

BANK CREDIT

Ashok Purohit
Dr. Ritu Meena



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CHAPTER 1

OVERVIEW OF BANK CREDIT: UNDERSTANDING THE BASICS

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ABSTRACT:

An introduction to bank credit provides a solid knowledge of a key financial idea that supports borrowing and lending in contemporary economies. Bank credit describes the lending of money by banks to people, organizations, and governments for a variety of uses. The fundamentals of bank credit are covered in this chapter, along with its kinds, significance, and essential components. Loans, credit cards, and overdraft facilities are only a few examples of the financial goods covered by bank credit. With the agreement to return the borrowed money plus interest over a certain time period, these credit instruments provide borrowers access to cash for immediate usage. In contrast to unsecured credit, which depends on the borrower's creditworthiness, secured credit needs collateral. This difference is explained in the chapter. In its capacity to promote financial transactions and economic progress, bank credit plays a crucial role in society. While corporations utilize credit for operational requirements and growth, individuals may use credit for personal purposes like house purchases or higher education. The importance of credit in facilitating investment, consumption, and liquidity management is described in this chapter.

KEYWORDS:

Bank Credit, Economic Progress, Growth, Investment, Liquidity Management.

INTRODUCTION

The terms and ideas pertaining to the practice of banking are referred to as banking basics. The banking sector handles credit facilities, cash holding, investments, and other financial dealings. Because it distributes money to borrowers who have profitable assets, the banking sector is one of the main forces behind most economies. Deposits and withdrawals, currency exchange, forex trading, and wealth management are just a few of the many tasks that banks carry out. Additionally, they serve as a conduit between depositors and borrowers by offering credit facilities to those who want to borrow using the money that clients deposit with them.

What are the fundamentals of banking?

Banks gain profit by levying an interest rate on loans that is greater than the interest rate on client deposits, which is how they generate revenue. They must, however, abide by the rules established by the national government or central bank.

Basics of Banking: Types of Banks

The following categories of American banks are the most prevalent ones:

1. Business banks

The most prevalent kind of bank is a commercial bank. They provide a range of services, including business loans, deposit acceptance, and basic investment products to both private persons and enterprises.

Additionally, commercial banks provide treasury services, insurance products, retirement products, merchant services, global trade services, and other financial services. They generate revenue by offering business loans to private and public borrowers and collecting interest payments from them as well as by charging service fees.

2. Second, credit unions

A credit union is a form of bank that accepts membership applications from a limited group of individuals. It is run on the principle of people assisting others and is member-owned. In the past, credit unions offered services to people who were either local community members, churchgoers, staff members of a certain business or institution etc. Credit unions are able to provide its members with more individualized and affordable banking services because to their ownership structure. Credit unions may provide greater interest rates than banks because of their smaller operational scale, and clients might establish stronger bonds with the banking staff. The activities of credit unions are constrained, and consumer deposits are less easily available[1]–[3].

3. Financial institutions

Investment banks provide business customers access to the capital markets so they may raise money for growth. They assist businesses in raising money on the stock and bond markets to pay for their growth, acquisitions, or other financial ambitions. They can make mergers and acquisitions easier by locating prospective target firms that fit the buyer's requirements.

Describe bank credit

The amount of credit made available to a company or person by a financial institution in the form of loans is known as bank credit. The entire amount of money that a person or corporation may borrow from a bank or other financial institution is consequently known as bank credit.

The capacity of a borrower to repay any loans as well as the total amount of credit that the banking institution has available to lend determine the borrower's bank credit. Mortgages, personal loans, and auto loans are examples of bank credit products.

A key mechanism for facilitating borrowing and lending between people, corporations, and organizations, bank credit is a basic idea in the fields of finance and economics. This summary gives readers a basic grasp of bank credit, including its varieties, importance, and major actors.

Definition and goals

Borrowing money from a financial organization, usually a bank, with the commitment to pay back the money borrowed plus interest within a certain time frame is known as bank credit. It provides a way for people, companies, and governments to acquire money for a range of uses, including investments, asset purchases, cash flow management and addressing crises.

Understanding bank loan

The money that banks and other financial organizations lend to their customers is how they earn money. Customers deposit money into their checking and savings accounts or make investments in certain types of investment instruments, including certificates of deposit (CDs), to provide these funds. Banks provide their customers a little amount of interest on their deposits in exchange for utilizing their services. As said, this cash is then loaned to others and is referred to as bank credit.

The entire sum of cash that financial institutions loan to people or companies is known as bank credit. It is a deal in which lenders, such as banks, lend money to borrowers. A bank basically trusts borrowers by giving credit that they will pay back the principle amount and interest at a later time. The evaluation of a person's creditworthiness determines whether or not they are authorized for credit and how much they get. The borrower's credit score, income, and other factors are taken into account while determining approval. This includes any assets, collateral, or the total amount of debt they now owe. Cutting the overall debt to income (DTI) ratio is one of the strategies to guarantee approval. A DTI ratio of 36% or less is considered appropriate.

In general, lenders advise borrowers to pay off all past-due bills and maintain their card balances at 20% or less of their available credit. Banks sometimes provide loans to customers with poor credit records on terms that are advantageous to the banks, such as higher interest rates, smaller credit limits, and more onerous conditions.

Particular Considerations

Bank credit for people has significantly increased as customers have gotten used to using debt to fund a variety of necessities. This covers credit that may be used to buy things required for everyday use as well as financing for major purchases like homes and cars. Businesses may finance their ongoing operations by using bank credit. Many businesses want money to cover initial expenses, purchase products and services, or boost cash flow. Therefore, small enterprises or startups need bank loans as short-term finance.

Bank Credit Types

There are two types of bank credit: secured and unsecured. Secured debt or credit is secured by some kind of collateral, such as money or another movable object. The actual property itself serves as security in the event of a mortgage. To qualify for a secured credit card, banks may additionally ask certain borrowers to put up cash as collateral.

Secured credit lowers the risk that a bank assumes in the event that the borrower fails on the loan. Banks have the option to take the collateral, sell it, and use the revenues to settle the debt in whole or in part. This kind of financing often has a lower interest rate and more palatable terms and conditions since it is backed by collateral.

On the other hand, unsecured credit is not secured by any kind of asset. Compared to secured debt, these credit instruments have a larger risk of default. As a result, banks often charge lenders higher interest rates for unsecured borrowing.

How Bank Credit Works

Bank credit is a loan that is given to a firm without any kind of security or collateral. Similar loans are made available to people via bank credit cards, while loans for businesses are made at a specific interest rate and paid back in installments, through open credit, or through revolving credit. Bank credit enables a company to satisfy its financial obligations, but for its financial statements to be sound, it must have the proper proportions of debt and equity. Borrowers are provided this credit in order to provide the paperwork the Bank requires. The loan covenant makes appropriate mention of interest rates and payback periods. Financial statements are one kind of documentation the Bank must get.

- a. Tax-related documents.
- b. Financial projections over the next three to five years.
- c. Variations depend on the kind of loan and the individual.

DISCUSSION

Characteristics

Before a bank credit letter is issued, several people and organizations work together. Through the debate that follows, let's have a better understanding of the parties and their personalities.

1. A borrower is someone who obtains credit.
2. Lender: The bank is often the one that makes loans.
3. Interest Rate: The interest rate may be either fixed or variable. Benchmark rates like LIBOR and MIBOR are used to determine the floating interest rate.
4. Repayment terms must be rigorously followed to avoid the prepayment penalty. These terms are outlined in the loan covenant.
5. Loan Mode: Usually donated in cash, but sometimes supplied as raw materials or fixed assets.

