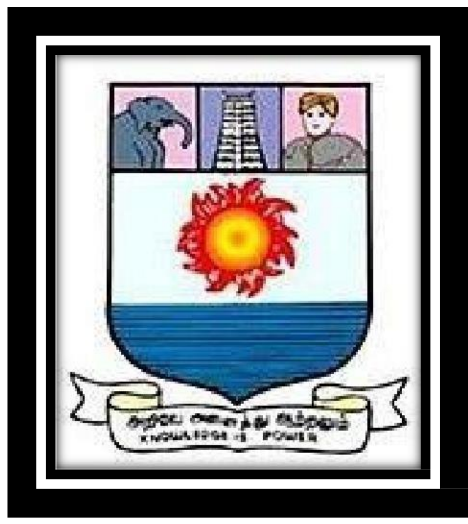


MANONMANIAM SUNDARANAR UNIVERSITY

Tirunelveli

DIRECTORATE OF DISTANCE AND CONTINUING EDUCATION

M.Com

CREDIT MANAGEMENT

Unit I

INTRODUCTION AND OVERVIEW OF CREDIT

Safety, Liquidity & Profitability – Purpose of Loan – Diversification Risk – Model Credit Policy for individual and all types of organization-

Types of Credit Facilities

Various types of credit facilities – cash credit – overdraft – Demand loan – Bills Finance – Drawee Bill Scheme and Bills Discounting

Credit Delivery

Types of facilities – Modes of Delivery – Sole Banking Arrangement – Multiple Banking Arrangement – Consortium Lending – Syndication – Credit Thrust – Credit Priorities –Credit Acquisitions Discounting – Dimensions of Credit Appraisals

UNIT I

INTRODUCTION AND OVERVIEW OF CREDIT

What is credit management?

Credit management is the discipline of reviewing, analyzing and setting the terms of requests for credit for a business. In the world of business-to-business (B2B) commerce, sales of goods and services are commonly made on credit with payment to come sometime after delivery.

Principles of Lending

Liquidity:

Liquidity is an important principle of bank lending. Bank lend for short periods only because they lend public money which can be withdrawn at any time by depositors. They, therefore, advance loans on the security of such assets which are easily marketable and convertible into cash at a short notice. A bank chooses such securities in its investment portfolio which possess sufficient liquidity. It is essential because if the bank needs cash to meet the urgent requirements of its customers, it should be in a position to sell some of the securities at a very short notice without disturbing their market prices much. There are certain securities such as central, state and local government bonds which are easily saleable without affecting their market prices.

The shares and debentures of large industrial concerns also fall in this category. But the shares and debentures of ordinary firms are not easily marketable without bringing down their market prices. So the banks should

make investments in government securities and shares and debentures of reputed industrial houses.

Safety:

The safety of funds lent is another principle of lending. Safety means that the borrower should be able to repay the loan and interest in time at regular intervals without default. The repayment of the loan depends upon the nature of security, the character of the borrower, his capacity to repay and his financial standing.

Like other investments, bank investments involve risk. But the degree of risk varies with the type of security. Securities of the central government are safer than those of the state governments and local bodies. And the securities of state government and local bodies are safer than those of the industrial concerns. This is because the resources of the central government are much higher than the state and local governments and of the latter higher than the industrial concerns.

In fact, the share and debentures of industrial concerns are tied to their earnings which may fluctuate with the business activity in the country. The bank should also take into consideration the debt repaying ability of the governments while investing in their securities. Political stability and peace and security are the prerequisites for this.

It is very safe to invest in the securities of a government having large tax revenue and high borrowing capacity. The same is the case with the securities of a rich municipality or local body and state government of a

prosperous region. So in making investments the bank should choose securities, shares and debentures of such governments, local bodies and industrial concerns which satisfy the principle of safety.

Thus from the bank's viewpoint, the nature of security is the most important consideration while giving a loan. Even then, it has to take into consideration the creditworthiness of the borrower which is governed by his character, capacity to repay, and his financial standing. Above all, the safety of bank funds depends upon the technical feasibility and economic viability of the project for which the loan is advanced.

Diversity:

In choosing its investment portfolio, a commercial bank should follow the principle of diversity. It should not invest its surplus funds in a particular type of security but in different types of securities. It should choose the shares and debentures of different types of industries situated in different regions of the country. The same principle should be followed in the case of state governments and local bodies. Diversification aims at minimising risk of the investment portfolio of a bank.

The principle of diversity also applies to the advancing of loans to varied types of firms, industries, businesses and trades. A bank should follow the maxim: "Do not keep all eggs in one basket." It should spread it risks by giving loans to various trades and industries in different parts of the country.

Stability

Another important principle of a bank's investment policy should be to invest in those stocks and securities which possess a high degree of stability in their prices. The bank cannot afford any loss on the value of its securities. It should, therefore, invest it funds in the shares of reputed companies where the possibility of decline in their prices is remote.

Government bonds and debentures of companies carry fixed rates of interest. Their value changes with changes in the market rate of interest. But the bank is forced to liquidate a portion of them to meet its requirements of cash in cash of financial crisis. Otherwise, they run to their full term of 10 years or more and changes in the market rate of interest do not affect them much. Thus bank investments in debentures and bonds are more stable than in the shares of companies.

Profitability:

This is the cardinal principle for making investment by a bank. It must earn sufficient profits. It should, therefore, invest in such securities which was sure a fair and stable return on the funds invested. The earning capacity of securities and shares depends upon the interest rate and the dividend rate and the tax benefits they carry.

It is largely the government securities of the centre, state and local bodies that largely carry the exemption of their interest from taxes. The bank should invest more in such securities rather than in the shares of new companies which also carry tax exemption. This is because shares of new companies are not safe investments.

Purpose of Debt:

1. **Consolidate debt**

` Consolidating debt is one of the most common reasons to borrow a personal loan. According to a 2022 Lending Tree study, debt consolidation was the most popular reason to apply for a personal loan among consumers with excellent credit.

Debt consolidation involves rolling multiple debts into a single personal loan. This approach can make sense to secure a low interest rate. Repayment of other debts shall be from the money of a personal loan. There will be only one fixed monthly payment and savings on interest.

The average APR on a 24-month personal loan was 8.73% in May 2022 — the latest data available from the Federal Reserve — while the average interest rate on all credit card accounts is 15.13%.

2. **Cover Emergency Expenses:**

While it's best to build an emergency fund to cover unexpected expenses, an emergency personal loan can help if not yet prepared to meet contingencies.

Unfortunately, many people are unable to put aside money for an emergency savings account.

In 2022, the Consumer Financial Protection Bureau performed a survey on consumers and found the following:

- 24% of consumers have no savings in case of emergency
- 39% of consumers have less than a month of income retained for emergencies
- Only 37% consumers have at least a month of income set aside to cover emergencies

  Some reasons for an emergency loan include:

- Job loss or reduced hours
- Auto repairs
- Medical bills
- Help for a friend or family member

3. Home Improvement Objects:

A personal loan help to cover the home improvement expenses, like renovating the kitchen, finishing the basement or reflooring the home.

In these scenarios, a personal loan can help to pay for the repairs over time – typically two to five years.

4. Finance Funeral Expenses

When someone dies without leaving behind sufficient funds for funeral costs, it can put an unexpected financial strain on the surviving family members.

The median cost of a funeral with a viewing and burial was $7,849 in 2021, according to the National Funeral Directors Association. Many consumers won't have enough saved to cover that cost all at once.

A funeral loan helps to cover the cost of a funeral. You may even be able to get a Funeral loan shall be sanctioned even for a bad credit.

5. Help cover moving costs

Another idea on the list of loan purposes: covering moving costs. There are many scenarios in which moving loans may make sense:

- When unsafe in the current environment
- When separated from the spouse
- When more space is required for a child
- job offer is in another location

6. Make a large purchase

Personal loan shall help to finance a large purchase, but that doesn't mean borrowing money to get a new entertainment system, patio set or car. Some large purchases are necessary, such as suddenly needing a new major appliance.

On the other hand, auto loans require collateral, which means borrower could lose the car if borrower fall behind on payments. It's a good idea to compare rates, especially if borrower is worried about risk.

7. Cover a major life milestone

Whether one is getting married, going on a honeymoon or thinking about adoption, a personal loan can put these ventures within reach.

Since many people don't have that kind of cash lying around, many lenders offer wedding and honeymoon loans to cover those costs.

Adoption loans are available to parents who are looking to cover the following expenses:

- Travel
- Home studies
- Attorney fees
- Court fees
- Adoption agency fees

8. Pay for a vacation

While taking a trip somewhere can be exciting, travel can be expensive. Between plane tickets, food, shopping, hotels and activities, a vacation can quickly feel unaffordable.

Vacation loans can ease some of the financial burden of having to pay for a trip upfront and instead divide into monthly payments instead.

a payday loan to cover a purchase. However, payday loans are problematic and

A lower credit score won't necessarily disqualify the borrower for a personal loan. There are a number of lenders who offer personal loans for bad credit and will work with despite low score.

Personal loan will almost always have lower rates and fees plus a longer repayment timeline.

Diversification of Risk

Diversification of risk is simply another way of looking at a diversified portfolio. The latter is an investment management strategy where we divide our investment between separate assets. Different assets carry different degrees of risk, reacting differently to any given event.

While some will stay stable, others may go down or buck up in value. A mixed bag of assets, therefore, allows the portfolio to absorb the impact of an adverse event, ensuring that any loss is compensated completely or in part by other investments. Diversification of risk is, therefore, a tactic to balance between maximising returns and minimising risks.

Ways to Diversify Risk

For diversification of assets, assets are to be considered across different markets and timelines. Even within the same asset class, it is best to go for a varied combination. Hence, a portfolio should contain a mix of stocks, mutual funds, bonds, commodities, money market instruments, and real estate.

Guidelines to be followed to diversify the portfolio:

Determine risk tolerance

Risk tolerance is the amount of risk that the investor is prepared to bear. It is distinctive for every investor and is influenced by many factors, one of the biggest of which is age. Younger people usually have a higher risk tolerance than someone in middle or near retirement age. They can invest in riskier, but high return ventures, knowing that they have the time to offset potential risks over time.

On the other hand, investors in their 50s will be looking for a stable avenue to park their lifetime's savings.

Similarly, personal liabilities such as a high number of dependents, personal expenses, or debts, can also lower the risk tolerance. Understanding the risk tolerance is the first step in diversification of risk. People with high risk tolerance, or aggressive investors, will be willing to undertake risky ventures for higher returns.

On the other hand, conservative investors will prefer lower volatility. Most people are moderate investors, falling somewhere in between.

Investor should start with an emergency fund and insurance

Then start diversifying risks by anticipating and creating a fund for financial uncertainties. The most preferred means of protecting against such risks is insurance, particularly, medical insurance and life insurance. While investing in these two instruments may seem unnecessary if investor is young, starting life insurance early also gives the advantage of lower premiums. Depending on investor's assets or lifestyle, he/she may want to invest in other kinds of insurance, such as that for property or car.

At the same time, the long timeline of an insurance cover can leave one exposed to other uncertainties in the immediate future.

The first step of an investment plan, therefore, is an emergency fund. As the name suggests, an emergency fund is intended to be used only during emergencies. It must be liquid, which means, available whenever required.

There are many options that allow short-term withdrawals according to convenience. For instance, money market securities such as treasury bills (T-bills) can be easily liquidated for a quick cash flow. Mutual funds with a systematic withdrawal plan (SWP) come with the option of withdrawing from the fund at a set date.

Diversifying Risk in Asset Allocation

Asset allocation is the distribution of the investment between different assets. The most familiar of these are stocks and bonds. Stocks are seen as more volatile, but with higher returns than bonds. Fortunately, there are many other options to pick from which straddle the entire risk spectrum. When diversifying risks in a portfolio, investor pick assets of different risk profiles, combining a risky venture with a safe and stable option.

For instance, cryptocurrencies have emerged as a popular choice among many aggressive investors. It has been seen as the dark horse that may win the race as it gains momentum. On the flip side, its future is still uncertain. Hence, a potential risk associated with cryptocurrencies can be offset by parking part of investor's fund in secure options, such as G-secs like T-bills or commercial papers.

Unless there is a professional at disposal to look after investor's wealth, the asset holdings should remain manageable. Investor must be able to keep a track of the growth of the portfolio and the fluctuation in each allocation, and take corrective action immediately.

Different Timelines to Diversify Risk

Diversification is not limited merely to asset classes. It also extends to the timelines of the different investments.

A long-term investment will necessarily contain instruments that will take months, if not years, to mature. However, it also locks money in for an extended period. A short-term investment in equities or mutual funds ensures that part of the portfolio will mature at a shorter interval, unlocking funds that investor can then re-invest or spend according to the requirements. They can also be used as emergency funds. Ideally, portfolio should have assets that mature at different intervals.

A buy-and-hold strategy is usually the recommended path for a long-term investment. In this passive investment strategy, an investor keeps the portfolio stable over a long period, allowing risks to play out and the asset to mature over time. While this is the preferred option and can safeguard against knee-jerk reactions or panic, it does not mean complete passivity.

Investor must keep track of the investments and the markets to understand how each is performing. Investor must know when to cut losses and make an exit. This is where the stop-loss strategy comes into play. A stop-loss strategy is when the investor or his/her broker sells the stock when it reaches a certain level. So, if investor's stop-loss order is at 5%, his/her broker will sell the stock the moment it falls to 95% of the original price at which investor bought the stock.

Rebalance Periodically to Offset Risks:

Once we have a portfolio with diversified risks, investor need to maintain this balance over its lifetime. This means reviewing the portfolio at periodic intervals to assess its performance. There are two factors to be considered when reviewing

a portfolio, the asset and the investor’s own risk profile. It is important to understand that the risk associated with an asset can change over time.

For instance, a mutual fund that was once seen as stable can become volatile later. Investor’s own risk tolerance will also change with circumstances, lowering with age or debts. On the other hand, it can also increase with a rising income. Investor’s portfolio must be rebalanced to reflect these changing priorities.

Model Credit Policy for Individuals and Organizations:

A credit policy should spell out these details:

- **Client qualifications for receiving credit.** It’s best to run credit checks on clients before offering them credit, though it could be done so with the client’s permission. Credit policy should thus state what a client’s credit report must look like for the client to qualify for credit. Clients with a poor borrowing history should be disqualified.
- **Credit limits.** If offering Rs10,00,000 as credit to a client would leave far too little cash in hand, then lower the credit limit. If several customers are expected to take credit from the company, figure out how maximum credit limit can accommodate several borrowers while keeping the cash flow adequate.
- **Credit terms**. There is an opportunity to earn interest if credit is offered. All details viz., interest rates, payment deadlines, acceptable payment methods (such as credit cards and personal checks), early payment discounts and late payment fees are to be disclosed.

- **Requests for customer information.** In the credit policy, state which types of information clients need to provide in order to approve them the credit. Such information could include how long they have been in business (for B2B clients), the services they expect, and their credit scores.
- **Invoicing terms.** Firmly establishing the invoicing practices goes hand in hand with setting a credit policy. That's because any company that invoices clients to receive payment for work already done is operating on a credit model.
- **Debt collection terms.** No credit policy can entirely prevent some debtors from failing to pay what they owe. That's why credit policy should describe the actions that would be taken in the event of an unpaid account. Such actions could include sending the debt to collections or suing the client in small claims court.

How to write a credit policy

To write a credit policy, combine the following sections in a written document:

1. Purpose statement

The top of the credit policy should state that the document is the company's credit policy. This purpose statement can be brief – two or three sentences should do.

2. Statement of scope

Types of clients and sales the credit policy governs has to be specified clearly. For example, some credit policies only apply to domestic sales made to businesses of a certain size, whereas others pertain only to international clients.

3. Credit and payment terms

More important stipulations viz., credit limit and details of interest and fees should be without any ambiguity.

4. Credit application and review

The credit policy should detail how the company will process credit applications and review the credit history of established creditors. Similarly, note any changes to established creditors' accounts that could affect their current credit.

5. Sales terms

After discussing how to qualify the creditors, include text that empowers the credit team to modify the sales terms. Mention that this flexibility exists to maximize sales outcomes, and restate the basic payment terms.

6. Statement of credit team roles

End the credit policy with a statement of particulars of the credit team that would execute the credit-related tasks. Thus, both the company and the

debtors are clear whom (i.e.,) the employees they shall contact or expect to hear from the credit-related matters. Without mutual clarity on these terms, other unauthorized people in the credit team would extend credit to unqualified clients. Retracting this credit will be challenging, if not impossible.

Different Types of Credit Facilities provided by Banks

At some stage, every Business needs funding for smooth operations. There are multiple funding sources available in the market for business organizations. Credit Facility offered by Banks is one such source. It can be understood as an agreement or arrangement between the borrower and banks where the borrower can borrow money for an extended period. Credit facilities are utilized by the Companies, primarily to satiate the funding-needs for various business operations. Banks on the other hand earn profit from the interest incurred on the principal amount lent to the borrower.

The different types of Credit Facilities can be broadly classified into two parts:

- Fund Based Credit
- Non-Fund Based Credit.

Fund Based Credit

Fund Based Credit is the one where the Bank provides the Fund directly to the Borrower without any third party involvement. It usually involves an immediate flow of funds to the borrower's account. For e.g. Loans, ODs (Over Drafts), CCs (Cash Credit), PAD (Payment against Documents), Consortium loans, etc.

Fund-Based Credit comes with multiple advantages.

1. The fund-based Credit offers immediate funding to the borrower.
2. The fund-based Credit offers actual funding for business operations.

Different types of fund based credits are as follows:

1. Loan

A loan is a type of Fund-Based Credit where the Borrower has to repay the Credit within the pre-agreed time and with interest. Loans are given to the business to meet their various running expenses such as production, distribution, expansion etc. A huge amount of loan can be given to the companies depending on their requirements. Although, to ensure the safety of returning of the funds, Credit Monitoring Arrangement Data reports are carefully monitored in funding cases that involve a large amount of principal.

A) Demand Loans & Term Loans

Demand loan:

Demand Loans, sometimes known as working capital loans, are offered by the lender to the Borrower for the short-term.

As the name suggests, the Borrower has to repay the loan on the demand of the lender. There is no fixed tenure for the repayment. The Borrower can repay the loan in advance without paying any prepayment charges. These loans are generally offered against tangible assets or similar securities.

Term Loan:

These loans come with a predefined repayment schedule and tenure. As the tenure is fixed, the Borrower will have to pay some pre-payment

charges in early payments. They are generally offered for the large funding requirements.

B) Unsecured Loan & Secured Loan

Unsecured Loan

These loans are offered to the borrower without any collateral but generally carry a high interest rate. This means, if the borrower defaults on the repayment of loan, there is no way for the lenders to acquire any asset of the borrower whether it is tangible or non-tangible. These loans include Personal loans and student loans as well.

Secured Loan

The lenders offer these loans against any tangible or non-tangible asset like home, piece of land, vehicle etc. If the borrower defaults on the payment, his/her assets can be acquired by the lender. Loans such as home loans and loans against property are a few types of secured loans.

2. Cash Credit

Cash credit is provided to the business owners to carry out their regular business expenses. In Cash credit, the borrower is given access to a current account from which they can withdraw money within a predefined limit for an agreed amount of time. The interest is charged on the daily closing balance of the account rather than the borrowing limit.

3. Overdraft

This Credit Facility is offered to Current Account holders in a particular bank, to borrow the fund more than their existing balance for a specific period. These credits are secured by the physical assets, pledge of FDs, Securities or Mortgage of some immovable property in some cases.

4. Credit Card

Under this facility, a Credit Cardholder can spend a fixed amount of money using the card offered to him/her by the Bank. The user has to pay the credits used within the stipulated time regularly. Any failure to pay the outstanding bills on time attracts a penalty from the Bank.

5. Export Finance

Export finance is the financing facility which is provided by the banks to fund exporters to meet their production and export needs.

The different type of export finance are:

A) Packing Credit Advances

These types of credits are offered to exporters to meet the expenses for manufacturing and packing the goods for export as per the buyer's need. The credit is offered against hypothecation of goods stock, and any other assets of the borrower.

B) Post Shipment Finance

These type of credits are offered to the exporters once they export their product to the buyers. These credits are offered to meet the interim cash requirement of the exporter. It is offered based on the document and invoices suggesting that the export is made.

6. Hire Purchase Finance

This type of finance is offered to the buyer when he/she is looking to buy some expensive product. Under this Credit, it is agreed that the buyer will pay some down payment initially and the rest of the amount will be paid in installments.

7. Bill Finance

In bill finance, a Bank draws a bill of exchange from another bank to transfer the funds due to Credit offered to the borrower. The different types of bill finance are:

A) Bill Discounted

This Credit allows the seller to borrow money from Bank in advance against the payment that will be received by the seller in the future. The Bank deducts some charges as the fees from the payment, once the buyer deposits it.

B) Bill Purchased

This Credit allows the seller to borrow funding based on a sales document not drawn under the Letter of Credit. The lending bank submits these documents to the buyer's bank for the payments.

8. Leasing Finance

Under this credit facility, the owner of an asset gives the right to use that asset to the borrower against the payment of a specific amount. It is one of the most important forms of medium and long-term finance. As the owner leases his/her property, he/she is known as the lessor, and the one who takes the property on lease is called the lessee.

9. Retail Credit

The banks offer Credit or loan to the Borrower to purchase certain moveable or immovable properties, durables, vehicles or similar products. This Credit

is offered to the borrower based on his/her credit history. This facility is offered on Business to Business transactions as well as Business to Customer transactions.

Non-Fund Based Credit

On the contrary, Non-Fund Based Credit is where the Fund is not transferred directly to the borrower. It is offered to a third-party as agreed upon by the borrower, on behalf of the borrower.

The bank usually acts as a guarantee provider to the seller on the behalf of the buyer. If the payment is not received by the seller within pre-agreed time, the bank pays the amount to the seller. For e.g. Bank Guarantee, Buyer Credit, Letter of Credit, Supplier Credit.

Following are the advantages of Non-Fund Based Credits:

1. It offers financial security to the seller if the buyer defaults due to any reason.
2. It offers Business expansion opportunities to the exporters.

The different types of non-fund based credit are:

1. Letter of Credit

A letter of credit is an assurance provided by the Bank to the seller on behalf of the buyer that the seller will receive the buyer's payment at regular intervals. It also states that if the buyer fails to pay the seller for any reason, the Bank will be responsible for the remaining or full payment.

Letter of Credit is offered based on the collateral of cash or certain securities. With the rising international trading, Letter of Credit is becoming a crucial tool to manage the payments between parties that hardly know each other and live in different countries with different laws. The bank charges a certain percentage from the buyer as the fees for offering the Letter of Security.

The Letter of Credit can be divided into the following parts:

A) Sight Credit

This letter of Credit is quicker than others. Here the Borrower can take the lender's funds by showing a bill of exchange and sight letter of Credit.

B) Revocable & Irrevocable Credit

Revocable Letter of Credits is the one that can be revoked or canceled by the issuing bank without prior notice to any party. Irrevocable Letter of Credit cannot be revoked or canceled by the issuing Bank. So once the LOC is generated, Bank will have to honor the letter.

C) Confirmed Credit

In this type of Credit, a bank other than the issuing Bank confirms the Letter of Credit by adding its confirmation. Only Irrevocable Letter of Credit is eligible for confirmation.

D) Back-to-Back Credit

Under this type of Credit, the exporter requests the Bank to offer an LC to his/her local supplier. The request is based on the export LC received by the

exporter from an overseas buyer. Here, an LC is issued based on an export LC and hence the name, Back-to-Back Credit.

The advantages of a Letter of Credit to the buyer are as follows:

1. Allows the buyer to trade with the parties from any corner of the world
2. The buyer can edit the terms and conditions that fit him/her after consulting the seller.
3. It acts as a credit certificate for the buyer, and he/she can perform multiple trades as a major financial institution like Bank backs him/her.
4. Letter of Credit offers better Cash flow to the buyer.

The advantages of a Letter of Credit to seller are as follows:

1. The seller receives the money on fulfilling the terms mentioned In the Letter of Credit.
2. There is no risk of losing money for the seller if the buyer fails to pay the money. Seller gets his/her dues from the Bank that has issued the Letter of Credit.
3. The letter of Credit is easy to quick to avail based on good credit.
4. If there is a dispute in trading, the seller can withdraw funds from the Bank even when the case is pending.

2. Bank Guarantee

`Under this type of Credit, Bank offers assurance that under any circumstances, the Guarantee issuing Bank will fulfill any financial losses incurred by the protected party as mentioned in the Contract.

Different guarantees are as follows:

A) Financial Guarantee

In this type of Guarantee, the Guarantor takes responsibility for the Borrower. This means, if the Borrower fails to repay the debt, Guarantor will be liable to pay the unpaid amount.

B) Performance Guarantee

The Guarantor issued a security bond that assures the lender that the Contractor will complete the work satisfactorily in the stipulated time.

C) Deferred Payment Guarantee

This type of Guarantee is usually given on deferred or postponed payments. The banks generally offer DPG on the purchase of certain machinery and goods.

3. Letters of Comfort for Availing Buyers Credit

Letter of Comfort can be understood as the Guarantee offered by the Bank of Importer or buyer. The Importer can use this Letter of Comfort to avail Buyer’s Credit from the overseas banks. The Importer or Buyer’s Bank charges certain fees for offering the Letter of Comfort.

4. Derivative Products

Derivatives are a type of financial security or financial contracts that are backed by some underlying securities. These underlying securities can be anything, ranging from currencies, bonds, commodities to stocks.

5. Buyer Credit

It is a short-term funding option, offered to the Indian Buyers or Importers by the Bank to manage their import Business. Using Buyer’s Credit, the Importers can avail loans from foreign financial institutions which offer Credit

at comparatively lower rates. Buyer's Credit can be availed for importing almost all types of capital and non-capital goods.

6. Supplier Credit

This type of Credit is used to support the importers financially in India. Here any overseas Financial Institute or Supplier offers the Credit to the Importer on the Libor rates, which are comparatively low. Such Credit is backed by the Letter of Credit offered to the Importer via Importer's Bank.

Modes of Credit delivery:

Overdraft/Cash Credit System:

In this system, the borrowers are allowed to draw funds from the account to the extent of the value of inventories and receivables less stipulated margin within the maximum permissible credit limit granted by the bank. Here, the drawing power of the borrower is computed by the banks by deducting the stipulated percentage of margin from the value of the various items of inventory and receivables.

Borrowers can draw cheques on their overdraft or cash credit account to the extent of the drawing power so calculated, subject to the maximum credit limit granted by the bank. Value of the inventory is taken at cost price or market price, whichever is lower. Any withdrawal of funds beyond this limit renders the account irregular, serving as a warning signal to the lending banker and also prompting him to monitor the account closely. The borrower is required to submit a statement of stocks and receivables to the bank on a monthly basis.

It is necessary to understand the difference between 'drawing power' and 'drawing limit'. Drawing power is worked out by deducting the stipulated

margin from the value of inventory and receivables, as declared in the monthly statements. If the amount so calculated is lower than the sanctioned limit, the drawing power becomes the drawing limit.

