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A Study of Lending Policies and Programmes of Commercial Banks In India (A case study of Gaya District)

ANCHHI KUMARI
RESEARCH SCHOLAR
DEPARTMENT OF ECONOMICS
MAGADH UNIVERSITY, BODH GAYA, BIHAR

Credit system originated from credit culture. With the change sin social and economic development in the society there came various changing in this regard.[39] In earlier time the dependence on credit was on mutual trust between individuals through contacts. Such credit culture only meets the needs when the scope for economic activities was very limited. But, with the introduction of reforms and opening up of economy, it adopted a unique, social, institutional, professional and commercial feature. In India, various financial institutions provide credit to borrowers and banks are one among them. Banks whether public sector, private sector or foreign banks which play an important role in mobilizing credit. [40]

Principles of Lending

The lending is one of the main activities carried out by the banks. This activity carries an inherent risk as a result the banking institutions cannot afford to bear the risk more than the calculated. to avoid such situation with regard to the risks in lending the lending institutions need to adhere certain principles by which the lending can be termed as safe. With the passage of time there have been various modifications in the lending principles which were being followed by the banks traditionally. Let's have an overview of principles of lending in details:

Safety: As the banks lend the funds entrusted to it by the depositors, the first and foremost principle of lending is to ensure the safety of the funds lent. Safety implies that the borrower is in a position to repay the loan, along with interest, according to the terms of the loan contract. The repayment of the loan depends upon the borrower's capacity to pay and willingness to pay. The borrower's capacity to depends upon his tangible assets and the success of his business; if he succeeds in his efforts, he earns profit and can repay the loan promptly. Otherwise, the loan is recovered out of the sale proceeds of his tangible assets. The willingness to pay depends upon the honesty and character of the borrower.

The banker should, therefore, taken utmost care in ensuring that the enterprise or business for which a loan is sought is a sound one and the borrower is capable of carrying it out successfully. He should be a person of integrity, good characterandreputation.Inadditiontotheabove,thebanker generally relies on the security of tangible assets owned by the borrower to ensure the safety of his funds. [41]

Nature ofassets

The loan disbursed by the banks is payable on demand. These are generally a need for working capital. While sanctioning the loan the bank should ensure the ability of the borrower to repay it. the nature of assets which is owned by the borrower should be of nature of conversion into liquidity. Now a day's all organizations are commercial in nature aiming for the profits. When the organization is profitable there will be serving the interest of all the stakeholders. Lending is the main business of the banks and the interest along with the principal amount is the main sources of income to them. the banks while sanctioning the amount should properly verify the credibility of borrowers so that the principle amount along with the interest should be repaid on time.

End use of theLoan

Banks/FIs should closely monitor the end-use of funds and obtain certificates from borrowers certifying that the funds are utilized for the purpose for which they were obtained. In case of wrong certification by the borrowers, banks/FIs may consider appropriate legal proceedings, including criminal action wherever necessary, against the borrowers.

Diversifying Risks

Diversification of the risks is one the cardinal principles in the mitigating risk which is also equally applicable to the lending principles. The banks and financial institutions should sanction the loans to various sectors of the economy. In economy there are fluctuations in different in various sectors of the economy. Some of the sectors may perform well while various sectors are not performing well. Various internal and external factors are important factors for the profitability of the organizations. the banker should aim at spreading the advances as widely as possible over different industries and different localities. this would enable him to compensate any losses which might arise as result of unanticipated factors adversely affecting particular industries. So banking and financial institutions should lend in all sectors of the economy.

(a) **Character**: the assessment of the credit worthiness of the borrowers is an essential requisite to the sound lending. the character of the borrower depends upon the variousfactors.

(b) **Capacity**: Capacity of a borrower requires two aspects to be assessed. First, the borrower must have legal capacity to borrow. For example, banks will not lend to minors. In the case of partnerships unless specifically prohibited in the partnership agreement, partners have the legal capacity to borrow money on behalf of the partnership. Limited companies will have the capacity to borrow if the articles of association of a company empower its board of directors to do so.[42] Lending banks will always inspect the articles to ensure that the directors can borrow and also mortgage a company's assets for the purpose of giving security. It will also check whether the Directors' powers to borrow are restrictive or not. An assessment of the 'financial capacity' of a borrower is relevant in ascertaining the repayment ability of a borrower.

