Chapter – I
INTRODUCTION AND DESIGN OF THE STUDY

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Since then, there have been several changes in the scope of priority sector lending and the target and sub-targets applicable to various bank groups. On the basis of the recommendations of the internal working group, set up in reserve bank to examine, review and recommend changes, if any, in the existing policy on priority sector lending including the segments constituting the priority sector, target and sub-targets, etc., and the comments/suggestions received thereon from banks, financial institutions, public and the Indian banks association (IBA), it has been decided to include only those sectors that impact large segments of population and the weaker sections, and which are employment-intensive, as part of the priority sector.

PURPOSE OF PRIORIY SECTOR LENDING

The banks are issue the lending on priority sector in the following purpose.

- Improve the economic condition of the country.
- Facilitate the community by the direct and indirect finance to agriculture people.
- Upliftment of living standard of rural and agricultural people
- The setup the more small industry in the rural area
- Generation employment in the rural people
- Reduction of mandatory credit to a large number of sectors and sections, including marginal farmers, cottage industries, small traders and services and low income housing incentives.
- Improve credit flow to small scale industries and food crop agriculture as well as temporary credit.
- Assure credit to new industries and new professions by the non- poor section.
- Improve the life quality of weaker section.

SEGMENTS ON PRIORIY SECTOR LENDING

Priority Sectors

The Reserve Bank of India classified in the following categories is priority sector namely, Agricultural and allied activities.

- Development of Dairy and Animal Husbandry.
- Development of Fisheries.
- Development of Poultry, Piggery etc.
- Development and maintenance of Stud farms, Beekeeping, Sericulture, etc. However, breeding of race horses cannot be classified under this head.
- Purchase of Bullock Carts, Camel Carts, Pack Animals etc.
- Distribution of inputs for allied activities such as poultry feed, cattle feed, etc.
- Small Scale Industrial Units, Equipment/System for development of new and renewable source of energy, etc.
- Small Scale and Ancillary Industries
  - Flaying and tanning
  - Leather goods
  - Pottery
  - Hand pounding of paddy and cereals
  - Rice Mills, including flour mills and bakeries
  - Canning of fruits and vegetables
  - Manufacturing and processing of agricultural and Marine products and forest produce including beverage industries
  - Other village industries such as carpentry and black-smithy, bee-keeping and honey and honey products
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1.1 INTRODUCTION

The banking system in India is significantly different from that of other Asian nations because of the country’s uniqueness in geographic, social, and economic scenario. India has a large population and land size, a diverse culture, and extreme disparities in income, which are marked among its regions. There are high levels of illiteracy among the people but, at the same time, the country has a large reservoir of managerial and technologically advanced talents. About 35 percent of the population resides in metro and urban cities and the rest is spread in several semi-urban and rural centres. The country’s economic policy framework combines socialistic and capitalistic features with a heavy bias towards public sector investment. India has followed the path of "growth-led exports" rather than the "expected growth" of other Asian economies, with emphasis on self-reliance through import substitution. These features are reflected in the structure, size, and diversity of the country’s banking and financial sector.

The banking sector plays an important role in the development of Indian economy. Before the dawn of independence, the development of the banking sector was not satisfactory. Initially the East India Company established the banks namely Bank of Calcutta in 1806, Bank of Bombay in 1840, and Bank of Madras in 1843. Later in 1921, these banks were amalgamated and Imperial Bank of India was formed. Soon after independence, the banking sector underwent a remarkable change. Moreover, the government was unable to control the commercial banks and divert the funds in accordance with the expectation of the government. Hence, these banks were brought under the control of government during 1969. As a result in 1980, 14 major commercial banks were nationalized and another 6 banks were nationalized in 1980. In 1993, New Banks of India merged with Punjab National Banks (PNB), which brought the number of nationalized banks in India to 19. It was a state sponsored commercial banking institutions, entrusted with the specific task of providing bank facilities to the low income group of sections and enlarging the branch network. It has also been entrusted with the responsibility of branch expansion in remote areas. So, the bankers introduced new and innovative schemes in the year 2005-06, that is, appointed the Business Correspondence / Business Facilitator (BC/BF) model to serve the poor people.
The banking system in India has come a long way during the last two centuries. Its growth was faster and converge was wider since 1969, with an extensive branch network which has diversified credit pattern. Traditional banking has gradually yielded to sophistication in credit management. In other words, the banking and finance industry in India is experiencing a period of dramatic change with disintermediation and interest rates. There is sudden flow of ability especially in the private and foreign banks in India. The present banking scenario is such that private sector, public sector and co-operative sector exist side by side. Apart from Commercial Banks, there are Industrial Banks and Development Banks. While appraising the service of commercial banks it is found that different banks follow different strategies to develop and render new services.