#1 - Borrower-based categorization

Let's talk about borrower-based categorisation.

Loan for Personal Use, Number One

Personal loans are provided to individuals and groups in order to satisfy their unique requirements. For instance, people take out personal loans to buy consumer items, gadgets, homes, automobiles, etc.

#2 - Loan for Professional or Business Needs

These loans are provided to help the firm with its demands. To address a short-term liquidity crisis, it may take the form of a cash credit facility or working capital loan. Businesses borrow money to diversify into new product lines, consumer groups, and significant fixed asset growth. Depending on the conditions, requirements, and surroundings in which the firm works, the purpose of a loan will vary for various companies. Let's talk about categorization based on security in section number two.

First, a secured loan

Secured loans are backed by collateral, which serves as a third party's guarantee to the bank. Loans may be backed by property, debts, stock, fixed deposits, and any other asset that the bank may be able to sell or liquidate in the event that the borrower defaults on an installment payment.

Bank will also provide credit in exchange for a guarantee from a third party provided on the borrower's behalf. If a guarantee is given, the guarantor will be responsible for paying the difference if the borrower doesn't make payments as agreed.

Second - Unsecured Loan

Unsecured loans are not backed by any assets, and the bank is not given any guarantees either. A borrower who has a strong track record of on-time payment of debts, a high credit score, and solid financial standing would often be approved for an unsecured loan. Unsecured loans are often given out by little banks, "Patpedhies," and family members.

#3 - Duration-Based Classification

Let's talk about categorization based on length.

First, short-term loans

These loans have shorter terms, ranging from one month to one year.

- a) Credit card loans: These are often made for a month. To meet the daily requirements of companies and people, the Bank offers credit cards to borrowers. Sales managers get credit cards with a set spending limit on them to use for travel and other sales-related costs. People use credit cards to pay for daily expenses.
- b) The Cash Credit Facility or Bank Overdraft Facility allows holders of current accounts to withdraw more money than their account's debit balance. When a firm has a cash constraint and needs to pay off unexpected expenses, CC or bank OD facilities are often utilised.

Working capital loans come in both short- and long-term varieties. It relies on the company's cycle of working capital. In a business that offers seasonal items, the working capital cycle may last for more than a year. When businesses are unable to successfully manage working capital, they must get a working capital loan. When working capital loans are required, the stock turnover ratio is larger and the credit duration granted by vendors is shorter than the credit period granted to debtors.

Second, long term loans

The stock turnover ratio indicates how rapidly companies can transform stock into revenues.

These loans are granted over a longer period of time, such as three to five years or more. These loans are offered for company growth, product portfolio diversification, significant fixed asset investments, and real estate purchases when it is not feasible to repay the loans within a year due to the high cost of the purchases[2], [4], [5].

Purpose

Even while banks provide a broad range of loans, including traditional mortgages, loans, and bank credit cards, these loans are appealing to companies for a number of reasons. Through the following explanation, let's better grasp why banks provide these loans and why firms choose them over other solutions.

- a) **Educational Loans:** These are offered to students who choose to pursue higher education, and they must be repaid after they have graduated. The loan accrues interest over time.
- b) **Housing Loans:** These are provided for house purchases. The EMI principal is used to determine how much principal and interest must be repaid. These loans include a house as security, and there is a lot of paperwork needed.
- c) **Vehicle Loans:** These may be used to buy trucks, automobiles, tempos, and other vehicles. Assets are typically hypothecated to the Bank up to and until the last payment is paid. On the rear of automobiles, you often find the writing "we banked.... Bank." This denotes that a loan was obtained from "Bank."
- d) **Vendor Financing:** This is a plan offered by the Bank in which the borrower agrees to pay the Bank after, say, 60 or 90 days, in exchange for the Bank paying the vendors in accordance with the agreed-upon credit conditions. The borrower is assessed interest by the Bank for making advance payments to suppliers. The Bank will just need a minimum amount of paperwork as a result.
- e) **Letter of Credit Facility:** Similar to vendor financing, but mostly used for importing products or paying foreign suppliers. The parties mutually agree on the terms of repayment and the interest rate.

Advantages

Let's examine the benefits of obtaining a bank credit letter using the examples below.

- a) The loan cannot be repaid immediately. Since the terms of repayment and the interest rate have already been determined, cashflows can be better controlled.
- b) When people or companies need money, it might be helpful.
- c) Only for a certain amount of time may interest payments be agreed upon and paid; for the remaining time, the borrower will only make principle payments.
- d) Because the cost of debt is lower than the cost of equity, a portfolio with the right amount of debt leverages the cost of debt to increase returns to equity owners.

Disadvantages

Despite the many benefits listed above, there are a few issues that make obtaining the necessary financing difficult or problematic. Let's look at the explanation below to see why, in certain circumstances, a bank credit card could be preferable than this kind of loan[6]–[8].

- a) If payments are not paid on time, a borrower can be forced to give up ownership of an asset.
- b) The bank assesses one-time processing costs that need advance payment.
- c) If the borrower repays the loan early, there is a prepayment penalty.
- d) Businesses should have the proper debt-to-equity ratio. It will be challenging to pay interest in the case of a crisis if the Companies heavily rely on loans.

CONCLUSION

In conclusion, it is critical for people, companies, and economies as a whole to obtain a general grasp of bank credit and its fundamentals. The primary engine of the economy, bank lending promotes investment, consumption, and expansion. Banks help people accomplish their personal objectives, businesses fulfill their corporate aspirations, and governments finance public initiatives by providing loans and credit lines. Borrowers are better equipped to manage their responsibilities and make wise financial choices when they have a firm understanding of the fundamental ideas, such as collateral, interest rates, and creditworthiness. In a similar vein, banks must carefully assess the characteristics of borrowers and the state of the economy to reduce the risk of non-repayment. The interaction between borrowers and lenders within the context of bank credit is what supports financial stability and economic cycles. It is essential for policymakers, economists, and investors to comprehend the supply and demand for credit as well as how it affects inflation, employment, and the general health of the economy.

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CHAPTER 2

TYPES OF BANK CREDIT: LOANS, OVERDRAFTS, CREDIT CARDS AND MORE

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ABSTRACT:

A wide range of financial products that meet different borrowing requirements are included in the idea of bank credit. This chapter examines the many forms of bank credit, stressing the differences between secured and unsecured credit and providing details on the functions that each kind performs in both personal and commercial finance. A variety of credit instruments, including loans, credit cards, lines of credit, and overdraft facilities, are included in bank credit. Unsecured credit is dependent on the borrower's creditworthiness, while secured credit, where collateral is pledged, offers lenders a safety net. This chapter explores each of these categories, highlighting its unique traits and repercussions. Mortgage loans and auto loans are two examples of secured credit that provide borrowers access to bigger quantities of money with the necessity of security. The chapter explains the benefit of secured credit's lower interest rates and longer payback durations. Credit is extended without the requirement for collateral with unsecured credit, which is exemplified by credit cards and personal loans. Instead, the lender relies on the borrower's credit history and income. For both forms of bank lending, the importance of credit ratings and financial history becomes clear as a key factor. This chapter emphasizes how important these elements are in determining the conditions of the loan and the total cost of credit.

KEYWORDS:

Credit Cards, Consumers, Financial History, Lenders, Mortgage Loans, Unsecured Credit.

INTRODUCTION

Credit is an arrangement in which the borrower accepts funds from the lender in exchange for agreeing to pay interest for the time the funds are kept with the borrower and making a commitment to return the funds after a defined length of time. Mortgage loans, letters of credit, bank guarantees, consumer credit, trade credit, etc. are only a few examples of the many forms of credit.

Describe bank credit.