On the contrary, if the drawing power is above the sanctioned limit, the drawing limit is restricted to the sanctioned limit only. Drawing power is helpful to the banker for taking a decision on a request by the borrower for allowing 'over limit', i.e., drawing beyond the sanctioned limit. Drawings allowed beyond the sanctioned limit should also be adequately secured by inventory and receivables after deduction of stipulated margins.

The overdraft and cash credit system of credit delivery dominates the scenario of credit dispensation by commercial banks all over the world. Despite several shortcomings, the system finds favour with both the commercial banks and the borrowers, in the form of short-term bank borrowings.

All sale proceeds are deposited in this account by the borrower; as and when necessary, the account is drawn up to the limit for making payments to the suppliers and other creditors. The system has been in vogue for a long time, mainly because of its flexibility, which can take care of temporary requirements of funds by the borrowers. The cash credit system enables continuous recycling of funds into the bank.

Loan System:

In some countries, term loans for short periods are the main form of short- term finance. Under this system, loans are sanctioned for definite purposes and periods. This is usually accompanied by the maintenance of a current account for routing the day-to-day transactions of the business

enterprise. This system forces the borrower to plan his cash budget in advance, thus ensuring a degree of self-discipline.

This system enables the bank to manage funds and the credit portfolio rationally. Unlike the overdraft or cash credit account, the borrower cannot liquidate the outstanding by deposit of sale proceeds on day-to-day basis and, therefore, the earnings of the banks get a boost under the loan system. Automatic review is built into the loan system, as every new loan has to be negotiated afresh.

This gives an opportunity to the bank to deny a loan if the performance of the company is not found to be satisfactory. The loan system is relatively simple to administer as there is no need to calculate the drawing power and giving various sub-limits against each item of inventory and receivables.

Bill System:

In bill system of financing, the borrower is financed against the bills of exchange drawn by him on his buyers. Financing is also done under the drawee bill system, where the borrower is a drawee of bill of exchange for his purchases. In case of sales bills, the borrower submits the bill of exchange along with the shipping documents, and the bank purchases or discounts the bill and credits the proceeds to the borrower's current account for his utilisation.

Thereafter, the relative bill is presented to the drawee (buyer) for payment and, upon receipt of the amount, the bill purchase/discounted account is squared off. Bill finance is self-liquidating in nature.

In case of drawee bills, the borrower is the buyer and the supplier draws the bill on him and presents the bill to the borrower's bank for payment. The bank discounts the bill and remits the proceeds to the supplier's bank and on due date of the bill, the borrower pays the amount with interest and other charges towards liquidation of the outstanding in the drawee bill discount account.

The cost of operation for borrowers under the bill system and also the cost of administering the system by banks are somewhat higher than other systems because of stamp duties, detailed book-keeping, etc.

Commercial Paper (CP):

Commercial paper is a popular form of raising working capital at a low cost by the corporate business houses. CP is a short-term money market instrument and the banks find it a convenient route to park their excess liquidity for a short period, not exceeding 12 months. The subscribers are other corporate houses, commercial banks, etc.

Commercial paper is a promissory note made by a highly rated corporate entity and is offered to the prospective investors including the banks for subscription. The banks invest in such commercial papers while discounting the promissory note at an underlying rate of interest, which is generally lower than the market rate of interest, including that of the prime lending rate of the commercial banks.

Commercial papers provide the corporate houses with an additional avenue of raising working capital, at a price substantially lower than the interest

charged by the commercial banks in their fund-based working capital limits of overdraft/cash credit granted to the borrowers.

DIMENSIONS OF CREDIT APPRAISALS – CCP FREE NOTES 2022

Credit Appraisal: Validation of proposal, Dimensions of Credit Appraisals, Structuring of Loan documents

Credit Appraisal: When a lender does an appraisal of Technical feasibility, economic viability, and bankability which also includes the creditworthiness of the applicant, the process is known as credit appraisal.

This process of credit appraisal assessment of whether the applicant will be able to repeat the loaned amount in the scheduled time or not. Different banks have different methods for the determination of the creditworthiness of a borrower. These methods are determined within the norms & standards which are set by the banks.

It is a very important step in sanctioning a loan because it is important that the borrowers carefully plan or their financing modes. Banks need to be careful while granting a loan because we could actually end up increasing their risk exposure. All banks have their own objectives which are subjective to them to evaluate the creditworthiness of the customers.

Validation of proposal

Every proposal is required to be explicitly validated i.e it should be confirmed that all the key aspects of the proposal are actually what the company wants some to be. And this cannot be done in just one sitting or at once.

It is a process of identification where what needs to be validated is identified to allow flexibility for every item to get validated as well as provides a mechanism where all the chosen items and methods to validate are insured for their efficiency to get the desired quality.

This way companies are ensured that all the key aspects are exactly what they are supposed to be before they get submitted for approval. This process helps in avoiding the disasters which can result from teams that work in isolation. Because in most of those cases proposals are used not worth what the companies want and they discover it too late to alter it.

In the process of developing of the proposal, the following actions, need to be taken:

- Making decisions
- Inventing approaches
- Incorporating required information
- Addressing the proposal requirements
- Delivering a message

- Seeking a superior score

Dimensions of credit appraisals

Service of credit includes monthly payments for utilities such as electricity bills, gas bills, telephone bill, and water bills. The payment on these credit services required to be made on time otherwise a deposit and late charge will be imposed.

While loans (secured or unsecured) can range from small to large amounts and range from a few days to several years. The amount can be repaid in one lump sum amount or in small installments until the principal amount and the finance charges are paid in full.

CREDIT APPRAISAL PROCESS:-

The process which is followed for the appraisal of credit is described below:

1) Credit Processing:

In this stage, all the information which is required to provide the credit is gathered and screening of applications are done. The application form which is used to apply should have sufficient columns for details so that all the information which is needed to assess the credit can be gathered.

For this purpose, banks and Financial Institutions should have a checklist so that this can actually be done.

2) Credit-Approval/Sanction:

There should be written guidelines on the credit approval process and authorities who will be responsible for the approval as well as there should be a proper basis on which their decisions will be dependent.

The authorities relating to approval should be duly sanctioned by the board of directors & should cover all the aspects of new credit approvals, renewables of credit and any changes in terms and conditions of the credit which have been provisionally approved. All these approvals should also be properly recorded and documented.

As a prudent norm, it should be ensured that the approval authority should not have the responsibility of building customer relationships.

3) Credit Documentation:

One of the most essential part of the credit processes documentation and it should be insured for each phase of the cycle in the credit process whether it is for the credit application, credit analysis, approval, monitoring, valuation or the recognition of impairment, foreclosure or realisation of security.

There should be a standard format for credit files and the proper maintenance system be there as well for cross indexing to assist in the process of review and follow up.

DOCUMENTS TO APPLY FOR A PERSONAL LOAN

Following are the main documents which are usually required when applying for a personal loan:

- **PAN** Card
- **Identity proof** which could be Aadhaar Card, Driving license, Passport or Voter ID, etc.
- **Signature Proof** such as Passport or PAN card, etc.
- **Address proof** could be a copy of Passport, Aadhaar card, driving license, utility bill; Gas or electricity bill, Voter ID, ration card or even a rent agreement, etc.
- **Bank statement** of the past 6 months

For a salaried individual, following documents are necessary in addition to the above-mentioned documents:

- **Salary slips** for the last 3 months
- ITRs or form 16

For **a self-employed individual,** additionally the below documents are needed to be submitted (**for self / business entity as applicable**):

- **Financial statements** for the last two years (balance sheet, profit and loss statement)
- **Income Tax Returns** for the last 2 years
- Proof of Business i.e License, registration certificate, GST number etc
- IT Assessment or Certificate of Clearance
- Challans of Income Tax or TDS Certificate (Form 16A) or Form 26 AS for income declared in ITR

An overview of credit card acquisitions from 2021 to 2022 reveals three trends, as noted in Insider Intelligence:

1. *An uptick in credit use* – While still behind debit use, credit use is growing and forcing issuers to make new and existing credit cards more compelling.
2. *Renewed card application activity* – Over a quarter of all U.S. consumers applied for a new credit card between October 2020 and October 2021 (+15.7% over prior year).
3. *Growth in perks and products*– To leverage increased usage and applications, issuers are focusing on expanding perks and adding new cards.

Rewards as a driver of credit card applications

Most new product launches, according to Competiscan, followed one of two paths: targeting a specific niche or offering more well-rounded rewards. For example, cards were introduced to reward pet lovers and cryptocurrency enthusiasts, among others.

Insider Intelligence shares observations on key categories:

- Post-pandemic reward value propositions have returned to prior constructs, with accelerated reward earning in categories like travel and lifestyle.
- At the same time, continued rewarding of e-commerce transactions – post-pandemic and now habituated – remains in play.

Redesigned credit card rewards

Redesigned card products include cashback cards with simplified value propositions, such as automatically adjusted rewards for top spend categories requiring no action by the cardmember.

In addition, there's increasing emphasis on rewards targeting the credit-building segment. Insights from Competiscan show that the sub-prime audience had typically been offered basic cards with low lines of credit and higher APRs. But Competiscan now observes, "A handful of top marketed credit-building cards offer cashback rewards in an effort to build deeper loyalty and to combat the runoff of cardholders to other card brands once they have established the proper credit to qualify for a rewards product."

Unit II

Overview of credit Policies and Project Appraisals

Credit Process – characteristics of different types of loans – Evaluating commercial loan requests – Financial statement analysis – cash flow analysis – Projections – management of the firm and Other factors – Feasibility study – Fundamental credit issues – Credit analysis – Project / Term Loan Appraisal – Technical Appraisal – commercial / market Appraisal – managerial appraisal – Financial Appraisal – Economic Appraisal – Environmental Appraisal.

UNIT – II

OVERVIEW OF CREDIT P OLICIES AND PROJECT APPRAISALS:

CREDIT PROCESS:

The credit process is a review of the business loan package by the Bank. Since the source of loan funds is the depositors' money and bank has to repay that money when requested, the credit review process helps Bank to make wise loans.

Banks will review the business loan package based on criteria known as the "Five C's of Credit."

1. Character - It involves a review of personal honesty, integrity, trustworthiness and management skills. A banking officer also makes a judgment of character based on the business plan, credit history and the quality.
2. Capitalization - The capital structure of the company is important because it helps determine the level of risk associated with the loan request. An analysis of capitalization includes a review of equity, total debt, the value of assets and permanent working capital.
3. Cash Flow - This is the cash the business has to pay for the debt. A cash flow analysis helps to determine if the company has the ability to repay the loan.
4. Collateral - This provides a secondary source of repayment, thereby minimizing the risk for the Bank. The amount and type of collateral required depends on the type and purpose of the loan.

5. Conditions - This refers to outside conditions that may affect the ability of the business to repay the loan. Factors such as general economic conditions or a large concentration of sales to a single customer are evaluated during the review of the loan application.

Loans

When a lender gives money to an individual or entity with a certain guarantee or based on trust that the recipient will repay the borrowed money with certain added benefits, such as an interest rate, the process is called lending or taking a loan.

A loan has three components – principal or the borrowed amount, rate of interest and tenure or duration for which the loan is availed.

Most of us prefer borrowing money from a bank or a trusted non-banking financing company (NBFC) as they are bound to the government policies and are trustworthy. Lending is one of the primary financial products of any bank or NBFC (Non-Banking Financial Company) .

Types of Loans :

Based on the Security Provided:

Secured Loans

These loans require the borrower to pledge collateral for the money being borrowed. In case the borrower is unable to repay the loan, the bank reserves the right to utilise the pledged collateral to recover the pending payment. The interest rate for such loans is much lower as compared to unsecured loans.

Unsecured Loans

Unsecured loans are those that do not require any collateral for loan disbursement. The bank analyses the past relationship with the borrower, the credit score, and other factors to determine whether the loan should be given or not. The interest rate for such loans can be higher as there is no way to recover the loan amount if the borrower defaults. Based on the Purpose:

Education Loan

Education loans are financing instruments that aid the borrower pursue education. The course can either be an undergraduate degree, a postgraduate degree, or any other diploma/certification course from a reputed institution/university. The admission pass provided by the institution is required to get the financing. The financing is available both for domestic and international courses.

Personal Loan

Whenever there is a liquidity issue, one can go for a personal loan. The purpose of taking a personal loan can be anything from repaying an old debt, going on vacation, funding for the down payment of a house/car, and medical emergency to purchasing big-ticket furniture or gadgets. Personal loans are offered based on the applicant's past relationship with the lender and credit score.

Vehicle Loan

Vehicle loans finance the purchase of two-wheeler and four-wheeler vehicles. Further, the four-wheeled vehicle can be a new one or a used one. Based on the on-road price of the vehicle, the loan amount will be determined by the lender. Applicant may have to get ready with a downpayment to get the vehicle as the loan rarely provides 100% financing. The vehicle will be owned by the lender until full repayment is made.

Home Loan

Home loans are dedicated to receiving funds in order to purchase a house/flat, construct a house, renovate/repair an existing house, or purchase a plot for the construction of a house/flats. In this case, the property will be held by the lender and the ownership will be transferred to the rightful owner upon completion of repayments.

Based on the Pledged Assets:

Gold Loan

Many financiers and lenders offer cash when the borrower pledges physical gold, may it be jewellery or gold bars/coins. The lender weighs the gold and

calculates the amount offered based on several checks of purity and other things. The money can be utilised for any purpose.

The loan must be repaid in monthly instalments so the loan can be cleared by the end of the tenure and the gold can be taken back to custody by the borrower. If the borrower fails to make the repayments on time, the lender reserves the right to take over the gold to recover the losses.

Loan Against Assets

Similar to pledging gold, individuals and businesses pledge property, insurance policies, FD certificates, mutual funds, shares, bonds, and other assets in order to borrow money. Based on the value of the pledged assets, the lender will offer a loan with some margin at hand.

The borrower needs to make repayments on time so that he/she can get custody of the pledged assets at the end of the tenure. Failing to do so, the lender can sell the assets to recover the defaulted money.

Important Factors Lenders Look at to Approve Loan Application

- **Credit Score**

Credit score plays an important role in deciding whether the lender would like to go ahead with your application or drop it off at the initial stage. This is especially the case when it comes to unsecured loans.

Since a credit score represents the credit history of the borrower, the lender analyses the repayment history of the borrower and concludes whether the

borrower can repay on time or will he default on payments. The loan approval is based on the lender's judgement after the necessary analysis.

- **Income and Employment History**

Applicant's monthly or annual income and employment history plays a crucial role in loan approval as well. Based on the income and income stability in the form of consistent and stable work history, the lender may or may not get convinced that applicant will be able to repay the loan.

Even if the applicant is self-employed, the lender assumes that the business is running well for the past few years and turnover of the business is satisfactory.

- **Debt-to-Income Ratio**

Not just having a good income, applicant's debt-to-income ratio is also important. In case applicant has an income of Rs.1 lakh per month and if the debt repayment commitments exceed Rs.75,000 already, a new loan will not be provided as the applicant will need the remaining income to take care of the domestic expenses.

Therefore, irrespective of applicant's income, he/she must have a low debt-to-income ratio so the lenders can think that the applicant has enough cash at hand every month to make the repayments as well as to handle the family expenses.

- **Collateral**

Based on the collateral applicant provides and its current market value, the lender may decide on the interest rate applicable to the loan. Providing collateral will make the deal more secure from the lender's perspective, which may result in more trust and less interest rate. An unsecured loan is not famous as it includes a higher interest rate comparatively.

- **Down Payment**

The money applicant has saved and the effective execution of the saving plan towards a down payment will increase the lender's trust. The higher the down payment, the lower is the loan amount requirement.

Features and Benefits of Loans

- There are several types of loans categorized based on various factors.
- Applicant can choose the type of loan he/she wishes to take based on the requirement and eligibility.
- The lender will be the ultimate power to decide the loan amount they wish to offer based on several factors, such as repayment capacity, income, and others.
- A repayment tenure and interest rate will be associated with every loan.

- The bank may apply several fees and charges to every loan.
- Many lenders provide instant loans that take a few minutes to few hours to get disbursed.
- The interest rate is determined by the lender based on the Reserve Bank of India's guidance.
- The lender determines the requirement for security.
- A third-party guarantee can be used instead of security in some cases.
- The loan repayments must be made in equated monthly instalments over the pre-determined loan tenure.
- There may or may not be the option for full/part prepayment.

Eligibility for Loan

The eligibility criteria to get a loan varies based on the type of loan. Generally speaking, the following simple criteria is applied to check the applicant's eligibility.

- A decent credit score
- Constant income flow
- Age between 23 years and 60 years at the time of entry
- A few assets such as FDs, investments, immovable property, etc.

- A good relationship with the bank
- A timely debt repayment history

Documents Required

Salaried Applicants

- Application form with photograph
- Identity and address proof
- Last 6 months' bank account statement
- Latest Salary Slip
- Form 16

Self-Employed Applicants

- Application form with photograph
- Identity and address proof
- Last 6 months' bank account statement
- Proof of business
- Business profile
- Income Tax returns (self and business) for the last three years

- Profit/loss statements and balance sheets of the last three years

Commercial Loan

A commercial loan is a loan that is extended to businesses by a financial institution. Commercial loans are generally used to purchase long-term assets or to help fund day-to-day operational costs.

Understanding a Commercial Loan

It is unfeasible for small and mid-sized businesses to access equity and bond markets for financing due to regulatory hurdles, associated costs, and the time required to secure the funds. Therefore, small and mid-sized enterprises use debt products such as commercial loans and/or lines of credit.

Commercial loans can ultimately be used for any purposes required for the business – acquiring assets, purchasing supplies, meeting daily operational costs, paying payroll, etc. In the loan application process, the business must specify the purposes for which the commercial loan will be used for.

Process for Securing a Commercial Loan

Depending on the lender, the process to secure a commercial loan may be different. The general process for securing such a loan is as follows:

1. Pre-approval (Qualifying process)

The lender (bank) will begin a pre-approval process for the business by evaluating the financial history and income of the business. In addition, the

lender will investigate the existing debt of the business and the purpose of the loan. Through a pre-qualifying process, the lender can gain a rough idea of how much the business would be able to borrow and the relative riskiness of the borrower.

2. Loan application

After the pre-qualifying process, the business must complete and submit a loan application. In the application, financial statements or similar documents dating back at least three years are generally required. This is to help ensure that the business can repay the loan.

3. Review of the loan application package

Once the application is submitted, a loan officer will review these documents. They will investigate things such as credit history, available collateral of the business, the current and projected income of the business, etc. A big part of the diligence process is the financial analysis.

4. Loan underwriter/Loan committee

If the loan request is deemed appropriate by the loan officer, a complete and formal credit application is submitted to a credit adjudicator or loan committee. The adjudicator reviews all relevant information and decides whether to approve or decline the loan. The process can take up to a week, and the business may be required to provide additional documentation during the review.

5. Term sheet

If approved, the processor will present the company with a term sheet. A term sheet is a formal document that outlines the parties involved, amount of financing, available collateral, fees, use of the loan, and the interest rate on the loan. After reviewing the term sheet and signing a letter of intent, payment may be required for third-party reports, e.g., appraisal reports.

6. Loan package and closing documents

Upon completing third-party reports, the complete loan application package is resubmitted to the loan underwriter for final approval. If approved, the business is required to sign finalized loan documents. Generally, businesses employ a closing agent (e.g., an authorized representative, an attorney, etc.) who handles all closing documents and completes any remaining paperwork.

Advantages of a Commercial Loan

1. Access to capital

A commercial loan provides additional cash for a business. The cash may be used to purchase new equipment, satisfy payroll expenses, etc.

2. Easier application process

Although the application process for a commercial loan may seem daunting, it is easier than raising money in the equity or debt markets. There are regulatory hurdles and significant costs and time required to raise money through equity and/or bond markets.

3. Retaining ownership

A commercial loan does not dilute the business owner's equity. For example, a business may issue equity to raise money. In doing so, the owner would be diluting their own equity in the business. As such, a commercial loan allows an owner to raise money without diluting their stake in the business.

Disadvantages of a Commercial Loan

1. Paperwork and application process

A commercial loan requires a significant amount of paperwork and involves a tedious application process. For example, a business may be required to submit an outline of its business plan and give a presentation outlining its business goals and objectives.

2. Inflexibility in the use of funds

When applying for a commercial loan, the business must specify what the money will be used for and how it will pay back the loan. This results in inflexibility of the funds, as the business is required to commit to its original plan(s).

3. Interest costs

A commercial loan comes with a stated interest rate, which may be floating or fixed. As such, the business is required to make monthly payments on the money it borrows.

Financial Statement Analysis

Financial statement analysis is the process of analyzing a company's financial statements for decision-making purposes. External stakeholders use it to understand the overall health of an organization and to evaluate financial performance and business value. Internal constituents use it as a monitoring tool for managing the finances.

Financial Statements Analysis

The financial statements of a company record important financial data on every aspect of a business's activities. As such, they can be evaluated on the basis of past, current, and projected performance.

In general, financial statements are centered around generally accepted accounting principles (GAAP) in the United States. These principles require a company to create and maintain three main financial statements: the balance sheet, the income statement, and the cash flow statement. Public companies have stricter standards for financial statement reporting. Public companies must follow GAAP, which requires accrual accounting. Private companies have greater flexibility in their financial statement preparation and have the option to use either accrual or cash accounting.

Several techniques are commonly used as part of financial statement analysis. Three of the most important techniques are horizontal analysis, vertical analysis, and ratio analysis. Horizontal analysis compares data horizontally, by analyzing values of line items across two or more years. Vertical analysis looks at the vertical effects that line items have on other

parts of the business and the business's proportions. Ratio analysis uses important ratio metrics to calculate statistical relationships.

Types of Financial Statements

Companies use the balance sheet, income statement, and cash flow statement to manage the operations of their business and to provide transparency to their stakeholders. All three statements are interconnected and create different views of a company's activities and performance.

Balance Sheet

The balance sheet is a report of a company's financial worth in terms of book value. It is broken into three parts to include a company's assets, liabilities, and shareholder equity. Short-term assets such as cash and accounts receivable can tell a lot about a company's operational efficiency; liabilities include the company's expense arrangements and the debt capital it is paying off; and shareholder equity includes details on equity capital investments and retained earnings from periodic net income. The balance sheet must balance assets and liabilities to equal shareholder equity. This figure is considered a company's book value and serves as an important performance metric that increases or decreases with the financial activities of a company.

Income Statement

The income statement breaks down the revenue that a company earns against the expenses involved in its business to provide a bottom line, meaning the net profit or loss. The income statement is broken into three

parts that help to analyze business efficiency at three different points. It begins with revenue and the direct costs associated with revenue to identify gross profit. It then moves to operating profit, which subtracts indirect expenses like marketing costs, general costs, and depreciation. Finally, after deducting interest and taxes, the net income is reached.

Basic analysis of the income statement usually involves the calculation of gross profit margin, operating profit margin, and net profit margin, which each divide profit by revenue. Profit margin helps to show where company costs are low or high at different points of the operations.

Cash Flow Statement

The cash flow statement provides an overview of the company's cash flows from operating activities, investing activities, and financing activities. Net income is carried over to the cash flow statement, where it is included as the top line item for operating activities. Like its title, investing activities include cash flows involved with firm-wide investments. The financing activities section includes cash flow from both debt and equity financing. The bottom line shows how much cash a company has.

Free Cash Flow and Other Valuation Statements

Companies and analysts also use free cash flow statements and other valuation statements to analyze the value of a company. Free cash flow statements arrive at a net present value by discounting the free cash flow that a company is estimated to generate over time. Private companies may

keep a valuation statement as they progress towards potentially going public.

Financial Performance

Financial statements are maintained by companies daily and used internally for business management. In general, both internal and external stakeholders use the same corporate finance methodologies for maintaining business activities and evaluating overall financial performance.

When doing comprehensive financial statement analysis, analysts typically use multiple years of data to facilitate horizontal analysis. Each financial statement is also analyzed with vertical analysis to understand how different categories of the statement are influencing results. Finally, ratio analysis can be used to isolate some performance metrics in each statement and bring together data points across statements collectively.

Below is a breakdown of some of the most common ratio metrics:

- **Balance sheet**: This includes asset turnover, quick ratio, receivables turnover, days to sales, debt to assets, and debt to equity.
- **Income statement**: This includes gross profit margin, operating profit margin, net profit margin, tax ratio efficiency, and interest coverage.
- **Cash flow**: This includes cash and earnings before interest, taxes, depreciation, and amortization (EBITDA). These metrics may be shown on a per-share basis.
- **Comprehensive**: This includes return on assets (ROA) and return on equity (ROE), along with DuPont analysis.

Advantages of financial statement analysis

Financial statement analysis evaluates a company's performance or value through a company's balance sheet, income statement, or statement of cash flows. By using a number of techniques, such as horizontal, vertical, or ratio analysis, investors may develop a more nuanced picture of a company's financial profile.

Most often, analysts will use three main techniques for analyzing a company's financial statements.

First, horizontal analysis involves comparing historical data. Usually, the purpose of horizontal analysis is to detect growth trends across different time periods.

Second, vertical analysis compares items on a financial statement in relation to each other. For instance, an expense item could be expressed as a percentage of company sales.

Finally, ratio analysis, a central part of fundamental equity analysis, compares line-item data. Price-to-earnings (P/E) ratios, earnings per share, or dividend yield are examples of ratio analysis.

Cash Flow Statement

A cash flow statement has three distinct sections, each of which relates to a particular component—operations, investing, and financing—of a company's business activities. Below is the typical format of a cash flow statement.

Cash Flow from Operations

This section reports the amount of cash from the income statement that was originally reported on an accrual basis. A few of the items included in this section are accounts receivables, accounts payables, and income taxes payable.

If a client pays a receivable, it would be recorded as cash from operations. Changes in current assets or current liabilities (items due in one year or less) are recorded as cash flow from operations.

Cash Flow from Investing

This section records the cash flow from sales and purchases of long-term investments like fixed assets that include property, plant, and equipment. Items included in this section are purchases of vehicles, furniture, buildings, or land.

Typically, investing transactions generate cash outflows, such as capital expenditures for plant, property, and equipment; business acquisitions; and the purchase of investment securities.

Cash inflows come from the sale of assets, businesses, and securities. Investors typically monitor capital expenditures used for the maintenance of, and additions to, a company's physical assets to support the company's operation and competitiveness. In short, investors can see how a company is investing in itself.

Cash Flow from Financing

Debt and equity transactions are reported in this section. Any cash flows that include payment of dividends, the repurchase or sale of stocks, and bonds would be considered cash flow from financing activities. Cash received from taking out a loan or cash used to pay down long-term debt would be recorded in this section.

For investors who prefer dividend-paying companies, this section is important since it shows cash dividends paid since cash, not net income, is used to pay dividends to shareholders.

Cash Flow Analysis

A company's cash flow can be defined as the number that appears in the cash flow statement as net cash provided by operating activities, or "net operating cash flow." However, there is no universally accepted definition. For instance, many financial professionals consider a company's cash flow to be the sum of its net income, depreciation, and amortization (non-cash charges in the income statement). While often coming close to net operating cash flow, the shortcut can be inaccurate, and investors should stick with using the net operating cash flow.