Credit is the life line of trade, industry and commerce. Infusion of credit to the economic sector is as important as that of understanding the needs of the factors and dispensation of the credit in required quantum and in appropriate time. A banker has to be practical as well as prudent while enabling credit to the needs of the people. The concept of credit management is undergoing unimaginable changes. From the days, when bankers were shy of expanding credit, because of interference of political parties and modern government rules and regulations, they have reached a stage where they would like to find new avenues of credit. Credit innovations are emerging in the present context. The commercial banks act as catalysts in the economic development of a country. This is achieved by mobilizing almost one third of the Gross National Product through their various deposit schemes. About 65 to 75 percent of these funds are deployed as bank credit in various sector of the economy. Thus, deposit mobilizing and lending credit dispensation are the two most important functions of the commercial banks. Banks are the trustees of the public funds and savings.

The issue of loan is crucial and important for every banker as it produces a major portion of the banks income. This is also one of the major area of concern and attracts the attention of the top management. An established loan policy translates into a concrete and unified direction for the implementation of the management’s policies, plans and programmes in this significant area. An imaginative and well conceived loan’s policy is also an outstanding marketing vehicle to assist top management in achieving desired goals of growth. Well crafted loans are the major source of a new deposit business. A good proportion of these new deposits becomes available for additional loans, which in turn attracts new deposits and so forth.
Loans and advances have always been one of the principle sources of income for commercial banks in India. The interest earned from loans and other loan related products not only offsets the interest paid on deposits but also contributes to the banks’ operating expenditure and profits. The interest earning loan portfolio is a prerequisite for sound lending. Banks in India have to operate in rapidly changing and highly competitive markets. The borrowers have also become more demanding in terms of cost of credit, loan products and quality of services. Bank lending is a strategic marketing function based on innovative products, loan pricing and service quality.

The bank has to deploy its funds in three main areas such as cash, investments and loans and advances. The first two are determined largely by the RBI from time to time. At present, the Cash Reserve Deployment (CRD) of funds in ratio is 4.75 percent of total time and banks demand liabilities. Cash Reserve Ratio (CRR) is kept in current account with RBI. This can vary between 3 and 15 percent, depending upon the decision of the Central Monetary Authority.

The Statutory Liquidity Ratio (SLR) comprises of two namely, cash in hand and balances at other banks and investment in government and other approved securities. In April 2012, these put together made up about 30 percent of total time and demand liabilities of a bank. The remaining 70 to 71 percent funds are left for lending to different sections of economy. Thus credit extended by the banks is a major avenue of deployment of funds.

1.2 STATEMENT OF THE PROBLEM

Finance is the lifeblood of a business and is also a problem to business. A business cannot move without adequate finance. Every business house requires money for which they approach the banks for the finance, and the banks provide loan to the business institutions after assessing the repayment capacity and other aspects of business units. Lending money is one of the core functions of banks. By deploying money in the form of loans and advances, banks earn interest which is the dominant source of income for them. The banks adopt cautions in lending money. Scientific appraisal of the project, timely disbursement and proper monitoring of credit pave way for better credit management in banks.
In India credit management has assumed much significance in the post reform period. Introduction of potential accounting norms such as income recognition norms, asset classification norms and provisioning norms had resulted in the emergence of sophisticated tools of credit management. Today banks have become a part and parcel of our life. There was a time when the dwellers of city alone could enjoy their services. The banks offer access to even a common man and their activities extend to areas hitherto untouched. Apart from their traditional business oriented functions, they have come out to fulfill national responsibilities. Banks cater to the needs of agriculturists, industrialists, traders and to all the other sections of the society. Thus, they accelerate the economic growth of a country and steer the wheels of economy towards its goals of self reliance in all fields. It naturally increases our interest in knowing more about the bank and the various men and activities connected with it.