The amount of credit made available to a company or person by a financial institution in the form of loans is known as bank credit. The entire amount of money that a person or corporation may borrow from a bank or other financial institution is consequently known as bank credit. The capacity of a borrower to repay any loans as well as the total amount of credit that the banking institution has available to lend determine the borrower's bank credit. Mortgages, personal loans, and auto loans are examples of bank credit products.

Variety of Credit

Let's examine the different credit categories.

1. **Revolving credit:** This kind of credit enables customers to borrow money up to a certain limit, pay it back, and then borrow more. Credit cards, retail cards, and lines of credit are a few examples of this sort of credit.
2. **With installment credit,** you borrow money up front and pay it back over time in a series of recurring installments. Loans for cars, students, and mortgages are a few examples of this form of finance.
3. **Charge Cards:** Users must settle their debt in full at the conclusion of each billing cycle. American Express and Diners Club credit cards are two examples of this kind of credit.
4. **Secured Credit:** This kind of credit requires the borrower to put up collateral, such a vehicle or home, to guarantee the loan. Car loans and home equity loans are two examples of this sort of financing.
5. **Unsecured Credit:** This does not need any kind of security and is usually determined by the creditworthiness of the borrower. Credit cards and personal loans are two examples.

Bank Credits by Type and Credit Purpose

Loans are categorized by their objectives into seven major groups by Ruse and Hudgins:

1. Short-term loans for construction and land development as well as longer-term loans to fund the acquisition of farms, houses, apartments, commercial buildings, and international assets are all examples of real estate loans that are secured by real property, which includes land, buildings, and other structures.
2. Credit given to banks, insurance firms, finance businesses, and other financial institutions is referred to as a financial institution loan.
3. Farms and ranches are given access to agricultural loans to help with crop planting and harvesting as well as animal feeding and care.
4. Businesses get commercial and industrial loans to support the cost of buying inventory, paying taxes, and making wages.
5. Loans to people may be given directly to them or indirectly via retail dealers and can be used to pay for the purchase of cars, mobile homes, appliances, and other retail products as well as house repairs and modernization projects.
6. All loans not mentioned above, including securities loans, are categorized as miscellaneous loans.
7. Receivables financed by leases, in which the lender purchases cars or equipment and leases them to its clients.

Types of Bank Credits By Credit Duration

Loans may be divided into three groups based on the length of time they are granted:

1. The repayment period for short-term loans is one year. To address their short-term borrowing requirements, businesses borrow money. The most common collateral for short-term loans is inventory and accounts receivable. These loans may also be unsecured, like a revolving credit line.

2. Midterm loans are paid back over a period of one to five years. Such loans are often secured by immovable property and are issued by banks. Mid-term loans have greater interest rates than short-term loans do.
3. Loans with a payback duration longer than five years are referred to as long-term credits. Long-term loans are used to build homes, factories, and other structures as well as to buy machinery, equipment, and land. For these loans, immovable property is utilized as security.

Types of Bank Credits Organized by Credit Nature

1. Through current accounts or loan accounts, the bank grants funded credits also known as non-documentary credits to people and organizations. Loans, cash credits, and bank overdrafts are all examples of financed credits [1]–[3].
2. Credits that are not financed or documented are granted via the issuance of different papers. In this kind of credit arrangement, the bank offers the loan by providing their good names and reputations rather than actual funds. The terms of a letter of credit (LC), a bank guarantee, etc. are examples of non-funded credit.

DISCUSSION

Credit in borrowing and lending

A financial transaction involving credit is one in which one party (the lender) lends money or other assets to another party (the borrower) with the understanding that they would return the money at a later time. The lender normally determines the amount of interest to be paid on the loan, and the borrower is obligated to repay the principle plus interest by the mutually agreed-upon date. As it allows people and organizations to borrow money to fund investments and other activities, it is a crucial component of the economy.

Illustrations of Bank Credit

A credit card is the most widely used kind of bank credit. Based on the borrower's credit history, a credit card application is approved along with a certain credit limit and annual percentage rate (APR). The card may be used for purchases by the borrower. To continue borrowing until the credit limit is reached, they must pay either the whole sum or the minimum payment due each month. Borrowers may also get vehicle and home loans from banks. These are secured credit products that employ an asset, such as a house or car, as collateral. Using a fixed or variable interest rate, borrowers are forced to make fixed payments at regular periods, often monthly, biweekly, or monthly [4]–[6]. A business line of credit (LOC) is one kind of commercial credit. These credit facilities consist of rotating loans given to a business. They allow businesses access to short-term finance and may be secured or unsecured. Due to corporate demands, creditworthiness, and capacity to repay, credit limits are often larger for companies than they are for individual consumers. Business LOCs often undergo yearly evaluations.

What Is a Bank Credit Example?

Any funds a bank has lent you are an example of bank credit. Mortgages, vehicle loans, personal loans, and credit cards fall under this category. A bank credit is a loan given to a borrower by a bank that must be repaid.

The minimum credit score required for a bank loan.

The amount of the loan, how much it will cost, and its purpose will all affect the credit score required for a bank loan. Typically, a credit score of 640, or between 600 and 702, is needed.

Can I Get a Loan With Bad Credit From a Bank?

Banks often provide loans to borrowers with poor credit. These might be other banks or internet lenders rather than conventional banks. Having poor credit makes getting a loan difficult and expensive. Banks often provide smaller loans with higher interest rates and may also impose additional conditions.

The overview

People may utilize bank credit to buy expensive products like homes and vehicles that would be challenging to buy with cash alone. While some bank credit, like mortgages, aids in the development of assets, other bank credit, like credit cards, may be risky if improperly handled. Maintaining an adequate debt-to-income ratio can help you manage any bank credit and maintain your personal finances in excellent condition.

Things to bear in mind about credit

The following are some things to be aware of while dealing with credit.

- a. **Remit your payments on time:** Your credit score might suffer and your interest rates can go up if you have late payments.
- b. **Keep an eye on your credit report:** Regularly check it to guarantee accuracy and watch out for unusual activities.
- c. **Avoid using all of your credit cards:** You can maintain a high credit score by keeping your credit use minimal.
- d. **Avoid requesting too many credit cards:** Your credit score might be lowered if there are too many hard queries made.
- e. **Apply it sensibly:** Use exactly what you can afford, and be sure to pay off your debt completely each month.
- f. **Keep open old accounts:** You may improve your score by maintaining previous accounts.
- g. Watch out for fraud. Inform your credit card provider or the credit reporting bureaus of any unusual behavior.

What makes credit so crucial to our economy?

The capacity to borrow money and make purchases that people and companies otherwise would not be able to do makes it crucial for our economy. As a result, there is an uptick in economic activity, the creation of jobs, and corporate expansion. Additionally, it enables people to finance expensive purchases like houses and vehicles, which may help the economy. Finally, it assists people in raising their credit scores, which may provide them access to extra finance and enable them to reach their financial objectives.

Different Bank Loan Types in India

In today's environment, loans may be used for many different purposes. It may be utilized to establish a business or to pay for the furnishings for a home you've just bought. Let's discuss the

many loan kinds that are offered on the market and the distinct qualities that make these loans beneficial to the clients. **Individual Loans:** Customers may get personal loans from the majority of banks, and they can use the funds for everything from paying bills to getting a new television. These loans are often unsecured loans. Before authorizing the personal loan amount, the lender or the bank requires certain papers like evidence of assets, proof of income, etc. To be able to repay the loan, the borrower must have sufficient assets or income. The application for personal loans is one or two pages long. Within a few days, the borrower learns whether the loan has been approved or denied. You must keep in mind that these loans may have higher than average interest rates. These loans have a short term of borrowing. Therefore, if you borrow a large sum, it may be difficult for you to return it if your finances are not adequately planned. When you want to borrow a modest amount and pay it back as quickly as you can, personal loans might be a big assistance.

