

Chapter 3

Loans and Advances

3.1 Introduction

3.2 Types of Loans and Advances

3.3 Conditions of Sanctioning Loans

3.4 Margin money

3.5 Security

3.6 Procedure Of Granting Loans

3.7 Opinion Survey of Borrowers

3.8 Observations

Chapter 3

LOANS AND ADVANCES - PROCEDURAL ASPECTS

3.1 Introduction

In 1955 'State Bank of India' was established to create banking facilities in rural and semi-rural area. In 1969, 14 major commercial banks were nationalized which helped to spread banking facilities to the rural areas and provide finance to neglected sector of the economy like agricultural, small business etc. and mobilizing saving. The Banking business in the past was in the hands of private banks owned mostly by industrialists in the urban areas and money lenders functioning in the rural areas. There was uneven spread of banking business in the country. With a view to regulate neglected sectors of economy like agriculture, small business etc.

Before 60 years, the financial needs of the people were largely supported by private money lenders. They were charging high rates of interest and exploiting the borrowers through number of malpractices. During this period co-operative banks were established in certain areas with the main objectives of calculating in the habit of theft among its members and extracting them from the clutches of money lenders. These co-operative banks used to give loans and advances to middle and lower income groups.

Initially, co-operative banks provided loans to consumption purpose and many other sectors from the community, such as small scale industries,

trade, commerce etc. always reminded among from the banking sphere.

The bank taking active part in respect of loans and advances, according to its bye-laws. The Reserve Bank of India introduced lending policy to bank to make optimum use of their resources in loans and advances, which would also improve the profit of bank. Initially, bank's confide itself to meeting consumption requirements, later, it followed a diversified lending policy by providing financing for better business, better living and it has helped many industrial units to improve there operational performance.

The banks main objective is provide loans to common people and help them to escape from the clutches of money lenders. Bank also provided loans to various needy persons for various purposes.

3.2 Types Of Loans And Advances

Banks are commercial enterprises. Therefore ; they are always busy in earning profit. Either deposits are mobilized or kept idle in stock room or these deposits are to be used to given ' Loans and advances '

The following are the main advances given by the bank.

a. Cash Credit

Cash credit is an arrangement by which the banker allows its customers to borrow money upto the certain limit. Cash credit arrangement are usually made against security of commodity hypothecated or pledged with the bank.

Cash credit facility is extended to manufacturing industry and business concern to meet working capital requirement. These document

create pledge hypothecation over the goods, book-debts and other current assets of the borrowers. The borrower can draw up to the extent of drawing power against the value of stock.

b. Overdraft

The customer is permitted to draw up to the sectioned limit. It is running, open and mutual account, the customer need draw only up to the required by him.

Interest is applied on overdraft every quarter on the last working days. Overdraft is extended on facility for the temporary requirement of the customer. Customer is not burdened by the interest component. He has to pay interest on account actually he has borrowed. He can also deposits the amount in the loan account. Whenever he has the excess money.

c. Term Loans

Term Loan is loan granted for the purpose of acquiring on asset which repay from the income generation of the assets. There are two types of term loan.

Long Term Loans

In this type of loan the repayment is spread over more than three year. This is generally given to acquire high value of assets.

Short Term Loans

In this type of the loan the repayment period is between 12 months to 36 months.

Purpose Of Loan

The bank sanctions loans and advances to its members for various purposes mainly agricultural and allied activities, educational, domestic, consumption, house construction and repair purpose, transport and other purpose.

a. Agricultural And Allied Activities Purpose

The bank sanctioned loan and advances mainly for agricultural and allied activities as well as water pipe-line, poultry, dairy, animal husbandry, fisheries, purchase of electrical motors etc.

b. Cottage And Small Scale Industrial Purpose

The cottage and industrial unit means a units engaged in manufacturing, processing, preservation or serving activities involving utilization of locally available natural and human resources normally undertaken by the beneficiaries in their homes on small scale.

c. Loans for professionals and self employed

The bank tries to solve the unemployment problem by financing loans to educated unemployed and self-employed persons and professionals such as Doctors, Lawyers, Chartered Accountants etc.

d. Commercial Purpose

Under the bye-laws of the bank, the bank sanctions loan for various commercial purposes such as small businessmen, small traders etc.

e. House construction and repair purpose

The bank sanctions loans and advances for house construction and repair purpose such as construction of new house, repair of old one etc. The amount of advances depends on the needs of the customer. The amount of advances is decided on the basis of the yearly income of the customer. Generally, it is 8 to 10 times of yearly income of the customers. While granting the loan the related documents of flat, plot house etc. are verified by the banker, lawyers and office. This is called "Search report".

f. Transport Purpose

The bank has sanctioned loans for purchasing of vehicles especially to young, educated unemployed members.

g. Personal consumption purpose

The bank sanctioned loans to individual members for marriage, repayment of old debt religious and traditional ceremonies etc.

h. Educational Purpose

Under this purpose the bank has sectional loans and advances to the poor but intelligent and needy students. This loan is granted to the students who prefer to higher studies.

