Chapter 3

Credit Service

INTRODUCTION

- Loan are those that are given to individuals to meet their needs as opposed to corporate to meet business or commercial imperatives.
- These may be secured or unsecured.
- Secured Loans is one that is given on the security of some assets. The security for a housing loan would be the mortgage of the house; the security for a loan to buy a car would be the hypothecation of the car.

INTRODUCTION

- Unsecured Loans are those given to customers without taking any security. This may be because of the reputation of the person or because of the nature of the loan.
- Loans given to individuals to meet medical expenses or holiday expense are usually unsecured.
Commercial Loan Product

1- Overdraft (OD)

- **Definition:** A revolving credit facility with an agreed limit, generally made available against the Business Current Account for working capital purposes.

- **Purpose:** To support business working capital i.e. to meet day-to-day cash flow requirements.

- **Term:** Revolving subject to annual review

- **Other Condition:** The account needs to be fluctuated to an acceptable level to the Bank. The constant unmoved portion will be converted to TL and amortize monthly.

2- Term Loan

- **Definition:** This product provides medium to long term funding for fixed assets acquisitions (including purchase of commercial property to be used as owner-occupied remises), and want to repay the loan, in part or in full, as quickly as possible.

- **Purpose:** To invest in fixed assets purchase.

- **Term:** Maximum term of 3-5 years.

- **Other Condition:** Principal and Interest need to be repaid every month (Interest will be paid every end of month, while Principal will be paid one month after the first draw down).
3- Revolving Short Term Loan (RSTL)

- **Definition**: It is the short term loan that borrowers could use to fund their working capital, it is used mainly for business clients that could not provide acceptable trade supporting documents.
- **Purpose**: To fund the business cash cycle.
- **Term**: Maximum term of 180 days.
- **Other Condition**: Interest will be paid every end of month, while principal will be settled at the maturity date.

4- Trade Finance Loan (TFL)

- **Definition**: It is the short term loan that borrowers could use to fund their cash cycle / pay LC.
- **Purpose**: To pay LC / fund the business cash cycle. All draw downs are to be supported by 1/3 trade supporting documents.
- **Term**: Maximum term of 180 days.
- **Other Condition**: Interest will be paid every end of month, while principal will be settled at the maturity date.

Retail Loan Product

- **Personal Loans**
- **Consumer Durable Loans**
- **Loans to Professionals and Self Employed Persons**
- **Education Loans**
- **Vehicle Loans**
- **Housing Finance**
Personal Loans

• Reasons for advancing loan
  – Personal loans are loans advanced to individuals for a need. These could be to meet marriage expense, hospitalization/medical costs, costs for a holiday or for some other need.

• Eligibility
  – These loans are advances to person over the age of 18/21 who have sufficient disposable income to repay the loan in monthly installments.

Personal Loans

• Eligibility (Con’t)
  – Usually these loans are not advanced to individuals who are likely to retire in one to two years.
  – A certain minimum annual income is also expected.
Personal Loans

• Types to whom loans advanced
  1. Permanent confirmed employees (minimum 1 year service) of:
         • Central/state government/autonomous bodies/ public/joint sector undertakings.
         • Reputed limited companies and educational institutions.

Personal Loans

• Types to whom loans advanced (Con’t)
  2. Self employed professionals
         • Doctors, architects, interior designers, engineers, chartered accountants, technical/management consultants and practicing company secretaries only, with a stable business (minimum – 1 year).
  3. Insurance agents subject to:
         • The agent is doing insurance business for the last 5 years.
         • The agent has regular and stable income and maintaining a/c with the bank.

Personal Loans

• Quantum of Loan
  – These loans are between $1,200 to $4,500. The amount does vary from bank to bank.

• Period of the loan
  – The loan is usually repayable between twelve to twenty four months.

• Rate of Interest
  – The rate of interest would vary from bank to bank.

• Security
  – These loans are usually unsecured.
Consumer Durable Loans

Consumer durable loans are for the purchase of consumer durables such as washing machines, dishwashers, mobile phones, refrigerators, cooking ranges, music systems, televisions and the like.

- **Eligibility**
  - These loans are normally extended to persons over the age of 18 who have sufficient disposable income to repay the loan in monthly installments.
- **Quantum of Loan**
  - These loans are not large and are usually below $2,500.
  - As the amounts are usually not large, normally 90% of the value (and in cases 100%) is advanced.
Consumer Durable Loans

- Period of the loan
  - The loan is usually repayable in a period between 12 months to 36 months.
- Interest
  - The rate of interest varies from bank to bank.
- Security
  - These are usually unsecured thought at times certain equipment such as computers may be hypothecated.