Loans on credit cards

When using a credit card, you should be aware that you will be required to pay back all of your purchases at the conclusion of the monthly cycle. Even when you go overseas, credit cards are often accepted. It has become a well-liked loan kind since it is one of the most practical methods to pay for the products you purchase.

All you have to do to apply for and get a credit card is complete a straightforward application form that the card issuer provides. A credit card application may also be made online. These plastic cards provide fantastic incentives and advantages. You are paid generously for utilizing the loan, but you must return it on time. It goes without saying that this kind of financing has its drawbacks. You need to be aware that the money you borrow with your credit card is subject to a high rate of interest. If you don't pay your credit card bills on time, interest will keep accruing and the amount on your account will likely increase, making it more difficult for you to manage your money. However, a credit card may become your greatest friend in your wallet if you utilize it responsibly and pay off all of your bills on time.

Housing loans

Applying for a home loan may be quite beneficial when you want to buy a property. It offers you financial assistance and enables you to purchase a home for your family and yourself. These loans often have longer terms (between 20 and 30 years). Some of India's leading banks provide house loans with rates that begin at 8.30%. Before the lender approves your loan request, your credit score is inspected. There is a decent probability that you may qualify for cheaper interest rates on your home loan if you have an excellent credit score. Most people who take out house loans do so to purchase new homes. But you may also use these loans to buy land, build homes that are still under construction, renovate your house, add on to your house, etc.

Auto Loans

You may undoubtedly have a huge feeling of satisfaction and happiness after purchasing an automobile. One of your major investments will be an automobile, which will continue to be your asset. You may get a vehicle loan to bridge the gap between wanting to purchase a car and actually doing it. It is advantageous to have a high credit score when you apply for a vehicle loan

since credit reports are important for determining your eligibility for any loan. It won't take long for the loan application to be granted, and the interest rate may even be reduced. Secured loans include auto loans. Your automobile will be taken back by the lender and the unpaid balance will be recovered if you don't make your installment payments.

Loans for two-wheelers

In today's world, a two-wheeler is very much a must. Bikes and scooters make it easy for you to travel, whether you're on a lengthy journey or crossing a crowded metropolitan street. Applying for a two-wheeler loan is simple. Your ability to buy a two-wheeler is made possible by the sum you borrow under this form of loan. However, if you don't make timely payments and pay off your obligation, the insurance will seize your two-wheeler to recoup the loan balance.

Loans to small businesses

Small and medium-sized firms may use loans from small and medium-sized lenders to cover a variety of needs. These loans may be used for a number of things that support company expansion. Equipment purchases, inventory purchases, staff wages, marketing costs, company debt repayment, administrative costs, and even opening additional branches or franchises are some examples of these. Various factors determine a borrower's eligibility for a small business loan, but the most common ones include the borrower's age, the length of time the business has been in operation, income tax returns, and a statement of the prior year's revenue that has been audited by a Chartered Accountant (CA).

Payday advances

Salary loans are another name for payday loans. These are unsecured, short-term loans where the borrower must have a job and a reliable source of income. Typically, their interest rates are hefty. This is determined by the applicant's income, age, and credit history. Salary statements and other forms of income documentation would be necessary.

Payday Loans

Credit card companies provide these loans, which let cardholders use their credit cards to withdraw cash from an ATM. The credit limit available will determine how much money may be taken out of a credit card in this manner. The money must be returned together with interest, which is typically computed as of the day the money was removed. Cash advance fees, ATM fees, and bank fees are some of the additional costs connected with them.

Loan for Home Renovation

Most lenders provide financing for home innovation. These may be used to cover costs associated with remodeling, fixing, or enhancing an existing residential property. There is a lot of freedom in what you may accomplish with a home improvement loan, depending on the lender. It may be used to make purchases or pay for services. You may use it, for instance, to pay a contractor, architect, or interior designer. Additionally, you may use it to purchase home items like a refrigerator, washing machine, air conditioner, and other furnishings and equipment. Additionally, it may be utilized for masonry, carpentry, and painting tasks.

Loan for Agriculture

Loans for agriculture are those given to farmers to cover the costs of their ongoing or general agricultural needs. Both short-term and long-term loans are available. They may be used to acquire agricultural equipment or to provide operating money for crop production.

Loan in gold

A gold loan may be utilized to obtain money for unforeseen or anticipated needs like company growth, education, urgent medical care, agricultural costs, etc. A loan against gold is a secured loan in which gold is used as security or collateral in exchange for an amount of money that is equal to the market value of gold per gram on the day that the gold is pledged. The value of the gold loan will not be determined by taking into account any other metals, diamonds, or stones that are included in the jewelry.

Cash Advance on Credit Card

A loan taken out against a credit card functions similarly to a personal loan. Typically, these are pre-approved loans for which no extra paperwork is needed. This might, after a set amount of time, be transformed into an interest-free personal loan depending on the lender. A certain amount of interest will then be generated after that. The conversion of the pre-assigned credit limit into a loan is subject to a processing charge.

Student Loan

A loan for education is taken out particularly to pay for school or college-related educational obligations. Depending on the lender, it may pay for the basic course costs, test fees, lodging expenses, and other incidentals. The student is the borrower, while any other immediate family member such as a parent, grandparent, spouse, or sibling is the co-applicant. It is available for both domestic and international courses. It may be used for many different recognized courses that are offered either full- or part-time. Along with undergraduate and graduate programs, they also include vocational courses.

Loan for Consumer Durables

Consumer durable loans are available to help pay for the purchase of durable goods like electronics and home appliances. They may be used to purchase anything, ranging from mobile phones to televisions, depending on the lender. The range of loans is from Rs.5,000 to Rs.5 lakh. Typically, no security deposit is needed. Some lenders provide consumer durable loans with rapid approvals, 0% interest rates, and little to no paperwork [7]–[9].

CONCLUSION

In conclusion, the investigation of many forms of bank credit illustrates the wide variety of financial tools that are essential to our economic system. Each variety, from loans and credit cards to overdrafts and lines of credit, performs a distinct function and meets a range of financial demands. This tour of the many bank loan products highlights how flexible and sensitive the financial sector is to the shifting needs of consumers, companies, and governments. Understanding the differences between secured and unsecured credit emphasizes

how important collateral and creditworthiness are in determining the terms of credit agreements. Unsecured credit is dependent on trust and credit history, while secured credit provides some certainty for lenders.

The complex balancing act between risk and reward present in the loan process is shown by this comparison. In general, the variety of bank loan products reflects the complex dance between borrowers looking for financial support and lenders trying to protect their interests. Individuals and organizations may make choices that are in line with their financial objectives and obligations by being aware of these categories. The variety of bank credit alternatives offers a route to reaching stability and success, whether it's buying a property, controlling operating costs, or dealing with unanticipated financial issues.

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CHAPTER 3

IMPORTANCE OF BANK CREDIT IN THE ECONOMY

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ABSTRACT:

One important pillar that supports economic stability, progress, and growth is the significance of bank credit. This chapter explores the critical role that bank lending plays in promoting investments, boosting economic activity, and promoting prosperity in general. By supplying people, corporations, and governments with the money they need to launch projects that would otherwise be impractical owing to capital limits, bank lending serves as a stimulus for economic growth. This chapter examines how bank lending helps people to buy houses, entrepreneurs to start enterprises, and governments to invest in public infrastructure. Additionally, consumer spending is lubricated by bank loans, essentially lubricating the wheels of trade. Credit availability allows customers to spend more money than they have available right now, which boosts demand for products and services. This chapter explains how this cycle leads to employment creation and economic prosperity.