While cash flow analysis can include several ratios, the following indicators provide a starting point for an investor to measure the investment quality of a company's cash flow.

Operating Cash Flow/Net Sales

This ratio, which is expressed as a percentage of a company's net operating cash flow to its net sales, or revenue (from the income statement), tells us how many dollars of cash are generated for every dollar of sales.

There is no exact percentage to look for, but the higher the percentage, the better. It should also be noted that industry and company ratios will vary widely. Investors should track this indicator's performance historically to detect significant variances from the company's average cash flow/sales relationship along with how the company's ratio compares to its peers. It is also essential to monitor how cash flow increases as sales increase since it's important that they move at a similar rate over time.

Free Cash Flow

Free cash flow (FCF) is often defined as the net operating cash flow minus capital expenditures. Free cash flow is an important measurement since it shows how efficient a company is at generating cash. Investors use free cash flow to measure whether a company might have enough cash, after funding operations and capital expenditures, to pay investors through dividends and share buybacks.

To calculate FCF from the cash flow statement, find the item cash flow from operations—also referred to as "operating cash" or "net cash from operating activities"—and subtract capital expenditures required for current operations from it.

For example, in addition to capital expenditures, dividend could also be included to the amount to be subtracted from net operating cash flow to arrive at a more comprehensive free cash flow figure. This figure could then be compared to sales.

If a company has a history of dividend payments, it cannot easily suspend or eliminate them without causing shareholders some real pain. Even dividend payout reductions, while less injurious, are problematic for many shareholders. For some industries, investors consider dividend payments to be necessary cash outlays similar to capital expenditures.

It's important to monitor free cash flow over multiple periods and compare the figures to companies within the same industry. If free cash flow is positive, it should indicate that the company can meet its obligations, including funding its operating activities and paying dividends.

Comprehensive Free Cash Flow Coverage

Comprehensive free cash flow ratio may be calculated by dividing the free cash flow by net operating cash flow to get a percentage ratio. Again, the higher the percentage, the better.

Credit Control

Credit control, also called credit policy, includes the strategies employed by businesses to accelerate sales of products or services through the extension of credit to potential customers or clients. At its most basic level, businesses prefer to extend credit to those with “good” credit and limit credit to those with “weak” credit, or possibly even a history of delinquency. Credit control

might also be called credit management, depending on the scenario under review.

Understanding Credit Control

A business's success or failure primarily depends on the demand for products or services. As a rule of thumb, higher sales lead to bigger profits, which in turn leads to higher stock prices. Sales, a clear metric in generating business success, in turn, depends on several factors. Some, like the health of the economy, are exogenous, or out of the company's control, other factors are under a company's control. These major controllable factors include sales prices, product quality, advertising, and the firm's control of credit through its credit policy.

In general, credit control seeks to extend credit to a customer to make it easier for them to purchase a good or service. This strategy delays payment for the customer, making the purchase more attractive, or it breaks the purchase price into installments, also making it easier for a customer to justify the purchase, though interest charges will increase the overall cost.

The benefit for the business is increased sales which leads to increased profits. The important aspect of a credit control policy, however, is determining who to extend credit to. Extending credit to individuals with a poor credit history can result in not being paid for the good or service sold. Depending on the business and the amount of bad credit extended, this can adversely impact a business in a serious way. Businesses must determine what kind of credit control policy they are willing and able to implement.

Credit Control Policies

A company can decide on the type of policy it wishes to implement when drafting its credit control policy. The options typically include three levels: restrictive, moderate, and liberal. A restrictive policy is a low-risk strategy, limiting credit only to customers with a strong credit history, a moderate policy is a middle-of-the-road risk strategy that takes on more risk, while a liberal credit control policy is a high-risk strategy where the company extends credit to most customers.

Businesses that aim to gain higher levels of market share or that have high-profit margins are typically comfortable with liberal credit control policies. This also applies to companies that have a monopoly in their industry so that they can hold onto the monopoly. That said, if the monopoly is firmly rooted, the firm may be inclined to adopt a restrictive policy, given the low threat of entrants to the market. A firm in this enviable position does not need to worry much about upsetting its customer base.

Credit Control Factors

Credit policy or credit control primarily focus on the four following factors:

- **Credit period**: Which is the length of time a customer has to pay
- **Cash discounts**: Some businesses offer a percentage reduction of discount from the sales price if the purchaser pays in cash before the end of the discount period. Cash discounts present purchasers an incentive to pay in cash more quickly.

- **Credit standards**: Includes the required financial strength a customer must possess to qualify for credit. Lower credit standards boost sales but also increase bad debts. Many consumer credit applications use a FICO score as a barometer of creditworthiness.
- **Collection policy**: Measures the aggressiveness in attempting to collect slow or late paying accounts. A tougher policy may speed up collections, but could also anger a customer and drive them to take their business to a competitor.

A credit manager or credit committee for certain businesses are usually responsible for administering credit policies. Often accounting, finance, operations, and sales managers come together to balance the above credit controls, in hopes of stimulating business with sales on credit, but without hurting future results with the need for bad debt write-offs.

Financial Projections means the projections of the financial condition of Borrower (together with the assumptions thereto) consisting of the balance sheet, statement of income and loss, and statement of cash flow, for the fiscal year.

Forecasts for average investment earnings beyond the three-year time horizon will be heavily dependent on economic and political developments.

Financial institutions attempt to mitigate the risk of lending to borrowers by performing a credit analysis on individuals and businesses applying for a new credit account or loan. This process is based on a review of five key factors that predict the probability of a borrower defaulting on his debt.

Called the five Cs of credit, they include capacity, capital, conditions, character, and collateral. There is no regulatory standard that requires the use of the five Cs of credit, but the majority of lenders review most of this information prior to allowing a borrower to take on debt.

Lenders measure each of the five Cs of credit differently—some qualitative vs. quantitative, for example—as they do not always lend themselves easily to a numerical calculation. Although each financial institution employs its own variation of the process to determine creditworthiness, most lenders place the greatest amount of weight on a borrower's capacity.

Capacity

Lenders must be sure that the borrower has the ability to repay the loan based on the proposed amount and terms. For business-loan applications, the financial institution reviews the company's past cash flow statements to determine how much income is expected from operations. Individual borrowers provide detailed information about the income they earn as well as the stability of their employment. Capacity is also determined by analyzing the number and amount of debt obligations the borrower currently has outstanding, compared to the amount of income or revenue expected each month.

Most lenders have specific formulas they use to determine whether a borrower's capacity is acceptable. Mortgage companies, for example, use the debt-to-income ratio, which states a borrower's monthly debt as a percentage of his monthly income. A high debt to income ratio is perceived

by lenders as high risk, and it may lead to a decline or altered terms of repayment that cost more over the duration of the loan or credit line.

Capital

Lenders also analyze a borrower's capital level when determining creditworthiness. Capital for a business-loan application consists of personal investment into the firm, retained earnings, and other assets controlled by the business owner. For personal-loan applications, capital consists of savings or investment account balances. Lenders view capital as an additional means to repay the debt obligation should income or revenue be interrupted while the loan is still in repayment.

Banks prefer a borrower with a lot of capital because that means the borrower has some skin in the game. If the borrower's own money is involved, it gives them a sense of ownership and provides an added incentive not to default on the loan. Banks measure capital quantitatively as a percentage of the total investment cost.

Conditions

Conditions refer to the terms of the loan itself, as well as any economic conditions that might affect the borrower. Business lenders review conditions such as the strength or weakness of the overall economy and the purpose of the loan. Financing for working capital, equipment, or expansion are common reasons listed on business loan applications. While this criterion tends to apply more to corporate applicants, individual borrowers are also analyzed for their need for taking on the debt. Common reasons

include home renovations, debt consolidation, or financing major purchases.

This factor is the most subjective of the five Cs of credit and is evaluated mostly qualitatively. However, lenders also use certain quantitative measurements such as the loan's interest rate, principal amount, and repayment length to assess conditions.

Character

Character refers to a borrower's reputation or record vis-à-vis financial matters. The old adage that past behavior is the best predictor of future behavior is one that lenders devoutly subscribe to. Each has its own formula or approach for determining a borrower's character, honesty, and reliability, but this assessment typically includes both qualitative and quantitative methods.

The more subjective ones include analyzing the debtor's educational background and employment history; calling personal or business references; and conducting a personal interview with the borrower. More objective methods include reviewing the applicant's credit history or score, which credit reporting agencies standardize to a common scale.

Although each of these factors plays a role in determining the borrower's character, lenders place more weight on the last two. If a borrower has not managed past debt repayment well or has a previous bankruptcy, their character is deemed less acceptable than a borrower with a clean credit history.

Collateral

Personal assets pledged by a borrower as security for a loan are known as collateral. Business borrowers may use equipment or accounts receivable to secure a loan, while individual debtors often pledge savings, a vehicle, or a home as collateral. Applications for a secured loan are looked upon more favorably than those for an unsecured loan because the lender can collect the asset should the borrower stop making loan payments. Banks measure collateral quantitatively by its value and qualitatively by its perceived ease of liquidation.

Credit Analysis

Credit analysis is a type of financial analysis that an investor or bond portfolio manager performs on companies, governments, municipalities, or any other debt-issuing entities to measure the issuer's ability to meet its debt obligations. Credit analysis seeks to identify the appropriate level of default risk associated with the loan.

How Credit Analysis Works?

To judge a company’s ability to pay its debt, banks, bond investors, and analysts conduct credit analysis on the company. Using financial ratios, cash flow analysis, trend analysis, and financial projections, an analyst can evaluate a firm’s ability to pay its obligations. A review of credit scores and any collateral is also used to calculate the creditworthiness of a business.

Credit Analysis Example

An example of a financial ratio used in credit analysis is the debt service coverage ratio (DSCR). The DSCR is a measure of the level of cash flow available to pay current debt obligations, such as interest, principal, and lease payments. A debt service coverage ratio below 1 indicates a negative cash flow.

For example, a debt service coverage ratio of 0.89 indicates that the company's net operating income is enough to cover only 89% of its annual debt payments. In addition to fundamental factors used in credit analysis, environmental factors such as regulatory climate, competition, taxation, and globalization can also be used in combination with the fundamentals to reflect a borrower's ability to repay its debts relative to other borrowers in its industry.

Special Considerations

Credit analysis is also used to estimate whether the credit rating of a bond issuer is about to change. By identifying companies that are about to experience a change in debt rating, an investor or manager can speculate on that change and possibly make a profit.

For example, assume a manager is considering buying junk bonds in a company. If the manager believes that the company's debt rating is about to improve, which is a signal of relatively lower default risk, then the manager can purchase the bond before the rating change takes place, and then sell the bond after the change in rating at a higher price. On the other side, an

equity investor can buy the stock since the bond rating change might have a positive impact on the stock price.

Term Loan Appraisal :

Terms Loans are granted to finance Capital Expenditure like plant & machinery, land and building or setting up an entire unit. Term Loans have a specific repayment period and are generally repayable in installments.

Cash generating capacity of the unit is the main consideration while appraising Term Loan. The concern of a lending institution is whether, the unit generate sufficient cash flows to serve the Term Loan installment and interest during the repayment period.

Management Evaluation

First step in Term Loan Appraisal is evaluating the Management of prospective borrower. It is to be ascertained that whether promoters have background, experience and knowledge to implement and run the project. Experience and qualifications and expertise of Key persons working in the entity in the functional areas, such as production, purchases, sales, administration, finance etc., should also be evaluated.

Technical Feasibility

It is to be analyzed that how the technical requirements of the project can be met. For example availability of infrastructural facilities, raw materials, labour and other utilities, technology required for the manufacturing process etc. are analysed before the sanction of the loan.

Profitability of the unit to very large extent depends upon productivity of the unit, accordingly, it is to be assessed that if the product mix, quality and quantity are produced as projected and whether the projections are realistic and achievable with given parameters.

Economic Viability

Economic viability of a unit depends upon the sales. Accordingly, sales projections should be analyzed critically and assessed keeping in view:

a) demand and supply of the product and its substitutes

b) proposed selling price per unit (to be compared with prices of competing products)

c) quality of the product (also to be compared with quality of competing products)

Financial Viability Determining Financial viability is a very important step in Term Loan Appraisal, since the repaying capacity of the project depends on financial viability of the project.

1. Financial viability study is done to ascertain that whether cost of project and means of finance as envisaged are realistic, whether the profitability projections are realistic and whether the project is capable of generating sufficient cash for servicing the debt and interest.
2. Estimates of cost of production and other establishment expenses should fully cover all items of expenditure and there should be neither understatement nor over statement of expenditure. Items of cost and

expenditures should be analyzed and it should be ensured that these are reasonable.

3. It should be ascertained that proper arrangements have been made for necessary finance to be available during the period of construction, erection of plant and machinery etc. as and when required.

Financial Viability:

1. Profitability of the project depends upon the sale price, sales volume and cost of production and establishment and sales overheads. Sales price should be compared with the competing products and sales volume can be ascertained based on installed capacity and capacity utilization of the project. It should be seen, if sufficient raw material, labor and other utilities like power, water are available for the projected level of production. Only production is not the criteria for the profitability, rather the product should be sold in order to earn profit, hence there should be adequate marketing arrangements to sell the quantity of products which are manufactured.
2. Items of cost/ expenditure should be analyzed according to the nature of cost, whether fixed, variable or semi variable. Fixed costs are fixed for a given period of time and will be incurred irrespective of level of production, such as rent. Variable costs varies with the production. Semi-variable costs are partly fixed and partly variable.
3. Repayment of Term Loan should be fixed after studying Cash flow statements according to the cash accruals.

4. Basic ratios which are to be considered are debt/Equity ratio, Debt Service Coverage ratio, Tangible Net Worth/ Outside Liabilities ratio, Profit/Sales ratio, Sales/Tangible Assets ratio, Current ratio.
5. While examining the cost of production & profitability, the break-even point of the project should be worked out. BEP indicate the minimum level of output as percentage of full capacity at which the project starts yielding profits.
6. Break-even point is calculated as under:

$$\text{Break-even point} = \frac{\text{Total Fixed Cost}}{\text{P/V ratio}}$$

Technical Appraisal:

Technical Appraisal is the technical review to ascertain that the project is sound with respect to various parameters such as technology, plant capacity, raw material availability, location, manpower availability, etc.

The technical appraisal, or the engineering review, of the project will deal with such questions as:

(a) Are the physical scale and quantity of inputs (materials, labour and plant) appropriate for the development?

(b) Is the quality of materials proposed suitable?

(c) Are the design criteria based on sound planning and engineering principles?

(d) Does the level of service proposed meet the project objectives and affordability levels?

(e) Are the levels of technology to be adopted appropriate?

(f) Do the capital cost estimates meet budget provisions?

(g) Is there adequate access to the site, and are transport facilities satisfactory?

(h) Do the project procurement and project delivery procedures (including the implementation schedule) meet the phasing requirements of the project?

(i) Are the arrangements for stormwater disposal ecologically sound? Has a comprehensive environmental impact statement been prepared?

Social and health impact appraisal

The social and health impact appraisal is concerned with the effects of the project on people, and thus is concerned with such questions as:

(a) Does the project require any houses or other buildings to be demolished? If so, what arrangements have been made for relocation? Are these acceptable to those households to be relocated?

(b) What arrangements have been made for access during construction? Are these acceptable?

(c) Has a detailed health impact statement been prepared? Does it cover malaria, Bancroftian filariasis and schistosomiasis as well as faeco-oral and geohelminthic infections?

(d) Does the project create any new health hazards, including during the construction phase?

(e) What arrangements have been made for selling new plots to the urban poor? Can they afford them?

(f) Do the urban poor need special help to participate in, or benefit from, the project? If so, has it been provided?

(g) What legal safeguards have been incorporated into the project to protect the poor?

Economic and financial appraisal

There are basic differences between financial analysis and economic evaluation. Financial calculations are used as a working appraisal tool throughout the later stages of project preparation to refine design standards and test the financial implications of various implementation policies.

Economic appraisal attempts to reflect the effect of the project on the national economy and so must take a much wider view than financial analysis. The purpose of economic appraisal is to estimate the likely net impact on an investment project, in terms of national welfare. A good project will increase national income, undifferentiated by type of recipient. Income by itself does not create welfare, but leads to the consumption of goods and services and

can serve as a proxy for such welfare-creating consumption. The viewpoint for the economic appraisal is that of a government official or agency concerned about the effect of a project on the overall economy.

The procedure for economic appraisal is complex and requires identification of the origin of the project inputs (labour, materials and plant) and the destination of outputs. An experienced economist is needed to prepare this analysis.

Once a project's inputs and outputs have been classified as traded and nontraded, the procedure is straightforward. The CIF or FOB prices of the traded items are identified, along with the domestic costs of moving the items to the project site or domestic marketplace. Then the domestic market prices of the nontraded items are identified and converted into border-price equivalents. When all inputs and outputs have been expressed in border prices (including the domestic transfer costs), one simply inserts those values into the cashflow in place of the financial values and computes the economic rate of return.

To calculate the economic (internal) rate of return one can employ a trial-and-error method of finding the discount rate that reduces the net present value of the economic time series to zero. Ideally, this rate should equal or exceed the country's opportunity cost of capital.

A financial analysis is also required, and this has three main objectives:

(a) Confirm that an adequate financing plan exists to cover expenses during the investment phase of the project;

(b) To ensure that funds are likely to be available as needed during the operational phase of the project to pay for current operating and maintenance costs and to repay debt;

(c) To verify that sufficient surplus will be generated, under plausible assumptions about the future, to reward equity investors for bearing risk and putting savings into the project rather than elsewhere.

Investors can use a variety of techniques to measure the potential rewards of putting funds into one activity rather than another. The objective is usually the same: to maximize the return flow of income without exceeding some tolerable level of risk. A disciplined appraisal helps to focus on the nature and extent of risk as well as the likely amount of income to be expected.

The investor, be it a government agency or private developer, will have similar objectives, but the decision to proceed or not may be based on different criteria. The government agency may need to meet some social criteria to meet its political objectives. The private sector, unless subsidized by government, will evaluate the project on the basis that the project will show a superior return on investment than other potential investments available at the time.

Project timing and phasing are critical factors in determining the rate of return. The phasing will be affected by the need to meet market demand for the developed land. Development ahead of the market will mean an investment lying idle, so generating holding costs on capital. Development

which is behind the market will be affected by competition from other developments.

Several techniques are used in testing the financial viability of a project. It is necessary, when comparing alternative scenarios, to establish the cash flow over the life of the project and to "discount" expenditure planned for the future to its present-day value. This discounted cash flow is dependent on the selection of a "discount rate". Again the private-sector investor will need to adopt a different discount rate from the government investor because of their costs and their opportunities for alternative investment.

From most agencies' viewpoint, an after-tax financial return to equity does not convey enough information. Analysts need to look into a project's fundamental strengths, without regard to specific financing considerations. They do not want to be misled by financial "gearing" and peculiar borrowing arrangements. For these reasons, the project's financial rate of return on all these resources, donated or borrowed, but before taxation, has to be determined.

Sensitivity testing.

Testing variables and assumptions to determine their relative influence on the financial and economic rates of return should be done. The objective is to discover the impact on the internal rates of return by changes in the assumptions. Items that are normally significant include the cost of investment and the unit prices of major current cost components (for example, the purchase price of land and the sale prices of developed lots).

Thus the question is asked, "What happens to the financial/economic rate of return if the sale price of the land is reduced by, say, 10 per cent?" Similar questions relating to increases in the cost of goods and the delay in completion of the project, and therefore the delay in the revenue stream, need to be answered. Generally, the greater relative importance of an item within the overall cash flow, the earlier it occurs in time and the more likely it will be to have an adverse impact on the internal rate of return.

It is also advisable to run the sensitivity analyses for simultaneous adjustment of several variables. The objective is to highlight the strengths and weaknesses of the project as an investment. It then may be possible to identify the potentially damaging factors and to apply appropriate measures to minimize their effects.

D. Institutional appraisal

The institutional appraisal considers topics such as:

(a) Land acquisition procedures and availability;

(b) Project ownership - public, private or mixed?

(c) Target population to be served;

(d) Community consultation;

(e) Operations and maintenance (O&M) of the project assets on completion;

(f) Executing agency capacity and capability and project implementation management;

(g) Levels of staffing for planning, implementation and operations and the scope and extent of the skills required for these functions;

(h) Staff training for on-going management (including O&M).

UNIT-III

Evaluating consumer loans and loans and advances against pledge:

Types of consumer loans – Credit analysis of consumer loans – Risk – return analysis of consumer loans – customer profitability analysis and loan pricing – Fixed Vs Floating rates – Hypothecation – Mortgage – Lien – Advances against goods – Document to title to goods – Life Insurance Policies _ Stock Exchange Securities – Fixed deposit receipts – Book debts – Supply bills – Real estates – Advance against collateral securities – Corporate Finance – Project Finance

UNIT-III

Evaluating consumer loans and loans and advances against pledge

What is a Consumer Loan?

A consumer loan is a loan given to consumers to finance specific types of expenditures. In other words, a consumer loan is any type of loan made to a consumer by a creditor. The loan can be secured (backed by the assets of the borrower) or unsecured (not backed by the assets of the borrower).

Types of Consumer Loans

- Mortgages: to finance the purchase of a house
- Credit cards: to finance everyday purchases
- Auto loans: to finance the purchase of a vehicle
- Student loans: to finance education
- Personal loans: for personal purposes
- Refinance loans: to refinance an existing loan
- Credit Card: to buy daily requirements

1. Mortgages

A mortgage is a secured loan given by a bank to a consumer for buying a house, which usually costs much more than what an average person earns in a year. This type of loan is stretched over a longer period of time to ease

out monthly installments, the most common mortgage being a 30-year fixed-rate loan.

2. Auto Loan

An auto loan is either extended by a bank or the car dealer itself to finance the purchase of a vehicle. The term of a typical auto loan ranges from 2 years to 7 years. The tenure is shorter, and the down payment is larger for an auto loan due to the rapid car value depreciation. It is typically secured in nature.

3. Education Loan

The objective of an education loan is to fulfill the education needs of a student by paying the college/tuition fees. In this way, students are able to pursue their life goals through proper education. This is an unsecured type of loan, and the repayment only starts few months after the student's graduation from college.

4. Personal Loan

A personal loan caters to various day-to-day needs of the borrower. It is the most versatile type of loan in the consumer loan market due to its wide range of end-use purposes, including debt consolidation, vacations, etc. This type of loan usually has a long tenure and can be either secured or unsecured in nature.

5. Refinance Loan

As the name suggests, this type of loan is used to refinance an existing loan. In fact, a refinance loan can be used to refinance any of the abovementioned loans. Typically, it has a fixed payment with a lower interest rate, which primarily attracts consumers.

6. Credit Card

It is the most commonly used and popular among the various types of consumer loans. A borrower usually uses it to buy daily need items, such as groceries, apparel, etc., on credit. The rate of interest charged on this type of loan is a bit on the higher side, and thus failure to pay on time can attract a very high penalty.

For qualified borrowers, consumer loans serve a multitude purposes and are essential for the consumers.

Secured vs. Unsecured Consumer Loans

Secured consumer loans are loans that are backed by collateral (assets that are used to cover the loan in the event that the borrower defaults). Secured loans generally grant the borrower greater amounts of financing, a longer repayment period, and a lower charged interest rate. As the loan is backed by assets, the risk faced by the lender is reduced. For example, in the event that the borrower defaults, the lender would be able to take possession of collateralized assets and liquidate them to repay the outstanding amount.

Unsecured consumer loans are loans that are not backed by collateral. Unsecured loans generally grant the borrower a limited amount of financing, a shorter repayment period, and a higher charged interest rate. As the loan is not backed by assets, the lender faces increased risk. For example, in the case of borrower default, the lender may not be able to recover the outstanding loan amount.

Categories of Loans

1. Open-end loan

An open-end consumer loan, also known as revolving credit, is a loan in that the borrower can use for any type of purchases but must pay back a minimum amount of the loan, plus interest, before a specified date. Open-end loans are generally unsecured. If a consumer is unable to pay off the loan in full before the specified date, interest is charged.

A credit card is an example of an open-end consumer loan. The consumer is able to make purchases on a credit card but must pay the outstanding amount when it becomes due. If the consumer fails to settle the outstanding amount on the credit card, he/she would be charged interest until the amount is paid off.

2. Closed-end loan

A closed-end consumer loan, also known as installment credit, is used to finance specific purchases. In closed-end loans, the consumer makes equal monthly payments over a period of time. Such loans are generally secured.

If a consumer is unable to pay the installment amounts, the lender can seize the assets that were used as collateral.

What is Credit Risk Analysis?

Credit risk analysis extends beyond credit analysis and is the process that achieves a lender's goals by weighing the costs and benefits of taking on credit risk.

By balancing the costs and benefits of granting credit, lenders measure, and analyze the risks their business is willing to accept.

The creditworthiness of the borrower, derived from the credit analysis process, is not the only risk lenders face. When granting credit, lenders also consider potential losses from non-performance, such as missed payments and potential bad debt. With such risks come costs, so lenders weigh them against anticipated benefits such as risk-adjusted return on capital (RAROC).

Purpose of Credit Risk Analysis

Credit risk analysis aims to take on an acceptable level of risk to advance the lenders' goals. Goals include profitability, business growth, and qualitative factors.

Although credit analysis can rate risks and estimate the probability of default, default risk is only one entity-specific risk factor. Lenders consider costs and benefits holistically when determining if the anticipated outcomes are acceptable to their business and the financial exposure.

To estimate the cost of risk, lenders employ a multitude of information from the borrower, the lender, and external parties such as credit agencies. Some measures, such as credit scores and credit risk analysis models, are tools that allow lenders to estimate their expected loss (EL) via the probability of default (PD), loss-given default (LGD), and exposure at default (EAD).

The direct benefit of taking on credit risk is interest, a combination of default risk premium, liquidity premium, and other factors; however, benefits extend beyond interest revenue. For example, lenders may take on additional credit risk to grow a credit portfolio (their asset base), gain market share and expand relationships, or ensure their portfolio achieves an acceptable risk-adjusted return on capital.

Individual outcomes of credit risk analysis include granting credit with specific credit conditions or even approving exceptional credit to borrowers who may not qualify within standard policies. Management's goal is to mitigate the portfolio credit risks sufficiently to optimize the firm's accepted risks in aggregate.

For example, credit risk analysis can determine that lending in the absence of financial risk (e.g., cash-secured lending) is still not acceptable, perhaps due to headline risk specific to the borrower's owner or the industry that the company operates in.

Conversely, credit risk analysis may support lending to a newer business model (i.e., without proven cash flow) as a business strategy to expand relationships and increase exposure to a growing segment.

Credit problems and risk management

Credit risk management is a key issue that lenders of all forms must address. BIS has identified three key areas: concentration, credit processes, and market and liquidity-sensitive exposures.