(a) Individual borrowers would be asked to submit a statement of income and expenditure, and of their assets and liabilities. In the case of corporate borrowers, lenders would insistoninspectingtheprofitandlossaccountsandthebalancesheetsofthe

(b) business and other financial information such as cash flow statements, management accounts and final projections.[43]

(a) **Capital**: The capital base of a corporate borrower is also an indication to a lender of the borrower's financial stability. The equity of a company is an important factor to consider if the potential borrower is small and also new to the bank, or where the business is relatively new. In the first few years of a small business it will usually have little or no retained earnings, and very little external financial help. It would, therefore, have to rely on its own capital in the event of externally imposed challenges such as interest rate fluctuations, inflation and changes in marketconditions.

(b) 'Collateral' is not mandatory in the securing o f a loan. Lenders, however, will favour the availability of security; if, in the bank's view, there is an element of doubt as to the repayment capacity o f a borrower. The amount of collateral that is taken must reflect that element of doubt. As Weerasooria writes:

Security improves the position of lenders in two circumstances. First, if a debtor becomes insolvent, a lender as a holder of valid real estate security will be in a position of pre-eminent advantage. As a holder of such security, a lender is entitled to enforce its rights of realization of that security independently, and thereby stand outside the insolvency process.

'Market conditions' as well as social and economic conditions; affect a potential borrower's business activities. It is quite possible that a borrower may satisfy all the other elements of credit assessment but if the potential borrower were engaged in a business that has an uncertain market, lenders would be reluctant to advance the money. For example, banks may be reluctant to lend for property developmentduringarecessionorwherethepropertypricesarereducing.A prudent lender will always closely study the prevailing conditions in a country before granting a loan.[45]

(i) Credit Information Bureau

The Indian Banking Commission felt there was a need for outside agencies to furnish banks with information but it recognised the difficulties of establishing such agencies under prevailing Indian conditions and suggested that these agencies should be set up by legislation as separate statutory bodies. The Saraiya Commission also recommended the establishment by Legislation of specialised credit agencies, but these recommendations by both Commissions remainunimplemented.[47]

Collection of Credit Information

With the availability of credit information of borrowers, the lenders are enabling to differentiate between those who have honoured their obligations responsibly and those who have defaulted. In India due to the absence of the specialized credit agency for the collection of information relating to the borrower, the task of a banker becomes difficult. Every bank maintains a Credit Investigation Department to collect information regarding the financial position of the borrower.

Assessing the credit rating of a potential borrower is a specialised function of a lender. Whilst there are lending guidelines, each loan application must be treated on its merits. Lenders must gather all the available information and then attempt to reach an objective decision. Experienced bankers no doubt have developed considerable expertise in this field. Nevertheless, for assessing fairly accurately the credit rating of both big and small customers, adequate and reliable information is essential. Most of the information is provided by the customer himself, whilst some information can be obtained from external sources such as specialised agencies or otherbanks.[46]

The credit information is collected through the following sources:

(ii) Borrower: The Reserve Bank of India has advised the Banks and Financial Institutions to submit the information in the prescribed format by end of financial year consisting the details of the information regarding the details of borrowal accounts which have been classified as doubtful and loss accounts by them with outstanding Rs. One crore andabove.[48]

(iii) Market Reports: one off the other mode for determining the creditworthiness of the customer is through market report. there are various mutual arrangement with regard to such publications which are helpful is assessment off the financialconditions.

Information Provided by Banks

Credit inquiries between banks may be formal or informal. Where one bank requests a credit reference from another bank, two problems arise. On the one hand, banks are inhibited in providing information because of their obligation to the customer to maintain secrecy about his financial affairs. On the other hand, banks are concerned with the possibility of being held responsible to the other party who may act upon the information provided by them.

According to the common law on bank confidentiality, (bank secrecy) the disclosure of information about customers to other banks or specialised credit agencies may be unlawful. That a bank is under an obligation to keep its customer’s affairs confidential, but the obligation imposed on banks were not absolute. [49]

Bankes LJ stated:

At the present day I think it may be asserted with confidence that the duty is a legal one arising out of contract, and that the duty is not absolute but qualified. It is not possible to frame any exhaustive definition of theduty.