KEYWORDS:

Bank Credit, Bank Loans, Capital Limits, Corporations, Credit Availability, Economy.

INTRODUCTION

Economic transactions can be carried out effectively and the economy may expand when consumers and firms are able to borrow money. Companies may get the tools they need via credit to generate the goods we purchase. A company that was unable to get financing would not be able to pay its workers or purchase the equipment and supplies it needs to produce items and turn a profit.

Why is credit so crucial?

Credit enables people to buy the necessities. Most individuals can't afford to pay for many things at once, from homes to vehicles. With credit, you may acquire necessary goods and services whenever you need them while spreading out your payments.

Why is credit necessary?

Even though it is obvious that credit is crucial for a healthy economy, you can still be perplexed as to why you personally need credit. "Loans are a necessary part of life for many," asserts Katie Ross, manager of education and development at American Consumer Credit Counseling. According to Ross, loans may help individuals grow wealth by enabling them to do things like pay for education, boost their earning potential, purchase a house and take advantage of increasing property prices, or launch a company.

"Having access to credit can also be helpful in an emergency," says Benjamin Jacobs, a certified financial adviser at Elwood & Goetz in Athens, Georgia. Being able to borrow money might come in handy if unanticipated costs crop up or you need something you can't afford, he adds [1]–[3].

In today's world, consumer credit reporting is another factor that makes accessing credit vital. Creditors that lend you money often record your actions to credit-reporting organizations like Equifax, Experian, and TransUnion. Credit reports are compiled using information about your financial conduct, including whether you miss or make late loan payments, and credit scores are calculated using this information. Lenders use these reports and ratings to determine how dangerous it would be to lend to you.

Why is having excellent credit essential?

So why are credit reports and ratings important in the first place? Your future capacity to get credit is impacted by your credit ratings. "If you have a low credit score, it will be harder for you to get credit or loans. Or you risk receiving a loan with unfavorable terms and circumstances and a high interest rate, says Ross. But what if you're determined to pay cash for your home, vehicle, and other major purchases and don't want to ever borrow money? Since credit ratings are utilized for many purposes in the United States, having high credit is important even in these situations.

When considering whether to rent to you, landlords could do a credit check on you. Your credit scores and reports are often examined when you apply for a mobile phone contract. Your credit scores may be taken into consideration by your vehicle insurance when determining the premiums you'll pay. And your employment chances may be impacted by your credit. According to Ross, employers may ask for a customized credit report from the credit agencies depending on the state in which you reside. "Denied status due to negative items on your credit report is possible."

What credit risks are there?

Now that you know, you no longer need to wonder why credit is so crucial. However, just because credit enables you to accumulate money and engage in the market does not imply that utilizing it is always beneficial. Credit may be utilized improperly since it is a tool. Since your credit ratings are used to gauge your dependability, individuals and businesses may be hesitant to do business with you if you have erratic borrowing habits and poor credit scores. A landlord could refuse to rent to you, or you might not be able to secure a mobile phone contract without paying a sizable deposit. Borrowing has expenses, like fees and interest, and it's easy to take on more debt than you can handle. "If a consumer doesn't know how to handle the credit they have available to them, they could end up paying a lot in interest, as well as paying fines or penalties," adds Jacobs. "This could turn out to be spiraling, and I've seen consumers who end up having to file bankruptcy because it spirals out of control so much." Ross advises limiting borrowing and only taking out loans if you can easily pay them back. She adds that it's crucial to differentiate between "good" debt, such as a mortgage or school loans, which may contribute to long-term wealth building, and "bad" debt, or debt used to purchase goods simply because you want them.

DISCUSSION

The importance of credit to economic growth!

Neither credit itself is capital nor does it produce it. The credit instruments just serve to assist the company and symbolize money. The following facts may be used to evaluate the significance of credit:

1. High Volume Production:

Less developed nations like Pakistan and India are having trouble raising financing. Our manufacturing options are constrained. Therefore, the industrialists have received funding via credit instruments. The cost per unit has decreased and manufacturing is now being done on a massive scale. Both number and quality have increased.

2. Rising Savings Rates:

Credit gives individuals the chance to save money, yet some people who do so are unable to operate a company. They lend it to financial institutions as a result. Money may be transferred to those who can utilize it for production thanks to credit.

3. Transferring Capital to Productive Uses:

There are a lot of individuals who have extra cash but are unable to start a company. They lend it to financial institutions as a result. Money may be transferred to those who can utilize it for production thanks to credit.

4. Efficiency in Metal Use:

Metal coins are replaced by credit instruments. Therefore, valuable metals are also being saved. Credit instruments may be used more effectively and conveniently in the future.

5. Offering Working Capital:

An industrialist may sometimes encounter financial difficulties while trying to buy raw materials or pay employees. He uses the credit facility as a result.

6. Selling Bonds:

Selling the bonds may sometimes help a business get financing. If the company's future prospects are promising, it will pay back the principle plus interest.

7. Case of A Young Company:

A fledgling company's management may quickly grow its resources thanks to credit.

8. Emergencies For New Entrepreneurs:

New talent may join the company industry thanks to credit. If a person has all the necessary traits for a successful entrepreneur but lacks the necessary resources, credit gives him the opportunity to put those traits to use.

9. Acquisition Of Goods:

The customer may buy consumer products like a TV thanks to credit. Car house, radio, etc.

10. Paying internationally:

International payments may be done quite simply with bills of exchange. Gold does not need to be imported or exported in order to conduct international commerce.

11. Beneficial To The State

In the event that the Gov. The deficit in the budget may be closed by selling bonds and obtaining loans. Credit is very advantageous for the state even in times of distress or conflict.

Risks of Credit

Without a question, credit is the lifeblood of business and industry, but it is not without flaws. The credit weapon has the following significant flaws if it is not adequately regulated and controlled:

1. Over Credit Issue:

Beyond the safe limit, credit growth often leads to excessive investment, output, and price increases. During the credit contraction.

2. Poor Debts:

If a customer or a country abuses credit, the loan will not be returned, which will cause fear in the financial community.

3. Ineffective Business Issues:

All of the businesses that have trade contacts with the financially shaky operator who is operating unprofitable businesses and is getting the credit suffer. Additionally, it will cause fear in the business community.

4. Explosion of Monopoly:

Any person or firm that has access to a lot of credit runs the risk of being exploited by monopolists, who may use any unethical tactics in their commercial operations.

5. The government is borrowing money. :-

In the event that the Gov. If the state excessively spends the borrowed funds, the citizenry will lose faith in the state's creditworthiness.

Banking Process

The foundation of all banking is holding financial assets, which is also where it all started in antiquity—though it has since evolved well beyond the days when it was only used to store gold coins for affluent clients [4]–[6]. The simplest kind of banking is when a bank accepts deposits from people or companies and promises that the money may be taken whenever the depositor wants it (though there may be a fee for an early withdrawal).

The bank may also pay interest on the depositor's money depending on the kind of account. The bank then extends loans to other people and companies using the money it has on deposit in exchange for interest payments from the borrowers. The difference between the lower interest rate that banks pay depositors for the use of their funds and the higher interest rate that they charge borrowers is where banks generate their profit. Banks are prohibited by law from lending out all of the money they have, but regulators require them to hold back a certain level of capital to satisfy withdrawals and other obligations. The regulations fluctuate and depend on the size of the bank, but lately many large U.S. banks had to hold back 8% of their capital.

