

Key learning points I

- What do banks do?
 - Banks provide three core banking services
 - Deposit collection
 - Payment arrangement
 - Underwrite loans
 - Banks may also offer financial services such as cash, asset, and risk management
 - Banks play a central role in facilitating economic activity through three interrelated processes
 - Financial intermediation
 - Asset transformation
 - Money creation

Key learning points II

- Types of banks
 - Retail banks serve primarily retail customers
 - Wholesale banks serve primarily corporate customers
 - A country's central bank
 - Regulates other banks
 - Provides services to other banks
 - Sets monetary policy on behalf of the country's government

Key learning points III

- What main risk impact banks?
 - Credit risk
 - Market risk
 - Operational risk
 - Other types of risk include
 - Liquidity risk
 - Business risk
 - Reputational risk

Key learning points IV

- Multiple forces shape the banking industry
 - Regulation
 - Competition
 - Product innovation
 - Changing technology
 - Uncertainty surrounding future interest and inflation rates

Key concept definitions

Key term	Definition
Asset transformation	Asset transformation is the process of creating a new asset (loan) from liabilities (deposits) with different characteristics by converting small denomination, immediately available and relatively risk free bank deposits into loans- new relatively risky, large denomination asset- that are repaid following a set schedule.
Banking book	Banking book is portfolio of assets (primarily loans) the bank holds, does not actively trade, and expects to hold until maturity when the loan is repaid fully; typically refers to the loans the bank has made.
Banks	A banking license, issued by a banking regulator or supervisor, allows the bank to engage in banking under the condition that they agree to be supervised by regulatory or supervisory authorities.
Basel Accords	The Basel Accords (Basel I Accord, the Market Risk Amendment and the Basel II Accord) are the cornerstones of international risk-based banking regulation, the results of a collaborative attempt by banking regulators from major developed countries to create a globally valid and widely applicable framework for banks and bank risk management.
Business risk	Business risk is the potential loss due to a weakening in the competitive position of the bank.
Commodities risk	Commodity risk is the potential loss from an adverse change in commodity prices. This applies to all commodity positions and any derivative commodity positions such as futures contracts.
Credit risk	Credit risk is the risk of loss due to non-payment of a loan, bond, or other credit.
Equity risk	Equity risk is the potential loss due to an adverse change in the price of stock.
Financial intermediation	Financial intermediation is the process bringing together those who need financing, such as businesses and governments, with those who provide financing, such as lenders, banks and private investors, and facilitating the flow of capital between them.

Key concept definitions

Key term	Definition
Foreign exchange risk	Foreign exchange risk is the potential loss due to an adverse change in the value of a currency against another.
Fractional reserve banking	Fractional reserve banking is a banking system where only a small fraction of the total deposits are available for immediate withdrawal, with the balance invested in loans and other securities.
Inflation rate	Inflation rate is the annual percentage rate change in the purchasing power of money.
Interest rate	Interest rate, the price of credit, is the rate a lender charges a borrower for using borrowed funds.
Interest rate risk	The interest rate risk is the potential loss of value due to the variability of interest rates, subsequently affecting a bank's lending and deposit-taking activities.
International or global banks	International banks are large commercial and investment/ merchant banks that have operations in several different countries.
Liquidity risk	Liquidity risk can be market (transactional) liquidity risk and funding (payment) liquidity risk. Market liquidity risk refers to the potential loss due to a decrease in the ability to trade in and out of a position without significant price concessions. Funding liquidity risk relates to a bank's potential inability to have funds available to repay depositors on demand and to fund loans when needed.
Market risk	Market risk is defined as the risk of losses in on- and off-balance-sheet positions arising from movements in market prices and under the Basel II Accord encompass the risks pertaining to interest rate related instruments and equities in the trading book, and foreign exchange risk and commodities risk throughout the bank.
Money multiplier	The money multiplier is the inverse of the reserve requirement and indicates how much new money each unit of currency, deposited with a bank, creates.

Key concept definitions

Key term	Definition
Operational risk	Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems, or from external events. This definition includes legal risk, but excludes strategic and reputational risk
Regulatory reserve capital	Regulatory capital requirement specifies how much minimum capital a bank must hold to guard against the various risks it takes.
Reputational risk	Reputational risk is the potential loss resulting from a decrease in a bank's standing in public opinion.
Risk management	Risk management is a structured approach to monitoring, measuring, and managing exposures to reduce the potential impact an uncertain event happening.
Trading book	A trading book in a bank consists of various positions in financial instruments and commodities that are held with the intention to either trade or hedge other positions in the trading book.
Underwriting (loans)	Underwriting assesses the borrower's eligibility to receive credit (loan or bond) by analyzing financial and other information furnished by the borrower or obtained elsewhere.
Universal banks	Universal banks offer core bank services and broader range of financial services, particularly insurance.
Wholesale banks	Business banks include commercial banks, correspondent/ wholesale banks and investment or merchant banks, and primarily serve corporations with banking and advisory services, such as corporate finance and project finance, which are specific to the need of large businesses.