Repayment of such loans is between 3 to 7 years which starts after completion of studies.

3.3 Conditions Of The Sanctioning Loan

1. The borrower, guarantors, acceptors are jointly and severally responsible to repay the loan within time.
2. Insurance policy of stock in hand should be assigned in favour of Bank by the borrower and policy is retained by Bank.
3. Rate of interest may be changed by the Bank without any pre-intimation.
4. The Bank has preferential right on the movable and immovable property of borrower and acceptors.
5. Bank has a right to inspect hypothecated goods. Any officer or employee of Bank can surprise make a check the stock of borrower.
6. The loan amount must be used for the purpose for which it was availed.
7. If the borrower is owner of any land he should give a declaration as prescribed by law, if the declaration not given previously. However, he should also give mortgage of double the loan amount in favour of Bank on his owned house if not given previously in the prescribed form of Grampanchayat / Municipality.
8. If the borrower does not fulfill the above rules or the Bank is not satisfied with the transactions of overdraft account, the Bank has a right to reduce the credit amount sanctioned and may demand the repayment of the outstanding amount with interest. If the Bank has sufficient reason to believe that the loan amount is not utilized for the purpose for which it was sanctioned or borrower has disposed off the hypothecated goods, then Bank has a right to recover the goods.

9. Bank has a right to modify/ cancel/ add any condition to the above mentioned without any prior notice. If Bank is not satisfied with the transaction of borrower Bank has a right to demand full amount of loan including interest.

3.4 Margin Money

As the prices of all kinds of securities are liable to fluctuations, and vary according to their nature and as the amount of money availing to the banker is likely to increase by the accrual of interest and other charges payable by the borrower, it is evident that no banker should advance an amount equal to the full market value of the securities offered. It is necessary that lending banker should insist upon getting securities worth more than the amount of the loan or overdraft he is called upon to grant. This difference, between the market value of securities and amount against them, is known as margin.

The margin depends upon the class to which the securities offered belong, as also to certain extent, upon the credit of the customers. For instance, in case of an advance against gold bullion, in a gold standard country, a banker in normal times may be satisfied with a margin of 5 percent as the price of gold in gold standard countries is ordinarily very steady. However, when the monetary standard of the country is not gold and the price of gold fluctuates a great deal, as it is happening at present in India a bigger margin than 5 percent should be insisted upon. Similarly as the price of silver, or silver ornaments. In a silver standard country, the position perhaps just to reverse of that stated above and therefore, a banker in that country will be satisfied with the smaller margin in the case of silver than

that in the case of gold. In normal times, in the case of gilt-edged securities, a margin of 10Percent is generally considered. As they fluctuate daily the prices of gold and silver are beyond the control of everyone. Hence, the valuation of gold by a recognized valuer appointed by Bank is done and upto 75Percent valuation of loan amount is sanctioned.

In case of goods and documents of title of goods, the margin varies more or less according to the extent to which their price are liable to fluctuations a great depends upon the nature of goods and commodities and the condition of the market for the particular offered. If goods are of a perishable nature, the banker may accept them, provided they are saleable and the advances against them are for very short periods. In case of durable and consumable products Bank has various policies in case of hire purchase or hypothecation. Polices differs from person to person and depend on the product of which he is willing to pay the margin money considerably varies to product to product.

3.5 Security

Bank provides loans against securities. The amount is mainly depend upon the generators as well as security, security takes an important part of sanctioning loan.

The list of such securities of loans and advances are given below.

1. Loan against Properties

The bank provide loans against the properties. The properties are like owned house, car or vehicle, bank deposits etc.

2. Long against personal guarantee :

Bank also accept personal guarantee and as security and provide loans who fulfills the conditions of personal guarantee.

3. Loan against cash-credit

Bank provide loans against cash –credit to the needy borrowers.

4. Overdraft secured Loan

Bank also provide secured loans threwh overdraft facilities to their members.

5. Loan against silver and golden ornaments

Against silver and golden ornament, the bank provide loans to needy borrowers.

6. Hire purchase loan

Bank provides loan for hire purchasing he mainly for moveable property. In the case of hire purchasing the actual security/ goods are not under the charge of the bank but the ownership of the goods belongs to banks still the last installment paid by the borrower.

