RETAIL CREDIT

A retail credit facility is a financing method which can provide capital for various purposes. Retail credit facilities are portfolios structured with different types of debt that can be used by a company for business needs or customer lending.It is helpful in financing essentially, a type of loan or line of credit used by retailers and real estate companies. Retail credit facilities can be business-to-business, as in a company obtaining financing from a bank, can be business-to-consumer, in which the retailer extends credit to customers for purchases.

BUSINESS CREDIT

Business credit is a track record of a business's financial responsibility that companies, investors or financial organizations use to determine whether or not that business is a good candidate to lend money to or do business with. Common factors that impact business credit are public records, such as liens or bankruptcies, credit such as outstanding balances and payment habits and demographic information such as business size and years on file.

MEANING OF NON-PERFORMING ASSETS

Non Performing Asset is a classification used by financial institutions that refer to loans that are in jeopardy of default. Once the borrower has failed to make interest or principal payments for 90 days the loan is considered to be a Non Performing Asset. Non Performing Assets are problematic for financial institutions since they depend on interest payments for income.

RECOVERY OF NON-PERFORMING ASSETS (NPA)

Recovery of NPA has become the critical performance area (CPA) for banks in India since NPA reduces the profitability of a bank, weaken its financial health and erode its solvency. The following paragraph discusses the various measures that the banks adopt to recover the non-performing assets.

a) REMINDERS SYSTEM - This is the simplest way to follow-up default cases. Generally, response to this recovery measure particularly from honest borrowers is encouraging.

b) PERSONAL VISITS/CONTACTS - It is an effective and simple mode for recovery. Banks experience has shown this as an effective measure especially in the case of small borrowal accounts. Involvement of staff at all levels in the bank branch is necessary. Frequent visits are called for in case of hardcore borrowers. Over the years it is observed that the number of visits to the borrower is going down due to cut in workforce in banks.

c) RECOVERY CAMPS - In respect of agricultural advances, recovery camps are organized during the harvest season. In organizing recovery camps, bankers take the help of outsiders, particularly revenue officers in the state government, local panchayat officials, etc. Banks give publicity of the recovery camp to be organized in the area.

d) RECOVERY AGENTS- Banks appoint outside professional agencies whose services are utilized to ascertain the whereabouts of the borrowers and enforcement of securities. There is some hesitancy on the part of public sector banks due to the unpleasant experience of some financial institutions in certain cases

e) RESTRUCTURING/REHABILITATION - The rehabilitation programme is for raising the unit's capacity to generate adequate internal surplus so that a certain portion of internal surplus could then be used for reducing the irregularity in the account. The bank undertakes the following actions as part of this programme - developing information system, review of performance, monitoring areas of weakness.

f) CORPORATE DEBT RESTRUCTURING - For large borrowers enjoying multiple banking accounts and with, credit facilities above Rs.20 crores, the Corporate Debt Restructuring (CDR) body has been created to facilitate debt restructuring. Cases of DRT, BIFR and willful defaults, doubtful and loss accounts and suit filed cases are outside the purview of the CDR. Thus, standard and sub204 standard accounts are only eligible to seek CDR shelter. No banker/ borrower can take recourse to any legal action during the 'stand-still' period of 90-180 days.

g) LOAN COMPROMISE - Once a NPA unit is evaluated and found that it cannot be revived, it becomes incumbent on the branch to initiate recovery proceedings. Since money has got time value whatever recovery means a branch adopts should result in quick repayment. As a recovery means, the, bank can either go to a court praying for negotiation with the customer for a compromised settlement. A compromise in bank loans means agreeing to borrower's request of accepting a part of outstanding dues in the books of the bank as full and final payment or allowing for the non-compliance of the terms of the loan, after analyzing the alternative courses of action, genuineness and capacity of the borrower to repay. It is also called as voluntary debt reduction or scaling down of dues. Loan compromise helps the bank to recover dues with least passage of time and minimize further the loss of earning opportunities.