What Is the Economic Driver of Banks?

The contemporary economy cannot function without the banking industry. As the main source of credit, it provides funding for individuals to purchase houses and vehicles as well as for companies to acquire equipment, grow their operations, and pay their employees. The Federal Deposit Insurance Corp. (FDIC), which protects many accounts up to specific amounts, has made banks a secure location for depositors to put their money as well as a place to earn interest.

Banks provide credit cards, debit cards, and checking accounts to help with a variety of daily transactions. They also support e-commerce, which mostly excludes the usage of currency. Another significant employment is the financial industry. For instance, the FDIC-insured commercial banks in the United States alone employed almost 2 million people in 2022.

On the other side, the financial industry has the potential to seriously undermine the economy. For instance, when the subprime mortgage crisis started in 2007, certain banks' careless lending caused the economy to collapse and ignited the Great Recession of 2007–2009. Since then, there have been regulatory improvements implemented that may assist prevent another catastrophe of this kind.

The significance of credit to a nation

Here are a few facts that explain the value of credit for a nation and how credit helps to strengthen an economy.

1. A person or company may "purchase ahead of ability" or "desire to pay" thanks to credit.
2. The bank credit sufficiently satisfies the economic requirements of the agricultural, commercial, and industrial sectors of the economy.
3. By providing timely loans to the industries, bank credit hastens the nation's economic growth.
4. Products are bought, processed, stored, and then sold to customers at the right moment.
5. Farmers need farm financing, which aids in the growth of their agricultural operations and increases agricultural output nationally.
6. Bank financing makes it easier to produce commodities and other requirements of life on a big scale, which promotes technical advancement and lowers the cost.
7. Commodity transportation between locations is also made simpler and more affordable thanks to bank loans.

8. Commercial credit also helps customers with their consumption demands for things like a car, a home, and other necessities.
9. Bank loan availability to households and businesses boosts economic development, which would have been constrained by personal savings.
10. The amount of bank credit has an impact on the interest rate as well. The adaptability of bank credit controls the rate of interest, which has positive consequences on economic growth.
11. Bills of exchange and other credit instruments significantly ease international trading. Payments are therefore done without a significant amount of treasure actually moving.
12. People with great minds might make use of their skills and attributes in managing businesses with the aid of credit. Without credit, their abilities would have been wasted.

The value of credit to businesses

We are aware that with a cash transaction, everything is paid in full at once. However, in a credit transaction, the value is paid after a certain amount of time. As a result, it demonstrates how crucial credit is to business. However, only trustworthy individuals are permitted to use this facility after paying a payment after some time. Credit thus comprises the two elements of "Time" and "Confidence".

Discuss in detail the significance of credit.

If we can't dispute the significance of money in business, we certainly can't dispute the significance of credit. Since the availability of money is essential to a borrowing economy, the capital needs of the firm may be met by two sources. These are consumer and business bank savings. Most likely, these commercial banks take the funds and lend them to both businesspeople and those in need.

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1. The ease of using credit to buy and sell items allows customers to spend more money than they have.
2. Credit was made available, allowing new businesses to flourish while successfully using their skills.
3. By employing credit money, it is possible to spend metal money more economically. Compared to metal money, credit money is safer and more practical.
4. The availability of government loans is facilitated by credit. These resources are used in the creation of public use projects.
5. Large-scale manufacturing is now being done. It is only conceivable if there are surplus cash for manufacturing as well as credit money. This demonstrates the critical role that credit plays in business.
6. The entire production of commodities in the nation is also aided by credit. Producers involved in various manufacturing processes might use the loan facility to meet their financial needs.
7. Instead of using cash or gold to make payments in international commerce, bills of exchange are used. This increases the value of credit in the commercial realm as well.
8. Additionally, the credit funds contribute to the stability of the pricing structure. Credit expansion raises the amount of goods and services produced.
9. Additionally, credit improves peoples' standards of life. When the overall amount of money supplies rises and income and per capita follow suit, a high quality of life is eventually the result.
10. If the government has a deficit in its spending, the gap may be filled by selling bonds. Only the use of credit is allowed.

CONCLUSION

In conclusion, it is impossible to exaggerate the value of bank loans to the economy. The lifeblood of the economy, bank lending provides the essential energy for expansion, investment, and development. It is essential for enabling people, organizations, and governments to achieve their goals and advance global development. Bank lending stimulates entrepreneurship and innovation by providing the capital required for corporate growth, R&D, and development. It encourages employment growth by allowing businesses to recruit new employees and grow their staff. Furthermore, bank credit promotes consumer spending by enabling people to make large purchases and make investments in the future. Credit availability affects the stability and cyclicity of the economy. Increased credit availability may boost growth during periods of economic development, but careful credit management is crucial to avoiding unsustainable bubbles. In contrast, having access to financing during a slump may help firms withstand the storm and help the economy bounce again. Banks are the main financial intermediaries that help with the effective distribution of resources by evaluating risks, pooling resources, and distributing them to those in need. This intermediary action promotes savings and turns them into investments, promoting growth and development of the economy.

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CHAPTER 4

FACTORS AFFECTING BANK CREDIT APPROVAL

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ABSTRACT:

Numerous variables that together impact the lending environment affect whether bank loan is approved. This chapter explores the complexity of these elements, highlighting their importance and how they interact to affect whether a borrower's credit application is approved. The chapter examines the crucial function of creditworthiness, which encompasses a person's credit history, credit score, and general capacity to pay back loans. It explains how an improved credit history and score, which represent a borrower's responsible financial conduct, increase the chance of loan acceptance. The chapter reveals that consistency of income and employment are crucial factors. A borrower's ability to repay debt is assured to lenders by providing evidence of a consistent and enough income. The borrower's long-term financial prospects may be gleaned from their employment history and level of job security. In secured loan settings, collateral acts as a safety for lenders, as explained in the chapter. The standard and worth of the collateral have a big influence on the conditions of loan acceptance since lenders want to be protected from prospective defaults.

KEYWORDS:

Bank Credit, Borrower, Credit Rating, Collateral, EMI, Loan.

INTRODUCTION

Lenders often review both your personal credit history and your company credit history when you submit a credit application. "You're almost always going to have to sign a personal guarantee on a small business loan," Wilson asserts. A personal guarantee is an enforceable commitment to repay money borrowed by your company from your personal assets.

Factors That May Affect Your Eligibility for a Personal Loan

One of the numerous considerations that is given top priority when you apply for a personal loan is your monthly income. But there are a lot of other things that lenders could take into account, such as your credit score and debt-to-income ratio. Here are five things you should be aware of that might influence your qualifying for a personal loan:

- a. **Credit Rating:** Your credit history, which includes your loan repayments and credit card bill payments, is reflected in your credit score. Since Personal Loans don't need collateral, your credit score has the most impact on your eligibility. You have been paying off your bills on schedule if you have a decent credit score of 750 or above. This demonstrates to lenders your commitment to timely repayment. In contrast, poor financial management leads to a low credit score, which lenders deem undesirable. However, timely EMI and credit card bill repayment will improve your credit score.