The most that can be done is to classify the qualification, and to indicate its limits on principle I think the qualifications can be classified under following heads:

- where disclosure is under compulsion bylaw
- where the interests of the bank requiredisclosure
- where discharge of obligation is for the public atlarge

Lending Agreements

Loan agreement must be just and equitable to lenders as w ell as borrowers. Bankers must feel confident that the provisions in the loan agreement will afford them adequate credit protection and give them power to exert influence over borrowers, or control over a loan if necessary. For example, if the bank were in an unsecured position it would insist on including restrictive covenants into the loan agreement to protect itself. If a bank were aware that a corporate borrower has had a doubtful past record or there are material doubts related to the loan, it may want the right to control the loan tightly. On the other hand, a borrower company may consider this an unwanted intrusion into the management's freedom to run the company. Nevertheless, it is the price to pay to obtain aloan.[50]

In India, loan agreements are governed by English legal principles. Judges will not enforce loan agreements that are harsh and unconscionable. [51]

Contract of Guarantee and surety's liability

Meaning of guarantee

In the common parlance the word guarantee means a promise or assurance. While in the context of financial transactions, guarantee means a legal promise to repay a loan if the original borrower makes default.

As per the Oxford dictionary of accounting guarantee means " a promise made by a third party (guarantor) , who is not party to a contract between two others, that the guarantor will be liable if failing in the contractual obligations.

As per the oxford dictionary of Law, guarantee means a secondary agreement in which a person (the guarantor) is liable for the debt or default of another (the principal debtor), who is the party primarily liable for thedebt.

A contract of guarantee is a contract under which a person is known as surety (orguarantor)givesapromisetodischargetheliabilityofathirdpersoncalled

principal debtor. The person whom the guarantee is given is called creditor. Guarantee is a collateral security. Guarantee is in addition to the security of mortgage or hypothecation of some property. As per section 126 of Indian Contract Act "contract of guarantee" is a contract to perform the promise, or discharge the liability, of a third person in case of his default. The person who gives the guarantee is called the "surety"; the person in respect of whose default the guarantee is given is termed as "principal debtor", and the individual to whom the guarantee is given is termed as the "creditor". A guarantee may be either oral or written.[52]

The essence of guarantee is that a guarantor agrees to discharge his liability, only when the principal debtor fails in his duty. "Let him have the loan, I will see you paid" or "if he does not pay I will" are the phrases ordinarily used when a guarantee is given. In other words, a guarantee presupposes the existence of a principal debtor, and if in any contract there never was at any time another person who can properly be described as a "principal debtor" in respect of whose default a guarantee can be given, there cannot be said to have been any "guarantee" either in its technical meaning or in its ordinary meaning. A promissory note executed jointly by a company and its managing agent does not come."

Surety's liability to pay is not deferred until the creditor has exhausted his remedies against the principal debtor. In the absence of special equity the surety has no right to restrain an action against him by the creditor on the ground that the principal debtor is solvent or that the creditor may have relief against the principal debtor in some other

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proceedings. Likewise, where the creditor has obtained a decree against the surety and against the principal debtor the surety has no right to restrain execution against him until the creditor has exhausted his remedies against the principal debtor. Thus, the surety's liability is not deferred until remedies against principal debtor are exhausted. Liability of surety is not deferred until the creditor exhausts his remedies against the principle debtor.

Usury and Money Lending Legislation in India

In India the Usurious Loans Act, 1918 gives power to a Court to prevent enforcing a contract that is unconscionable and usurious. If a Court has reason to believe that the amount payable on a loan transaction is high or unfair due to a high interest rate that is being charged, the Act empowers the court to re-open the transaction and relieve the debtor of all liability in respect of any excessive interest. [53]

In 1984, the Banking Regulation Act, 1949 was amended by inserting section 21A which provided that, notwithstanding the provisions of the Usurious Loans Act and comparable state legislation, a court was prohibited from re-opening transactions between a bank and its debtor on the ground that the interest charged was excessive. This amendment has caused much controversy in the High Courts, and its scope and application has been interpreted differently, giving borrowers a useful defence in such cases.[54]Money lending Legislation enacted at state level provides for the registration of moneylenders, maintenance of accounts in a particular form, exemption to specific lenders or types of transactions etc. In practice, moneylenders' Legislation is not a problem to banks because most of the laws are confined to transactions involving small amounts and does not apply tobanks.