7. Hypothecation Loan

Loan provided by bank to facilitate and expansion existing business by mortgaging any movable property to the bank is termed as hypothecation.

It is not necessary to acquire the same asset by mortgaging that particular assets. It is generally long term nature and provided to acquire or

create a new assets. The ownership of the mortgaged the property rate with the bank and allowed to use that assets for running his business.

8. Loan against the mortgage of goods

In this type of security also the goods are actually not in the charges of bank. It was at the godown and still just installment of the loan, the goods are actually belong to the bank.

9. Loan against fixed deposits

Bank accept fixed deposits as security. It is very safe or secured for bank to provide such loan. It is also beneficial for the borrower. The borrower can enjoy the cash as well as the interest on the fixed deposits.

10. Loan against recurring deposits

It is facility provided by bank to small investors generally individuals. Who are saving their income per month fixed amount deposited in recurring account maintained by the bank. In case of need of money or funds they are allowed to withdraw up to 85Percent of amount standing to the credit of their recurring deposits account. Bank generally charge a 2Percent higher than interest rate on given on recurring deposits for this type of loan. There is no compulsion to repay the loan during the tenure of loan. After maturing R.D account bank transfer amount equivalent of loan account from recurring account and access of if any refunded to investors.

11. Loan against provident fund

Bank provide loans to their employees against provident fund as per their need.

12. Loan against household goods

Bank provide loans against the household goods with the security of valuable goods bank provide loans to the people.

13. Loan against bills

Bills are also like a promissory note for the future money. So with the security of such bills the bank provide loans to the people.

3.6 Procedure For Granting Loans

The following are the step in the procedure of bank to granting loans.

1. Personal interview

When the borrower asks for any loan to the bank, manager discusses with him about his requirement and the project. In the interview bank manager guesses the habits, behaviour and attitude towards the bank and business. Also profitability of the business is considered. In the mean time bank enquires separately about the capacity, creditworthiness and character of the borrower and profitability of the business of borrower. Reliability of that person is also seen. On this basis an opinion is formed and the member assured of loan otherwise his proposal is rejected in next meeting.

2. Proposal in writing

Loan applications, reliable guarantors application and couset are prepared. The bank application includes following forms –

1. The loan demand application form contains the personal information of the members demanding the loan from the bank. It includes the name, address, occupation, age of the applicant and his membership number of the Bank. It also contains the loan demanded the purpose the term and loan, the name, address, age, membership numbers of the guarantors the details of the security offered the signature of the borrowers and guarantors.
2. Second form is assurance letter to directors, it include the information about the membership. It is assurance of the borrower to repay the loan amount with interest in stipulated period of time.
3. Third form is the office information form about the borrowers. It contains date, name of the applicant, amount of loan required, the past loan repayment details, loan from other places, security offered etc.
4. In case of loan against the security of the goods, a statement of closing stock has to be given to the Bank with an undertaking that this closing stock is hypothecated to any other bank.
5. Consent letter has to be obtained from the members of joint family/ business in separate form ; to be signed in the presence of two witnesses.
6. There is letter of guarantee and contract by the member borrowed to the effect that in case the loan is not repaid in the time it should be recovered from the bill of sugarcane or any other amount standing to credit of the member borrower.
7. A promissory note and bond duly signed by the borrower and two guarantors in the fevour of the Bank has to be submitted to the bank.

8. A guarantee letter to the effect that the borrower is the member of the bank and has not taken loan from any other bank.

9. On disbursement of the loan the borrower has to sign a voucher and submit it to the Bank as legal evidence of the loan taken.

Before the sectioning of the loan the Bank makes the detailed the enquiry about the loan availed from the Banks or credit institutions in the neighborhood area. A search report of the property is obtained from the advocate a valuation report from the authorized valuer is taken. Also the financial statement submitted by the borrower are scrutinized. Then only the proposal is put before the meeting of the Board of directors for final decision.

3. Scrutiny of proposal and sanctions

The entire proposal is scrutinized carefully in the bank office. The officers assess the income generation potential and feasibility of the project. Then with other recommendations the proposal is sent to the Assistant General Manager. He signs the report and passes it on to the Chairman for final sanction of loan. If the loan amount is above limit sanction will be given only in in the board meeting. The proposal is sanctioned by majority of the Directors.

4. Execution of documents

After sanction of the loan by the head office a sanction letter with the necessary conditions is sent to the related branch for disbursement of loan. After receiving the sanction letter, borrower and guarantors are called up on execute to necessary documents.