- b. **The debt-to-income ratio and monthly income:** Lenders assess your monthly income in addition to your credit score to determine if it is adequate for you to make loan payments on time. To be qualified for a personal loan, the majority of lenders normally ask you to have a minimum annual income of \$25,000 on hand. Additionally, if your debt-to-income ratio is smaller, loans are approved more quickly. The implication of this is that your monthly income should be more than your monthly costs, including any debts you may have.
- c. **Age:** In order to determine your ability to repay loans, lenders must also know your age. Whether you are a salaried employee or a sole proprietor will determine what age you must be to qualify for a personal loan. Typically, self-employed people between the ages of 25 and 60 and salaried workers between the ages of 21 and 55 are seen as the best prospects for personal loans.
- d. **Work Situation:** When evaluating your loan application, the lender may also take into account your job situation and the standing of your company. The likelihood of the lender granting your personal loan is significantly increased if you have worked for a reputable company for a considerable amount of time. Lenders often favor candidates who have been working for the same company for two years or more and have a steady salary. If you often change employment, lenders can see this behavior as a red signal and exclude you from consideration for the loan.
- e. **Loaner Relationships:** Choosing a loan from the bank where you have your savings account, current account, or fixed deposits may be what you are more likely to do. Furthermore, the bank may provide new loans at lower interest rates if you have previously obtained and repaid loans from it. If you've been a client for a while, you could be in a position to bargain for better interest rates and bigger loan amounts. In a timely manner, the bank may, in good faith, accept your terms and grant the loan.

How to Improve Your Eligibility for Personal Loans

- i. Pay off your current debts before requesting a new loan.
- ii. Ensure that you pay off your credit card balance in whole and on time.
- iii. Keep up your good credit history and debt payback track record.
- iv. Ensure that it constantly exceeds 750 points.
- v. To increase your eligibility, demonstrate any other income sources you may have, such as variable wages, bonuses, passive income from hobbies, etc.

Elements that influence loan choices-

What you'll do with the loan

Lenders desire to be certain that you're using the best merchandise for your requirements. A line of credit, which is often used for short-term working capital requirements, small company credit cards, which are intended to assist you manage daily spending, and a commercial term loan are your best options for financing significant investments over time [1]–[3].

Ask your lender for guidance if you're unsure about the sort of finance you need. According to Roderick Wilson, an officer from Bank of America's Small Business Lending Product, "they can help you look at different options and decide which one is best for your situation."

Your requested financial contribution amount

Lenders are suspicious when a firm tries to borrow more money than it can afford. In addition, if you don't borrow enough to cover your shown need, the lender can challenge your application. "Doctors risk running out of money if they seek for a loan for a new practice without taking the office build-out into account. To ensure they have more cash on hand in the near future, it could make sense to borrow those extra sums, according to Wilson. Consult your accountant or lender for guidance on how much money you should borrow.

Your credit history, both personal and corporate

Before submitting a credit application, check both your personal and company credit reports with all of the main credit reporting agencies for past-due accounts (or improperly stated delinquencies). You may check your personal credit reports with Experian, Equifax, and TransUnion, while Dun & Bradstreet, Experian, and Equifax provide business credit reporting services. In order to help the lender better comprehend the issue, provide an explanation if there is any unfavorable information on your credit report.

Your financial capability

Additionally, your application has to show that you can repay loans. According to Chris Ward, a small company credit specialist at Bank of America, "a lender may request for at least two years' worth of personal and business tax returns, a debt schedule that includes specifics of all of your business debts, and personal financial statements." Lenders may now additionally want year-to-date balance sheet and profit-and-loss statements, he continues, "in order to understand how your business has been doing recently, especially in light of the added challenges many companies are facing due to the current economic environment." You can be asked to provide evidence of your financial resources as well as personal and professional assets. Lenders often inquire about the capital assets, such as cash and equipment, as well as any outside investments in your company. Lenders may inquire about your accounts receivable, inventory, equipment, and commercial real estate if you are requesting a loan that is backed by collateral.

How to boost the chance of approval

Obtain information prior to beginning.

Prior to applying, gathering the relevant data might save time and lessen the chance that you will forget to include anything crucial. Depending on the kind of funding, you may need to give different amounts of information. Applications for credit cards are often quite straightforward, but because of their greater credit limits and possible borrowing terms, loans and lines of credit may need additional supporting documents.

Typical data requests include:

Information about the company

1. The business's name
2. The street address and the date have changed for the business.
3. Company phone number

4. Company Tax ID number
5. The kind of business
6. The year the company was founded
7. The date the current owner bought the company
8. Number of workers
9. Annual net income
10. Gross sales per year
11. A list of any unpaid debts, if applicable (including lender, current credit limit or loan amount, and monthly payment)
12. Tax returns for two years of businesses
13. Details about collateral, including receivables, stock, equipment, and commercial real estate

Details on the owners

Additionally, your bank could need the following details from each controlling manager, guarantor, and company owner:

1. The account opening party's name and position
2. The entity's name and address for the account.
3. Each beneficial owner and controlling person's name, date of birth, Social Security number, residential address, country of citizenship, country of residence, and percentage of ownership (this information is required even if no equity owner has 25% or greater ownership), as well as their passport number and country of issuance.
4. Verification that the beneficial owner's and/or controlling manager's information given is correct
5. Individual household earnings
6. Personal financial disclosure

Two years' worth of individual tax returns

Housing situation (own vs. rented) and recurring housing costs

Work with a consultant

You may improve your application and raise your chances of acceptance by knowing what lenders are looking for. To compile these papers, Ward advises working with your accountant or business counselor.

An advisor may assist you by helping you see the package through the eyes of a lender. "Something like a dip in revenue isn't necessarily a deal-breaker, but the lender will want to understand your business's story," adds Ward.

How long will it take to complete your application?

Due to the uniqueness of each borrower's circumstance, approval and financing times may change. A line of credit might take three to four weeks whereas a normal business mortgage could take up to 60 days. It might take a week or less to approve a credit card. The procedure could take longer if the lender needs more information.

DISCUSSION

Creditworthiness: The Six Cs

When a firm applies for funding, lenders use these six "Cs" to assess its creditworthiness.

Capacity

Lenders will assess your company's ability to pay both operational costs and the loan obligation. A firm typically requires \$1.25 in revenue to cover every \$1 spent on debt payments. Your company may use the additional \$0.25 as a buffer to handle unforeseen costs or a downturn.

Capital

Capital assets owned by your company, such as cash and equipment, may be utilized to support your credit application. A lender will take into account the fact that you and others may have contributed money to the company. Your chances of obtaining finance will be greatly influenced by the quantity of capital assets and equity you currently own.

Collateral

Collateral is a term used to describe assets that lenders may accept as security for loans, such as accounts receivable, inventory, cash, equipment, and commercial real estate. A lender will search for liens, or outstanding debts owing, on your collateral while determining its value. The collateral may not be acceptable as a supporting asset for the loan if there is a lien on it.

Conditions

Lenders will evaluate your loan application while taking into account the health of the economy, industry trends, and any forthcoming legislation that may affect your firm.

Character

Lenders will take into account a borrower's work history, industry experience, and personal credit history. The success of the company depends heavily on your own integrity and good standing, as well as the integrity and standing of individuals connected to it.

Communication

A successful financial relationship depends on your commitment to be open and honest with your banker and other advisers about the possibilities and obstacles your company confronts.

When does CIBIL score suffer a hit?

Let's examine some of the main elements that might adversely impact your CIBIL score:

Careless Payment Practices:

The primary factor affecting your score is your payment history. It's crucial to make on-time monthly payments for your loan EMIs and credit card obligations. According to CIBIL study, a 30-day delinquent may lower your score by 100 points (as reported by the Financial Express).

It is advisable to set up reminders and notifications if you have many credit cards and loans so that you don't miss or postpone payments. Any late or missing payments have a negative impact on your score and give the impression that you are inconsistent in repaying credit [4]–[6].

2. A high ratio of credit use:

You should monitor your credit usage ratio as one of your guiding principles. It is the amount of credit utilized in relation to your available credit limit. Experts advise not utilizing more than 30% of your credit limit in any one month. If your credit card has a limit of Rs. 1 lakh, for instance, you should spend around Rs.30,000. Your credit score may be negatively impacted if you have utilized more than 50% of your credit limit. Lenders will be alerted if you have a high credit exposure since it shows you are more likely to default.