- Concentration reflects not the largest borrowers but exposures where the expected loss can sizably deplete the capital. For example, in trade credit, if a lender offers the same terms (amount, repayment, etc.) to a business with no track record and a publicly traded company, the credit concentration is considered more significant with the former compared to the latter. If this exposure has an expected loss that will deplete the lender's capital to an unacceptable level, that risk must be adjusted accordingly.
- Credit processes encompass lenders' steps to assess, measure, and conduct credit risk analyses. Errors in the process lead to credit problems for the lender, for example:
    - Leveraging value-at-risk (VaR) models with unvalidated tail risks and loss.
    - Decisions that are not easily replicable, resulting in inconsistent results and unmanaged portfolio risk.
    - Poor monitoring and control of collateral and fraud, leaving any losses higher than expected.
    - Consistent mispricing and assessment of non-financial collateral in light of market conditions or business cycles, resulting in poor risk-adjusted return and higher than planned concentration risk.

- Market and liquidity-sensitive exposures include foreign exchange risks, financial derivatives, and contingent liabilities. There is a difference between willingness and ability to pay, particularly for illiquid collateral or volatility, causing an outsized increase in exposure compared to the collateral value. If the borrower cannot access sufficient liquidity, the risk to the lender will rise regardless of willingness to repay. Stress testing is one way to structure and manage credit risk.

What is Customer Profitability Analysis?

- Customer Profitability Analysis is a tool from managerial accounting that shifts the focus from product line profitability to individual customer profitability. Activity Based Costing looks at the various cost drivers to accurately isolate costs and determine a product's profitability.
- In contrast, Customer Profitability Analysis is a method of looking at the various activities and expenses incurred in servicing a particular customer. In other words, it focuses on analyzing profit per customer rather Calculating Customer Profitability
- Calculating customer profitability begins by identifying the various costs incurred specifically in relation to servicing a specific customer or segment of customers.
- For example, a solar panel company serves two types of customers: Individuals and Small Medium Enterprises (SMEs). For the attainment, servicing, and retention of its customers, the company is required to provide consulting and service visits, as well as process sale orders. Individuals require only one site visit before placing an order.

- SMEs require more frequent visits, as they are based in multiple locations and are provided with after-sale service as part of the bulk purchase.

Benefits of Customer Profitability Analysis

These insights might not be attainable from traditional reporting methods. In a company's income statement, there is no granularity provided in the calculation of its Selling, General, and Administrative Expense line.

One of the most common marketing metrics of sales per segment may also be misleading. If the company reported 120 customers in the Individual segment and 80 customers in the SME segment, managers might believe that SMEs contribute to two-thirds of their annual sales.

Criticism of Customer Profitability Analysis

The biggest criticism regarding Customer Profitability Analysis is the selection of a limited time frame and segmentation criteria. However, with the emergence of Big Data, customer profitability can be calculated using new methods that determine a customer's lifetime value rather than just the sales within a restricted time frame.

Additionally, with respect to segmentation, predictive analytics will be able to estimate the value of individual customers by identifying drivers in behavioral patterns rather than just the value of the average customer in its respective segment.

LOAN PRICING

Loan pricing is the process of determining the interest rate for granting a loan, typically as an interest spread (margin) over the base rate , conducted by the bookrunners. The pricing of syndicated loans requires arrangers to evaluate the credit risk inherent in the loans and to gauge lender appetite for that risk.

Benefits of Loan Pricing

This methodical approach can help ensure the best loan and terms are matched to the borrower so that the financial institution makes the sale and keeps the customer. Loan pricing models or loan profitability models can allow banks or credit unions to set prices based on other institution goals, too, including goals related to profitability targets or loan portfolio composition.

One overall benefit of effective loan pricing is that it is one of the many ways a financial institution can optimize capital. Optimizing capital is important because it provides institutions with the ability and freedom to deploy capital for developing new products and new markets, addressing regulatory issues or navigating shifts in the macroeconomic environment.

Another benefit of having a loan-pricing policy or model is that it provides the institution with defensible measures for justifying pricing changes and for avoiding charges of discriminatory pricing, which some lenders have faced in recent years. Officials with the banking regulatory agencies have outlined best practices they encourage as they relate to evaluating an institution’s fair

lending risk, and one of those best practices was to document pricing and other underwriting criteria, including exceptions.

Considerations of Loan-Pricing Models

Pricing is a key underwriting factor that should be addressed as part of a sound loan policy. A simple cost-plus loan pricing model is one method of pricing loans. A cost-plus pricing model requires that all related costs associated with extending the credit be known before setting the interest rate and fees, and it typically considers the following:

Cost of funds: Operating costs associated with servicing the loan or loans Risk premium for default risk and a reasonable profit margin on capital.

The risk premium for default risk takes into account the borrower's risk rating as well as the risk rating of the credit facility.

FIXED RATE

BENEFITS

Interest Rate remains fixed irrespective of Market Conditions.

A fixed rate home loan is good for those who want a fixed monthly repayment schedule

It brings a sense of Certainty and Security.

DRAWBACKS:

Usually 1 - 2.5% more than the floating rate home loan.

FIXED RATE Vs FLOATING RATE OF INTEREST

What is Fixed Rate of Interest

Fixed Interest Rate means repayment of home loans in Fixed Equal Instalments over the entire period of loan.

What is Floating Rate of Interest

Floating rate varies with the market conditions. Floating interest rate home loans are tied up to a base rate plus a floating element.

FLOATING RATE

BENEFITS

At least 1-2% cheaper than fixed interest rates.

Over a long period, interest rates may fall.

Floating interest rates bring savings.

DRAWBACKS:

Uneven nature of monthly instalments make financial planning difficult.

What Is Hypothecation?

Hypothecation occurs when an asset is pledged as collateral to secure a loan. The owner of the asset does not give up title, possession, or ownership rights, such as income generated by the asset. However, the lender can seize the asset if the terms of the agreement are not met. Hypothecation is different from a mortgage, lien, or assignment.

Hypothecation in Mortgages

Hypothecation occurs most commonly in mortgage lending. A mortgage is a type of loan that's secured by an underlying property. The borrower technically owns the house, but because the house is pledged as collateral, the mortgage lender has the right to seize the house if the borrower cannot meet the repayment terms of the loan agreement—which occurred during the foreclosure crisis.

Auto loans are similarly secured by the underlying vehicle. Unsecured loans, on the other hand, do not work with hypothecation because there is no collateral to claim in the event of default. As hypothecation provides security to the lender because of the collateral pledged by the borrower, it is easier to secure a loan, and the lender may offer a lower interest rate than on an unsecured loan.

Hypothecation in Investing

Margin lending in brokerage accounts is another common form of hypothecation. When an investor trades on margin, they're borrowing money from the brokerage to do so. This can allow them to leverage their existing account balances to make larger investments and potentially net larger profits on the sale of securities.

This type of hypothecation can be risky, however. When an investor chooses to buy on margin or sell short, they are agreeing that those securities can be sold if necessary if there is a margin call. The investor owns the securities in their account, but the broker can sell them if they issue a margin call that the investor cannot meet to cover the investor's losses.

This can be costly for the investor because it can amplify losses well beyond the initial investment made. For that reason, it's important to understand how margin trading works and what hypothecation could mean on a personal level.

Hypothecation in Commercial Real Estate

Hypothecation in commercial real estate is the same as it is in residential real estate lending. The borrower posts collateral in order to secure a loan. An investor who borrow to purchase a rental property, such as an apartment building or duplex, would use the property itself as collateral for the loan.

Construction loans in commercial real estate work a little differently. Because the property that would otherwise serve as collateral has yet to be built, the borrower would need to provide other property as substitute collateral. The same rule, however, would apply with regard to default. If the borrower fails to pay the loan, the lender could claim ownership of the collateral.

What Is Rehypothecation?

When banks and brokers use hypothecated collateral as collateral to back their own transactions and trades with their client's agreement, in order to secure a lower cost of borrowing or a rebate on fees, this is called rehypothecation. For example, the lender may use an apartment building

offered as collateral for a commercial real estate loan as collateral for a new loan. This newly created debt is now a derivative.

Rehypothecation is regulated by the Securities and Exchange Commission. Banks and lenders must have permission from the owner of the property or assets to do this.

Distinction between Hypothecation and Mortgage

Hypothecation is the pledging of an asset as collateral for a loan, without transferring the property's title to the lender. In a mortgage, the property purchased is used to secure the loan, but the lender holds the title.

Assignment vs Hypothecation

Assignment is an arrangement involving contracts, in which one party assigns rights and responsibilities outlined in a contract to another party. Hypothecation allows a borrower to hold onto a property while using it as security for a loan.

Hypothecation vs. Lien

With hypothecation, the borrower is allowed to hold the property used as collateral for the loan. The borrower agrees to repay the loan on the condition that if they don't, the lender can claim the property. A lien, however, requires a property owner to satisfy outstanding debts before an underlying property can be refinanced or sold.

Loan Against Pledge of Goods

Advances against goods are allowed to traders for their trading activities, to manufacturers and producers for their requirements of raw materials etc., and also to enable them to sell their products at better prices. The account is to facilitate the borrower to hold on to the goods for a short period, by creating a pledge in favour of the Bank. This is a type of account where the credit for a specified period of time, generally for one year and release of goods are allowed any number of times during the currency of the limit, within the limit/Drawing power. This limit cannot be allowed to be operated by the borrower by issuance of cheques or by deposit of cash and other instruments for collection.

Advances against goods are allowed on the basis of pledge or hypothecation of goods depending upon the credit worthiness and the requirements of the borrower, keeping in mind that the security by way of pledge, where possible and practical is always preferable to hypothecation.

Advances should not be made against goods which are not the sole property of the borrower or where the borrowers right to sell is restricted.

Pledge of goods means bailment of goods as security for payment of debt or performance of a promise. This is a voluntary transfer of possession of goods. Delivery may be either physical or constructive. Pledge is created when the actual possession of goods is transferred to the Bank as security or by any other means by which delivery is affected, as in the case of endorsement and delivery of a document of title to the goods.

Document to title of goods:

Document of title to goods means any bill of lading, dock warrant, warehouse keeper's certificate, and warrant or order for the delivery of goods, and any other document used in the ordinary course of business as proof of the possession or control of goods, or authorizing or purporting to authorize, either by endorsement or by delivery, the possessor of the document to transfer or receive goods thereby represented. Document of title means a record that in the regular course of business or financing is treated as adequately evidencing that the person in possession or control of the record is entitled to receive, control, hold, and dispose of the record and the goods the record covers and that purports to be issued by or addressed to a bailee and to cover goods in the bailee's possession which are either identified or are fungible portions of an identified mass. The term includes a bill of lading, transport document, dock warrant, dock receipt, warehouse receipt, and order for delivery of goods. "Electronic document of title" means a document of title evidenced by a record consisting of information stored in an electronic medium. "Tangible document of title" means a document of title evidenced by a record consisting of information that is inscribed on a tangible medium.

Life Insurance Policy:

Life insurance is a contract wherein an individual is offered financial coverage by an insurance company in exchange for a payment over a period. The payment made to the insurer is referred to as the premium. In case the policyholder passes away during the policy tenure, the insurance

company will offer a lump sum amount to his/her nominee. This lump sum amount is called the sum assured on death or the death benefit. Upon completion of the policy term, the policyholder receives a sum assured on maturity or the maturity benefit from the insurer along with some bonuses.

A pure protection plan, such as a term insurance policy, offers only the death benefit. However, there are several types of life insurance policies that offer savings in addition to protection. The savings can be in the form of a maturity benefit or bonus. Premiums paid and benefits received under life insurance are liable to tax benefits under Section 80C and Section 10(10D) of the Income Tax Act, 1961.

Top Life Insurance Companies in India:

When it comes to life insurance, the standard idea of the product is that if you pass away, an insurance company will pay your family a large sum of money. But that is not the only benefit that a life insurance product has to offer. A life insurance policy can also be used to plan for upcoming and unforeseen expenses through schemes like ULIPs (Unit Linked Insurance Plans) that provide returns through investment in the markets.

Below are some of the popular life insurance companies in India:

Life Insurance Corporation of India

Life Insurance Corporation of India or LIC is one of the oldest state-owned insurance companies in India. The corporation made its IPO public on 4 May 2022. The claim settlement ratio of LIC in 2022 is 98.62%.

SBI Life Insurance

SBI Life Insurance is responsible for providing life insurance policies to more than a million Indians in today's date.

The company was established as a public limited company in Mumbai on 11 October 2000. On November 20, 2000, the RoC issued the company a Certificate of Commencement of Business. On 29 March 2001, the company registered with the IRDAI to conduct the business of life insurance.

The headquarters for SBI Life Insurance is situated in Mumbai.

SBI life insurance has a minimum entry of age of 18 years to take a life insurance. The insurer achieved a claim settlement ratio of 93.09%.

HDFC Standard Life Insurance

HDFC Standard Life Insurance is a highly reputed private insurance company operating in India today. The insurance corporation is considered one of the most reliable life insurance companies in India. The company produced effective returns on operating Earning Value (EV) of 20% for the previous three fiscal years. The claim settlement ratio of HDFC Standard Life Insurance is 98.66% for 2021-22.

Max Life Insurance

Max Life Insurance is a renowned general insurance company currently offering policies to millions of Indians. The channels of distribution for Max Life include, among others, banks, private agents, brokers, and corporate agents. It offers things that are linked, participating, and not participating. It provides both people and groups with child protection, retirement, savings,

and growth plans. The minimum age of entry for Max life insurance is 18 years. In 2021-22, this insurance company's claim settlement ratio stands at 99.34%.

Bajaj Allianz Life Insurance

Bajaj Allianz is a highly reputed and renowned insurance company that offers the best deals on policies. The insurance company provides insurance ranging from car insurance, life insurance, health insurance, etc. To their customer base. Bajaj Allianz life insurance has a minimum age of entry of 18 years. The claim settlement ratio of this insurer is 98.48% for the fiscal year 2021-22.

Kotak Mahindra Life Insurance

Kotak Mahindra is one of the best insurance companies currently operating in India with millions of customers. The products offered by Kotak Life Insurance include rural plans, term plans, savings plans, children's plans, retirement plans, and investment plans at low premium rates. These products are affordable to individual investors and can meet their lifetime needs.

Each insurance plan is created to offer the maximum protection possible in addition to benefits and keeping in mind the needs of the various segments of society. For Kotak Mahindra life insurance plan, the minimum age of entry is 18 years. According to the IRDAI annual report, this insurer provider has a claim settlement ratio of 98.50%.

Reliance Nippon Life Insurance

Reliance Nippon Life Insurance is one of the most reputed life insurers currently functioning in India. The company caters to four different segments: protection, children, retirement, and investment programs. It offers life insurance policies that are aimed at both individuals and organisations. For many years, the company has been ranked as one of the top five private insurance companies in the country. The minimum age of entry to take a policy with Reliance Nippon life insurance is 18 years of age. It has a claim settlement ratio of 98.7% for the financial year 2021-22.

PNB MetLife Insurance

PNB MetLife is a highly reputed insurance company currently providing life insurance policies to more than a million Indians in today's date. Through its bank agreements with PNB, Jammu & Kashmir Bank Limited (JKB), and Karnataka Bank Limited, PNB MetLife today operates more than 150 branches around the nation and services clients in more than 7,000 locations. The minimum age of entry for this scheme is 18 years. As per the IRDAI annual report, PNB MetLife holds a claim settlement ratio of 97.33% in 2021-22.

Edelweiss Tokio Life Total Protect Plus

Edelweiss Tokio Life Insurance is a reputed insurance company with a claim settlement ratio of 98.09%. As on April 2022, the insurer has a widespread network of 109 branches, 63,693 agents, and 4,000 points of contact across the country. The Great Place to Work Institute named Edelweiss Tokio Life Insurance one of the Best Workplaces in Life Insurance India in 2022. The

insurance company offers a broad range of online plans, term plans, investment plans, etc.

ICICI Prudential Life Insurance Company Limited

ICICI Prudential Life is a leading life insurance company that started operating in the financial year 2001. It is the first Indian insurance company that was listed on the Bombay Stock Exchange (BSE) and National Stock Exchange (NSE). ICICI Prudential Life offers a host of insurance products such as term insurance plans, ULIPs, child plans, retirement plans, etc.

The insurer has been honoured with various awards and accolades including the Best Contact Centre at The Customer Fest Leadership Awards 2022 and Technology Champion of the Year – Life Insurance at the Quantic 3rd Annual BFSI Technology Excellence Awards 2022. The claim settlement ratio of ICICI Prudential Life for 2021-22 is 97.8%.

Stock Exchange

Stock Exchange market is a vital component of a stock market. It facilitates the transaction between traders of financial instruments and targeted buyers. A stock exchange in India adheres to a set of rules and regulations directed by Securities and Exchange Board of India or SEBI. The said authoritative body functions to protect the interest of investors and aims to promote the stock market of India.

The stock exchange in India serves as a market where financial instruments like stocks, bonds and commodities are traded. It is a platform where buyers and sellers come together to trade financial tools during

specific hours of any business day while adhering to SEBI's well-defined guidelines. However, only those companies who are listed in a stock exchange are allowed to trade in it.

Stocks which are not listed on a reputed stock exchange can still be traded in an 'Over the Counter Market'. But such shares would not be held high in esteem in the stock exchange market.

How does it work?

Mostly, a stock exchange in India works independently as no 'market makers' or 'specialists' are present in them. The entire process of trading in stock exchange in India is order-driven and is conducted over an electronic limit order book.

In such a set-up, orders are automatically matched with the help of the trading computer. It functions to match investors' market orders with the most suitable limit orders.

The major benefit of such an order-driven market is that it facilitates transparency in transactions by displaying all market orders publicly.

Brokers play a vital role in the trading system of the stock exchange market, as all orders are placed through them.

Both institutional investors and retail customers can avail the benefits associated with direct market access or DMA. By using the trading terminals provided by stock exchange market brokers, investors can place their orders directly into the trading system.

Benefits of listing with Stock Exchange

Listing with a stock exchange extends special privileges to company securities. For instance, only listed company shares are quoted on a stock exchange.

Being listed on a reputed stock exchange is deemed beneficial for companies, investors and the public in general and they tend to benefit in these following ways –

- Increased Value

Only stocks listed with a reputable stock exchange are considered to be higher in value. Companies can cash in on their market reputation in the stock exchange market by increasing their number of shareholders. Issuing shares in the market for shareholders to acquire is a potent way of increasing shareholder base and base, which in turn increases their credibility.

- Accessing capital

One of the most effective ways of availing cheap capital for a company is by issuing company shares in the stock exchange market for shareholders to acquire. Listed companies can generate comparatively more capital through share issuance owing to their repute in a stock exchange market and use it to keep their company afloat and its operations running.

- Collateral value

Almost all lenders accept listed securities as collateral and extend credit facilities against them. A listed company is more likely to avail a faster approval for their credit request; as they are deemed more credible in the stock exchange market.

- Liquidity

Listing helps shareholder avail the advantage of liquidity better than other counterparts and offers them ready marketability. It allows shareholders to estimate the value of investment owned by them.

Additionally, it permits share transactions with a company and helps them to even out the associated risks. It also helps shareholders to improve their earnings from even the slightest increase in overall organisational value.

- Fair price

The quoted price also tends to represent the real value of a particular security in a stock exchange in India.

The fact that the prices of listed securities are set as per the forces of demand and supply and are disclosed publicly, investors are assured to acquire them at a fair price.

Investment Methods

Investors can invest in a stock exchange of India through these two ways –

1. Primary market – This market creates securities and acts as a platform where firms float their new stock options and bonds for the general public to acquire. It is where companies enlist their shares for the first time.
2. Secondary market – The secondary market is also known as the stock market; it acts as a trading platform for investors. Here, investors trade in securities without involving the companies who issued them in the first place with the help of brokers. This market is further broken down into – auction market and dealer market.

Major stock exchanges in India

There are two major types of Stock Exchanges in India, namely the –

Bombay Stock Exchange (BSE): This particular stock exchange was established in 1875 in Mumbai at Dalal Street. It renowned as the oldest stock exchange not just in Asia and is the 'World's 10th largest Stock Exchange'.

National Stock Exchange (NSE): The NSE was established in 1992 in Mumbai and is accredited as the pioneer among the demutualized electronic stock exchange markets in India. This stock exchange market was established with the objective to eliminate the monopolistic impact of the Bombay Stock exchange in the Indian stock market.

Here is a **list of stock exchanges in India**

The Bombay Stock Exchange Ltd

India International Exchange or India INX

Metropolitan Stock Exchange of India Ltd (valid up to September 15th, 2019)

National Stock Exchange of India Ltd.

NSE IFSC Ltd.

Being a vital part of the Indian stock market, a stock exchange in India tends to influence the country's financial sector to a great extent. Their collective performances happen to be a deciding factor of economic growth.

Also, all major types of stock exchanges are closely integrated with each other; if one major stock exchange falls, it will have a ripple effect on all other major exchanges across the globe.

For example, if the index of Bombay Stock Exchange falls, its effect will be felt across stock exchanges like New York Stock Exchange, Tokyo Stock Exchange, Shanghai Stock Exchange, etc. as well.

Fixed Deposit Receipt (FDR)

Fixed Deposit Receipt (FDR) can be asked by the bank on various occasions like:

At the time of renewal – In the case of an offline FD, the depositor may be asked by the bank to surrender the FDR so that the existing FD can be renewed for a new tenure and a new receipt be issued.

For premature withdrawal – In case the depositor wishes to withdraw funds before the maturity date, they will be required to produce FDR as the proof of ownership.

To get a loan against FD – To address a cash crunch, depositors can apply for a loan against their fixed deposit at lower interest rates than an unsecured loan. To do so, they are required to deposit the FDR as alien to the bank for the term of the loan. Once the loan is repaid, FDR is returned to the depositor with the updated details.

Factors to Check in a Fixed Deposit Receipt

Fixed Deposits, also known as term deposits in banking parlance, work on some factors which should be checked to understand the terms at which one's FD will perform. These factors are:

1. Applicable Rate of Interest and Deposit Term: These are the basic things to look for in an FD receipt and it is always better to double-check the details i.e. the applicable rate of interest and the maturity term of the scheme, especially at the time of renewal of an old fixed deposit.

It is because the rate of interest is subject to change from time to time without any prior notice and it may be possible that the previous interest rate is different than the one offered at the time of renewal.

2. Maturity and Auto-Renewal Dates: The maturity date of the scheme is always mentioned on the deposit receipt. To address certain goals like aiding for higher education, it is extremely important to check the date of maturity so that the amount can be accessed at the right time.

Otherwise, one may have to opt for premature withdrawal and lose some interest.

Moreover, if the depositor has opted for the auto-renewal facility, they must not forget to check the time of auto-renewal on the Fixed Deposit Receipt date.

Penalties and Charges: Some banks charge a certain amount as a penalty if the deposit is withdrawn by the depositor before the maturity of the FD or a specified time period. If there is any sort of penalty on the same, it should be on the receipt.

The charges for premature withdrawal may differ from one bank or company to another and must always be squared to avoid any confusion later.

3. Nomination Details: The nominee is the person who will get the FD amount (principal + interest earned) in case something unfortunate happens to the depositor. Therefore, it is important to check this particular detail to ensure the right name is mentioned in it.

BOOK DEBTS:

A book debt is a sum of money due to a business in the ordinary course of its business. It has been described as a debt that would normally be entered in the books of the business regardless of whether or not it is in fact entered. Book debts include sums owed to a business

for goods or services supplied or work carried out. Sums due under loans may also be treated as book debts.

Book Debts means all book and other debts, revenues and claims both present and future (including things in action) which may give rise to a debt, revenue or claim due or owing or which may become due or owing to the Assignor under, or by virtue of, the Assigned Agreements or in connection with the rights of the Assignor evidenced by them and the present and future rights, titles, benefits and interests of the Assignor to, or in, them together with all rights and remedies relating to, or for enforcing, the Assigned Agreements including but not limited to all reservation of proprietary rights, rights of tracing and all other rights and remedies of whatsoever nature now or hereafter held by the Assignor in respect of all or any of the foregoing and all moneys from time to time becoming due or owing thereunder or in connection therewith.

Book Debts means all present and future book and other debts and monetary claims due or owing to the Company and any proceeds of such debts and claims including any claims or sums of money deriving from or in relation to any Intellectual Property, any Investment, the proceeds of any Insurance Policy, any court order or judgment, any contract or agreement to which the Company is a party and any other assets, property, rights or undertaking of the Company.

SUPPLY BILLS:

A business registered under GST issues a tax invoice to the buyer. Such an invoice mentions the GST rate charged on the goods and services sold. However, some businesses registered under GST cannot charge any tax on the invoice issued by them. Such dealers have to issue a Bill of Supply. A Bill of Supply is issued when GST is not applicable on a transaction or when GST is not to be recovered from the customers.

Composition Dealer

A taxpayer whose turnover is less than Rs 1.5 crores* (Rs. 75 lakhs for north-east states and Uttarakhand) can opt for composition scheme. A dealer opting for composition scheme has to deposit tax on their receipts themselves, they are not allowed to collect any tax from their buyers. The GST has to be paid out of pocket by the composition dealer. They cannot charge GST in the invoice. Thus a composition dealer has to raise a Bill of Supply instead of a Tax Invoice. The composition dealer has to mention the words 'composition taxable person not eligible to collect taxes on supplies' on the Bill of Supply.

*CBIC has notified the increase to the threshold limit to Rs. 1.5 crores.

The notification comes into effect from 1st April 2019.

Exporters

An exporter is also not required to charge GST on their invoice. This is because exports supplies are zero-rated. Hence a taxpayer exporting goods can issue a Bill of Supply in place of a tax invoice. The dealer has to mention the following in their Bill of Supply- "Supply

Meant for Export on Payment of IGST" "Supply Meant for Export Under Bond or Letter of Undertaking Without Payment of IGST"

Exempted Goods Supplier

When a registered dealer supplies exempt goods or services they are required to issue a Bill of Supply. For example, when a registered taxpayer provides unprocessed agricultural products they have to issue a Bill of Supply instead of a tax invoice.

Contents of Bill of Supply

The GST law has specified certain particulars that should be present in a Bill of Supply. These are the details a Bill of Supply should have:

1. Name, address, and GSTIN of the supplier
2. Bill of Supply number (it must not exceed 16 characters, be generated consecutively and each Bill of Supply will have a unique number for that financial year)
3. Date of issue
4. If the recipient is registered then the name, address, and GSTIN of the recipient
5. HSN Code of goods or Accounting Code for services. The number of digits that are required to be mentioned is based on turnover in the preceding financial year.

Loan Against Securities

Loan against security is a loan advance to a customer against a pledge of security. It can be loan against insurance policy, mutual funds, National Savings Certificate and other securities.

Loan against security can be given against the following securities:

- Insurance policies
- Non-convertible debentures
- NABARD Bonds
- UTI Bonds
- Mutual fund units
- Demat shares
- National Savings Certificate or KVP, these are accepted in demat form only.

How Loan against Securities works?

Loan against security helps to avail timely finance instead of selling off the securities in a haste. The limit of the financial assistance depends on the security that was pledged. Usually a current account is opened in the borrower's name and the rate of interest is calculated on the amount that is withdrawn during the period of utilisation.

