

CHAPTER

I



CHAPTER I

Introduction- Importance, Scope, object of study

1.1 Introduction:

Most of the developing countries of the world today are concerned with the crises of unemployment and underemployment, and the political leverage. For removing unemployment and creating job opportunities for the millions of jobless people, various countries have come up with various tools and instruments. One such instrument, which emerged in the Western countries got nurtured in the countries like Japan and was adopted by the countries like India, is of Financial Corporations.

In India, the financial institutions have been playing a promotional role in the field of industrial development of the country. In the developing country like ours financial organizations have no substitute and therefore different face of our economy financial corporations have been playing a very effective role. In banking sector its role is also significant. Financial corporation is one of the institution provides assistance in the form of underwriting and or direct investment. If this function is not performed, then the institution is called just a finance corporation or term lending institution.

Like any other business organizations, banking organization, also faces certain problems like deposit mobilization, recovery management etc. Here we have study of the recovery of loans and advances of Maharashtra State Financial Corporation- Regional Office, Kolhapur.

1.2 Meaning of Recovery:

Financial organizations give loans and advances to the individuals or various industries for surviving the industry or doing any legal type of business. The organization gives loan facilities on time limit. These loans are given to customers under three categories-

- a) Short term loans
- b) Medium term loan
- c) Long term loan

The period of short term loan is one to two years. The period of medium term loan is five to ten years. The period of long term loans is up to twenty years or even more.

When above loan given by the corporations is not refunded by the customers/ borrowers, in time, at that time the problem of recovery occurs, and if the corporation fails to recover its dues from borrowers either directly or through the court then the problem of recovery arises.

Credit is a very scarce resource, particularly into a country like India, where poverty, unemployment and double light inflation are pervasive phenomena. In a prudential economy both lending and recovery are considered to be two side of the same coin. While, inadequate and improper allocation of credit endangers the basic socio-economic philosophy of the country, mounting of over dues of credit endangers the very foundation on which the banking system rests. The timely recovery of funds lent, is a prerequisite for the continuous recycling of funds. Stock-piling of over dues results in poor recycling of funds, which in turn has many effects on the utilization of credit. That is non repayment of loans by the borrower lead to blocking up of funds in the hands of a few and ultimately the benefits of credit cannot be passed on to a large section of people who are in the need of credit. On the other hand mounting of over dues weakens the corporate strength of the credit agencies. Sometimes, the problem of over dues threatens the liquidity position of putting the financial planning and decision making in disarray. Then once a loan is arrears, collection of such a loan becomes a difficult and an uneconomical task. Therefore, judicious paying of credit and also timely repayment of credit are very important for the healthy and effective functioning of financial corporations system.

1.3 Procedure of Recovery:

When recovery problem arises to the banks or financial institutions like Maharashtra State Financial Corporation (MSFC), then one of the following steps are taken by the corporation for its recovery:

- a) Postal reminders
- b) Go on personal visits
- c) Try to arrange payment through marketing agency.
- d) Take help from guarantors.
- e) Seek help from block revenue authorities
- f) Remind the borrower through his neighbours
- g) Send reminder through the borrowers.

Each of the above recovery measures may be set with a number of problems, but a concerted effort by the institute may bring fruitful results. Some of the problems faced in the recovery are:

- a) Non availability of borrower
- b) Missbehaviour of the borrower
- c) Weak explanations and presumptions by the borrower
- d) Refusal by the borrower to accept registered postal reminders.
- e) Local leaders interference
- f) Selling of hypothecated goods
- g) Borrowers demand for more loan for wasteful expenditure
- h) Inaccessible villages

Some of the following steps can be taken towards recovery:

- a. Approach the borrower through governmental agencies.
- b. Contacting the guarantors
- c. Approaching through marketing agencies
- d. Seeking the interference of influential and honest persons of the village.
- e. Seeking the help of friends and relatives

If all these fail in recovery of the loan, the only course left is “legal action” i.e. through court.

1.4 Causes of Default:

“For every action there is equal and opposite reaction”, this is one of the laws of physical science and this applies ailing loans too.

The causes of default are classified as:

- a. Uncontrollable causes and
- b. Uncontrollable causes

The uncontrollable causes are beyond the human control and are unforeseen where as controllable causes can be controlled to some extent, if not full, if detected in time.

In every financial institute, credit operation depends on three factors:

- a. Financial institute
- b. The borrower
- c. The enterprise which the borrower runs

The credit availed of from institute, client of earning of a profit sufficient to bring him an income to earn his living as well as to pay of the installment of loans.