Loans to Professionals and Self Employed Persons

- This category includes loans granted to medical practitioners (including dentists), chartered accounts, cost accountants, lawyers or solicitors, engineers, architects, surveyors, constructions contractors or management consultants or to a person trained in any other art or craft who holds either a degree or diploma from any institution established or to a person who is considered by the bank as technically qualified or skilled in his field.
- Purpose for purchase of equipments, repairing or renovating of existing equipments, acquisition or repairing of business premises and purchase of tools.
Loans to Professionals and Self Employed Persons

• Quantum
  — The amount advanced will depend on the amount required, the nature of the expense and the earnings of the professional.
  — To qualify within this category it should not exceed $25,000 of which working capital finance should not exceed $2,500.

• Period of the loan
  — The period is usually between 36 months and 60 months.

Loans to Professionals and Self Employed Persons

• Rate of Interest
  — The rate will vary from bank to bank

• Security
  — These loans are secured by the asset purchased with these loan.
The central bank suggests that the main emphasis should be to ensure that every meritorious student though poor is provided with an opportunity to pursue education with financial support from banking system with affordable terms and conditions and that no deserving student be denied an opportunity to pursue higher education for want of financial support.

**Eligibility criteria**
- Those eligible for loans are nationals who have secured admission to professional/technical courses in local or abroad through entrance test based selection process.
- There is no minimum age for a student to be eligible.
- The course that are eligible in local and abroad for a loan are:
  - Graduation courses: BA
  - Post graduation courses: Masters & PhD.
  - Professional courses: Engineering, Medical, Agriculture, Law, Dental, Management, Computer etc.
  - Courses like: CPA, CFA


Education Loans

- Expenses considered for loan
  - Fee payable to college/school/hostel.
  - Examination/library/laboratory fee.
  - Purchase books/equipments/instruments/uniforms.
  - Travel expenses / passage money for studies abroad.
  - Purchase of computers
  - Any other expense required to complete the course such as study tours, project work, thesis, etc.

- The amount of loan
  Need based finance subject to repaying capacity of the parents/students with margin and the following ceilings:
  - Studies in local – Maximum $25,000
  - Studies abroad – Maximum $50,000.
  - No security needs to be insisted upon for loan up to $10,000. However, co-obligation of parents is required.

- The amount of loan (Con’t)
  - For loans above 10,000 and up to $20,000 co-obligation of parents together with collateral security in the form of third party guarantee.
  - Above $20,000 co-obligation of parent with tangible collateral security of suitable value along with the assignment of future income of the student for payment of installments.
Education Loans

• Documentations
  – Both the students and the parent/guardian should execute the document.
  – The security can be in the form of land / building / government securities / public sector bonds / gold / shares / bank deposit in the name of student or parent or any other third party with suitable margin.
  – Wherever the land / building is already mortgaged, the unencumbered portion can be taken as security provided it cover the required loan amount.

Education Loans

• Rate of Interest
  – Loan up to $20,000 – Bank base rate
  – Loan above $20,000 – Base rate + 1%
  – The interest to be debited quarterly/half yearly on simple basis.
  – Penal interest @ 2% can be charged for above loans above $20,000 for the overdue amount and overdue period.

Education Loans

• Repayment
  – The loan to be repaid in 5-7 years after commencement of repayment. If the student is not able to complete the course within the scheduled time extension of time for completion of course may be permitted for a maximum period of 2 years.
  – If the student is not able to complete the course for reasons beyond his control, sanctioning authority may at his discretion consider such extensions as ‘may be deemed necessary’ to complete the course.
Education Loans

• Follow up
  – Banks to contact college/university authorities to send the progress report at regular intervals in respect of students who have availed loans.

• Processing Charge
  – No processing/upfront charges should be collected on education loans for studies.

Vehicle Loans

• Vehicle loans are advanced to enable individuals
  – Purchase new two-wheeler/motorcar of any make for private use of professional or business use.
  – Purchase second hand/used two-wheeler/motorcar not more than 5 years old.