h) SECURITY ADJUSTMENT or APPROPRIATION OF SUBSIDY - Where readily encashable securities such as Fixed deposits, LIC Policies, Government Securities, etc. are available and if borrowers are not responding to request for regularization of accounts, such securities are encashed after giving due notice to the borrowers, guarantors, etc. In case of sponsored schemes, the subsidy amount is kept in deposit accounts of the bank for appropriation after a specified lock-in period. In such cases where subsidy is available and the account is likely to become NPA, the subsidy amount is appropriated in the loan account.

i) RECALLING OF ADVANCES - When rigorous follow-up efforts do not yield any fruitful result, a final recall notice is usually served asking the party to rectify the irregularity in the account immediately. Recall notice should be sent only if the borrower is a willful defaulter, bank liability is significantly uncovered, borrower refusing to renew the credit limit, etc. The exercise of recalling of advances is one of the recovery

k) FILING SUIT - Filing of suit is the last resort available to a bank for recovery considering the disadvantages of filing suit. It involves incurring court fees and expenses for providing the witness of the bank. The long drawn process of legal proceedings results in delay in disposal of securities, by which time, the value and conditions of the same may deteriorate. Generally, it may take 6-7 years to get the suits decreed. The money value would have eroded substantially by that time. Sale through court turns out to be distress sale on account of lack of bidders and hence no fair return is guaranteed. After filing the suit, borrowers/ guarantors start disposing of their personal assets and hence recovery of bank dues is likely to prove difficult. Moreover, the realized value sometimes does not meet even the expenses towards maintenance, safe keeping of the securities and liquidator's/ Commissioner's expense/ fees. (Canara Bank, 2001). In this light, the issue that needs deliberation is that despite banks resorting to filing of suits, whether the legal process has been beneficial in recovery of dues of banks and enforcement of credit discipline (RBI, 1999).

l) WRITE-OFF - If it is un-remunerative either to file suit and / or continue the account in the bank's books, banks waive off legal action and/ or write-off outstanding dues. By waiver of legal action, banks may take a decision not to pursue recovery through court of law. But for write-off, the banks decide to close the account by transfer of funds from their profits to the loan account. Write-off is proposed under certain circumstance such as : (i) borrowers are adjudicated as insolvents, (ii) revenue authorities under the State Public Recovery Act have recovered some amount and there is no further chances of any recovery, (iii) both borrower and guarantor are untraceable after selling their assets, and (iv) decrees remain unexecuted several times due to reasons beyond the control of the bank. However, even after write-offs, a bank continues its recovery efforts.

MANAGEMENT OF NON-PERFORMING ASSETS (NPA)

STRATEGIES FOR MANAGEMENT OF NPAS Indian commercial banks are adopting the measures to reduce and control the NPAs in accordance with the recommendations of RBI. These strategies are necessary to control NPAs. (A) Preventive management and (B) Curative management

A) PREVENTIVE MANAGEMENT Preventive measures are to prevent the asset from becoming a non performing asset. Banks has to concentrate on the following to minimize the level of NPAs.

1) EARLY WARNING SIGNALS (EWS) - Banks should continuously monitor loans to identify accounts that have potential to become non-performing. It is important in any early warning system, to be sensitive to signals of credit deterioration. A host of early warning signals are used by different banks for identification of potential NPAs. Most banks in India have laid down a series of operational, financial, transactional indicators that could serve to identify emerging problems in credit exposures at an early stage. Further, it is revealed that the indicators which may trigger early warning system depend not only on default in payment of installment and interest but also other factors such as deterioration in operating and financial performance of the borrower, weakening industry characteristics, regulatory changes, and general economic conditions. Early warning signals can be classified into five broad categories viz: (A) Financial, (B) Operational, (C) Banking, (D) Management and (E) External factors.

