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PROBLEMS RELATED TO LOAN GRANTING AND ITS RECOVERY ON COMMERCIAL BANKS

A special reference in Bagalkot District

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ABSTRACT:

Introduction: Loan has become a vital function on operation because of its direct effect and impact on economic growth and business development. And also Loan recovered could adversely affect banks. Therefore a need for arriving a strategies for efficient loan recovery.

Review of literature: J D Jam (1971) in his article the role of commercial banks in financing agriculture' suggested that for extending quicker and easily available, timely credit to the farmers at lesser cost, a credit information bureau must be set up in each village.

Objective of study: To find out the several problems facing loan recovery, the effects of loan default on commercial banks and the measures that will be used in reducing the incidence of loan default.

Methodology of study: The study depends upon primary data only. For selecting the sample, the researcher has followed stratified random sampling method. From each branches 5 samples were selected on the basis of the beneficiary list given by the banks. From the list, the beneficiaries were classified into Agriculture-10, Corporate enterprises -25, Industries-15 and 25 from self-employment.

Reference period: Reference period must be one year for this research i.e. 2018

Sources of data: Relevant data were collected from both primary and secondary sources. Questionnaires were the main primary data collection instrument employed while data from various relevant publications constituted the sources of secondary data.

Statistical tools: Primary data are analysed by using appropriate statistical tools such as percentage, and Chi

square.

Hypothesis of the study: Ho: The measures taken by banks do not reduce the incidence of loan default and H1: The measures taken by banks to reduce the incidence of loan default.

Data analysis and Interpretation: The researcher assembled, presented and analyzed the relevant data gathered. In this article should be the bank's system of classifying the nature of loans and loan beneficiaries are to be used in this analysis.

Finding: In this article researcher find that there has been default on loan repayment and also find the major effects these have on banks is that the loan is reduced to minimum.

Suggestion: This article was suggested that commercial banks should use some risk control measures to guide against loan default. In addition, before granting loan, they should examine critically the project statement submitted by the customer or borrower, which will help them to find out the realistic repayment pattern and help them in knowing if the projects are realistic based on the customer's past performance.

Conclusion: This article wish to conclude by saying that risk in credit creation through loan granting cannot be completely wiped out.

Key word: Commercial Banks, Loan Granting, Loan Recovery

INTRODUCTION:

Commercial banks carry on ordinary banking business with the general public, changing cash for bank deposits and bank deposits for cash, transferring bank deposit from one corporation to another, giving bank deposit in exchange of bills of exchange, providing of trustees and executor's services, providing safe custody of funds and valuables as well as foreign exchange remittance. Though commercial banks differs from country to country, their profit and banking motives are the same. Their activities are of interest to their customers, staff, and shareholders. The commercial objective of the bank is to maximize profit, though other social and economic function tends to deflect banks from profit maximization. The aims and objectives of commercial banks have therefore paved way for their customers to make and obtain credits, in form of loan of which the researcher is interested in.

Lending has become a vital function on operation because of its direct effect and impact on economic growth and business development. The banking sector mobilize surplus funds from small and big savers who have no immediate need for such funds. The users of these funds are the business entrepreneurs and investors who have brilliant ideas on how to create additional wealth in the economy but lack the necessary capital to execute their ideas. These groups of people approach banks to obtain loan. Lending is a risky venture which banks only engage on after a rigorous and satisfactory analysis of the project for which lending is being made. The main preoccupation of banks is extending loans to their customers. Thus, the formulation and implementation of such lending policies are some of the important responsibilities of the management of the bank. The lending

policy of a bank must be specific on how much loan will be made available to whom, what period and for what reason. For this reason, lending policies should be well documented so that lending officers will be able to know the areas of prohibition and the area of where they can operate. In addition, such policies should be subjected to periodic review to make the banks keep abreast with the dynamic and innovation nature of the economy as well as competing with other changing economic sector.

Banks in recent times has failed as a result of loan recovery problems. Loan is the major source of bank profitability. However, in going about their lending activities, banks have their own objectives among which are profitability, growth, safety, suitability and liquidity. Loan, when not recovered could adversely affect banks. It is easily granted than recovered. It usually needs proficiency i.e. competency and expertise in the recovery process. It sometimes become an uphill task to recover. When they are not recovered, the impact is often disastrous to the bank. It can lead to illiquidity, insolvency and even distress as the case may be. Therefore a need for arriving at strategies for efficient loan recovery. That is the peak of the problem associated with borrower's character and willingness to repay a loan is not directly measurable.