When a security is pledged, there is steady cash at the time of need it the most and which means that shares need not be sold and also not to forego the benefit of the bonus and dividends.

Features of Loan against Securities

- Loan against security is a secured Loan. Debentures, shares, bonds or mutual funds are offered as collateral.
- The tenure of the loan against security is one year, but it can be easily renewed.
- The rate of interest usually ranges from 12 – 15%. The rate varies from bank to bank.
- The processing fee is usually charged at the rate of 2% of the loan amount.
- The loan amount depends on the security the borrower is offering.
- There is no charges for prepayment of the loan.
- The borrower is required to be within the age bracket of 18 – 65 years to apply for a loan against security.
- The loan has to be repaid within the fixed period. If the borrower fails to make the payment, the lender can file a case for recovery and the balance amount has to be repaid within 3 years from the date of sanction of the loan.

Features of a good security is:

- The loan is not dependent on the creditworthiness of the borrower but is dependent on the security that he has submitted. The security offered is marketable and doesn't incur loss. Preference is given to liquid assets like raw materials, manufactured goods, gold, silver, etc.
- The value of the security should be stable and steady and not fluctuate widely.

- The security must be easily transferable. Immovable property is not easily transferable.
- The security must be easily marketable.
- The security must be free from disabilities.

Eligibility criteria for Loan against Securities

Given below are some of the eligibility criteria to avail loan against securities from a bank:

- Should be a resident of India
- Should be at least 21 years of age
- Should either be a salaried or a self-employed individual
- The security for the loan should be approved by the bank

Documents required for Loan against Securities

Borrower who is salaried must submit the following documents:

- PAN card
- Identity and address proof
- Photograph
- Last 6 months bank statement
- Cancelled cheque
- Demat account statement
- Income proof

Borrower who is self- employed must submit the following documents:

- PAN card
- Identity and address proof
- Photograph

- Last 6 months bank statement
- Cancelled cheque
- Demat account statement
- Income proof
- Balance sheet and profit and loss account
- Office address proof and existence of business proof

Points to be considered before availing loan against securities

- Check the eligibility criteria: Applicant must ensure that he/she meets the eligibility criteria before applying for loan against securities from a bank. Most lenders require the applicant to be 21 years of age in order to be eligible for loan against securities.
- Choose a bank which accepts varied investments as security: Applicant must go for a lender which accepts various forms of investments such as mutual fund, IPO, insurance policies from partner companies, retail shares, etc.
- Choose a bank which offers high amount of loan at low interest: Applicant must avail loan against securities from a bank which offers a high amount of loan against the collateral. There are various lenders in India which offers a high loan amount at attractive interest rates depending on the securities.
- Repayment tenure: Applicant must look to avail loan against security from a lender which offers a flexible repayment tenure. Generally, the repayment tenure offered is between 1 year to 3 years. However, the repayment tenure chosen must depend on the loan amount availed .

Project finance:

Project finance is the long-term financing of infrastructure and industrial projects based upon the projected cash flows of the project rather than the balance sheets of its sponsors. Usually, a project financing structure involves a number of equity investors, known as 'sponsors', and a 'syndicate' of banks or other lending institutions that provide loans for the operation. They are most commonly non-recourse loans, which are secured by the project assets and paid entirely from project cash flow, rather than from the general assets or creditworthiness of the project sponsors, a decision in part supported by financial modeling. The financing is typically secured by all of the project assets, including the revenue-producing contracts. Project lenders are given a lien on all of these assets and are able to assume control of a project if the project company has difficulties complying with the loan terms.

Generally, a special purpose entity is created for each project, thereby shielding other assets owned by a project sponsor from the detrimental effects of a project failure. As a special purpose entity, the project company has no assets other than the project. Capital contribution commitments by the owners of the project company are sometimes necessary to ensure that the project is financially sound or to assure the lenders of the sponsors' commitment. Project finance is often more complicated than alternative financing methods. Traditionally, project financing has been most commonly used in the

extractive (mining), transportation, telecommunications, and power industries, as well as for sports and entertainment venues.

Risk identification and allocation is a key component of project finance. A project may be subject to a number of technical, environmental, economic and political risks, particularly in developing countries and emerging markets. Financial institutions and project sponsors may conclude that the risks inherent in project development and operation are unacceptable (unfinanceable). Several long-term contracts such as construction, supply, off-take and concession agreements, along with a variety of joint-ownership structures are used to align incentives and deter opportunistic behaviour by any party involved in the project. The patterns of implementation are sometimes referred to as "project delivery methods." The financing of these projects must be distributed among multiple parties, so as to distribute the risk associated with the project while simultaneously ensuring profits for each party involved. In designing such risk-allocation mechanisms, it is more difficult to address the risks of developing countries' infrastructure markets as their markets involve higher risks.

A riskier or more expensive project may require limited recourse financing secured by a surety from sponsors. A complex project finance structure may incorporate corporate finance, securitization, real options, insurance provisions or other types of collateral enhancement to mitigate unallocated risk.

Corporate finance

Corporate finance is the area of finance that deals with the sources of funding, the capital structure of corporations, the actions that managers take to increase the value of the firm to the shareholders, and the tools and analysis used to allocate financial resources. The primary goal of corporate finance is to maximize or increase shareholder value.

Correspondingly, corporate finance comprises two main sub-disciplines. Capital budgeting is concerned with the setting of criteria about which value-adding projects should receive investment funding, and whether to finance that investment with equity or debt capital. Working capital management is the management of the company's monetary funds that deal with the short-term operating balance of current assets and current liabilities; the focus here is on managing cash, inventories, and short-term borrowing and lending (such as the terms on credit extended to customers).

The terms corporate finance and corporate financier are also associated with investment banking. The typical role of an investment bank is to evaluate the company's financial needs and raise the appropriate type of capital that best fits those needs. Thus, the terms "corporate finance" and "corporate financier" may be associated with transactions in which capital is raised in order to create, develop, grow or acquire businesses.

Although it is in principle different from managerial finance which studies the financial management of all firms, rather

than corporations alone, the main concepts in the study of corporate finance are applicable to the financial problems of all kinds of firms.

UNIT IV

AGRICULTURE FINANCE AND RETAIL LENDING

Crop loans – Crop insurance schemes – Dairy – Sericulture – Poultry – Animal husbandry –Horticulture – Kisan credit cards –NABARD initiatives – Lead bank schemes – Retail lending – Characteristics of retail loans – advantages of retail loans – Retail banking vs Corporate Banking – Various retail banking products – Model retail banking products

UNIT IV

AGRICULTURE FINANCE AND RETAIL LENDING

Crop loans

Agriculture is the most important sector in India. But, the farmers face a lot of difficulties with regard to procure the best seeds, to buy the best fertilizer and machinery. To help the farmers and agriculturists with the finance, the lenders are offering crop loans.

Crop loan is a short term advance that is given to the farmers and agriculturists by banks and co-operative societies. The loan amount can be used to purchase improved seeds, fertilizers, machinery etc. The crop loans are provided, as agriculture is a priority sector. The loan is usually repaid in single instalment after the crop production. Crop loan is a Secured Loan and the interest is debited on a half- yearly basis at simple rate of interest. The loans provided by any lenders and co-operative societies can be refinanced by NABARD.

Steps to get a Secured Loan on Credit

- Compare all the lenders and the rates that the lender is providing for the crop loans. Look into private sector as well as specified organisations.
- Based on the initial check, choose certain lenders and make a list so that the borrower shall know who to approach for different purposes.

- Borrower should do a background checks on the lenders and look into their financial stability and those who have a good customer service.
- Borrower should approach a lender and get a quote and then approach the remaining lenders and try to negotiate the rates.
- Borrower should choose a lender capable of understanding borrower's situation and who is willing to go out of his way to help him/her.
- Borrower should prepare a document that includes details of previous performance of the crop that he/she wishes to use as a collateral to avail the loan. Borrower must include information about assets, current liabilities and other relevant information. Include information that may have negative impact on crop production as well.
- Finally submit the application along with the required documents.

In India, the following banks offer Crop Loans

- Union Bank of India
- IDBI Bank
- State Bank of India
- HDFC Bank
- UCO Bank
- Axis Bank
- Allahabad Bank
- Andhra Bank
- Bank of Baroda
- Bank of India
- Bank of Maharashtra
- Canara Bank

- Central Bank of India
- Corporation Bank
- Dena Bank
- Indian Bank
- Indian Overseas Bank
- Oriental Bank of Commerce
- Punjab and Sind Bank
- Punjab National Bank
- Syndicate Bank
- United Bank of India
- Vijaya Bank

The following Cooperative Banks also offer Crop Loan Schemes

- National Bank for Agriculture and Rural Development
- Bihar State Co-operative Bank Limited
- Haryana State Co-operative Apex Bank Limited
- National Federation of State Co-operative Banks Limited
- Odisha State Co-operative Bank Limited
- Repatriates Co-operative Finance and Development Bank Limited
- Punjab State Cooperative Agriculture Development Bank Limited
- Andhra Pradesh State Cooperative Bank Limited

No.	Scheme	Assistance

1	Pradhan Mantri Fasal Bima Yojana	• Insurance protection for food crops, oilseeds and annual horticultural/commercial crops notified by state government.
		• Uniform maximum premium for all farmers:
		    ○ Kharif season - 2% of sum insured.
		    ○ Rabi Season 1.5% of sum insured.
		    ○ Annual commercial/horticultural crops - 5% of sum insured
		• The difference between actual premium and the rate of Insurance payable by farmers shall be shared equally by the Centre and State.
		• Claims of full Sum Insured (SI), without capping or reduction in SI.

		• If the sowing is not done due to adverse weather/climate, claims upto 25% of sum insured will be paid for prevented sowing/planting risk. • When the crop yield is less than the guaranteed yield of notified crops,the claim payment equal to shortfall in yield is payable to all insured farmers. • If 50% loss in mid season of crop then on account advance payment, upto 25% of likely claims will be paid as immediate relief. • Losses caused due to inundation, hail storm and landslide would be assessed at individual farm level. • Post harvest losses assessment for damage to crops in cut and spread in the field up to 14 days on account

		of cyclonic rain and unseasonal rain in the entire country. • Use of remote sensing Technology and drones to supplement Crop cutting experiments for faster settlement of claims. • Implementing agency will be selected by the State Government through bid.
2	Weather Based Crop Insurance Scheme (WBCIS)	• Insurance protection for notified food crops, oilseeds and horticultural /commercial crops • Uniform maximum premium for all farmers like PMFBY : ○ Kharif season - 2% of sum insured. ○ Rabi Season 1.5% of sum insured.

		- Commercial/horticultural crops 5% of sum insured. - The difference between actual premium and the rate of Insurance payable by farmers shall be shared equally by the Centre and State. - When the Weather indices (rainfall/temperature/relative humidity/wind speed etc) is different (less/ higher) from the Guaranteed Weather Index of notified crops, the claim payment equal to deviation/shortfall is payable to all insured farmers of notified area. - Provision for assessment of losses caused by hailstorm and cloud burst at individual farm level.

		• Implementing agency will be selected by the State Government through bid.
3	Coconut Palm Insurance Scheme (CPIS)	• Insurance protection for Coconut Palm growers. • Premium rate per palm ranges from Rs. 9.00 (in the plant age group of 4 to 15 years) to Rs. 14.00 (in the plant age group of 16-60 years). • 50-75% subsidy of premium is provided to all types of farmers. • When the palm damaged, the claim payment equal to input cost loss damage is payable to the insured in notified areas.

4	Unified Package Insurance Scheme (UPIS) as pilot in 45 districts	• To provide financial protection and comprehensive risk coverage of crops, assets, life and student safety to farmers. • Pilot will include 7 section Viz.., - Crop Insurance (PMFBY / WBCIS), Loss of life (Pradhan Mantri Jeevan Jyoti Bima Yojna (PMJJBY)), Accident Insurance (Pradhan Mantri Suraksha Bima Yojana - PMSBY) , Student safety, Household, Agriculture implements and Tractor. • Crop insurance will be compulsory. However farmers can choose atleast 2 sections from remaining. • Farmers may be able to get all requisite insurance products for farmers through one simple proposal/ application Form and through single window. • Two flagship schemes of the Government viz PMSBY &

	PMJJBY have been included apart from insurance of assets. • Pilot scheme will be implemented through single window. • Processing of claims (other than Crop Insurance) on the basis of individual claim report.

Animal Husbandry Infrastructure Development Fund (AHIDF)

The Animal Husbandry Infrastructure Development Fund (AHIDF) has been approved for incentivizing investments by individual entrepreneurs, private companies, MSME, Farmers Producers Organizations (FPOs) and Section 8 companies to establish (i) the dairy processing and value addition infrastructure, (ii) meat processing and value addition infrastructure and (iii) Animal Feed Plant.

OBJECTIVES:

To help increasing of milk and meat processing capacity and product diversification thereby providing greater access for unorganized rural milk and meat producers to organized milk and meat market.

To make available increased price realization for the producer.

To make available quality milk and meat products for the domestic consumer.

To fulfill the objective of protein enriched quality food requirement of the growing population of the country and prevent malnutrition

To develop entrepreneurship and generate employment.

To promote exports and increase the export contribution in the milk and meat sector.

To make available quality concentrated animals feed to the cattle, buffalo, sheep, goat, pig and poultry to provide balanced ration at affordable prices.

Kisan Credit Card

The Kisan Credit Card (KCC) scheme was introduced in 1998 for issue of Kisan Credit Cards to farmers on the basis of their holdings for uniform adoption by the banks so that farmers may use them to readily purchase agriculture inputs such as seeds, fertilizers, pesticides etc. and draw cash for their production needs. The scheme was further extended for the investment credit requirement of farmers viz. allied and non-farm activities in the year 2004. The scheme was further revisited in 2012 by a working Group under the Chairmanship of Shri T. M. Bhasin, CMD, Indian Bank with a view to simplify the scheme and facilitate issue of Electronic Kisan Credit Cards. The scheme provides broad guidelines to banks for operationalizing the KCC

scheme. Implementing banks will have the discretion to adopt the same to suit institution/location specific requirements.

Applicability of the Scheme

The Kisan Credit Card Scheme detailed in the ensuing paragraphs is to be implemented by Commercial Banks, RRBs, Small Finance Banks and Cooperatives.

Objective / Purpose

The Kisan Credit Card scheme aims at providing adequate and timely credit support from the banking system under a single window with flexible and simplified procedure to the farmers for their cultivation and other needs as indicated below:

To meet the short term credit requirements for cultivation of crops;

To meet Post-harvest expenses;

To produce marketing loan;

To meet consumption requirements of farmer household;

To finance Working capital for maintenance of farm assets and activities allied to agriculture;

To meet Investment credit requirement for agriculture and allied activities.

Eligibility

i. Farmers - individual/joint borrowers who are owner cultivators;

ii. Tenant farmers, oral lessees & share croppers;

iii. Self Help Groups (SHGs) or Joint Liability Groups (JLGs) of farmers including tenant farmers, share croppers etc.

Fixation of credit limit / Loan amount

The credit limit under the Kisan Credit Card may be fixed as under :

All farmers other than marginal farmers:

The short term limit to be arrived for the first year (For cultivating single crop in a year):

Scale of finance for the crop (as decided by District Level Technical Committee) x Extent of area cultivated + 10% of limit towards post-harvest/household/ consumption requirements + 20% of limit towards repairs and maintenance expenses of farm assets + crop insurance and/or accident insurance including PAIS, health insurance & asset insurance.

Limit for second & subsequent year

First year limit for crop cultivation purpose arrived at as above plus 10% of the limit towards cost escalation / increase in scale of finance for every successive year (2nd, 3rd, 4th and 5th year) and estimated term loan component for the tenure of Kisan Credit Card, i.e., five years. (Illustration I)

For cultivating more than one crop in a year

The limit is to be fixed as above depending upon the crops cultivated as per proposed cropping pattern for the first year plus an additional 10% of the limit towards cost escalation / increase in scale of finance for every successive year (2nd, 3rd, 4th and 5th year). It is assumed that the farmer adopts the same cropping pattern for the succeeding four years. In case the cropping pattern adopted by the farmer is changed in the subsequent year, the limit may be reworked.

Term loan for investment

The term loan for investment is to be made towards land development, minor irrigation, purchase of farm equipment and allied agricultural activities. The banks may fix the quantum of credit for term and working capital limit for agricultural and allied activities, etc., based on the unit cost of the asset/s proposed to be acquired by the farmer, the allied activities already being undertaken on the farm, the bank's judgment on repayment capacity vis-a-vis total loan burden devolving on the farmer, including existing loan obligations.

The long term loan limit should be based on the proposed investment(s) during the five year period and the bank's perception on the repaying capacity of the farmer.

Maximum Permissible Limit

The short term loan limit arrived for the 5th year plus the estimated long term loan requirement will be the Maximum Permissible Limit (MPL) and is to be treated as the Kisan Credit Card limit.

Fixation of Sub-limits

i. Short term loans and term loans are governed by different interest rates. At present, short term crop loans upto ₹ 3 lakh are covered under Interest Subvention Scheme/Prompt Repayment Incentive scheme of the Government of India. Further, repayment schedule and norms are different for short term and term loans. Hence, in order to have operational and accounting convenience, the card limit is to be bifurcated into separate sub-limits for short term cash credit limit cum savings account and term loans.

ii. Drawing limit for short term cash credit should be fixed based on the cropping pattern. The amount(s) for crop production, repair and maintenance of farm assets and consumption may be allowed to be drawn as per the convenience of the farmer. In case the revision of scale of finance for any year by the district level technical committee exceeds the notional hike of 10% contemplated while fixing the five year limit, a revised drawable limit may be fixed in consultation with the farmer. In case such revisions require the card limit itself to be enhanced (4th or 5th year), the same may be done and the farmer be so advised.

iii. For term loans, installments may be allowed to be withdrawn based on the nature of investment and repayment schedule drawn as per the economic life of the proposed investments. It is to be ensured that at any point of time the total liability should be within the drawing limit of the concerned year.

iv. Wherever the card limit / liability so arrived warrants additional security, the banks may take suitable collateral as per their policy.

For Marginal Farmers

A flexible limit of ₹ 10, 000 to ₹ 50, 000 may be provided (as Flexi KCC) based on the land holding and crops grown including post-harvest warehouse storage related credit needs and other farm expenses, consumption needs, etc., plus small term loan investment(s) like purchase of farm equipment(s), establishing mini dairy/backyard poultry as per assessment of the Branch Manager without relating it to the value of land. The composite KCC limit is to be fixed for a period of five years on this basis.

Wherever higher limit is required due to change in cropping pattern and / or scale of finance, the limit may be estimated.

Disbursement

The short term component of the KCC limit is in the nature of revolving cash credit facility. There should be no restriction in number of debits and credits. The drawing limit for the current season/year could be allowed to be drawn using any of the following delivery channels.

operation through branch;

operation using cheque facility;

withdrawal through ATM /debit cards

operation through Business Correspondents and 'banking outlet/part-time banking outlet'

operation through PoS available in Sugar Mills/Contract farming companies, etc., especially for tie-up advances;

operations through PoS available with input dealers;

Mobile based transfer transactions at agricultural input dealers and mandies.

Issue of Electronic Kisan Credit Cards

All new KCC must be issued as smart card cum debit card as laid down in Part II of the Annex. Further, at the time of renewal of existing KCC; farmers must be issued smart card cum debit card.

The short term credit limit and the term loan limit are two distinct components of the aggregate KCC limit bearing different rates of interest and repayment periods. Until a composite card could be issued with appropriate software to separately account transactions in the sub limits, two separate electronic cards may be issued for all new/renewed cards.

Validity/Renewal

i. Banks may determine the validity period of KCC and its periodic review.
ii. The review may result in continuation of the facility, enhancement of limit or cancellation of the limit/withdrawal of the facility depending upon increase in cropping area/pattern and performance of the borrower.

iii. When the bank has granted extension and/or re-schedule the period of repayment on account of natural calamities affecting the farmer, the period for reckoning the status of operations as satisfactory or otherwise would get extended together with the extended amount of limit. When the proposed extension is beyond one crop season, the aggregate of debits for which extension is granted is to be transferred to a separate term loan account with stipulation for repayment in installments.

Rate of Interest (ROI):

The rate of interest will be as stipulated in DBR Master Directions on Interest Rate on Advances.

Repayment Period:

The repayment period may be fixed by banks as per the anticipated harvesting and marketing period for the crops for which the loan has been granted.

The term loan component will be normally repayable within a period of 5 years depending on the type of activity/investment as per the existing guidelines applicable for investment credit.

Financing banks may, at their discretion, provide longer repayment period for term loan depending on the type of investment.

Margin

To be decided by banks.

Security

Security will be applicable as per RBI guidelines prescribed from time to time.

Security requirement may be as under :

i. Hypothecation of crops: For KCC limit upto ₹ 1.00 lakh banks are to waive margin/security requirements.
ii. With tie-up for recovery: Banks may consider sanctioning loans on hypothecation of crops up to card limit of ₹ 3.00 lakh without insisting on collateral security.
iii. Collateral security: Collateral security may be obtained at the discretion of Bank for loan limits above ₹ 1.00 lakh in case of non-tie-up and above ₹ 3.00 lakh in case of tie-up advances.
iv. In states where banks have the facility of on-line creation of charge on the land records, the same shall be ensured.

Other features

Uniformity to be adopted in respect of following:

The applicable interest subvention /incentive for prompt repayment as advised by Government of India and/or State

Governments. The bankers will give adequate publicity of the facility so that maximum farmers may benefit from the scheme.

Besides the mandatory crop insurance, the KCC holder should have the option to avail the benefit of any type of asset insurance, accident insurance (including PAIS), health insurance (wherever product is available) and have premium paid through his/her KCC account. Premium has to be borne by the farmer/bank according to the terms of the scheme. Farmer beneficiaries should be made aware of the insurance cover available and their consent (except in case of crop insurance, it being mandatory) is to be obtained, at the application stage itself.

A one-time documentation at the first time of availment of KCC loan and thereafter simple declaration (about crops grown/proposed) by farmer from the second year onwards.

Classification of account as NPA:

The extant prudential norms on income recognition, asset-classification and provisioning will apply for loans granted under the KCC Scheme.

Charging of interest is to be done uniformly as is applicable to agricultural advances.

Processing fee, inspection charges and other charges may be decided by banks.

Other conditions while implementing revised guidelines of KCC Scheme :

In case the farmer applies for loan against the warehouse receipt of his produce, the banks would consider such requests as per the established procedure and guidelines. However, when such loans are sanctioned, these should be linked with the crop loan account, if any, and the crop loan outstanding in the account could be settled at the stage of disbursal of the pledge loan, if the farmer so desires.

The National Payments Corporation of India (NPCI) will design the KCC card to be adopted by all the banks with their branding.

Delivery Channels - Technical features

1 Issue of cards

The beneficiaries under the scheme will be issued with a Smart card / Debit card (Biometric smart card compatible for use in the ATMs / Hand held Swipe Machines and capable of storing adequate information on farmers identity, assets, land holdings and credit profile etc). All KCC holders should be provided with any one or a combination of the following types of cards:

2 Types of Card

A magnetic stripe card with PIN (Personal Identification Number) with an ISO IIN (International Standards Organization International

Identification Number) to enable access to all banks ATMs and micro ATMs

In cases where the Banks would want to utilize the centralized biometric authentication infrastructure of the UIDAI (Aadhaar authentication), debit cards with magnetic stripe and PIN with ISO IIN with biometric authentication of UIDAI can be provided.

Debit Cards with magnetic stripe and only biometric authentication can also be provided depending on customer base of the bank. Till such time, UIDAI becomes widespread, if the banks want to get started without inter-operability using their existing centralized bio metric infrastructure, banks may do so.

Banks may choose to issue EMV (Europay, MasterCard and VISA, a global standard for interoperation of integrated circuit cards) and RUPAY compliant chip cards with magnetic stripe and pin with ISO IIN.

Further, the biometric authentication and smart cards may follow the common open standards prescribed by IDRBT and IBA. This will enable them to transact seamlessly with input dealers as also enable them to have the sales proceeds credited to their accounts when they sell their output at mandies, procurement centers, etc.

Delivery Channels

The following delivery channels shall be put in place to start with so that the Kisan Credit Card is used by the farmers to effectively transact their operations in their KCC account.

1. Withdrawal through ATMs / Micro ATM
2. Withdrawal through BCs using smart cards.
3. PoS machine through input dealers
4. Mobile Banking with IMPS capabilities / IVR
5. Aadhaar enabled Cards.

Mobile Banking / Other Channels:

Mobile banking functionality for KCC Cards / Accounts as well along with Interbank Mobile Payment Service (IMPS of NPCI) capability allows customers to use this inter-operable IMPS for funds transfer between banks and also to do merchant payment transactions as additional capability for purchases of agricultural inputs.

This mobile banking should ideally be on Unstructured Supplementary Data (USSD) platform for wider and safer acceptance. However, the banks can also offer this on other fully encrypted modes (application based or SMS based) to make use of the recent relaxation on transaction limits. Banks can also offer unencrypted mobile banking subject to RBI regulations on transaction limits.

It is necessary that Mobile based transaction platforms enabling transactions in the KCC use easy to use SMS based solution with authentication thru' MPIN. Such solutions also need to be enabled on IVR in local language to ensure transparency and security. Such mobile based payment systems should be encouraged by all the banks by creating awareness and by doing proper customer education.

With the existing infrastructure available with banks, all KCC holders should be provided with any one or a combination of the following types of cards:

* Debit cards (magnetic stripe card with PIN) enabling farmers to operate the limit through all banks ATMs / Micro ATMs

* Debit Cards with magnetic stripe and biometric authentication.

* Smart cards for doing transactions through PoS machines held by Business Correspondents, input dealers, traders and Mandies.

* EMV compliant chip cards with magnetic stripe and pin with ISO IIN.

In addition, the banks having a call centre / Inter active Voice Response (IVR), may provide SMS based mobile banking with a call back facility from bank for mobile PIN (MPIN) verification through IVR, thus making a secured SMS based mobile banking facility available to card holders.

Long-Term Refinance

To ensure increased and uninterrupted credit flow to farmers, as also to give a boost to capital formation in the agriculture sector, NABARD provided refinance to the Cooperative Banks and RRBs out of Long Term Rural Credit Fund, at a reasonable rate of interest. An amount of Rs.14,481.50 crore was allocated for the year 2020-21.

Short-Term Refinance

Short Term Cooperative Rural Credit - STCRC (Refinance) Fund was set up in NABARD in 2008-09 to provide Short Term refinance to Cooperatives for their crop loans. The allocation for the year 2020-21 was Rs. 44,644.50 crore. Short Term RRB (Refinance) Fund was set up in NABARD in 2012-13 to provide Short Term refinance to RRBs for their crop loans. The allocation for the year 2020-21 is Rs. 9,921 crore.