(a) Financial warning signals: Financial related warning signals generally emanate from the borrowers‟ balance sheet, income expenditure statement, statement of cash flows etc. Following common warning signals are captured by some of the banks having relatively developed EWS: Persistent irregularity in the account, Default in repayment obligation, Devolvement of invocation of guarantees, Deterioration in liquidity/working capital position, Substantial increase in long term debts in relation to equity and declining sales.

(b) Operational signals: Following operational signals are captured by some of the banks: Operating losses/net losses, Rising sales and falling profits, Disproportionate increase in overheads relative to sales, rising level of bad debt losses Operational warning signals, Low activity level in plant, Disorderly diversification/frequent changes in plan, Non-payment of wages/power bills, Loss of critical customer/s, Frequent labor problems, Evidence of aged inventory/large level of inventory.

(c) Banking related signals: Following are the banking related signals: Declining bank balances/declining operations in the account, Opening of account with other bank, Return of outward bills/dishonored cheques, Sales transactions not routed through the account, frequent requests for loan, frequent delays in submitting stock statements, financial data, etc.

(d) Management related warning signals: These following signals are related with management: Lack of co-operation from key personnel, Change in management, ownership or key personnel, Desire to take undue risks, Family disputes, Poor financial controls, Fudging of financial statements, Diversion of funds, etc.

(e) Signals relating to external factors: Signals like Economic recession, Emergence of new competition, Emergence of new technology, Changes in government / regulatory policies, Natural calamities are related to external factors

2) KNOW YOUR CLIENT (KYC) - Most banks in India have a system of preparing `know your client‟ (KYC) profile/credit report. As a part of KYC system, visits are made on clients and their places of business/units. The frequency of such visits depends on the nature and needs of relationship.

3) CREDIT ASSESMENT AND RISK MANAGEMENT - Credit assessment and Risk management mechanism are ever lasting solution to the problem of NPAs. Managing credit risk is a much more forward-looking approach and is mainly concerned with managing the quality of credit portfolio before default takes place. The documentation of credit policy and credit audit immediately after the sanction is necessary to upgrade the quality of credit appraisal in banks. In a situation of liquidity overhang the enthusiasm of the banking system is to increase lending with compromise on asset quality, raising concern about adverse selection and potential danger of addition to the NPAs stock. It is necessary that the banking system is equipped with prudential norms to minimize if not completely avoid the problem of credit risk and develop an effective internal credit risk models for the purpose of credit risk management.

4) ORGANISATIONAL RESTRUCTURING - With regard to internal factors leading to NPAs the onus for containing the same rest with the bank themselves. These will necessities organizational restructuring improvement in the managerial efficiency, skill up gradation for proper assessment of credit worthiness and a change in the attitude of the banks towards legal action, which is traditionally viewed as a measure of the last resort.

5) REDUCE DEPENDENCE ON INTEREST - The Indian banks are largely depending upon lending and investments. The banks in the developed countries do not depend upon this income whereas 86 percent of income of Indian banks is accounted from interest and the rest of the income is fee based. The banker can earn sufficient net margin by investing in safer securities though not at high rate of interest. It facilitates for limiting of high level of NPAs gradually. It is possible that average yield on loans and advances net default provisions and services costs do not exceed the average yield on safety securities because of the absence of risk and service cost.

6) WATCH LIST - The grading of the bank"s risk assets is an important internal control tool. It serves the need of the Management to identify and monitor potential risks of a loan asset. The purpose of identification of potential NPAs is to ensure that appropriate preventive / corrective steps could be initiated by the bank to protect against the loan asset becoming non-performing. Most of the banks have a system to put certain borrowable accounts under watch list or special mention category if performing advances operating under adverse business or economic conditions are exhibiting certain distress signals. These accounts generally exhibit weaknesses which are correctable by closer attention. The categorization of such accounts in watch list or

special mention category provides early warning signals enabling Relationship Manager or Credit Officer to anticipate credit deterioration and take necessary preventive steps to avoid their slippage into non performing advances.