- a. **The financial institute:** The institute should never lend without studying a proposal carefully or without following the age old credit rating tests. The set norms are these only to safeguard the interest of the institute. During times of crises it is absolutely necessary to ascertain market views of securities offered to various loans.
- b. **The borrower:** The character, capital and capacity of the borrower are the three pillars on which stands entire financial institute credit. Any of three pillars become weak, makes the entire credit operation shaky. The borrower before availing of the credit facility pretends to be very honest, polite and polished on several occasions; subsequently he has proved to be a rank to cheat. Those who are honest may become dishonest because of the compelling circumstances. A person may be very honest but in the absence of experience, competence and skills, managerial, organizational and entrepreneurial the humans may fail resulting into losses.

c. **The enterprise which the borrower runs:** Lack of skills in managing the business will reflect in faulty financial planning, resulting in the following situations:

1. Underestimation:

Inaccurate estimate of cost of project results in underestimation of the financial needs causing shortage of working capital.

2. Over ambition:

Floating new ventures or expanding the existing ventures without having sufficient base of backing or foresight which is often calling over trading.

3. Mismanagement:

The term mismanagement means of the funds by over timing sales, profits of the short term finance being used for long term capital needs and being at the mercy of the creditors for short finance.

4. Over investment:

Heavy investment in fixed asset which is out of proportion to the earning capacity of the enterprise or locking up funds in building up large inventory causing shortage of liquid funds.

Following are the main causes of default:

- 1) **Lack of contacts with officials:** In that operation there is not contact between defaulters and official staff, i.e. recovery officers. The institutes were simply served with the notices of demand for repayment of loans and advances but there is no direct connection between the defaulters and officials.
- 2) **Specific cause:** Postponement of repayment without any special reason- In this point it is observed that lack of prompt and effective action on the part of officials was mainly responsible. For the most of the officials was mainly responsible for most of over dues recorded by the borrower of this category.
- 3) **Failure of project:** Some defaulters reported to have failed their loans because of failure of projects, which they had launched with the funds borrowed from the institute. It was the defective and hasty formulation of the schemes that was

reported to be mainly responsible for the failure of projects and the consequent liability of the schemes to generate sufficient additional incomes for the redemption of debts.

- 4) **Expectations:** Some defaulters have failed to repay their loans on account of their expectations of declaration a moratorium on the credit raised by them.
- 5) **Insufficient income:** The additional income that was generated as a result of investment of credit was diverted mostly for private consumption needs from borrowers and not much was left out for the repayment of loan.
- 6) **Unsuitable repayment schedule:** The repayment of loan was highly faulty and the time chosen for one repayment of installments was also quite unsuitable. It was also pointed out that the timing of payment of installment was not in agreement with timing generation of income and in some cases the amounts of installments demanded from the borrowers were also rather comparatively higher than the amounts of surplus income which the investments would generate. So the unsuitable repayment schedule resulted in the inability of the borrowers to keep up their promises in the matter of repayment and naturally they became defaulters.
- 7) **Other causes:** Some defaulters could not repay their loans because of their pressing engagements and commitments such as celebration of social ceremonies, repayment of old debts raised from private credit agencies.

1.5 Importance, scope and limitations of the study:

The importance of such study lied in their potential strength of bringing about the results which would indicate the quantitative performance and the drawbacks if any, in the working of the corporation. These results need not necessarily resemble in all the aspects with the results elsewhere, but they certainly indicate the trend of the working about recovery of loans of the corporation. Hence, the present study will help the corporation to know the performance about recovery of loans and advances of regional office, Kolhapur.

Scope of study:

The 'Maharashtra State Financial Corporation' very well known as MSFC, Regional office, Kolhapur is selected for studies. Under the regional office of Kolhapur there are three districts i.e. Kolhapur, Sangli and Satara. MSFC provides loans to small scale industries.

The present study is related with the recovery of difficulties of loans and further it throws light on recovery management of the corporation. The recovery problem arises due to the non repayment of loans and defaulters.

Limitations of the study:

The officers of the corporation are very co-operative and having academic bent of mind because of their schedule they could not be made available more than one time for the purpose of study.

Most of the information utilized for the study purpose is obtained through inspection of corporation's office record instead of visiting the defaulters personally as they were reluctant to furnish the required information, this could be form into limitation of the study.

1.6 Objectives of the study:

- 1) To examine the policies and procedures of loans and advances.
- 2) To examine the post sanction follow-up and supervision of loans and advances.
- 3) To measure the magnitude of outstandings in relation to loans and advances sanctioned.
- 4) To examine the rate of recovery and changes in these rates over the period.
- 5) To understand the problems and of recovery of loans and advances.
- 6) To suggest the measures to solve the problems of recovery of loans and advances.