Terms of a Loan

When a loan agreement is being drafted, the covenants must be designed to achieve at least three objectives for the lenders. First, in addition to repaying the loan, a bank must commit the borrower to obligations such as providing financial information regularly to the bank, undertake not to dispose of its assets, or change its business activities. Second, the covenants must put the lender in a strong position when there is inability to pay. The bank must have the right to terminate the agreement, and where relevant, be released from providing further loans that were agreed. Third, they must enable lenders to recover the money when default occurs without difficulty, preferably without recourse to court. From a borrower's stand point, agreeing to these covenants may be regarded as the price he has to pay to secure a loan at areasonable interest rate. The borrower's concern, however, will be to minimize the intrusiveness of a bank into the freedom of how it conducts its affairs.

Documentation

It is fundamentally important that loan agreements are carefully drafted and documentation for security properly prepared. Loan documentation becomes most important at the time when steps are being taken to recover overdue debts, particularly if legal action has to be initiated. In such an event, the loan documents must be capable of being admitted as evidence in a court of law. When a borrower defaults and disputes arise, the defects at the outset of a loan are often used by borrowers to defend legal actions filed against them by the banks. Loopholes and defects in documentation offer strong defences to borrowers and consideration of these at trials are often very time consuming, resulting in long delays in litigation. If the documents were defective, the very purpose of obtaining documents at the stage of granting the loan would be defeated. It is therefore essential that due care is taken when loan documents are prepared, and the required procedure is followed.

Another aspect that must be looked at is the various disincentives in the law that prevents proper documentation. The problem revolves around minimising high stamp duty and registration fees when loan agreements are signed and security is taken. In India, an English mortgage is subject to heavy stamp duty. The advantage to a bank of taking this type of mortgage is that in the event of default, the security can be enforced by way of extra-judicial sale but banks tend to ignore this advantage because of the high cost involved in stamp duty. Banks prefer to take mortgages by way of a deposit of title deeds simply because they are not subject to stamp duty, even though to realise the security a court order is required. It is doubtful whether high stamp duty needs to deter banks from taking proper security. Inevitably, these charges will be passed on to the borrower and if it can be spread over the loan period the burden will not be prohibitive. The Supreme Court of India has also ruled that such costs and charges are allowable deductions for the purpose of income tax. If thetax deduction is taken into account, the argument that taking legal mortgages are expensive is considerably weakened.[55]

In India, a genuine attempt has been made to evolve an effective credit monitoring system throughout banks. The first step in this direction was taken in 1965 when the Credit Authorisation Scheme was introduced. Thereafter, several credit monitoring schemes were implemented following the recommendations of various study groups and working committees. The Tandon Committee, Chore Committee, Marathe Committee and Pendharkar Working Group have all made various recommendations. The greater part of these recommendations were on new lending norms, effective follow up systems and management information services (MIS) for monitoring of loans and the parameters for financing sick units.[56]

Types of credit facilities

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The lending activity is carried out by various banking and financial institutions. These institutions are providing various kinds of credit facilities to borrowers which are

Cash Credit, Overdrafts, Bills Finance, Term loans, Bridge loans, Composite Loans, Consumption Loans. In addition to the above there are various other non-based facilities like bank guarantee including financial guarantee, performance guarantee and deferred payment guarantee.

In India banks favor the granting of advances in the form of cash credit. In share of the entire bank credit the cash credit amount to fifty percent of the total credit. Under this method the bankers allow the customer to borrow up to a certain amount known as cash credit limit. Usually the borrower is required to provide security in the form of pledge or hypothecation of tangiblesecurities.

The method of granting advances under overdraft resembles the cash credit system. However, to avail of an overdraft facility the borrower has to open a current account. This account is allowed to be overdrawn up to a certain limit.

Securities for BankLoans

General Principles of Secured Advances

While granting advances on the basis of securities offered by customers, a banker should observe the following basic principles:

During the sanctioning of the amount on the basis of the collateral offered by the borrower the lending institutions should adhere to the basicprinciples.

(a) **Adequacy of Margin**: adequacy of the margin is very significant factor in the lending process. The lending institutors keep a safe margin during the sanctioning of theamount.

(b) **Marketability of Securities**: the loans are sanctioned for a period by the banking and financial institutions which are repayable on the demand. In case of the default of the payment by the borrower the collateral can be converted into liquidity. There it is very necessary that the collateral should be of such quality having quality ofmarketability.