Accepting deposits and lending money are the core functions of a bank. Through this process of financial intermediation, banks channelize the funds for productive endeavours and pave way for economic growth. They encourage savings by mobilizing deposits and provide funds for a variety of economic activities. Banks offer a wide range of deposits and advances to fulfill the requirements of different segments of the society. Banks lend in the form of credit card, overdraft, term loans and discounting bills. When a bank lends money it is able to generate interest, which is the dominant source of income for a bank. In fact, through the interest earned from advances, a bank is able to pay interest to the depositors, meet out its operating expenditure and gain some surplus in the form of profit. Loans and advances also generate reasonable volume of non-fund based business, thus creating non-interest income in the form of commission, exchange, fee and the like.

In India, prior to nationalization of banks, they were lending mostly to large industrial houses, whereas agriculture, small scale industries, and tiny sector were totally out of the focus of bank credit. Moreover, banks adopted security oriented approach in their lending decisions. But after nationalization of banks in 1969 and 1980, there were significant changes in the lending operations of the banks. With massive branch expansion and introduction of priority sector lending, banks began to lend to the hitherto neglected sector such as agriculture, small scale industries, tiny sector and so on. They were driven by the principle of diversification while lending, with due focus on the purpose of the loan.
Financial Sector Reforms introduced in the Indian Banking Sector in 1994 and in 1998 have given a new dimension to the lending policies of banks. Banks have begun to concentrate much on recovery of advances in order to minimize the volume of nonperforming assets (NPAs). As NPAs affect the profitability of the banks severely through the impact of asset classification and provisioning norms, banks are extra cautious while lending. Interest rate deregulation in the aftermath of reforms has given more freedom to bank to price their loans and advances scientifically. At present, they adopt a competitive interest rate policy based on the base rate and risk rating.

Retail lending has gained popularity among banks and retail loans such as housing loan, consumer loan, education loan, weaker section loans and so on, are considered very safe and profitable for banks. They have widened their retail loan portfolios by exploiting the strong demand for retail loans due to a sizeable increase in the disposable income of people in the liberalized era. In short the lending practices of banks in India have become more pragmatic; aggressive marketing strategies, technology driven appraisal and sophisticated tools of credit management have become the hallmark of the lending policies of banks in India. Hence the researcher has made an attempt to compare and study the credit management of private and public sector banks in India.

1.3 SIGNIFICANCE OF THE STUDY

In our present day's highly competitive and dynamic scenario, Indian banks too are introducing newer approaches for extending credit to their customers. The banks in India have to contend with a credit market, which has become highly selective in respect of pricing of loan products and quality of services.

Banks are the catalyst of economic development of all the countries whether developed or developing. In India, banks have been playing a unique role in mobilizing savings, credit disbursement, investment and providing other services; therefore they are the heart of our financial system. As per the report released by the RBI, the commercial banks deposited amount touched around Rs. 59,09,100 crores, outstanding bank credit amount to Rs.46,11,900 crores and investment of Rs. 17,37,800 crores as on March 2012. The ability of the banking system to perform its tasks efficiently and in harmony with our need and economic goals depends on a large measure on the wise management of its resources.
Credit has always been one of the principle sources of income for commercial banks. The extension of credit on a sound basis is very essential for the growth and prosperity of bank. The central banks of any developed as well as developing countries are much focused on the quality of credit portfolio of commercial banks due to the implementation based on the committee reports. The globally accepted standards of capital adequacy, norms for asset classification, income recognition and provisioning, exposure norms, risk management, supervision and control of bank credit are some of the key areas. In India, the central government implemented various credit policies based on the recommendation made by the two reports of the Narasimham committee, that is, committee on financial system in 1991 and the committee on banking sector reforms in 1998 which helped in making the system of banks sound and strong.

1.4 OBJECTIVES OF THE STUDY

This study is undertaken with the following objectives:

1. To evaluate the loans and advances offered by the public sector banks in India.
2. To analyse loans and advances provided by the private sector banks in India.
3. To compare the loans and advances lent by both the private and public sector banks.
4. To assess the non-performing assets of both the private and public sector banks.
5. To offer suggestions based on findings of the study.

1.5 SCOPE OF THE STUDY

The present study examines the lending performance of commercial banks. The study comprises the theoretical background of credit management, lending performance of both the Pvt.SBs and PSBs in India. This study analyses the type of credit offered by the PSBs and Pvt.SBs in India. It is done by measuring the progress of loans and advance and its classification by analyzing the loan status of the bank through various financial tools and also by framing some models and lastly by examining the extent and causes of Non-Performing Assets (NPAs) of the banks.

