money-printing and issuing of currency note.
2. They instruct and direct commercial banks to give more loans to development project.
3. They help the capital and money market which as well provide for developmental project.
4. It advises the government on economic and financial matters and participate in budget formulation.
5. It helps foreign trade and obtained loans from international organisation like world banks, international monetary fund (IMF) etc. on behalf of the government.

EVALUATION

The teacher evaluates by asking the following question

1. What is banking financial institution?
2. What is commercial bank?
3. Define central bank
4. What are the roles of central bank in controlling commercial banks?