(c) **Documentation**: loan agreements must be drafted, preferably by lawyers, to incorporate the individual terms and conditions of the loan. Properly drafted loan agreements could provide lenders with credit protection or give them influence over borrowers, or control over a loan. Detailed covenants, clearly setting out reporting and monitoring obligations by borrowers, also enhance credit protection to lenders. It I also an effective method of monitoring a borrower's performance after a loan have been granted. Covenants that require a borrower to provide information regarding its financial status would provide lenders with early warning signals of any financial difficulties a borrower may beexperiencing.

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Forms of securities for secure advances

Traditionally the land and building has been used as a security very well but with the passage of time there has been the change in the nature of security. There are series of the items which can be used as a security. The major categories are land, stocks & shares, debentures, goods, life policies, fixed deposits.

Charges overSecurities

In banking terms, creation of charge is a mode of creation of security for lending. In banking terms, creation of charge is a mode of creation of security for lending. Such a can be created by way of mortgage, hypothecation or pledge. in case of hypothecation the hypothecator can be in possession of the goods hypothecated and enjoy the same without causing any damage to the rights of the hypothecatee whereas in the case of pledge the possession of goods will be transferred to the pawnee and he will be in possession and the pawnor will not be able to enjoy the same as the possession has already been parted with.[57]

(d) Under Section 2(n) SARFAESI Act charge induced during hypothecation includes floating charge and crystallization of such charge into fixed charge on movable property. So the charge created in or upon any movable property, existing or future, created by a borrower in favor of a secured creditor without delivery of possession of the movable property to such creditor, as a security for financial assistance and includes floating charge and crystallization of such charge into fixed charge on movable property.

(e) Floating charge holders cannot be said to be holding a security interest in the asset until the charge crystallized.

(f) The governing idea of a floating security is to allow a going concern to carry on its business in the ordinary course, the effect of which would be to make the assets liable to constant fluctuation, and some event must happen or some act must be done by the mortgagee to crystallize the same.[58]

(g) In Evans v. Rival Granite Quarries Ltd. Buckley LJ observed:

(h) "A floating security is not a future security; It is a present security, which possibly affects all the assets of the company expressed to be included in it On the other hand, it is not a specific security; the holder cannot affirm that the assets are specifically mortgaged to him. The assets are mortgaged in such a way that the mortgagor can deal with them without the concurrence ofthe mortgagee. A floating security is not a specific mortgage of the assets, plus a license to the mortgagor to dispose of them in the course of the business, but is a floating mortgage applying to every item comprised in the security, but not specifically affecting any item until some event occurs or some act on the part of the mortgagee is done which causes it to crystallize into a fixed security." [59]Such a security can be created by way of mortgage, hypothecation orpledge.

Pledge of Security

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Pledge of security is a contract whereby an article is deposited with a lender as a promise or security for the repayment of a loan or performance of a promise. For the completion of the contract of pledge,, delivery of the goods to the banker is necessary. Delivery of title documents relating to the goods, or the key of the godown where the goods are stored, may be the sufficient to create a valid pledge. In the case of pledge an important precautions that a banker should take is to ensure that the pledged goods to the bank are free from prior encumbrance.

Hypothecation over Securities

Where a mortgage of movables is created by delivery of possession of goods, it is known as pledge, and where no possession is given it is termed as hypothecation. Hypothecation is used for creation of charge against the security of movable assets, but in this case the possession of the security remains with the borrowerhimself.

Lien

A lien may be defined a right to retain property belonging to a debtor until he has discharged the debt due to retainer of the property. Banker's lien is a general lien bankers have a general lien on all securities deposited with them as bakers by a customer, unless there be an express contract, or circumstances that show an implied contract, inconsistent with lien. in case of lien banker's right of sale extends only to fully negotiable securities.as far as such securities are concerned, the banker may exercise his right of sale after serving reasonable notice to thecustomer.

Assignment

This is also one of the modes of creating the charge on securities offered to the lender. It is transfer of ownership from one person to another person.