1.6 RESEARCH METHODOLOGY

The study was purely based on the secondary data. These were collected from annual accounts of the RBI report, books, magazines, journals and the like. Moreover, unstructured interview schedule has been prepared by the researcher and the discussions were also held
with various branch managers and the special officers of the bank, to collect the relevant information relating to effective credit management.

1.7 SAMPLE COMPOSITION

The study covers the credit portfolio of all scheduled Commercial Banks in India except foreign banks and Regional Rural Banks (RRBs). Thus, the study includes the following groups of commercial banks:

a) State Bank of India and its associate banks (SBI & its associate banks),
b) Nationalized Banks (NBs),
c) Old Private Sector Banks (OPSBs) and
d) New Private Sector Banks (NPSBs).

For this purpose, the detailed information were also collected from the various special issues of RBI publication from the RBI bulletin, as this study was restricted to the private and public sector banks in India.

1.8 PERIOD OF THE STUDY

This study covers a period of 11 years commencing from 2002 – 03 to 2012-13.

1.9 SOURCE OF DATA

The data were collected from the annual accounts, reports of trends and progress of banking in India, reports of State Level Bankers Committee, RBI bulletin, IBA bulletin, www.iba.org, www.rbi.org.in, www.financeindia.org.in, political and economic weekly, published and unpublished M Phil dissertations, Ph.D theses and Business World newspaper of the private and public sector banks in India.

1.10 TOOLS OF ANALYSIS

The nature and scope of the loans and advances offered by the private and public sector banks had been analyzed with the help of secondary data by using statistical package like Microsoft excel sheet 2007, SPPS 16 version and E-views.

These analysis tables have been utilized to present the data in a suitable form. The mean had been used for describing the relationship between the whole year of loans and advances of both Pvt.SBs and PSBs.
The standard deviation had been administered for the purpose of measuring of variability of loans and advances; if low standard deviation indicates that the loans are to be very close to the average whereas high standard deviation indicates that the advance is spread out over the large range. The coefficient of variation had been utilized to measure the performance of the loans and advances by the banks; a lower coefficient of variation indicates a higher performance of advances offered.

The Compound Annual Growth Rate (CAGR) had been used to measure the annual growth over from the initial advances amount to the last year ending advances offered by the banks. The growth rate had been calculated to find out the growth over the previous year.

The Multiple Regression Analysis was calculated to assess the influences of the variations on loans and advances of the banks throughout the study.

The Structural Equation Model (SEM) had been used to study the performance of bill finance, term loan and demand loan offered by the PSBs in India.

The SEM had also been used to understand the performance of advances offered by the Pvt.SBs in the area of bill finance, term loan and demand loan.

The SEM had been applied to compare the performance of loans and advances offered by both the PSBs and Pvt.SBs in India.

The General Autoregressive Conditional Heteroscedasticity (GARCH) model had been formulated to find out the credit volatility performance of the banks. Hence the researcher had attempted to assess the credit volatility of both the PSBs and Pvt.SBs individually, and this GARCH model had also been used to compare the performance of both the banks.

All banks face the problem of the NPAs in the present days. The government, RBI and banks try to reduce this problem. The researcher had used a model which is suggested by the RBI to find out the NPAs status of the Pvt.SBs and PSBs.

The SEM had been used to find out how one asset influences other assets, such assets are standard asset, sub-standard asset, and doubtful asset and loss asset.
1.11. OPERATIONAL DEFINITIONS

1.11.1 CREDIT MANAGEMENT

Credit Management is the process of controlling and collecting payments from customers. This is the function within a bank or financial institution to control credit policies that would improve revenues and reduce financial risks to the banks as well as the financial institutions.

11.2 RESERVE BANK OF INDIA (RBI)

The Reserve Bank of India (RBI) is India’s central banking institution, which controls the monetary policy of the Indian rupee; hence, it is the banker to the Government. It controls all banks for which it is called bankers’ bank.

11.3 COMMERCIAL BANKS (CBs)

All banks are commercial banks except RBI. It is a type of bank that provides services to the customers such as accepting deposits, making business loans, and offering basic investment products. It refers to a bank or a division of a bank that mostly deals with deposits and loans from corporations or large businesses, as opposed to individual members of the public.