LITERATURE REVIEW:

J D Jam (1971) in his article the Role of 'Commercial Banks in financing agriculture' suggested that for extending quicker and easily available, timely credit to the farmers at lesser cost, a credit information bureau must be set up in each village.

Sharma B.P. (1974) in his book 'The Role of Commercial Banks in India's developing economy' stated that the commercial banks had a very important role to play in shaping the economy of the nation. They could serve as 'shock absorbers' and 'effective-feelers' on the one hand and the 'circulator of funds' in the arteries and veins of the money and capital market on the other.

Akuakaelem Maria .M. (2000), in her contribution enumerated some of the causes of loan default as decline in business, abandonment of account, delay in project completion, diversion of funds and increase in interest rate. Also bad debt in lending are caused by highly defective loan administration operations at the bank which stem from the over bearing influence of directors who relegates central rules in favour or personal and political interest by virtue of the nature of appointments.

OBJECTIVES OF THE STUDY:

- To know the effects of loan defaults on commercial banks.
- To find out the several problems facing loan recovery.
- To measures that will help to reduce the incidence of loan default.

RESEARCH METHODOLOGY:

➤ **Research design:**

The research design used for this work is survey design. Here, group of people were studied by collecting and analyzing their data. These groups of people were selected from the population to represent the population sample. This is a field survey type of research, supported by library research work..

➤ **Sample size:** 75

➤ **Reference period:** One year i.e. 2018

➤ **Source of data collection:**

Information was gathered through primary and secondary source of data collection.

The **primary source** constituted the major source due to the responses to the questionnaire that was distributed to the staff of the bank.

The **secondary source** was collection from textbooks, journals and write-ups of some scholars.

➤ **Method of data collection:**

The method of data collection was structured questionnaire, which were distributed to the staffs of the bank to get at facts as regards to the nature of the loan granted, the number of loan beneficiaries and the number of loan defaults, those that pay promptly and other relevant questions.

STATISTICAL TOOLS:

Primary data are analysed by using appropriate statistical tools such as:

- percentage, and
- Chi square

HYPOTHESIS OF THE STUDY:

Ho: The measures taken by banks do not reduce the incidence of loan defaults.

H1: The measures taken by banks to reduce the incidence of loan defaults.

ANALYSIS AND INTERPRETATION OF DATA:

The researcher used some methods in the cause of carrying out this research. These includes: questionnaire, tables, figures and percentages. The researcher assembled, presented and analyzed the relevant data gathered. Structured questionnaire were distributed to the staff of the bank. Only the branch manager, accountants and top officials of the bank, including other staffs of the bank were chosen to fill the questionnaire. It is from the information from the respondents, that the analysis was made possible. It should be noted also that the bank's system of classifying the nature of loans and loan beneficiaries are to be used in this analysis. The researcher at this point starts to present the data.

Table 4.1:**Type of loan grant**

Types of loan grant	Respondents	Percentage
Short-term	44	58.67%
Medium-term	21	28%
Long-term	10	13.33%
Total	75	100

(Sources: Field survey 2018)

Table 4.1 depicts that 44 respondents or 58.67% of the sample size agreed that the bank grants short-term loan. 21 respondents or 28% of the sample size said that the bank grants medium-term loan and 10 respondents or 13.33% sample size said that the bank grant long –term loan.

Table 4.2:
Sectorial allocation of loan

Types of Sectorial	Respondents	Percentage
Agricultural loan	8	10.67%
Industrial loan	39	52%
Personal loan	19	25.33%
Corporate enterprises	9	12%
Total	75	100

(Sources: Field survey 2018)

Table 4.2 depicts that 8 respondents said that they grant agricultural loan. 39 respondents of the sample size said that they grant industrial loan while 19 respondents of the sample size said that they grant personal loan. Only 9 grant Corporate enterprises.

Table 4.3:**Problems faced during loan recovery**

Problems faced during loan recovery	Respondents	Percentage
Customer unable to pay	11	14.67%
Lack of collateral	23	30.67%
Inability to arrest customer	41	54.66%
Total	75	100

(Sources: Field survey 2018)

Table 4.3 shows that the entire respondent said that they faced the problem of lack of collateral, customers unable to pay or repay loans during loan recovery and inability to arrest customers

Table 4.4:**Defaulters of loan repayment on sectorial**

Defaulters of loan repayment on sectorial	Respondents	Percentage
Agriculturalists	11	14.67%
Industrialists	14	18.67%
Personal	4	5.33%
Corporate enterprises	46	61.33%
Total	75	100

(Sources: Field survey 2018)

Table 4.4 depicts that 46 respondents or 61.33% of the sample size agreed that corporate enterprise are the greatest defaulters of loan repayment.