Mortgage

When the banker is securing advances with collaterals, the question whether particular collateral is a movable or an immovable property assumes significance. a mortgage may be created only by a transfer of interest in an immovable property. The mortgage may be created either by deposit of titled deeds, delivery of possession or by a registered document. It is relevant for determining the period of limitation for suit for declaration of the title to the property or for recovery of possession of the property. If the property is movable, then such suit is required to be filed within three years.

Summary of the chapter

This chapter has dealt with the overview and framework of the Indian banking sector. It focused on the credit system in India's banking industry during liberalization era. It also

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provides a brief overview of historical perspective of Indian banking industry with special emphasis on the reforms during liberalization phase since 1991.

In the phase of post-independence and before nationalization, Banking sector remained in the private hands of large industrialists who had their control in the management of the banks and were utilizing the major portion of financial resources of the banking system and as a result low priority was accorded to priority sectors. Like as other sectors of Indian Economy the baking sector also had suffered various structural problems by the end of 1980s. By the 1990 the Indian Banking sector was characterized as unprofitable, inefficient and financially unsound. India faced a serious economic crisis in 1991. There was a steep fall in the country's foreign exchange reserves to about $1billion, equal to the value of only two weeks' imports. There was a large fiscal deficit close to 10 per cent of GDP and an unsustainable external balance with current account deficit at 3 per cent of GDP. Faced with such a crisis, India adopted reforms involving macroeconomic stabilisation and structural adjustment programmes. They aimed at improving economic performance and accelerating the rate of economic growth through a transition from an inward- looking strategy to an outward-looking one and from a regime of licenses and controls to a system of incentives and price mechanism. At the core of the programme was a phased deregulation of the financial sector, along with reforms of trade and industrial policies. Until the late 1950s, the financial system in India was fairly liberal with no ceilings on interest rates and low reserverequirements.

In the early 1960s, the government tightened its control over the financial system by introducing lending rate controls, higher liquidity requirements and by establishing state development banks for industry and agriculture. This process culminated in the Nationalisation of the fourteen largest commercial banks in July 1969. Again in April 1980, six more commercial banks were Nationalised.

Various policies were used for the banking sector to gain influences such as interest rate controls, directed credit programme and statutory preemptions. In early 1980 the interest rate regulation almost steadily increased but in the late 1980s the degree of interest's rate controls was lowered. Since the beginning of the 1990s, the degree of interest rate controls has steadily declined which reflects that today most interest rates are determined by the market. the Indian economy initiated economic reforms, the Indian banking industry also made great advancement in terms of quality, quantity, expansion and diversification in keeping with the updatedtechnology.

The statutory ration of CRR and SLR has been gradually lowered since 1991. This statutory reduction resulted a greater flexibility for banks in determining both the volume and terms of lending. In the following years, reforms covered the areas of interest rate deregulation, directed credit rules, statutory pre- emption's and liberalization of the financial sector.

Removal of regressionist policies leads to an increased availability of capital. Introducing the globally accepted best practicing norms on Capital to Risk Asset Ratio (CRAR) requirement, accounting, income recognition, provisioning and exposure. Steps to strengthen risk management though recognition of different component of risk, assignment of risk weights to various asset classes, norms of connected lending, risk concentration, application of market tomarket

principle for investment portfolio limits on deployment of fund in sensitive activities. Introducing capital charge for market risk, higher graded provisioning for NPAs, guidelines for ownership and governance, securitization and debt restructuring mechanism norms, etc.

The liberalisation processes with a set of objectives especially the financial market has witnessed a strong revival of the Economy since 1991 especially the banking, insurance and capital market. The Banking sector in India consists of scheduled Commercial banks, Development Banks, Cooperative Banks, Regional Rural Banks, and even Non-Banking Financial Companies. The reforms in this sector introduced a new creative and competitive environment for the affluence of banking sector as a whole. In India laws facilitating free market economic policies are being actively promoted, by the introduction of new laws as well as the amendment of existinglegislation.

India has completed more than two decades of its economic reforms. The economic reforms can be successful if the country keeps pace with the global trends and maintains parity with important economic and finance sector legislations in other countries. The biggest challenge is hence to create efficient, well integrated and transparent machinery.