Initiatives taken during the year (2020-21)

- Disbursement of Rs.25500 crore was made under Special Liquidity Facility (SLF1) to Cooperative Banks, RRBs and NBFCs (Rs.16800 crore to Cooperative Banks, Rs.6,700 crore to RRBs and Rs.2,000 crore to NBFCs) for unhindered flow of credit to banks and farmers in the wake of the lockdown due to COVID-19 pandemic.
- Additional SLF of Rs.1,567 crore was provided to NBFCs/ NBFC-MFIs with asset size less than Rs.500 crore.
- SLF to SCARDBs of Rs.783 crore was provided as front ended liquidity support from NABARD's own funds.

- Allocation of 25% of STRRB and LTRCF was made to aspirational and credit starved districts.
- Preliminary eligibility criteria for RRBs for availing refinance was revised and set on the basis of internal risk rating by NABARD.

Special Refinance Schemes

To address the issue of reverse migration, give boost to the agriculture & rural sector and income generating activities and focus on health and hygiene, NABARD introduced following special refinance schemes at concessional rates to eligible financial institutions:

i. PACSs as Multi Service Centers (MSCs) - NABARD introduced Special refinance scheme to saturate all the potential PACS for conversion as Multi Service Centres, over a period of three years commencing from the year 2020- 21. The scheme intends to develop all the potential PACS as Multi Service Centres (MSCs) over a period of three years commencing from the year 2020- 2021 by providing concessional refinance to StCBs at 3% to support PACS to create quality infrastructure (capital assets) and increase their business portfolio in tune with needs of members. Under this line of credit, NABARD has envisaged transformation of 35,000 PACS in three years commencing with the transformation of 5,000 PACS in FY21. During 2020-21, 3055 PACS were given in-principle sanction by NABARD with estimated Project cost of Rs.1,760.82 crore and estimated loan of Rs.1,568 crore.

ii. Scheme for beneficiaries of Watershed and Wadi project areas – The objectives of the scheme are to promote sustainable economic activities, livelihood and employment opportunities for the beneficiaries in NABARD supported watershed and wadi project areas by encouraging banks to lend at concessional rate to these beneficiaries to address the issue of rural migration and to give boost to the agriculture and rural sector in the post COVID era.

Refinance is available to all the eligible banks/FIs at 3% for maximum period of 5 years. The ultimate lending rate to be charged by banks/FIs under the scheme is revised as 06 months MCLR+1% or EBLR+2.5%, whichever is lower.

NABARD has earmarked refinance amount of Rs.5,000 crore during 2020-21 to 2022-23. During FY 2020-21, refinance of Rs.126.80 crore has been disbursed under this product.

iii.Scheme for promoting Micro Food Processing Activities – The objective of the scheme is to encourage banks to lend micro-food processing activities and create sustainable livelihood and employment opportunities for rural youth as well as reverse migrants due to COVID-19 pandemic in the rural areas. The scheme also envisages modernization and enhancing the competitiveness of the existing individual micro enterprises and ensure their transition to formal sector in rural areas. The refinance scheme will give fillip

to the recently launched "PM Scheme for Formalisation of Micro Food Processing Enterprises (PM FME)" under Aatmanirbhar Bharat Abhiyan by

MoFPI, GoI. Concessional refinance at 4% is available to eligible financial institutions viz., commercial banks, SFBs, StCBs, RRBs and NABARD Subsidiaries.

iv. Special refinance scheme on Water, Sanitation and Hygiene (WASH) - A Model Refinance Scheme on WASH activities has been prepared keeping in view the need to protect human health during infectious disease outbreaks, especially in the times of on-going COVID-19 pandemic. WASH has been conceptualized by NABARD to enable banks to provide credit to entrepreneurs for building social infrastructure relating to drinking water facilities, sanitation facilities including construction/ refurbishment of household toilets and health care facilities.

v. Extension of interest subvention benefits for extended period from March 2020 to 31 August 2020 and from March 2021 to June 2021

vi. COVID-19 deferment of loan instalments for client borrowers of NABARD.

vii. KCC Saturation Drive to cover PM Kisan Samman Scheme beneficiaries who do not possess Kisan Credit Cards - Department of Agriculture, Cooperation and Farmers' Welfare, Ministry of Agriculture and Farmers' Welfare, Govt. of India, has launched a campaign from

08.02.2020 to cover all PM Kisan Samman Scheme beneficiaries under Kisan Credit Cards. Adequate publicity and awareness campaigns were conducted to ensure maximum coverage. Phase-II of KCC Saturation- As a part of the Atmanirbhar Bharat Package, the Government has announced to cover 2.5 crore farmers under the Kisan Credit Card (KCC) scheme with a credit boost of Rs.2 lakh crore through a special saturation drive. Department of Animal Husbandry and Dairying, Govt. of India also decided to simultaneously launch a special drive to provide KCC to 1.5 crore dairy farmers belonging to milk unions and milk producing companies and 1 crore fish farmers. As a result of concerted and sustained efforts by Cooperative Banks and RRBs in this direction of providing access to concessional credit to the farmers, the progress during the year is as under: Phase No. of KCCs (Lakh Limits sanctioned (Rs. Crore) I 12.58 8,499.86 II (As on 31.05.2021) 58.56 47,685.68

viii. Government Sponsored Programmes with Bank Credit - The Administrative approval conveying the continuation of the followings subsidy schemes for 2020-21 (till 30 June 2021) has been received from the GoI: ● Agri Clinics and Agri Business Centers Scheme (ACABC). ● National Livestock Mission for Entrepreneurship Development & Employment Generation (EDEG), component of National Livestock Mission, Poultry Venture Capital Fund (PVCF), Integrated Development of Small Ruminants and Rabbit (IDSRR), Pig Development (PD), Salvaging and Rearing of Male Buffalo Calves (SRMBC), Effective Animal Waste Management, Construction of

Storage Facility for Feed and Fodder. ● Revised AMI sub scheme of ISAM - Communication from GoI regarding continuation of the scheme during 2021-22 is awaited. 1.4 Rural Infrastructure Development Fund (RIDF)

The major policy changes and initiatives during 2020-21 were as under: 1. The corpus under RIDF was increased from Rs. 30,000 crore to Rs. 40,000 crore, as announced in Union Budget 2021-22. 2. Total sanctions of Rs. 34,830 crore and disbursements of Rs. 29,193 crore were made during the year to various State/UT Governments. 3. Normative Allocation parameters for state-wise sanctions, under RIDF, were fine-tuned to include rural poverty and per capita priority sector credit flow. 4. The phasing of projects sanctioned under RIDF XX and XXI was extended up to 30 September 2021 and reimbursement of expenditure was allowed upto 31 December 2021.

To ensure better quality control and supervision through specialised agencies, the expenses on account of Quality Control/PMC/Supervisory Charges/Third

Party Monitoring are considered under RIDF upto a maximum of 2% of eligible project cost, wherever an external agency is engaged by the State Government.

A dedicated Web-portal and Mobile App for digitization of RIDF operations and real time monitoring of projects was launched.

A corporate film on completion of 25 years of RIDF was launched.

Important Funds:

A. Micro Irrigation Fund (MIF)

 MIF with a corpus of Rs.5000 crore was operationalized in NABARD in 2019- 20 with the Ministry of Agriculture and Farmers Welfare (MoA&FW), GoI being the Nodal Ministry. The fund was fully utilised and the GoI announced additional allocation of Rs.5,000 crore in the Union Budget for 2021-22.

● MIF facilitated State Govts'. efforts in mobilizing additional resources and incentivizing its adoption beyond provisions of Pradhan Mantri Krishi Sinchayee Yojana - Per Drop More Crop.

● During 2020-21, loan amount of Rs.1128.60 crore was sanctioned and Rs.1827.47 crore was released. As on 31 March 2021, the cumulative loan sanctioned and released under MIF was Rs. 3970.17 crore and Rs.1827.47 crore,respectively.

B. Long Term Irrigation Fund (LTIF)

 LTIF was operationalized in NABARD in 2016-17 for fast tracking completion of 99 identified Medium and Major Irrigation projects. Under LTIF, NABARD provides loan towards Central Share as well as State Share. During 2020-21, loan amount of Rs.2461.84 crore was sanctioned and Rs.7761.20 crore was released. As on 31 March 2021, the cumulative loan sanctioned and released stood at Rs.84326.60 crore and Rs.52479.71 crore, respectively.

C. Pradhan Mantri Aawas Yojna - Grameen (PMAY-G)

● PMAY-G aims at providing a pucca house, with basic amenities, to all households / households living in kutcha and dilapidated house, by 2022. Under the scheme, NABARD has extended loan towards part funding of Central Share.

● Under PMAY-G, 2.95 crore houses (1 crore in Phase-I and 1.95 crore in PhaseII) are targeted to be constructed from 2016-17 to 2021-22.

● During 2020-21, loan amount of Rs. 20,000.00 crore was sanctioned and Rs.19999.80 crore was released towards part funding of Central share under PMAY-G. As on 31 March 2021, the cumulative loan sanctioned and released under PMAY-G stood at Rs.61,975.00 crore and Rs.48,819.03 crore, respectively.

D. Swachh Bharat Mission-Gramin (SBM-G) ● SBM-G was launched by Govt. of India on 2nd October 2014 with the goal to achieve universal sanitation coverage in rural areas. Under the scheme, NABARD extended loan during 2018-19 to 2019-20 towards part funding of Central Share. ● The cumulative sanction and disbursement as on 31 March 2020 under SBMG stood at Rs. 15,000 crore and Rs. 12,298.20 crore, respectively. ● During 2018-19 and 2019-20, total 3.29 crore household toilets (2.23 crore in 2018-19 and 1.06 crore during 2019-20) were constructed (Source –MoJS, GoI).

E. Rural Infrastructure Assistance to State Governments (RIAS) NABARD launched a new product "Rural Infrastructure Assistance to State Governments (RIAS)", with an initial corpus of Rs. 15000 crore. Under RIAS, NABARD will provide financial assistance to State

Governments in Eastern Region, for creating infrastructure that supports rural livelihoods, hinging on 5-J approach – Jan (Human being), Jal (Water), Jameen (Land), Janwar (Livestock) & Jungle (Forest). 1.5 Initiatives on micro Finance ● Revision of grant support to JLGPIs: To incentivise promotion of JLGs, the grant assistance to JLGPIs was enhanced from Rs.2,000/- to Rs.4,000/- per JLG. ● MEDP/LEDP: To strengthen NABARD's efforts at skilling SHG members, the grant assistance was enhanced for MEDPs to Rs. 1.00 lakh and for LEDPs to Rs. 8.80 lakh (Farm Sector) and to Rs. 7.15 lakh (Off Farm Sector). ● For 2020-21, the number of MEDPs has tripled and LEDPs doubled from previous year to augment supply for skills required for rural employment. ● NABFINS as JLGPI: NABFINS was sanctioned a pilot project as a JLGPI in five States of Assam, Chhattisgarh, Madhya Pradesh, Maharashtra and Jharkhand for a period of three years. ● MY PAD MY RIGHT: NABFOUNDATION, through LEDP channel, was sanctioned the Project 'My Pad My Right' for Rs.1.99 crore for sanitary pad making machine for producing/marketing the pads to provide livelihood opportunities to SHGs and improve menstrual hygiene of rural women. During 2020-21, an amount of Rs.1.59 crore has been utilized and machines have been installed in 33 districts. ● EShakti: As on 31 March 2021, the project was being implemented in 281 districts. The data pertaining to 12.33 lakh SHGs (140.91 lakh members in 1.67 lakh villages was on-boarded to EShakti portal). From 2021-22, the project will be implemented in 130 districts of 16 States/UTs for a focused approach to reduce the credit gap. EShakti portal was used for sending 40 lakh

health advisory SMS to SHG members and during the pandemic, the SHGs were also engaged for making face masks, hand sanitizers, PPE kits, etc. for earning additional income.

Lead Bank Scheme

The Lead Bank Scheme is **a scheme which aims at providing adequate banking and credit in rural areas through an 'service area approach', with one bank assigned for one area**. It was introduced in 1969. On the recommendation of the Gadgil Study Group and Banker's Committee, the Scheme was introduced by RBI.

(i) The genesis of the Lead Bank Scheme (LBS) can be traced to the Study Group headed by Prof. D. R. Gadgil (Gadgil Study Group) on the Organizational Framework for the Implementation of the Social Objectives, which submitted its report in October 1969. The Study Group drew attention to the fact that commercial banks did not have adequate presence in rural areas and also lacked the required rural orientation. The Study Group, therefore, recommended the adoption of an 'Area Approach' to evolve plans and programmes for the development of an adequate banking and credit structure in the rural areas.

(ii) A Committee of Bankers on Branch Expansion Programme of Public Sector Banks appointed by the Reserve Bank of India under the Chairmanship of Shri F. K. F. Nariman (Nariman Committee) endorsed the idea of an 'Area Approach' in its report (November 1969), recommending that in order to enable the Public Sector Banks

to discharge their social responsibilities, each bank should concentrate on certain districts where it should act as a 'Lead Bank'.

(iii) Pursuant to the above recommendations, the Lead Bank Scheme was introduced by the Reserve Bank of India in December 1969.The Scheme aims at coordinating the activities of banks and other developmental agencies through various fora in order to achieve the objective of enhancing the flow of bank finance to the priority sector and other sectors and to promote banks' role in the overall development of the rural sector. For coordinating the activities in the district, a particular bank is assigned 'Lead Bank' responsibility of the district. The Lead Bank is expected to assume a leadership role for coordinating the efforts of the credit institutions and the Government.

(iv) In view of the several changes that had taken place in the financial sector, the Lead Bank Scheme was last reviewed by the High Level Committee headed by Smt. Usha Thorat, former Deputy Governor of the Reserve Bank of India in 2009.

(v) The High Level Committee held wide ranging discussions with various stakeholders viz. State Governments, banks, development institutions, academicians, NGOs, MFIs etc. and noted that the Scheme has been useful in achieving its original objectives of improvement in branch expansion, deposit mobilisation and lending to the priority sector, especially in rural/semi urban areas. There was overwhelming consensus that the Scheme needs to continue. Based on the recommendations of the Committee, the guidelines were issued to SLBC Convenor banks and Lead Banks for implementation.

(vi) Envisaging greater role for private sector banks, Lead Banks were advised to ensure that private sector banks are more closely and actively involved in the implementation of the Lead Bank Scheme, by leveraging on Information Technology and bringing in their expertise in strategic planning. They were also advised to involve themselves in the preparation as well as implementation of the District Credit Plan (DCP).

(vii) Further, Reserve Bank of India constituted a "Committee of Executive Directors" of the Bank to study the efficacy of the Scheme and suggest measures for its improvement. Based on the Committee's recommendations and feedback received from various stakeholders, certain 'action points' were issued to SLBC Convenors/Lead Banks and NABARD on April 6, 2018.

Fora under Lead Bank Scheme

Block Level Bankers' Committee (BLBC)

Block Level Bankers' Committee (BLBC) is a forum for achieving coordination between credit institutions and field level development agencies at the block level. The forum prepares and reviews the implementation of the Block Credit Plan and also resolves operational problems in the implementation of the credit programmes of banks. The Lead District Manager (LDM) of the district is the Chairman of the Block Level Bankers' Committee. All the banks operating in the block including the Small Finance Banks, Wholly Owned Subsidiaries (WOS) of Foreign Banks, RRBs, the District Central Co-operative Banks, Block Development Officer, technical officers in the block, such

as extension officers for agriculture, industries and co-operatives are members of the Committee. BLBC meetings are held at quarterly intervals. To strengthen the BLBC forum which operates at the base level of the Lead Bank Scheme, it is necessary that all branch managers attend BLBC meetings and enrich the discussions with their valuable inputs. Controlling Heads of banks may also attend a few of the BLBC meetings selectively. Participation by the District Development Manager (DDM) of NABARD in BLBCs would ensure better and more meaningful discussions for the development of the Block. Therefore, NABARD has been advised that DDMs should attend all Block Level Bankers' Committee meetings in their districts and actively participate in the credit planning exercise and review meetings at the block level. The Lead District Officer (LDO) of the Reserve Bank of India (RBI) selectively attends the BLBC meetings. The representatives of Panchayat Samitis are also invited to attend the meetings at half yearly intervals so as to share their knowledge and experience on rural development in the credit planning exercise. Payments Banks should also be invited to attend the meetings.

District Consultative Committee (DCC)

Constitution of DCC

The District Consultative Committees were constituted in the early seventies as a common forum at the district level for bankers as well as Government agencies/departments to facilitate coordination in implementing various developmental activities under the Lead Bank Scheme. The District Collector is the Chairman of the DCC meetings.

Reserve Bank of India, NABARD, all the commercial banks including Small Finance Banks, Wholly Owned Subsidiaries (WOS) of Foreign Banks, RRBs, Payments Banks, Co-operative banks including the District Central Cooperative Bank (DCCB), various State Government departments and allied agencies are the members of the DCC. The Lead District Officer (LDO) represents the Reserve Bank as a member of the DCC. The Lead District Manager (LDM) convenes the DCC meetings. The Director of Micro, Small and Medium Enterprises Development Institute (MSME-DI) in the district is an invitee in districts where MSME clusters are located to discuss issues concerning MSMEs.

Conduct of DCC Meetings

i. DCC meetings should be convened by the Lead Banks at quarterly intervals.

ii. At the DCC level, sub-committees as appropriate, may be set up to work intensively on specific issues and submit reports to the DCC for its consideration.

iii. DCC should give adequate feedback to the SLBC on various issues that need to be discussed on a wider platform, so that these receive adequate attention at the State Level.

Agenda for DCC Meetings

While Lead Banks are expected to address the problems particular to the concerned districts, some of the important areas which are

common to all districts which the lead banks should invariably discuss in the fora are as under:

i. Review of progress under Financial Inclusion Plan (FIP).

ii. The specific issues inhibiting and enabling IT enabled financial inclusion

iii. Issues to facilitate 'enablers' and remove/minimise 'impeders' for banking development for inclusive growth

iv. Monitoring initiatives for providing 'Credit Plus' activities by banks and State Governments such as setting up of Financial Literacy Centres (FLCs) and RSETI[#] type Training Institutes for providing skills and capacity building to manage businesses.

v. Scaling up financial literacy efforts to achieve financial inclusion.

vi. Review of performance of banks under District Credit Plan (DCP)

vii. Flow of credit to priority sector and weaker sections of the society

viii. Doubling of Farmers' Income by 2022

ix. Assistance under Government sponsored schemes

x. Grant of educational loans

xi. Progress under SHG - bank linkage

xii. SME financing & bottlenecks thereof, if any

xiii. Timely submission of data by banks

xiv. Review of relief measures (in case of natural calamities wherever applicable)

The above list is illustrative and not exhaustive. The Lead Banks may include any other agenda item considered necessary.

Rural Self Employment Training Institutes (RSETIs) should be more actively involved and monitored at various fora of LBS particularly at the DCC level. Focus should be on development of skills to enhance the credit absorption capacity in the area and renewing the training programmes towards sustainable micro enterprises. RSETIs should design specific programmes for each district/ block, keeping in view the skill mapping and the potential of the region for necessary skill training and skill up gradation of the rural youth in the district.

Role of LDMs

As the effectiveness of the Lead Bank Scheme depends on the dynamism of the District Collectors and the Lead District Managers (LDMs), with the support of the Regional/Zonal Office, the office of LDM should be sufficiently strengthened with appropriate infrastructural support. Apart from the provision of a separate office space, technical infrastructure like computers, printer, data connectivity, etc. which are basic necessities for LDMs to discharge their core responsibilities may be provided to LDMs' Office without exception. Officers of appropriate level, attitude and possessing requisite leadership skills should be posted as LDMs. Additionally, it is suggested that a dedicated vehicle may be provided to LDMs' to facilitate closer liaison with the bank officials, district administration officials as also to organise/ attend various financial literacy initiatives and meetings. The absence of a

specialist officer/assistant for data entry/analysis is a common and major issue faced by LDMs. Liberty to hire the services of skilled computer operator may be given to the LDMs to overcome the shortage of staff/ in case appropriate staff is not posted at LDM office. Further, for successful functioning of the Lead Bank Scheme, we expect Lead Banks to go the extra mile to provide facilities over and above the bare minimum to these critical field functionaries. Apart from the usual role of LDMs like convening meetings of the DCC/DLRC and periodical meetings of DDM/ LDO/ Government officials for resolving outstanding issues etc., the new functions envisaged for LDMs include the following:

i. Monitoring the implementation of the District Credit Plan
ii. Associate with the setting up of Financial Literacy Centres (FLCs), RSETIs by banks
iii. Associate with organizing financial literacy camps by FLCs and rural branches of banks.
iv. Holding annual sensitisation workshops for banks and Government officials with participation by NGOs/Panchayati Raj Institutions (PRIs).
v. Arranging for quarterly awareness and feedback public meetings, grievance redressal etc.

Quarterly Public Meeting and Grievance Redressal

The Lead District Manager should convene a quarterly public meeting at various locations in the district in coordination with the LDO of Reserve Bank, banks having presence in the area and other

stakeholders to generate awareness of the various banking policies and regulations relating to the common person, obtain feedback from the public and provide grievance redressal to the extent possible at such meetings or facilitate approaching the appropriate machinery for such redressal.

District Level Review Committee (DLRC) Meetings

DLRC meetings are chaired by the District Collector and attended by members of the District Consultative Committee (DCC). Public Representatives i.e. Local MPs/MLAs/ Zilla Parishad Chiefs are also invited to these meetings. The DLRC meetings should be convened by the Lead Banks at least once in a quarter. The DLRC is a forum to review the pace and quality of the implementation of various programmes under the Lead Bank Scheme in the district. Hence, association of non-officials is considered useful. Public representatives (MPs/ MLAs / Zilla Panchayat Chiefs) shall invariably be invited to DLRC meetings. Therefore, Lead Banks should fix the date of DLRC meetings with due regard to the convenience of the representatives of the public i.e. MPs/MLAs etc., to invite and involve them in all functions conducted by the banks in their districts, such as opening of new banking outlets, distribution of Kisan Credit Cards, SHG credit linkage programmes, etc. Responses to queries from public representatives need to be accorded highest priority and attended to promptly. The forum may also have representatives of State Minority Commission, SC/ST Corporation and representatives of the group of beneficiaries of rural lending. The forum may also

consider inviting people with the expertise in the fields, such as progressive farmers and local industrialists as special invitees. The follow up of the DLRC's decisions is required to be discussed in the DCC meetings.

DCC/DLRC meetings- Annual Calendar of Meetings

i) DCC and DLRC are the important fora facilitating coordination among commercial banks, Government agencies and others at the district level to review and find solutions to the problems hindering developmental activities. Therefore, it is necessary that all the members participate and deliberate in these meetings. On a review of the DCC/DLRC meetings, it was observed that late receipt/non-receipt of intimation of the date of meetings, clash of dates with other events, commonality of dates etc., hinder participation of members in these meetings, thus undermining the prime objective of conducting the above meetings.

ii) Lead Banks have, therefore, been advised to prepare an Annual Schedule of DCC and DLRC meetings on Calendar year basis for all districts in consultation with the Chairperson of the meetings, Lead District Officer of the RBI and Public Representatives in case of DLRC. This yearly Calendar should be prepared in the beginning of each year and circulated to all members as advance intimation for blocking future dates to attend the DCC and DLRC meetings and the meetings should be conducted as per the calendar. While preparing the calendar, it should be ensured that DCC and DLRC meetings are not held simultaneously. Lead Banks must fix dates of DLRC meetings

taking into account the convenience of the MPs and circulate the agenda papers to MPs well in advance.

State Level Bankers' Committee (SLBC)

Constitution of SLBC

i) The State Level Bankers' Committee (SLBC) was constituted in April 1977, as an apex inter-institutional forum to create adequate coordination machinery in all States, on a uniform basis for development of the State. SLBC is chaired by the Chairman/ Managing Director/ Executive Director of the Convenor Bank. It comprises representatives of commercial banks including Small Finance Banks, Wholly Owned Subsidiaries (WOS) of Foreign Banks, RRBs, Payments Banks, State Cooperative Banks, RBI, NABARD, heads of Government departments including representatives from National Commission for Scheduled Castes/Tribes, National Horticulture Board, Khadi & Village Industries Commission etc. and representatives of financial institutions operating in a State, who come together and sort out coordination problems at the policy implementation level. Representatives of various organizations from different sectors of the economy like industry bodies, retail traders, exporters, farmers' unions, etc. are special invitees in the SLBC meetings for discussing their specific problems, if any. SLBC meetings are held on quarterly basis. The responsibility for convening the SLBC meetings would be of the SLBC Convenor Bank of the State.

ii) Recognising that SLBCs, primarily as a committee of bankers at the State level, play an important role in the development of the

State, illustrative guidelines on the conduct of State Level Bankers' Committee meetings have been issued.

Conduct of SLBC Meetings

i) SLBC meetings are required to be held regularly at quarterly intervals. The meetings are chaired by the Chairman/ Managing Director/ Executive Director of the Convenor Bank and co-chaired by the Additional Chief Secretary or Development Commissioner of the State concerned. In cases where the Managing Director/Chief Executive Officer/Executive Director of the SLBC Convenor Bank is unable to attend SLBC Meetings, the Regional Director of the RBI shall co-chair the meetings along with the Additional Chief Secretary/Development Commissioner of the State concerned. A High Level of participation in SLBC/UTLBC meetings ensures an effective and desired outcome with meaningful discussion on issues of public policy of both the Government of India and the Reserve Bank of India.

ii) The Chief Minister/Finance Minister and senior level officers of the State/RBI (of the rank of Deputy Governor / Executive Director) may be invited to attend the SLBC meetings. Further, the State Chief Ministers are encouraged to attend at least one SLBC meeting in a year.

iii) State Level Bankers' Committee meetings should primarily focus on policy issues with participation of only the senior functionaries of the banks/ Government Departments. All routine issues may be delegated to sub-committee(s) of the SLBC. A Steering Sub-committee may be constituted in the SLBC to deliberate on

agenda proposals from different stakeholders and finalise a compact agenda for the SLBC meetings. Typically, the Sub-Committee could consist of SLBC Convenor, RBI & NABARD representatives & senior State Government representative from the concerned department, e.g. Finance/ Institutional Finance and two to three banks having major presence.

iv) Other issue-specific sub-committees may be constituted as required. The sub committees may examine the specific issues relating to agriculture, micro, small/medium industries/enterprises, handloom finance, export promotion and financial inclusion, etc. in-depth and devise solutions/recommendations for adoption by the full committee. They are expected to meet more frequently than the SLBC. The composition of the sub-committees and subjects/ specific issues impeding/enabling financial inclusion to be deliberated upon, may vary from State to State depending on the specific problems/issues faced by the States.

v) The secretariat/offices of the SLBC should be sufficiently strengthened to enable the SLBC Convenor Bank to effectively discharge its functions.

vi) The various fora at lower levels may give adequate feedback to the SLBC on issues that need to be discussed on a wider platform.

vii) Several institutions and academicians are engaged in research, studies etc. that have implications for sustainable development in agriculture and MSME sector. Engaging with such research institutions and academicians would be useful in bringing in

new ideas for furthering the objectives of the Lead Bank Scheme. The SLBCs may, therefore, identify such academicians and researchers and invite them as 'special invitees' to attend SLBC meetings occasionally both for adding value to the discussions and also associate them with studies appropriate to the State. Other 'special invitees' may be invited to attend SLBC meetings depending on the agenda items/issues to be discussed in the meetings.

viii) The activities of NGOs in facilitating and channelling credit to the low income households are expected to increase in the coming years. Several corporate houses are also engaged in corporate social responsibility activities for sustainable development. A linkage with such NGOs/Corporate houses operating in the area to ensure that the NGOs/corporates provide the necessary 'credit plus' services can help leverage bank credit for inclusive growth. Success stories could be presented in SLBC meetings to serve as models that could be replicated.