11.4 PUBLIC SECTOR BANKS (PSBs)

Public sector banks (PSBs) are banks where a majority of the stake (more than 50 percent) is held by the government.

11.5 SBI AND ITS ASSOCIATE BANKS (SBI and Its Associate banks)

State Bank of India (SBI) is a multinational banking and financial services company based in India. It is a government-owned corporation with its headquarters in Mumbai of Maharashtra.

11.6 NATIONALIZED BANKS (NBs)

Nationalized banks mean the Central and State government owned banks. The 14 major banks were nationalized in the year 1969, and another 6 banks were nationalized in 1980. In 1993, New Bank of India merged with Punjab National Bank (PNB), which brought the number of nationalized banks in India to 19⁴.
11.7 PRIVATE SECTOR BANKS (Pvt. SBs)

The Pvt.SBs are banks where greater parts of stake or equity are held by the private shareholders and not by government.

11.8 OLD PRIVATE SECTOR BANKS (OPSBs)

The banks, which were not nationalized at the time of bank nationalization that took place during 1969 and 1980, are known to be the Old Private Sector Banks. These were not nationalized, because of their small size and regional focus. Most of the old private-sector banks are closely held by certain communities and their operations are mostly restricted to the areas in and around their place of origin. Their Board of Directors mainly consist of locally prominent personalities from trade and business circles.

11.9 NEW PRIVATE SECTOR BANKS (NPSBs)

The NPSBs, which came in operation after 1991, with the introduction of economic and financial sector reforms are called "New Private Sector Banks". These banks should have a minimum net worth Rs. 200 crores. These are called new generation private sector banks.

11.10. SHORT TERM LOAN

Short term credit is a credit which is repayable within 12 months

11.11. MEDIUM TERM CREDIT

Medium term credit is the one, which is repayable after 12 months and within five years.

11.12. LONG TERM CREDIT

Long term credit is the one, which is repayable after a period of five years and upto twenty years.

11.13. NON PERFORMING ASSET (NPAs)

Credit facilities in respect of which interest or instalment of principle is in arrears for more than 90 days.
1.12. LIMITATIONS OF THE STUDY.

The following are the limitations of the study:

1. The study is restricted to only eleven years from 2002-03 to 2012-13.
2. The analysis is made purely from the financial point of view.
3. This study does not include Foreign Banks, RRBs and Co-operative Banks.
4. The reliability and correctness of the study depends on the information provided in the report on trend and progress of banks in India.
5. The study concentrates only on the quantitative analysis of financial data. The emerging trends in the qualitative aspects of performance of a bank in areas such as customer relationship management, marketing strategies, impact of technology on profitability are not considered.

1.13. CHAPTER SCHEME

This work is presented in eight chapters

The first chapter presents the introduction of the study, statement of the problem, objectives of the study, methodology and framework of analysis, scope of the study, period of study, limitations of the study and the chapter scheme.

The second chapter presents a bird’s view of the review of literatures in three dimensions namely priority sector, non priority sector and non performing assets in India and abroad.

The theoretical backgrounds of the credit management are presented in the third chapter. It includes the significance of credit, principle of lending, schedule 9 of banking balance sheet, priority sector advances, non priority sector advances, RBI guidelines for interest rates on advances, concept of NPAs, classification of NPAs, consequence of NPAs, effective credit management and so on.

The fourth chapter deals with the various loans and advances of public sector banks in India and such advances include bill finance, term loan, demand loan, secured advances, unsecured advances, priority sector advances, government guarantee loan programme, public advances, syndicated loan, foreign bill finance and so on.
The fifth chapter evaluates the performance of loan and advances of the private sector bank. The advances include bill finance, term loan, demand loan, secured advances, unsecured advances, priority sector advances, government guarantee loan programme, public advances, syndicated loan, foreign bill finance and so on.

The comparative analysis of loans and advances of both public and private sector banks are given in the sixth chapter.

The seventh chapter analyzes the position of NPAs of the Bank. This chapter includes gross NPAs, net NPAs, standard asset, sub standard asset, doubtful asset, loss asset, comparative analysis of NPAs through SEM model, RBI suggested model and so on.

The eighth chapter is the summation of the findings, suggestions and conclusion of the study.
REFERENCES


4. Ibid- P. xix