The introduction of financial sector reforms in 1993 brought to fore the extent of NPAs in a structured fashion, and the stock of NPAs is being tackled through various measures. Detailed steps have been introduced by the Government of India on lines of the recommendations of two reports of Narasimhan Committee on arresting and containing the growth of NPAs. In the year 1993, RBI introduced prudential norms as conveyed by the Basel Accords of 1988 applicable to IndianBanks.[60]

Institutional and Legislative Reforms

- Establishment of Debt Recovery Tribunals, Asset Reconstruction Companies, Corporate Debt Reconstructing Mechanism and Lok-Adalats (people's court), etc. for quick recovery ofdebts.
- Introducing the asset reconstruction and by the Legislative framework and its subsequent amendment for ensuring the rights of thecreditors.
- Setting up of Credit Information Bureau of India Limited for sharing of information of the borrowers anddefaulters.

- Establishment of Board of Financial Supervision as the watchdog for the banking, financial and non-banking financialcompanies.
- Introduction of the consolidated supervision, strengthening of off-site surveillance through control returns.

Till 1990s, Indian Banking Sector was mostly used by the government as one of its departments to finance its fiscal deficits at low costs, channelize money towards the weaker sections of the society. Reserve Bank of India (RBI) controlled all Banks with iron fist and banks had very little discretion in fixing the interest rates for advances and deposits, recruitment policies, decision on branch expansion, etc. Consequently, banking industry was flooded with loans or assets, which failed to perform, or turned out bad.

Loan transactions may be secured or unsecured. Lenders will be prepared to grant unsecured loans if the creditworthiness of borrowers sufficiently assures that the loan will be repaid. Most lenders in developing countries however, do not lend without security. Lending institutions demand security as a pre- condition to the granting of credit irrespective of the extent of the risk involved. If bankers were to grant unsecured loans, their credit appraisal must be carried out to an extremely high standard, where the risk element is assessed as accurately as possible.

Security improves the position of lenders in two circumstances. First, if a debtor becomes insolvent, a lender as a holder of valid real estate security will be in a position of pre-eminent advantage. As a holder of such security, a lender is entitled to enforce its rights of realisation of that security independently, and thereby stand outside the insolvency process. If security had not been taken, a lender would be regarded as an unsecured creditor, and would have to prove a claim in the insolvency proceedings, for a pro rata settlement of its debt. Second, if a borrower defaults payment, a lender who has taken security would be able to recoup his losses by enforcing the security. Under SICA Act ,1985 regime there it effectively blocks secured creditors from enforcing theirsecurity in the event the debtor becomes "sick" or "potentially sick. According to section 22 of the Act, notwithstanding any law, if an inquiry were pending or a rehabilitation scheme were under consideration, and various other actions only with the consent of the Board. Clearly, as a matter of law, section 22 blocks the exercise by creditors' of their rights of security. The suspension imposed on secured creditors is not time bound. Consequently, creditors will be unable to exercise their rights until a rehabilitation scheme either succeeds or fails which in practice may take severalyears.

Credit is no longer solely based on the assessment of individuals of the borrowers who they know personally but also on assessment of others that the borrower has no direct contact at all. It is no longer solely based on information obtained from face-to face contacts but also on the analysis and judgment of a specialized third party, and limited to the use of borrower and lender, but also acquires the nature of public goods. These features of modem credit culture develop it into a huge industry and hence have a far reaching impact on the social and economic life.

'Collateral' is not mandatory in the securing of a loan. Lenders, however, will favour the availability of security, if, in the bank's view, there is an element of doubt as to the repayment capacity of a borrower. The amount of collateral that is taken must reflect that element of doubt. As Weerasooria writes:

"Many customers believe that the primary requirement for obtaining a loan from a bank is the availability of satisfactory security, but this is a misconception. No doubt banks are concerned assessment but if the potential borrower were engaged in a business that has an uncertain market, lenders would be reluctant to advance themoney.

Assessing the credit rating of a potential borrower is a specialised function of a lender. Whilst there are lending guidelines, each loan application must be treated on its merits. Lenders must gather all the available information and then attempt to reach an objective decision. A country aiming to achieve economic growth by promoting private investment must secure creditors' rights. Unless creditors' rights are recognised and protected, lenders would be compelled to adopt restrictive lending policies. This may lead to high interest rates, and low volumes of lending that directly affect the economic growth of a country. it is to be concluded that none of the principles mentioned above should be read in isolation while considering the a proposal for an advance. What is required is a judicious blending of all these principles when evaluating a loan proposal. in individual cases, it may be necessary.

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