

Banks as Financial Intermediaries

All financial institutions do or enable some form of intermediation. Some of them collect deposits, some others lend, while some others, such as Life Insurance Corporation [LIC], cater to the needs of insurance.

Mutual fund organizations concentrate in pooling the resources from individuals, invest them in the market, and pass on the profits to the investors. Banks enjoy the benefit of being the only institutions through which the money can be transferred from one person to another and from one place to another.

Therefore, banks become the constituent of the payment system of the economy. All other financial intermediaries at one point or other depend on banks and cannot work efficiently in their absence. Banks, because of their reach, trust of the people, and other roles that they play, have enabled them to emerge as the largest financial intermediaries of the world. By virtue of this, the economic prosperity of the economy as a whole and of different regions and industries depends upon the banks.

Banks are able to lend a major portion of their deposits, and play the role of a financial intermediary and constitute the payment system because of the understanding that banks will honor the commitments that they have made to the people. If this trust is broken for any reason, the banks will not be able to survive. Failure of one bank will lead to the failure of other banks too because their role as a constituent of the payment system make them have substantial dealings with and dependence on each other.

Isolation of a region or an industry can take place if banks lack interest. Not only those who are discarded suffer, but such an outlook may impact the economy as a whole. Therefore, banks being the largest financial intermediaries have a crucial role to play in achieving balanced growth of industries, regions, and the economy at large.

Services offered by banks as financial intermediary

1. Deposit services
2. Loan or credit services

1. **Deposit Services:** Banks accept demand deposits and fixed or time deposits.

Demand deposits are repayable on demand while fixed deposits have a fixed maturity period and are repayable only after the agreed period. Since demand deposits are more liquid as compared to fixed deposits, the interest paid on such deposits is at a low rate or no interest is paid at all. Lower the liquidity, higher is the rate of interest. Therefore, longer the period of the fixed deposit, higher will be the interest that is paid.

While demand deposits are cheaper in terms of the interest paid on them, the cost of maintaining demand deposit accounts is higher than that of fixed deposit accounts in view of the large number of transactions involved in demand deposits.

The various products offered by banks within the deposit services are:

- Current accounts
- Savings bank accounts
- Fixed deposit accounts
- Recurring deposit accounts

2. **Loan or Credit Services:** The products offered by banks within loan services are as follows:

- Retail loans
- Personal overdrafts
- Credit cards
- Business/Corporate credit
- Working capital facilities
- Business card
- Post-sale finance or trade finance