Revised Agenda for SLBC Meetings

1. Review of financial inclusion initiatives, expansion of banking network and Financial Literacy:

a. Status of opening of banking outlets in unbanked villages, CBS-enabled banking outlets at the unbanked rural centres (URCs)
b. Review of Operations of Business Correspondents – hurdles/issues involved

c. Progress in increasing digital modes of payment in the State, provision of continuous connectivity with sufficient bandwidth, resolving connectivity issues/ connectivity options (Bharat Net, VSAT, etc.), installation of ATMs and PoS machines and status of implementation of e-receipts and e-payments in the State

d. Status of rollout of Direct Benefit Transfer in the State, Aadhaar seeding and authentication

e. Review of inclusion of Financial Education in the School Curriculum, financial literacy initiatives by banks (particularly digital financial literacy)

f. Creating awareness about various schemes, subsidies, facilities e.g. crop insurance, renewable energy

g. Review of efforts towards end to end projects involving all stakeholders in the supply chain.

2. Review of credit disbursement by banks:

a. Achievement under ACP of the State, Priority Sector Lending

b. Discussion on lending towards government sponsored schemes (DAY-NRLM, DAY-NULM, MUDRA, Stand-Up India, PMEGP, etc.) and impact of these schemes

c. Flow of credit to MSMEs and for affordable housing

d. KCC loan, crop insurance under PMFBY

e. Grant of Education Loans

f. Progress under SHG-bank linkage.

3. Doubling of Farmers' Income by 2022.

4. CD Ratio, Review of Districts with CD Ratio below 40% and working of Special Sub-Committees of the DCC (SSC).

5. Position of NPAs in respect of schematic lending, Certificate Cases and Recovery of NPAs.

6. Review of restructuring of loans in natural calamity affected districts in the State, if any.

7. Discussion on policy initiatives of the Central/State Government/RBI (Industrial Policy, MSME Policy, Agriculture Policy, Start-Up Policy, etc.), and expected involvement of banks.

8. Discussion on improving rural infrastructure/ credit absorption capacity:

a. Any large project conceived by the State Government to help improve C-D Ratio

b. Explore the scope of state-specific potential growth areas and the way forward – choosing partner banks

c. Discussion on findings of region-focused studies, if any, and implementing the suggested solutions

d. Identification of gaps in rural and agriculture infrastructure which need financing (rural godowns, solar power, agro processing, horticulture, allied activities, agri-marketing etc.)

e. Implementation of Model Land Leasing Act 2016 (exploring possibility).

9. Efforts towards skill development on mission mode partnering with Krishi Vigyan Kendra (KVK), Horticulture Mission, National Skill Development Corporation, Agriculture Skill Council of India (ASCI), etc. including a review of functioning of RSETIs.

10. Steps taken for improving land record, progress in digitization of land records and seamless loan disbursements.

11. Sharing of success stories and new initiatives at the district level that can be replicated in other districts or across the State.

12. Discussion on Market Intelligence Issues e.g.:

a. Ponzi Schemes/ Illegal Activities of Unincorporated Bodies/ Firms/ Companies Soliciting Deposits from the Public
b. Banking Related Cyber Frauds, phishing, etc.
c. Instances of usurious activities by lending entities in the area, cases of over indebtedness
d. Credit related frauds by borrower groups, etc.

13. Issues remaining unresolved at DCC/DLRC meeting.

14. Timely submission of data by banks, adhering to the schedule of SLBC meeting.

15. Any other item, with the permission of the Chair.

The above list is illustrative and not exhaustive. SLBC Convenor Banks may include any other agenda item considered necessary.

SLBC - Yearly Calendar of Meetings

To improve the effectiveness and streamline the functioning of SLBC/UTLBC meetings, SLBC Convenor Banks have been advised to prepare a yearly calendar of programmes (calendar year basis) in the beginning of the year itself, for conducting the meetings. The calendar of programmes should clearly specify the cut off dates for data submission to SLBC and acceptance thereof by the SLBC Convenor. This yearly calendar should be circulated to all the concerned as an advance intimation for blocking of future dates of senior functionaries of various agencies like Central Government, State Governments, banks, RBI, etc. The SLBC/UTLBC meetings should be conducted as per the calendar under all circumstances. The agenda should also be circulated in advance without waiting for the data from defaulting banks. The matter should, however, be taken up with the defaulting banks in the SLBC meeting. In addition, the SLBC Convenor Bank should write a letter in this regard to the controlling office of the defaulting banks under advice to the Regional Office of RBI. The SLBC Convenor Bank will, however, continue to follow-up with banks for timely data submission. Further, in case the Chief Minister, Finance Minister or other very senior functionaries are not able to attend the SLBC on some very rare occasion, then if so desired by them, a special SLBC meeting can be held.

Retail Lending:

Retail lending is defined as closed- and open-end credit extended to individuals for household, family, and other personal expenditures.

India has emerged as one of the largest and fastest growing economies of the world during the last decade. The strengthening of the economy in India has been fuelled by the convergence of several key influences, like growth of the key economy sectors, liberalization policies of the government, well-educated work force and the emergence of a middle-class population. India, having the second largest population in the world, is on its way to become the world's fourth largest economy in a span of 2 decades. Due to the restrictive regulatory environment and strict policies of the government of India until the early 1990's the public sector banks and other scheduled banks were the major lenders. Even with the entry of private banks, in the initial phase, there was limited competition between the public sector banks and private banks. Also, the thrust was not on developing the economy consistently through credit growth. Hence, banks did not feel the need to foray into the sectors that were under served. In the current scenario, banks have been thriving on retail lending. The focus of banks now, is to increase the probable profits while limiting possible losses. An increase in market penetration brought about a change in the business environment and in the way banks conducted their business. There was a change in terms of innovation in products as well as processes to cater to the demands of the new age customer on

one hand and to protect the bank from multiple risks on the other. Retail exposure of banks includes various types of retail credit, such as residential mortgages, consumer credit cards, automobile and personal loans, loans against securities, and small business loans.

Retail loans

Retail loan is generally provided to an individual by a certified financial institution, a commercial bank or a credit union to purchase property, vehicles or other assets such as essential electronics, etc. Retail loans are provided to individuals with a decent credit score.

Retail loans are loans taken by individuals from banks or financial institutions for personal use. These loans can be used for various purposes, such as buying a car, paying for education, renovating a house, etc. Retail loans are generally unsecured, meaning they do not require any collateral.

One of the most widely availed services under Retail Banking includes loan services. This includes home loans, auto loans for new/used vehicles, consumer loans, education loans, crop loans to farmers, business loans for small scale businesses.

A Retail loan is generally provided to an individual by a certified financial institution, a commercial bank or a credit union to purchase property, vehicles or other assets such as essential electronics, etc.

Retail loans are provided to individuals with a decent credit score. Banks and financial institutions want to ensure timely repayment of such loans; hence having a good repayment history and credit score plays a very important role in availing a Retail loan. Interest is to be paid monthly or annually as per the pre-determined terms and conditions of the financial institution.

People primarily opt for retail loans in case they want to make an immediate purchase but lack the funds to pay for it. One of the most common types of Retail loans is a Housing Loan. Buying a house is an expensive affair, and an average middle-class individual in India can barely afford to pay for a house in lumpsum. So, in such a case, the bank agrees to lend the amount, and the borrower agrees to pay the money back bit by bit along with the interest amount over a period of several years.

Retail Loans - Characteristics

- These are small size loans
- These loans meet the needs of a large number of customers with well diversified portfolios
- The target customers are generally individuals or small organizations
- These loans offer standard products to customers. Very rarely a customer's requirement is customized
- The operations of retail credit are centralized in most of the banks
- Bankers can make quick credit related decisions because of decentralization

- These loans are designed to cover varied segments of risks
- High volume business
- High number of transactions

Retail Banking

Retail banking is a banking facility that offers financial services to the general population rather than companies. It certainly helps retail customers conduct their daily financial dealings more effectively and safely. Also labeled as "consumer banking," it occurs between consumers and their banks.

Retail banking is a banking facility that provides financing solutions to only individual clients and not businesses.

Retail loan industry is significantly benefiting the consumers by enabling them to purchase the necessary assets without paying in full at once. Banks nowadays have become cautious of who they are lending money to. Timely repayment is essential not only for the banks but also for the economy.

Retail banking, also called consumer banking or personal banking, is a type of banking that serves individuals instead of businesses. Retail banking is a way for regular people to manage their own money, get credit, and safely put cash in the bank. In terms of services, there are checking and savings accounts, mortgages, personal loans, credit cards, and certificates of deposit services that retail banks offer (CDs).

Most people use local branch banking services, which take care of all of a retail customer's banking needs on-site and are used by most people. Financial representatives help with customer service and give financial advice at local branch locations.

A customer might not use all these retail banking services, but the most important is putting money into a checking or savings account. This is a common and safe way for people to keep their money. Also, it lets them make money on their money by earning interest. Both checking and savings accounts come with debit cards that make it easy to get money out of the account and pay for things.

How a Retail Bank makes money

A retail bank keeps the cash that its retail customers deposit. It then lends the money it gets from these deposits to other clients. The banks make money by charging higher interest rates on these loans than they pay on deposits from customers.

Retail bank types

Basis their size, there are many different kinds of retail banks, from small, locally run local community banks to the retail banking services of large, global corporate banks like JPMorgan Chase and Citibank.

Small Banks.

They work in a small area through branch banking and offer almost all the same services as the big banks. This makes them well-known among the public. But compared to them, they have smaller market shares and less money in the bank.

Large Banks.

These big banks are based in big cities and have many branches. They also have a lot more employees than small banks. Also, many retail customers buy them because they are so popular.

Online Banks.

As the name suggests, online banks do their business over the Internet and do not have physical offices. Also, they run through an official website that can be accessed anywhere in the world. Most people now prefer to do their banking from the comfort of their own homes.

Products and Services for Retail Banking

Saving Bank accounts.

Also called "interest-bearing accounts," this is an excellent example of retail banking for basic deposit accounts to keep cash safe and earn a reasonable interest rate. The banks put the money away for short-term needs and usually limit cash transfers and withdrawals.

Deposit accounts.

These deposit accounts make cash withdrawals and deposits for regular payments easy and, in most cases, unlimited. They are also called "transactional accounts" because customers can use debit cards to buy things and pay bills online. Still, they pay less interest than savings accounts.

Debit Cards.

These payment cards are used to pay for things without cash. The money is taken directly from the savings or checking account. They also link directly to the bank account and can be used at ATMs (ATMs).

Deposit certificates (CDs).

This savings account holds a set amount of capital for a set amount of time, and the bank that offers these accounts pays interest in exchange. When the money is cashed in, the person gets both the original amount and the interest.

Credit Cards.

Banks give out credit cards so customers can borrow money for digital transactions with a set line of credit. Cardholders must pay back the total amount, plus any interest, on or before the due date to avoid credit risk.

TYPES OF RETAIL LOANS

1. Housing loans:

Considering the fact that real estate is expensive, and it may take years for someone to save the amount of money required to purchase a house, a Housing Loan is the most commonly availed Retail loan in India. These bank loans enable customers to purchase homes. Also, second mortgages mean that customers can use the value of their home as collateral to borrow money.

2. Educational loans:

This type of loan is provided by banks to students who want to avail education but cannot afford to pay for the same. Students can use the loan money to pay for foreign education, tuition fees, hostel expenses and other similar expenses.

3. Vehicle loans:

For individuals looking to buy a new car or a two-wheeler, vehicle loans are provided by banks. A part of the total purchase amount shall be paid as down payment and the rest in instalments with interest. Interest amount may vary from bank to bank.

4. Personal loans:

A personal loan can be availed for a variety of reasons such as travelling, marriage, medical expenses or any such situation that may need immediate financial assistance.

These loans involve getting money from banks, online lenders, or credit unions to pay bills. Also, monthly payments pay the multi-purpose unsecured loan back over a few months or years.

Advantages of retail banking

The benefits of retail banking to the bank and the economy are indisputable. Few of these advantages are as follows:

Brand building: The retail banking system serves many people who prefer running transactions with a branch financial house. Of course, bringing in large individual consumers ensures there is enough liquidity to provide loans for other consumer clients. But on the flip side, it is building awareness for the bank. The more people walk into the bank to transact, the higher the chances of retaining a mental picture of the bank, which is good for brand creation.

Constant liquidity with non-negotiable interest: Retail client deposits are stable and create core deposits. Such deposits come with non-negotiable interest. Hence, there is less room for extra interest negotiating. Since they serve many people, they also have access to large funds.

Improve client relationship: Retail banking has a better client management score and that in turn helps in building a dedicated and loyal client base

Increase diversification: With retail banking in place, banks can now look into more side businesses like pension schemes, mortgage processing, mutual funds, etc. Through increasing output, retail banks contribute to the country's economic progress.

Retail banking provides quick and easy soft loans to consumer clients, thus improving the standard of living of low and average-income earners.

Disadvantages of retail banking

Increased rate of long-term loans becoming non-performing assets: There is a high chance of consumers defaulting on long-term loans in retail banks, which could become non-performing long if not properly supervised.

Retail banks incur heavy expenses on human resources to keep tabs on many disbursed loans.

The future of retail banking

With the closure of many bank branches, the retail banking industry has undergone significant changes in recent years. Although it is impossible to pinpoint the exact cause of these closures, given the current state of internet retail banking, there is no doubt that online and

mobile banking is playing a role in all of these difficulties. Experts believe this trend will continue in the retail banking segment, as it had done for the past 25 to 30 years when the government deregulated banks. It should, however, be noted that not all banks are closing branches; some are forming credit unions.

Most people think of a retail bank when they think of a bank. Retail banks offer their customers a wide range of products and services. Every city has bank branches where people can get retail banking services like mortgages, credit cards, personal loans, CDs, and checking and savings accounts.

Digital banking platform vendor

The adoption of digitalization has given birth to many modern banking models that offer branchless banking services. These banks employ improved fintech solutions to offer people fast, secured, and seamless basic banking services. Since branchless banking is getting more and more popular, and the demand for digital banks is growing, building new digital banks is easier

Retail Banking vs Corporate Banking:

Major Differences between Retail and Corporate Banking:

Retail Banking is a banking service provided to the general public or individual to regulate their funds in their savings account or fixed deposit account and to perform various other day-to-day banking transactions like depositing money and opening bank account.

Corporate banking is a type of commercial banking that focuses on small and large businesses and corporations, offering services such as trade finance, derivatives, and other financial products.

Personal loans, vehicle loans, home loans, and other customer-oriented retail banking products are available. Corporate banking is focused on the needs of businesses and can be adapted or adapted to meet specific needs, such as loan facilities. When it comes to customer base, retail banking often attracts a huge number of customers, but corporate banking does not attract a significant number of customers but does attract affluent clients.

The processing cost in retail banking is low, whereas the processing cost in corporate banking is substantial. Corporate banking is more profitable than the retail banking segment of the banks in terms of profitability.

Retail banking refers to the division of a bank that deals directly with retail customers while corporate banking is the part of the banking industry that deals with corporate customers.

Retail banking is the visible face of banking to the general public, with bank branches located in abundance in most major cities. Corporate banking, on the other hand, works directly with businesses to provide them loans, credit, savings accounts, and checking accounts which are specifically designed for companies rather than for individuals

While retail banking services are provided to individuals in the general public, corporate banking services are only provided to small or large companies and corporate bodies. The scope of the products and services offered is also different: retail banking is customer-oriented and corporate banking is business-oriented.

The financial worth of transactions is comparably higher in corporate banking than in retail banking. The source of profit is also different: the difference between the margin of interest of borrowers and lenders is the main source of profit in retail banking, while corporate banking's source of profit is the interest and fees charged on the services provided.

UNIT-V

CREDIT MONITORING AND NPA MANAGEMENT

Credit monitoring – Supervision – Follow up- Credit Monitoring – Meaning – Monitoring Goals – Process of Monitoring – Different monitoring tools – Check list for monitoring – Monitoring by using various statements – NPA – Causes and remedial Measures – identification of NPA- Debt Recovery Tribunals – Asset Reconstruction Fund –Effect of NPA on profitability.

UNIT-V

CREDIT MONITORING AND NPA MANAGEMENT

What Is a Credit Monitoring Service?

A credit monitoring service tracks changes in borrower behavior to notify consumers of potential fraud, as well as changes to their creditworthiness.

For example, credit monitoring services can guard against identity theft, when an individual's personal information is stolen and used without the person's permission for nefarious purposes. If a credit card is stolen and used, a credit monitoring service should detect the different buying patterns and alert the credit card account holder.

How Credit Monitoring Works

Although consumers primarily use credit monitoring services to guard against identity theft, a credit monitoring service also tracks a consumer's credit report and credit scores. Criminal activity related to identity theft can range from illegal purchases at retail or online outlets using a stolen credit card number to filing fake Social Security or Medicare claims. Since thieves use this information without the victim's knowledge, such criminal activity can be difficult to detect until well after the fact, by which time an individual's credit could be utterly destroyed.

The best credit monitoring services notify consumers of changes to their credit activity; for example, if a new account has been opened or

if a large purchase is made, such as a car. Some credit monitoring services also offer more comprehensive tracking of credit scores, which keeps consumers up to date on the quality of their credit. Fraudsters use social engineering techniques to obtain the personal information of individuals with which to commit identity theft. These techniques include phishing, cat fishing, tailgating, and baiting.

This type of monitoring allows the account holder to plan ahead and repair any issues that might inhibit major credit-based activities, such as applying for an automobile loan or a mortgage.

Choosing Credit Monitoring Services

Pricing and features vary from service to service. Some financial institutions offer free services that track credit scores on a limited basis, while other paid services offer more comprehensive scans that collect data across the internet on a consumer's bank account, credit card, or Social Security number. When choosing a credit monitoring service, consumers should note the service limitations. Paid services may offer more comprehensive coverage than free services, but a higher cost does not automatically translate to superior services. While many services offer access to a consumer's credit score, they may not track that score across all providers. For example, some credit card issuers provide free access to a consumer's credit scores, which means there is no need to pay a second provider for that service.

While credit monitoring services can provide early warnings of identity theft or fraud, for the most part, such warning occurs after the fact. These services work best as part of a broader strategy to protect and monitor personal information. In particular, consumers should be vigilant before disseminating important personal information including Social Security numbers, bank account numbers, and credit card numbers. In many cases, an awareness of the social engineering techniques used by criminals to obtain such information can provide substantial protection against identity theft. Checking the accuracy of credit card statements and reliable credit monitoring services offer a useful second line of defense.

Each credit monitoring service will have its own features and suite of services, but the client can generally expect to get access to at least one credit report and credit score, credit monitoring, and account alerts. Premium services will include benefits like identity theft insurance, restoration assistance, dark web surveillance, and three-bureau monitoring.

Benefits of Credit Monitoring-

Helps in planning finances well in advance

Not managing and planning the finances can make things difficult in the long run. It is one of the biggest reasons behind a low credit score. A credit monitoring service will alert the client about the changes to the credit score and this knowledge will help in giving a

better understanding of how client's financial activities are affecting his/her score. It will also help to make better financial decisions. Besides this, client will also be able to evaluate his/her credit health, all about the financial activities, identify the wrong areas, and the corrective measures.

It can help to prevent identity theft

Identity theft is a very serious problem that can easily go undetected if client doesn't pay close attention to it. The longer the fraud persists, the worse the credit report and credit score will get. To avoid such a situation, client can take the help of credit monitoring services to fix the credit with the credit reporting agencies in less time. To avail of this service, client would need to pay a few extra bucks to the credit monitoring companies to get such information.

Customise alerts

Some credit monitoring companies provide with the comprehensive services. Clients can customise the reports, notifications, and alerts. For example, client can choose to receive a notification whenever there's a particularly suspicious purchase on one of his/her credit cards, or while applying for any loan, they can send information on the best rates depending on client's financial requirement and condition.

Process of Credit Monitoring

The credit process evaluates the ability and willingness of a borrower to repay the debt, underwrites the risk, prices the loan, and determines whether the loan fits the bank's portfolio. An integral part of the credit process is analysis of the borrower's cash flows and financial statements.

What is credit monitoring assessment?

Credit Monitoring Assessment (CMA) Format :- CMA format is a report on Past and Projected Performance of the applicant. It has an aim to understand Financial Health, It also provide information as to how applicant has procured funds and used them in past 2 years and how it will be done in next 3 years.

A traditional credit analysis requires a strict procedure that involves three key steps: obtaining information, a detailed study of this data and decision-making.

Credit Monitoring Tools :

Certified statement of the actual cost of the project (upon completion) vis-a-vis the original envisaged cost of the project.

Stock and book-debts statements.

Monthly Cash Budget, wherever applicable.

Returns of Quarterly Information System.

Credit Report Checklist

Keeping a track of records for every individual seems like a tedious task. It becomes very difficult to match names, date of birth, contact number, address, PAN card details, Passport number, Voter IDs etc of every individual. To overcome this problem, CIBIL has developed an algorithm to consider several fields before making a match before raising the credit report. But being said that, there may be some errors or mistakes done on the part of the lenders or identity theft lenders or identity theft, lack of updated information, errors in personal data etc. This all needs to be checked after getting the credit report. This will help to ensure all personal and financial information is complete and accurate. If in case, some mistakes are discovered in the credit report, lender has to be immediately contacted.

Below given is the checklist that you must need not miss while reading your credit report:

1. **Make sure there are no errors in reporting by the lender**
   You need to check your credit reports very frequently, especially when you are applying for any loan or credit card to know your current standing. Checking your reports from time to time will help you to know the possible errors which might have done by your lender while reporting your credit transactions. It will not only help you to spot errors on your report, but it will also enable you to avail

the best terms on the credit product. This is what all you need to check while reading your credit report-

- The first thing you need to do is to read every section of your credit report carefully
- Now, check for the outstanding amount on your credit cards and loan. You might have cleared then but, it may not be updated on your report. If this happens, it means something is wrong that needs to be corrected on time as your credit score will be affected
- When you spot an error in your personal data, address or outstanding balance, immediately report it to the credit reporting bureau. And write a letter to the creditor who reported the wrong information. You can also raise a dispute with any of the three credit bureaus for correction

2. Check for identity theft

Check for enquiries that are not made by you. For example, if there is a loan application reported in your credit report which has not been initiated by you, then you can be sure that it is a case of identity theft. What you need to look for while checking possible frauds are-

- Credit inquiries not made by you
- Loan accounts that were not initiated by you
- Credit inquiries not made by you
- Late payments or defaults that you did not make
- Wrong address and other identifying information

- Wrong contact number

If there is a case of identity theft, immediately report it to the credit bureau that issued the report and notify the lender immediately.

3. Check your account information

Most of the information in your credit report is your account information. While reading your credit report, you need to check the following things-

- Review all your accounts (loans and credit card account. They should be in your name
- Cross-check your credit limit, current balance and payment history
- Note that which of your accounts were inactive and closed
- Note all your missed or late payments and their negative remarks
- Check for the active loans and credit cards account and see if you can consolidate them
- Organise paperwork relating to your accounts and keep the details in order so that you can track them easily

4. Dispute resolution process

Following given is the dispute resolution process that you need to take after you find errors in your credit report. These steps will help you to file a dispute with the credit bureau easily.

- Review your credit report carefully and identify the mistakes

- Contact your credit bureau to fix the errors in your credit report
- Review and submit the dispute form
- Wait for the credit bureau response to your credit report dispute
- Review the results of the investigation
- Check for updates in your credit report

The credit bureau generally takes 30-45 days to report the results back to you after receiving your dispute as they need to investigate and verify information with the furnisher. Make sure that you have all the proofs with you ready before you file a complaint.

So, by following the above-mentioned things, you will be able to keep a track on the information mentioned in your credit report which will, in turn, help you to take remedial actions on time by correcting what's wrong. Therefore, it is your prime responsibility to check your credit report and score consistently to stay away from errors that can hamper your credit score.

NPA :

India aims to become a $5 trillion economy by the year 2024-25 – and for this purpose it needs to expand its infrastructure capabilities exponentially. To support its infrastructure growth, a healthy financial sector – in particular a healthy banking sector is needed. The growth of any economy largely depends on its banking

sector (Liang & Reichert, 2006). An efficient banking system has to achieve three goals: profit, high-quality service to customers, and sufficient funds to lend to borrowers. Furthermore, a profitable banking sector also has more capacity to absorb shocks and provide relative stability to the economy. For this purpose, it is important to analyze the impact of bad loans on the performance of the banking sector.

NPA

A loan (and even a leased asset) that is not paid on or after the due date, and stops generating income for the lending bank is called a Non-Performing Asset (or NPA). In general, any loan instalment or EMIs that remain overdue for a period of 90 days or more are put into NPA category.

Growing Non-performing assets (NPA) may have a potentially significant impact on bank's profitability. RBI has defined NPA as those assets for which the principal or interest payment remains overdue for a period of 90 days. Within NPA there are 3 sub-category- substandard assets, doubtful assets and loss assets depending upon the number of days the loan has remained overdue. If assets are NPA for a period less than or equal to 12 months then it is a substandard asset. Similarly, a doubtful asset is defined as an asset which has remained as an NPA for a period of more than 12 months. The combination of the above three types of assets forms total NPAs in a bank. Through NPA, an asset becomes unproductive

and also the bank is unable to recover the initial loan amount. So while the earnings of banks fall as interest income falls, there is also the cost of capital erosion of banks. This means that banks have to keep a larger amount as provision to account for this NPA – which means there is impact on the future earning ability of banks. Non-performing loans have a negative impact on operating costs and cost efficiency of banks (Allen N.Berger, 1997). A rise in NPA beyond the risk threshold can have significant effects on the stability of bank, reducing consumer confidence in functioning of these banks.

Definition

NPA DEFINED

The asset classification is broadly guided by the RBI's Master Circular dated July 1st, 2015 which deals with 'Prudential norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances.' Accordingly a non performing asset (NPA) is a loan or an advance where;

i. interest and/ or instalment of principal remain overdue for a period of more than 90 days in respect of a term loan,

ii. the account remains 'out of order' in respect of an Overdraft/Cash Credit (OD/CC),

iii. the bill remains overdue for a period of more than 90 days inthe case of bills purchased and discounted,

iv. the instalment of principal or interest thereon remains overdue for two crop seasons for short duration crops,

v. the instalment of principal or interest thereon remains overdue for one crop season for long duration crops,

vi. the amount of liquidity facility remains outstanding for more than 90 days, in respect of a securitization transaction undertaken in terms of guidelines on securitization dated February 1, 2006.

vii. in respect of derivative transactions, the overdue receivables representing positive mark-to-market value of a derivative contract, if these remain unpaid for a period of 90 days from the specified due date for payment.