7) WILLFUL DEFAULTERS - RBI has issued revised guidelines in respect of detection of willful default and diversion of funds. As per these guidelines a willful default occurs when a borrower defaults in meeting its obligations to the lender when it has capacity to honor the obligations or when funds have been utilized for purposes other than those for which finance was granted. The list of willful defaulters is required to be submitted to Securities Exchange Board of India (SEBI) and RBI to prevent their access to capital markets. Sharing of information of this nature helps banks in their due diligence exercise and helps in avoiding financing unscrupulous elements. RBI has advised lenders to initiate legal measures including criminal actions, wherever required, and undertake a proactive approach in change in management, where appropriate.

B) CURATIVE MANAGEMENT - The curative measures are designed to maximize recoveries so that banks funds locked up in NPAs are released for recycling. The Central government and RBI have taken steps for controlling incidence of fresh NPAs and creating legal and regulatory environment to facilitate the recovery of existing NPAs of banks. They are:

1) ONE TIME SETTLEMENT SCHEMES / COMPROMISE SETTLEMENT SCHEMES - This scheme covers all sectors sub-standard assets, doubtful or loss assets as on 31st March 2000. All cases on which the banks have initiated action under the SRFAESI Act and also cases pending before Courts/DRTs/BIFR, subject to consent decree being obtained from the Courts/DRTs/BIFR are covered. However cases of willful default, fraud and malfeasance are not covered. As per the OTS scheme, for NPAs up to 148 Rs. 10crores, the minimum amount that should be recovered should be 100% of the outstanding balance in the account.

2) LOK ADALATS or PEOPLE'S COURT - Lok Adalats are voluntary agencies created by the State Government to assist in matters of loan compromise. Lok Adalat institutions help banks to settle disputes involving account in "doubtful" and "loss" category, with outstanding balance of Rs.5 lakh for compromise settlement under Lok Adalat. Debt recovery tribunals have been empowered to organize Lok Adalat to decide on cases of NPAs of Rs. 10 lakh and above. This

mechanism has proved to be quite effective for speedy justice and recovery of small loans. The progress through this channel is expected to pick up in the coming years.

3) DEBT RECOVERY TRIBUNALS (DRTs) - The Debt Recovery Tribunals have been established by the Government of India under an Act of Parliament (Act 51 of 1993) for expeditious adjudication and recovery of debts due to banks and financial institutions. The Debt Recovery Tribunal is also the appellate authority for appeals filed against the proceedings initiated by secured creditors under the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act.

4) SECURITIZATION AND RECONSTRUCTION OF FINANCIAL ASSETS AND ENFORCEMENT OF SECURITY INTEREST (SARFAESI) ACT, 2002 The Government has passed the SARFAESI Act on 21 June 2002 in order to give teeth to the banks to proceed against the "willful defaulter", and affect recoveries without the intervention of courts and tribunals. Securitization is a relatively new concept that is taking roots in India of late. It is still in its infancy with only a few market players. Securitization is considered an effective tool for improvement of capital adequacy. It is also seen as a tool for transferring the reinvestment risk, apart from credit risk helping the banks to maintain proper match between assets and liabilities. Securitization can also help in reducing the risk arising out of credit exposure norms and the imbalances of credit exposure, which can help in the maintenance of healthy assets. The SARFAESI Act intends to promote Securitization, pool together NPAs of banks to realize them and make enforcement of Security Interest Transfer. The SARFAESI Act-2002 is seen as a booster, initially, for banks in tackling the menace of NPAs without having to approach the courts.

SECURITY AGAINST BANK LOAN

For obtaining a bank loan a customer is required to place certain securities against the loan. Secured loans are backed by an investment/asset. Securities like shares, debentures, mutual funds, bonds, life insurance policies are offered as collateral. Physical shares are accepted in market lots only. Banks accept a minimum of one and a maximum of 20 scrips.