• Eligibility
  – Most bank expect the applicant to be at least 21 years of age and not more than 60 years old.
Vehicle Loans

- Eligibility (Con’t)
  - As a safety criteria to satisfy themselves that the person has the ability to repay other aspects may be looked at such as for how long the person has been employed, other assets and the like.
  - In addition the net take home pay/disposable income will be checked to determine whether the applicant can repay the loan.
  - With regard to professionals & self employed persons such as doctors, engineers, architects, charted accountants, lawyers, consultants, businessmen etc. their income should be adequate to pay the monthly installments.

Vehicle Loans

- Quantum of Loan
  - While this may vary, usually the loan is up to 80% (in case of both new and old vehicles; but not older than 5 years) of the cost/invoice value of the vehicle including accessories and registration expenses in the case of new vehicles.

- Rate of Interest
  - The rate of interest will vary from bank to bank.

- Repayment
  - Entire loan with interest is required to be paid in 36 to 60 equated monthly installments.

Vehicle Loans

- Security
  - Hire purchase is to be noted in the registration book issued by the Regional Transportation Officer.

- Insurance
  - The vehicle purchased must be comprehensively insured to its full value with a clause stating that if it is damaged beyond repair, the insurance money be paid to the bank.
Housing Finance

• Type of direct housing finance
  The following types of bank finance are considered direct housing finance:
  – Bank finance extended to a person who already owns a house in a town/village where he resides, for buying/constructing a second house in the same or other town/village for the purpose of self-occupation.

• Type of direct housing finance (Con’t)
  – Bank finance extended for the purchase of a house by borrower who proposes to let it out on a rental basis on account of his posting outside the headquarters or because he has been provided accommodation by his employer.
  – Bank finance extended to a person who proposes to buy an old house where he is presently residing as a tenant.
Housing Finance

• Type of direct housing finance (Con’t)
  – Bank finance granted only for purchase of a plot, provided a declaration is obtained from the borrower that he intends to construct a house on the said plot, with the help of bank finance.

• Supplementary finance
  – Banks may consider requests for additional finance within the overall ceiling for carrying out alterations/additions/repairs to the house/flat already financed by them.

Housing Finance

• Housing Loans are advanced for:
  – The purchase of a house/flat or the purchase of a plot of land for the construction of a house.
  – The renovation/repair of an existing house/flat.
  – Extending an exiting house.
  – Short term bridge finance while purchasing another house/flat

Housing Finance

• Housing Loans for building construction
  – This is extended when the applicant owns land and approaches the bank for a loan to construct a house.

• Eligibility
  – Those eligible are all individuals above the age of 18 years with adequate income to repay the loan in equated monthly installments.
  – Housing loans are not normally extended to individuals who are above 58 years of age they would retire in a short while.
Housing Finance

• Quantum
  – The quantum will vary from bank to bank.
  – Bank would normally stipulate a minimum of $1,500.
  – The maximum would depend on the bank and could vary from $25,000 to $450,000.
  – The loan amount for repairs would normally be less – usually around $25,000

• Margin
  – The entire amount is rarely advance. The loan is usually between 80% and 85% of the cost of the house/flat.
  – Banks normally assume that 55% to 60% of the monthly disposable/surplus income is available for the repayment

• Term of the loan
  – The term is dependant on the age of the buyer – the intent being that it should be repaid before the person retires.
  – Most loan are for 15 to 25 years.

• Rate of Interest
  – Interest may be fixed or floating

• Repayment
  – Repayment is made in equated monthly installments which comprises of both interest and principal repayment.

• Security
  – The property purchased is usually the security and a mortgage is taken on the property.
  – As an additional security guarantees may be taken.
Consumption Loans
• Eligibility: Small and marginal farmers with land holding up to two hectares, landless laborers, rural artisans.
• Purpose and Ceilings for Loans: Loans may be granted for the following purposes within the ceilings prescribed per family.
  1. General consumption $100
  2. Medical expenses $300
  3. Educational needs $250
  4. Marriage ceremonies $300
  5. Funerals, births etc, $200
  6. Certain religious ceremonies $100

Credit Analysis
• Retail Credit Analysis
  — Retail credit analysis relates to the determination of the credit worthiness of an individual before a loan is disbursed.
  — It is different from lending to companies as the amounts involved are much smaller and are given to support a lifestyle as opposed to run a business.

Credit Analysis
• Principles of Sound Lending
  — The purpose the loan is being sought for.
  — The ability of the borrower to repay.
  — The term the loan is sought for.
  — The integrity of the borrower. If there is any doubt on this score, the loan should not be disbursed.