In case of interest payments, banks should, classify an account as NPA only if the interest due and charged during any quarter is not serviced fully within 90 days from the end of the quarter. Broadly speaking, classification of assets into above categories should be done taking into account the degree of well-defined credit weaknesses and the extent of dependence on collateral security for realization of dues. RBI has constantly asked the Banks to establish appropriate internal systems (including technology enabled processes) for proper and timely identification of NPAs, especially in respect of high value accounts. The banks may fix a minimum cut off point to decide what would constitute a high value account depending upon their respective business levels. The cutoff point should be valid for the entire accounting year. Responsibility and validation levels for ensuring proper asset classification may be fixed by the

banks. The system should ensure that doubts in asset classification due to any reason are settled through specified internal channels within one month from the date on which the account would have been classified as NPA as per extant guidelines

Causes for NPA

Before the financial crisis of 2008 India's economy was in a boom phase. During this period banks lent extensively to corporates in the expectation that the good times will continue in future. But future does not always play out as it had been in the past. The businesses of most of the corporates were adversely affected due to slowdown in the global economy following the financial crisis.

The ban in mining projects, and delay in environmental related permits affected power, iron and steel sector with added volatility in prices of raw material. All these factors weighed heavily on the earning of the corporates. Low earnings affected their ability to pay back loans. This is the one of the most important reason behind increase in NPA of public sector banks.

Another major reason of rising NPA was the relaxed lending norms for corporate houses.Their financial status and credit rating were not analysed properly. The banks were willing to accept higher leverage and less promoter equity. They even

accepted reports by the promoter's investment banks rather than doing their own analysis. Around 40% of the outstanding loans have been made to companies with interest coverage ratio less than one. Also, to stay competitive, banks were selling unsecured loans which contributed to the high levels of NPAs.

Public Sector banks provide major portion of the credit to industries and it is this part of the credit distribution that forms a great portion of NPA. In the case of kingfisher airlines financial crisis, SBI provided a huge amount of loan which it is not able to recover from it.

The priority sector lending (PSL) sector has contributed substantially to the NPAs. Priority sector includes agriculture, education, housing, MSMEs. As per the estimates by the SBI, education loans constitute 20% of its NPAs.

There are also cases of credit default by promoters, where the funds have been diverted by over-invoicing imports, sourced via, a promoter owned subsidiary abroad or exporting to shell companies and then declaring, that they defaulted.

Why NPAs occur?

Non-performing Assets (NPAs) are widely known as defaults or bad loans. Behind these defaults are causes that result in their increase in the numbers.

i. Bad Lending Practices

` When loans are given away by banks without doing a thorough background check of borrowers for their repaying capacity, financial health and intent to repay etc.

ii. Competition

When banks compete among themselves and as a result disburse unsecured loans.

iii. Incremental Component

When the internal bank management is affected such as the terms of credit, credit policy etc.

iv. Crisis

When the revenues and profits are observed lower than the average rate.

v. Overhang Components

When NPAs are an outcome of environmental factors like when the agricultural loans are not repaid due to the slow crop yield or lack of natural facts like rain, water, sunlight etc.

Impact of NPAs

Not just the books of accounts in a bank, NPAs impact a lot more than we think of. Check out the impact of NPAs in detail.

Depositors get lower returns on their investments and may also lose any uninsured deposits.

Borrowers have to pay a higher rate of interests on the loans to compensate bad loans.

Reputation of the bank's shareholders is negatively affected.

Increased failure due to bad investments and redirection of funds from good to bad projects.

Liquidity of banks is influenced.

IDENTIFICATION EXERCISE FOR BANK NPA The Statutory Auditors may consider the following exercise to dig out the hidden accounts which are shown as Standard but are required to be classified as NPAs. 1. Verification of Concurrent Audit / Internal Audit Report The first thing an auditor should do is to go through the Concurrent Audit/ Internal Audit reports. These reports will give the real insight of the functioning of the Branch. This will also give a fair idea of those loan accounts which are chronic, frequently irregular, overdrawn and where terms and condition of sanction are not complied with. From the list of such accounts an exercise can be made to ascertain new

NPAs accounts. 2. Screening of accounts Screening of accounts can give a fair idea of correct classification of advances of a Branch. Payment of interest at the end of each month may prevent a cash credit account from being classified as NPA account, but if the credits in the account are not commensurate with the limits sanctioned, then this may indicate diversion of funds , closure of business or a considerable fall in the business activity of the borrower entity. For e.g. if a borrower firm is enjoying a c.c. limit of Rs.100 lacs, then the credits in the accounts through sale proceeds should ideally be near to Rs.500 lacs (Working Capital limit being 20% of the turnover). If the credits are low then it could be a sign of stress and in that case an auditor should thoroughly look into the account and other details. In respect of irregular term loan accounts, the source of credit at the end of the month should be verified to ascertain that the credits are coming out of genuine sources. Similarly high value debit & credit transactions are also required to be seen as suspicious as the transactions may not reflect the correct value of sale & purchase. 3. Coding of accounts Identification of NPAs by the system itself solely depends on the parameters set in the system. In respect of agriculture advances the account is classified as NPA if the instalment of principal or interest thereon remains overdue for two crop seasons for short duration crops and for one crop season for long duration crops. But housing loans sanctioned for rural houses cannot be treated as agriculture loans. But while opening the loan accounts in the

computer system , if coding of such housing loans is erroneously done as the agriculture loans then the system can never identify such loans as NPAs on three continuous defaults in repayment of interest/ installments. It will wait for a default of 12 months to recognize these accounts as NPAs. 4. Restructuring of accounts Restructuring of accounts with out obtaining application from the borrower entity, without executing additional loan documents and with out ascertaining the future viability and cash generating capability of business may lead to classification of these accounts as NPAs. Accounts where restructuring is frequently done are also required to be classified as NPAs. Special care is to be taken in those accounts where change in repayment schedule in the computer system is done without actually restructuring the account . Core banking solution will never identify such accounts as NPAs. 5.Non achievement of DCCO For all projects financed by the banks , the 'Date of Completion' and the 'Date of Commencement of Commercial Operations' (DCCO), of the project is clearly spelt out at the time of financial closure of the project and the same is formally documented. These is also documented in the appraisal note by the bank during sanction of the loan. The statutory auditors should examine the DCCO in respect of term loan accounts . Non achievement of DCCO may lead to classification of the account as NPA. 6.Pending Review/Renewals Statutory Auditors should generate the date of renewals from the core banking software. Where limit sanctioned is over Rs. 25.00 lacs , in such cases

audited financials are required. A list of those borrower accounts should be prepared where audited balance sheet is not furnished. Renewal of limit without obtaining audited financials is not desirable. Regular and ad hoc credit limits need to be reviewed/ regularized not later than three months from the due date/date of ad hoc sanction. In case of constraints such as non--availability of financial statements and other data from the borrowers, the branch should furnish evidence to show that renewal/ review of credit limits is already on and would be completed soon. In any case, delay beyond six months is not considered desirable as a general discipline. Hence, an account where the regular/ ad hoc credit limits have not been reviewed/ renewed within 180 days from the due date/ date of ad hoc sanction will be treated as NPA. 7. Loss of Primary Security In respect of cash credit accounts it is stipulated to submit stock and book debts statement monthly/ quarterly. These statements are required to ascertain the availability of primary security at all the times. The drawing power is drawn based on the availability of these securities. Therefore in respect of cc accounts drawing limits are set to the extent of limit sanctioned or drawing power available, whichever is less. Hence the sanction limit can never be treated as drawing power. Banks should ensure that drawings in the working capital accounts are covered by the adequacy of current assets, since current assets are first appropriated in times of distress. Drawing power is required to be arrived at based on the stock statement which is current. However,

considering the difficulties of large borrowers, stock statements relied upon by the banks for determining drawing power should not be older than three months. The outstanding in the account based on drawing power calculated from stock statements older than three months, would be deemed as irregular. A working capital borrowal account will become NPA if such irregular drawings are permitted in the account for a continuous period of 90 days even though the unit may be working or the borrower's financial position is satisfactory. 8.Debit & Credit Entries of same value In respect of Cash Credit / Overdraft accounts, if the account remains "out of order" it is to be classified as NPA. As per RBI guidelines, the account should be treated as "out of order" if the outstanding balance remains continuously in excess of sanctioned limit / drawing power for 90 days. In cases where outstanding balance in the principal operating account is less than the sanctioned limit / drawing power, but there are no credits continuously for 90 days as on the date of balance sheet or credits are not enough to cover the interest debited during the same period, these accounts should be treated as NPA. It is observed that taking advantage of the above provisions, few superfluous Credit entries are passed in Cash Credit / Overdrafts accounts and the same are reversed within next 3-4 days. On passing such entry, the system appropriates the amount towards interest debited, showing no arrears of interest as per system and while reversing that entry it becomes part of the principal, showing the account as temporarily overdrawn, on the basis of

which the account is not shown as NPA. To locate such entries, it is necessary to view the statement of account and see whether there are any Debit and Credit entries of the same amount within a period of 3-4 days, and if so, the vouchers pertaining to such transactions can be verified to find the genuineness of the entries. 9.TOD in current and saving account Granting of TODs in current / saving account at the end of the month and then transferring funds from there to the overdue loan accounts is a very prevalent practice amongst the bankers. So any debit balance in current / saving account and TODs granted at the end of the month may be treated with extra care. If the funds are transferred from these accounts to overdue loan accounts , then such loan accounts are required to be classified as NPAs. 10.EDUCATION LOANS/ HOME LOANS The recovery trend in education loans is not very encouraging. There is steep rise of NPA accounts in this segment. There is common practice of restructuring these accounts to save their slippage to NPA category. Quite often restructuring is done without ascertaining the employment particulars of the borrower. Any restructuring done without appropriate justification and without documentation should not stop the auditor in classifying these accounts as NPAs. Similarly home loans accounts, which are over 10 years old & where principal outstanding is still over 50% of the loan amount sanctioned, such accounts may be screened carefully. OTHER POINTS FOR CONSIDERATION IN ASSET CLASSIFICATION BY BANKS: Following points can also be

useful to a Statutory Auditor while certifying the assets classification : ♣ Availability of security / net worth of borrower/ guarantor The availability of security or net worth of borrower/ guarantor should not be taken into account for the purpose of treating an advance as NPA . ♣ Accounts with temporary deficiencies The classification of an asset as NPA should be based on the record of recovery. Bank should not classify an advance account as NPA merely due to the existence of some deficiencies which are temporary in nature such as non-availability of adequate drawing power based on the latest available stock statement, balance outstanding exceeding the limit temporarily, non-submission of stock statements and non-renewal of the limits on the due date, etc. ♣ Accounts regularized near about the balance sheet date The asset classification of borrowal accounts where a solitary or a few credits are recorded before the balance sheet date should be handled with care and without scope for subjectivity. Where the account indicates inherent weakness on the basis of the data available, the account should be deemed as a NPA. In other genuine cases, the banks must furnish satisfactory evidence to the Statutory Auditors/Inspecting Officers about the manner of regularization of the account to eliminate doubts on their performing status. ♣ Asset Classification to be borrower-wise and not facility-wise Where a borrower entity is enjoying different kind of credit facilities, then asset classification is to be done borrower wise and not facility wise. Therefore, if one account of the borrower is

classified as NPA, all the facilities granted by a bank to a borrower will have to be treated as NPA and not the particular facility or part thereof which has become irregular.

Banking NPA Solution & Role of RBI

GoI is struggling to come up with solutions thus it set up inter-creditor agreements to speed up resolution under the Insolvency and Bankruptcy Code (IBC). It proposed a combination of a bank-led asset management company, alternate investment funds, and a platform to auction bad assets. To comprehend the scenario, as per estimate, there are nearly Rs 12 lakh crore of stressed assets in the country’s banking system.

The stressed asset constitutes 15 percent of the outstanding loan books of these banks. Banks have sold around Rs 2 lakh crore worth of such loans to asset reconstruction companies (ARCs), leaving about Rs 10 lakh crore on their own books. In such a scenario, the RBI direction on referring companies to the National Companies Law Tribunal (NCLT) could help tackle the NPA menace to a great extent. While the action plan details are being worked out, the process has already been initiated for a few cases.

As per the estimates, more than 70 percent of these cases will be restructuring and resolutions wherein the debt will be written down to sustainable levels. It is estimated that around Rs 40,000-50,000 crore of additional capital will have to be infused to make these companies perform efficiently again. This will be infused by a mix of existing promoters, ARCs, stressed asset funds, and private equity (PE) investors. These investors will also drive the turnaround for these companies through stronger management.

Ways to Reduce NPAs

The Indian banking system is reeling under a glut of Non Performing Assets (NPA's). The unpaid debts of Indian corporations and households have risen to alarming levels. High level bureaucratic meetings are being held to get rid of this menace. Nonperforming assets could appear on the balance sheet of banks. This could cause a ripple effect as fears that one bank is unstable makes the entire banking industry unstable. Hence it is absolutely imperative that these bad debts be taken off the books immediately.

It is high time financial institutions must take some serious steps to control the unstoppable rise in the number of NPAs. Unless strict ways to reduce NPA are introduced, they will keep piling up and will be an alarming economic concern.

1. SARFAESI ACT, 2002

The SARFAESI empowers banks to deal with NPAs, without the involvement of court, through three alternatives:

Asset Reconstruction

Enforcement of Security

Securitisation

Any outstanding amount of more than ₹1 lakh can be dealt under SARFAESI. However, an amount that is less than 20% or principal and the interest amount is not considered under the Act. The Act also allows banks to:

To release a notice to borrower (and their guarantor) asking them to release the payment within 60 days from the receipt of notice.

To release notice to anyone who acquires the borrower's secured assets to produce the same to the bank.

To advice any of the borrower's debtors to pay off the loan due with the bank.

In case of failure from the borrower's end with respect to the issue notice, the bank may:

Take possession of the secured assets of the borrower

Sell or lease the security

Manage the borrower's security or appoint someone to manage the same.

2. Debt Recovery Tribunals

The Debts Recovery Tribunals (DRTs) and Debts Recovery Appellate Tribunals (DRATs) were established under the Recovery of Debts and Bankruptcy Act (RDB Act), 1993 with the specific objective of providing expeditious adjudication and recovery of debts due to Banks and Financial Institutions. Brought into being existence in year 1993 by the Indian Parliament, the Act allows financial institutions to speedily recover dues of ₹10 lakhs and above. DRTs are capable of handling larger number of cases as compared to regular courts by cutting down delays in the initial proceedings.

The main objective and role of DRT is the recovery of funds from borrowers which is payable to banks and financial institutions. The Tribunals power is limited to settle cases regarding the restoration of the unpaid amount from NPAs as declared by the banks under the RBI guidelines.

Debts Recovery Tribunal may, from time to time, extend the said period for reasons to be recorded in writing, so, however, that the total period of pendency of the application with the Debts

Recovery Tribunal, shall not exceed four months from the date of making of such application

Debt Recovery Tribunals (DRTs): Background

Bad loans and Non-Performing Assets (NPAs) are a perpetual source of trouble for banks in India. This was an acute problem in the period before 1993, as such cases were listed in civil courts where the proceedings used to drag on for years.

In 1993, the Recovery of Debts due to Banks and Financial Institutions (RDDBFI) Act was passed which led to the establishment of Debt Recovery Tribunals (DRT) to facilitate the debt recovery involving banks and other financial institutions.

The Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act passed in 2002 also provides access to DRTs.

Recovery of Debts due to Banks and Financial Institutions (RDDBFI) Act

The RDDBFI Act provides speedy redressal to lenders and borrowers through the filing of Original Applications (OAs) in Debts Recovery Tribunals (DRTs) and appeals in Debts Recovery Appellate Tribunals (DRATs).

What are Debt Recovery Tribunals (DRT)?

DRTs and DRATs are established by the Central Government and consist of one person each referred to as the Presiding Officer of the Tribunal and the Chairperson of the Appellate Tribunal respectively.

DRTs are empowered to go beyond the Civil Procedure Code and pass comprehensive orders. It can hear cross-suits, counterclaims and allow set-offs.

DRTs were empowered to adjudicate claims equal to or greater than ten lakh rupees. This limit was raised to twenty lakh rupees in 2018.

After adjudication, the DRT issues order and Recovery Certificate, certifying the amount payable by the borrower. This is executed by Recovery Officers as per the procedure for recovery of income tax.

There are 39 DRTs and 5 DRATs at present.

Jurisdiction of Debt Recovery Tribunals

DRTs can entertain applications from banks and financial institutions for recovery of debts which are due to them.

The banks may make an application to the Tribunal within the local limits of whose jurisdiction the defendant resides or carries on business.

The Act bars all other Courts from the adjudication of matters relating to debt recovery apart from the Supreme Court and High Court.

Proceedings of Debt Recovery Tribunals

Banks need to make an application to the DRT which has jurisdiction in the region in which the bank operates and pay the required fees.

The defendant shall present a written statement of his defense before the first hearing and set up a counter-claim during the course of the hearing.

The Tribunal may, after giving the applicant and the defendant an opportunity of being heard, pass such interim or final order.

The interim order passed against the defendant can restrict him from disposing or transferring his property without the prior assent of the Tribunal.

DRT after hearing both the parties and their submissions would pass the final judgment within 30 days from hearing. DRT will issue a Recovery Certificate within 15 days from the date of judgment and pass on the same to Recovery Officer.

The Tribunal may direct the conditional attachment of the whole or any portion of the property specified by the applicant.

The Tribunal may also appoint a receiver and confer him all powers to defend the suit in the court and to manage the property.

Where a certificate of recovery is issued against a company registered under the Companies Act, 1956 the Tribunal may order the sale proceeds of such company to be distributed among its secured creditors.

Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act (SARFAESI), 2002

Even after the enactment of the RDDBFI Act, problems like lack of liquidity, asset-liability mismatch, and long-term blocking of assets persisted. Banks could not recover their dues to the extent expected even after the constitution of DRTs. This led to the enactment of the SARFAESI Act in 2002.

This Act provides access to banks and financial institutions covered under the Act for recovery of secured debts from the borrowers without the intervention of the Courts at the first stage.

When a loan is classified as a Non-Performing Asset (NPA), a notice is sent to the borrower. If the borrower fails to comply with it, then the creditor is entitled to take ownership of the secured asset including the right to transfer the asset.

The transition into DRTs happens when the collateral asset is not sufficient enough to fulfil obligations to the creditors. In such cases, the creditors may file an application to the DRT for the recuperation of the rest of the part of the dues.

Issues with Debt Recovery Tribunals

Most DRTs are over-burdened with some Tribunals in major cities handling far more cases it can ideally handle at a given time. This is adversely affecting the success rate of the Tribunals.

DRTs got tangled with peripheral issues such as state dues, dues of workmen, etc.

Borrowers also tend to adopt delaying tactics by filing claims against lenders in civil courts.

Some courts have interpreted some provisions of the Act to be in favour of debtors and invoking principles of natural justice to protect debtors.

DRTs are not equipped to deal with complex questions of law and evolving methods and techniques of committing fraud.

Less than 40 DRTs are established right now and they are not sufficient to handle the large volume of cases arising across the country.

Corrective Measures connected with DRTs

Amendments made to the RDDBFI Act in 2016

It provides time limits in the various steps of the adjudication process.

Central Government is empowered to uniform procedural rules across all DRTs and DRATs.

Increasing the retirement age of Presiding Officers and Chairpersons.

Banks to file cases in DRTs having jurisdiction over the area of the bank branch where the debt is pending, instead of the defendant's area of residence or business.

Insolvency and Bankruptcy Code give powers to DRTs to consider cases of bankruptcy from individuals and unlimited liability partnerships.

The rising NPAs and debt issues are hurting the banking industry and the economy as a whole.

3. Lok Adalats

Small loans of ₹5 lakhs and less can be recovered through the Lok Adalats as per the guidelines issued by RBI in year 2001.

This alternative for dispute redressal mechanism covers both suit and non-suit filed cases.

4. Compromise Settlement

This scheme helps in recovery of NPAs up to ₹10 crores through a simplified non-discretionary mechanism.

5. Credit Information Bureau

Third party agencies such as CIBIL helps banks with data on the financial health of the borrower. The Credit Information Bureau maintains records of individual defaulters and shares it with the respective banks to aid them in making effective lending decisions. For this, banks may be charged a fee.

6. An Asset Reconstruction Company is a specialized financial institution that buys the NPAs or bad assets from banks and financial institutions so that the latter can clean up their balance sheets. In other words, ARCs are in the business of buying bad loans from banks.

Asset Reconstruction Companies (ARCs) have been created under a special statute SARFAESI Act, 2002 as an institutional framework for acquiring NPAs (non-performing assets) from banks and other financial institutions. They are registered with and regulated by the RBI. The only permissible business for ARCs is asset reconstruction and related activities.

There has been an exponential growth in NPAs of banks with the present level at around Rs 9 lakh crore. Banks try to resolve the NPAs through various measures like resolution both within IBC and outside. They also seek settlement with the borrower or enforcement through DRT and SARFAESI.

Functions of Asset Reconstruction Company (ARC)

As per RBI Notification No. DNBS.2/CGM (CSM)-2003, dated April 23, 2003, ARC performs the following functions:-

(i) Acquisition of financial assets (as defined u/s 2(L) of SRFAESI Act, 2002)

(ii) Change or takeover of Management / Sale or Lease of Business of the Borrower

(iii) Rescheduling of Debts

(iv) Enforcement of Security Interest (as per section 13(4) of SRFAESI Act, 2002)

(v) Settlement of dues payable by the borrower

Asset reconstruction companies are in the business of buying bad loans from banks. For instance, if a bank lends money to a person or company, they expect to receive periodic

payments of principal and interest. However, when they do not receive those periodic payments for an extended period of time, (let's say 90 days) these loans are classified as nonperforming assets. If these NPA's are allowed to stay on the bank's balance sheet, they erode investor confidence in the bank.

Hence, banks sell these bad loans to specialists called asset reconstruction companies. The business of these companies is to buy bad loans from banks at a steep discount. These companies then take special measures to recover the money owed. If they are able to recover the money, they make a profit, if not they lose the money.

Impact on NPAs on Banks

The increasing NPAs not only reduce the profitability of banks but also affect its credibility. In fact the massive amount of NPAs with commercial banks is threatening to erode half of the capital base of public sector banks.

Once a bank started incurring losses and if the fundamentals are not corrected, the problem may become chronic and destabilize the confidence of the depositors. Once the depositors start withdrawing their money from the banks, the banking system will collapse. It is because of this reason that NPAs must always remain within the sustainable limit and the current level of NPAs is threatening the stability.

Higher amount of NPAs also pressurise banks to decrease the interest rate on saving deposits to increase the margin. Already there is a gap between interest rate on bank savings vis-a-vis savings in other non-banking accounts like PPF, post office saving schemes etc. Further, several mutual funds are providing returns of more than 10%. Further diversion in interest rates will divert the funds from banking sector to non-banking sector further eroding the capital with banks.

The impact of rising NPAs can be as follows: Rising NPAs undermine the bank's image, making the public lose trust in banks. The depositors may withdraw their deposits causing liquidity issues for banks. The lack of liquidity prevents banks from lending for other productive activities in the economy.

Higher NPA translates into lower profits for banks as it reduces the interest income and also causes capital erosion. Thus, the increasing NPAs pose long-term threats to the stability of banking sector.

Impact of NPAs on Industry

The credit growth to the industrial sector was higher as compared to the GDP growth and over credit growth during the period 2006-11. As a result, the proportion of NPAs in industrial sector was much higher vis-à-vis other sectors. Consequently, in the later phase, banks were reluctant to fund the needs of

industrial sector hampering its growth. In fact, in some cases like that of the Micro, Small and Medium Enterprises (MSME) industry, credit actually shrank.

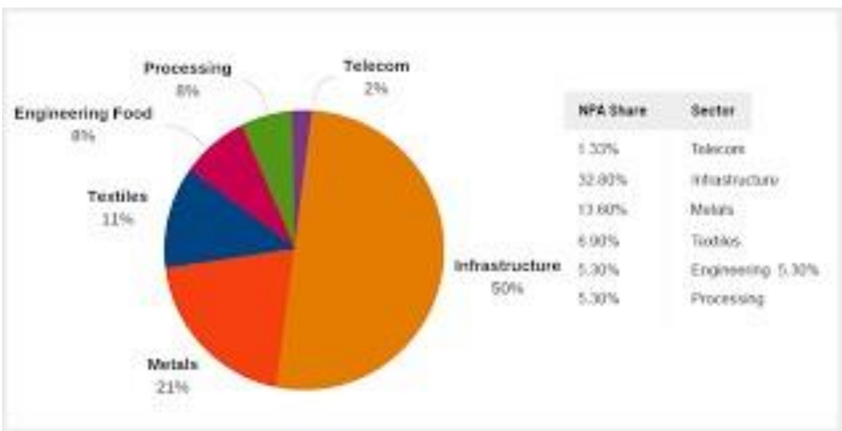
The slowdown in growth in post-demonetization period also resulted in reduced profitability of the manufacturing sector which further prompted the banks to stall the credit growth to the industrial sector. In the long term, the shortage of funds to the industrial sector will affect the growth of the industrial sector.

After 2014-15, the credit growth to the industrial sector is least as compared to the credit growth to the agriculture and service sector. The continuous shrinking of credit to industrial sector is detrimental to not only industries but overall economy as well.

Impact on Indian Economy

Strong banking sector is one of the most significant prerequisite of strong economy because it channels the savings into the investment. A fragile banking sector will ultimately give way to the fragile economy.

The major sectors of the Indian economy contributing to the NPAs are as under –



It is clear that infrastructure accounted for biggest chunk of NPAs. Because of massive amount of NPA in infrastructure, the banks are now reluctant to fund this sector. As the infrastructure is one of the most important sectors in economy which fuels the growth of other sectors, draining of resources to infrastructure may hamper the growth of Indian economy.

Among the other sectors, food processing also accounted for 5.3% of total NPAs. Food processing is one of the most employment intensive industries and its growth also pushes the growth of agriculture. Any loss to the food processing industry will ultimately percolate to the employment as well as agriculture sector.

Other sectors will also directly or indirectly affect the overall economic scenario due to the exposure to the bad loans. Hence, the issue of NPA must be resolved on urgent basis.

NPA plays an important role in every economic condition and also the main cause of the increase in the current account deficit. Interest rates, Loan, Housing Loans, CRR, SLR all are directly affected by the system.

Conclusion

Government of India is trying hard to rescue the banks, particularly looking at the downfall of PSBs in the country. Recently, the centre had announced recapitalisation of PSBs with ₹2.11 lakh crores. However, there is still a strong need felt for stricter laws in NPA management. Wilful defaulters particularly must be treated under a separate, dedicated Act. Moreover, there must be rigorous practices adopted to take correct decisions for granting loans to individual borrowers or companies.

****

Prepared by

Dr.B.Revathy
Dean of Arts
Professor and Head
Department of Commerce
Manonmaniam Sundaranar University
Tirunelveli – 627 012