5. Disbursement

After completion of all above formalities, payments is made by pay order or demand draft to the borrower. In case of cash credit an account with the bank is opened and cheque book is issued to the customer for withdrawals.

6. Reporting

After disbursement of the loan a report official to the Bank is sent back to the bank head office for information that loan has been disbursed according to the terms and conditions.

3.7 Survey Of Borrower

A questionnaire was administered to random sample of 45 borrowers. The data collected was analyzed and tabulation as follows.

1. Educational Level Of Borrowers

Table 3.1

Educational Level Of Borrowers

Education	No. Of Borrowers	Percentage (%)
Upto 10 th Std	13	28.5%
Upto 12 th Std	13	28.5%
Graduation	12	27%
Post Graduation	3	7%
Technical	3	7%
Any other	1	2%
Total	45	100

An enquiry into the educational level of borrower revealed that nearly 28.5 per cent of borrower had studied upto 10th and 12th standard, 27 percent borrower were graduates; 7 percent borrower were post graduates, another 7 percent borrowers had taken technical educational from industrial training institutes. Thus, most of the borrower had low education level because they were agriculturists.

2. Occupation Of Borrowers

Table 3.2

Occupation Of Borrowers

Occupation	No. Of Borrowers	Percentage (%)
Agricultural	12	28%
Silver making	6	13%
Retailer	11	24%
Small enterprise	9	20%
Service	6	13%
Professional	1	2%
Total	45	100

Table 3.2 shows the occupational break-up of the borrower 28 percent borrower were engaged in agriculture and allied occupation. Where as 13 percent borrower were doing silver article business, 24 per cent borrower had retail stores, 13 per cent borrower were employed person.

3. Opinion Of Borrower As To Loan Procedure

Table 3.3

Opinion of Borrowers As To Loan Procedure

Opinion	No. Of Borrowers	Percentage (%)
Simple	27	44%
Complicated	29	46%
Can't tell	06	10%
Total	45	100

When asked about the nature of the loan procedure, 27 borrower (44 percent) opined that the procedure was simple and contained enough documents to verify the purpose of loans and capacity of the borrower. However, 29 borrower (46 percent) felt that the procedure was complicated and the borrower were require to collect a number of documents from different sources. Borrower could not give any firm opinion in this regard.

4. Opinion Of Borrowers About Rate Of Interest

Table 3.4

Opinion of Borrowers About Rate of Interest

Opinion	No. Of Borrowers	Percentage (%)
High	27	60%
Reasonable	8	18%
Can't tell	10	22%
Total	45	100

Table 3.4 shows the opinion of borrower regarding the rate charged on loan. 60 per cent borrower found the rate of interest as high, according to 18

per cent borrower the rate of interest was reasonable where 22 per cent borrower could not give only opinion in this regard.

5. **Opinion Of Borrowers About The Limit Of The Amount Of Loan Sanctioning**

Table 3.5

Opinion Of Borrowers About The Limit Of The Amount Of Loan Sanctioning

Opinion	No. Of Borrowers	Percentage (%)
Inadequate	31	68%
Adequate	07	16%
Can't tell	07	16%
Total	45	100

Opinion of borrower regards the adequacy of loans was shown in Table 3.5. According to 68 per cent borrower the amount of loan sanctioned was not adequate. But 16 per cent borrower told that the loan amount was adequate and met their requirements. Remaining 16 per cent borrower could not give any opinion as to the adequacy or otherwise of the loan.

3.8 Observations About The Procedure Of Sanctioning Application And Supervision Of Loans

1. The bank follows a very elaborate procedures for application of loans. There is a large number of documents to be submitted with the loan application to the Bank.

2. The procedure of loan application is complicated and time consuming. The borrower has to fill in a numbers of documents and consent-holders to the Bank.
3. Even-through the form are in vernacular language, the borrowers find it difficulty to fill in those forms due to the technical nature of language.
4. The borrowers has to after some kind of security to the Bank. The security may be in the form of property, agricultural land, trading stock, gold or other tanginable assets. A borrowers with a good purpose but inability to provide necessary security may remain deprived of loan facility.
5. Finding two guarantors, convincing them and obtaining their signatures is also tough and time consuming task for the borrowers.
6. In case of a members applying for the loan a period of one month is required for sanction of the proposal or otherwise. This period increase to two months case of non- members applicants.
7. A Nominal processing fee is charged for processing of loan proposal.
8. The banks makes all efforts to super wise the utilization of loan. However that is modify for supervision is inadequate no separate staff is appointed for this purpose. The regular staff is assigned for the supervision work. It is not formally trained and looks the knowledge of agricultural operations.