Table 4.5:**Highest rate of loan repayment on sectorial**

Highest rate of loan repayment on sectorial	Respondents	Percentage
Agriculturists	8	10.67%
Industrialists	13	17.33%
Personal	48	64%
Corporate enterprises	6	8%
Total	75	100

(Sources: Field survey 2018)

Table 4.5 depicts that 48 respondents or 64% of the sample size agreed that individuals have the highest rate of loan repayment.

Table 4.6:**Reduce the incidence of loan default**

Reduce the incidence of loan default	Respondents	Percentage
Demand notice	9	12%
Taking legal action	43	57.33%
Realizing the security	23	30.67%
Total	80	100

(Sources: Field survey 2018)

Table 4.6 depicts that respondents or 12% of the sample size agreed that demand notice is the measure that will be used to reduce the incidence of loan default. 43 respondents or 57.33% of the sample size said that taking legal action will be used to reduce the incidence of loan default. While 23 respondent or 30.67% of the sample size agreed that realizing the security will also help in reducing the incidence of loan default questionnaire. The relevant answer will be considered in order to determine the causes of variation in individual banks operations.

HYPOTHESIS OF STUDY:**Hypothesis 1:**

Ho: The measures taken by banks do not reduce the incidence of loan defaults.

H1: The measures taken by banks do reduce the incidence of loan defaults.

Chi Square of Hypothesis

Variable	O	E	(o-e)	$o-e^2$	$(o-e)^2/e$
Demand notice	9	11	2	4	0.36
Taking legal action	43	41	-2	- 4	0.09
Realizing the securities	23	23	0	0	0
Total	75	75	0	0	0.45

Computed value of $x^2 = \sum (o-e)^2/e$ Degree of freedom = $(R-1)(C-1)$

= $\frac{0.45}{2} = 0.225$ = (2-1)(3-1)

Level of significance = 0.05 X^2 distributions (2, 0.05)

The table value of X^2 is 5.991

Decision:

If the computed value of $X^2 >$ than the table value of X^2 rejected the Ho hypothesis and accepted H1 hypothesis but if the computed value of $X^2 <$ than the table value of x^2 accepted the Ho hypothesis and rejected the Hi hypothesis, which means that there are measures that will not reduce the incidence of loan defaults.

Hypothesis 2:

Ho: Loans to individuals do not record higher rate of loan defaults.

H1: Loans to individuals record higher rate of loan default repayments.

Chi Square of Hypothesis

Variable	O	E	(o-e)	o-e ²	(o-e) ² /e
Agriculturist	8	10	2	4	0.4
Industrialist	39	39	0	0	0
Individual	19	21	2	4	0.19
Corporate bodies	9	5	-4	16	3.2
Total	75	75	0	24	3.79

Computed value of $\chi^2 = \sum (o-e)^2/e$ Degree of freedom = (R-1)(C-1)

$$= (2-1)(4-1) \\ = 3$$

Level of significance = 0.05 χ^2 distributions (3, 0.05)

The table value of χ^2 is 7.815

Decision:

If the computed value of $\chi^2 >$ than the table value of χ^2 rejected the Ho hypothesis and accepted H1 hypothesis but if the computed value of $\chi^2 <$ than the table value of χ^2 accepted the Ho hypothesis and rejected the Hi hypothesis which means that there are measures that will not reduce the incidence of loan defaults.

FINDINGS:

The researcher have so far tried to make a combined analysis given by the banks to the question asked. Most commercial banks grants short-term loan. It was also discovered that there has been default on loan repayment. The major effects these have on banks is that the loan is reduced to minimum. And this affects the lending capacity. This is done as a last resort because it is cumbersome, time consuming and expensive and also because it represent a sad way to terminate what probably was an interesting banker-customer relationship.

SUGGESTION:

The following recommendations were made:

- Commercial banks should monitor its outstanding loans in order to identify promptly loans, which a borrower fails to repay as scheduled.
- Commercial banks should use some of the risk control procedures to guide against losses. An example of this is covenant, which is a written agreement whereby the borrower commits himself of providing specific financial statement at specific intervals during the life of the loan.
- Before granting loans, commercial banks should examine critically the project of financial statement provided by the customer (cash budget, income statement). This will help them find out the realistic repayment pattern and help them I knowing if the projects are realistic based on the customers past performance.

CONCLUSION:

The researcher wish to conclude by saying that risk in credit creation through loan granting cannot be completely wiped out because of the futuristic nature of loan repayment schedule. Most of the loans granted by Bagalkot district Commercial Banks are not repaid and turn out to be bad Debt.

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