3. Remaining Debt:

You should constantly make an effort to pay off any unpaid bills. Your credit score suffers when outstanding debts are shown on your credit record. Even if the balance is just a modest amount, it is advisable to settle the past-due debts.

4. Making the Minimum Payment Required:

A little part of the principle that is payable each month is the minimum amount due. If you consistently pay just the minimal amount owing, you risk falling into a debt trap. The interest on your outstanding balance will grow if you roll over the loan by making just the minimum payment. So, it is recommended that you pay off all of your credit card debt. Additionally, it exhibits sluggish repayment habits.

5. Submitting many credit application

Lenders will obtain your credit record in order to determine your creditworthiness when you apply for a loan or credit card. It's referred to as a hard inquiry. Numerous credit inquiries will take place at the same time if you submit numerous applications. These challenging questions are publicized and harm your score. You'll come out as credit-hungry.

It's best to delay applying for credit if your loan or credit card application was recently denied. It is preferable to raise your CIBIL score before reapplying.

Your CIBIL report contains errors.

Your current and previous credit accounts are fully documented in your CIBIL report. Your score may suffer if your report contains any mistakes. Therefore, you must get any errors in your report corrected very away.

Your lenders are the only ones who can correct these mistakes. Without lenders informing CIBIL of the necessary adjustments, reports cannot be corrected.

Additionally, reviewing your credit report might assist you in determining if you are a victim of identity theft.

- a. Lack of a Credit Mix: A healthy ratio of secured and unsecured loans must be kept in place. Examples of secured loans include mortgages and vehicle loans, while an example of an unsecured loan is a credit card. Your credit score may be impacted if you have a lot of one particular sort of credit. Additionally, having a balanced mix of various loan forms indicates that you have expertise managing both sorts of loans. Lenders find this to be desirable.
- b. Duration of Credit: The total number of years that have elapsed since you initially established a credit account is your credit history, to put it simply. A lengthy credit history aids creditors in making an informed choice when extending loans to you. It is best to concentrate on establishing credit history early in life so that you have a solid credit history by the time you apply for a house loan or auto loan.

Old credit card accounts may be closed.

A good way to establish credit history is with credit cards. But when you terminate an old account, you lose the lengthy credit history that was attached to it. Keeping the card open for as long as possible, if possible, is suggested if you have used it for a significant amount of time. A very fresh card could be closed [7]–[9].

Advantages of a High CIBIL Score

1. Faster loan and credit card approval
2. Lower loan interest rates
3. Better credit card offers
4. Cards with increased credit limits
5. Reduction in the processing fee and other costs associated with loan applications

CONCLUSION

In conclusion, the complicated network of variables influencing bank loan acceptance highlights the intricacy and subtlety of the lending process. The choice to provide credit requires a careful balancing act between lenders' caution and borrowers' desires. The borrower's financial situation including credit history, income, and debt levels determines whether credit is granted. Macroeconomic factors that affect borrowing costs and repayment capability, such as interest rates, inflation, and general economic stability, are also quite important. The lender has a safety net thanks to the borrower's supplied collateral, which has an effect on the conditions of the loan arrangement. The goal of the loan, whether it is for investment, corporate growth, or personal consumption, has an impact on how risks are evaluated and approved. Lending practices are influenced by the regulatory framework, which also ensures consumer protection and financial stability. Additionally, the approval procedure is influenced by the lender's own risk tolerance, rules, and ability to handle credit risk.

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CHAPTER 5

CREDIT SCORING AND ITS ROLE IN BANK CREDIT ASSESSMENT

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ABSTRACT:

Credit scoring, which acts as a quantitative tool to estimate a person's creditworthiness, is a crucial part of the bank credit evaluation process. This chapter explores the workings of credit scoring and how it influences loan choices. The chapter guides the reader through the basics of credit scoring, which is based on a variety of financial information, including credit history, payment behavior, outstanding debts, and credit history length. A credit score, a numerical depiction of a person's credit risk, is produced by the combination of several data components. The chapter describes the importance of credit scores and emphasizes how they provide lenders a consistent and impartial tool to evaluate risk. Credit scores are used by lenders to determine how likely a borrower is to pay back the money they have borrowed, which influences choices about interest rates, loan conditions, and credit limitations. The chapter also explores the elements that affect credit ratings, such as timely payments, credit use, the kinds of credit utilized, and length of credit history. It emphasizes how damaging negative information, such as missed payments or defaults, may be to a credit score.

KEYWORDS:

Business, Credit Scoring, CSP, Customer Relationship Management, Global Economy.

INTRODUCTION

Lenders and financial institutions use credit scoring, which is a statistical study, to assess a person's or a small, owner-operated business's creditworthiness. Lenders use credit scoring to determine whether to grant or refuse credit. Your ability to qualify for financial goods including mortgages, auto loans, credit cards, and private loans might be impacted by your credit score. It is generally acknowledged that credit scoring has enormous potential to help the global economy expand economically. It is a useful instrument for increasing efficiency, financial inclusion, and access to finance for people and micro, small, and medium-sized businesses.

Due to improved access to a larger range of data, higher processing power, increasing desire for efficiency gains, and economic development, both the usage of credit scoring and the diversity of scoring have considerably risen in recent years. In addition, the use of credit scoring has changed from the traditional acceptance or denial of credit applications to the inclusion of other elements of the credit process, such as the pricing of financial services to reflect the risk profile of the customer or business and the setting of credit limits.

Credit scoring is also used to enhance customer relationship management, establish minimum regulatory and financial capital requirements, and, in certain nations, to entice potential customers and clients with incentives. In recent years, the techniques utilized for credit rating have become more sophisticated.

They have progressed from conventional statistical techniques to cutting-edge approaches like artificial intelligence, which includes deep neural networks, gradient boosting, and random forest machine learning algorithms. The range of information that may be deemed relevant for credit scoring models and choices has sometimes increased with the implementation of new approaches.

Why Do We Score Our Credit?

Greater financial inclusion and credit access, an increase in model accuracy, process automation efficiency improvements, and even a better customer experience are all benefits of utilizing novel methodologies for credit scoring. However, the use of cutting-edge techniques for credit scoring also raises issues with data privacy, fairness and the potential for discrimination against minorities, the interpretability of the models, and the possibility of unintended consequences because the models built on historical data may learn and maintain historical bias.

However, a lack of innovation in credit scoring poses hazards to consumers and companies if it prevents advancements in risk management and financial inclusion. The efficiency of credit scoring techniques and technology is another issue. These issues are particularly relevant in areas where there is little or no industry rules or governmental monitoring to control the behavior of credit service providers (CSPs). The recommendation acknowledges that there are market-specific variations in utilization, accuracy, and robustness as well as the ongoing evolution of the technology underpinning innovative credit scoring. For instance, in developing economies, CSPs may still rely on the human judgment of the credit officer, subjective scorecards, or at best, conventional regression models.

In many areas, there is still a severe lack of the people and data infrastructure needed to implement the most creative techniques. The recommendation promotes the use of a human-centric strategy, in which innovation is implemented with the human being in mind. This guideline presents seven policy suggestions for credit scoring, including both models and choices, in an attempt to support openness and assist regulators in their supervision responsibilities. The following are the suggested policy changes:

1. Credit service providers (CSPs) must be governed and given precise instructions within a moral and legal framework.
2. Credit scoring-based choices need to be clear, fair, and comprehensible.
3. Practices for data accountability should be improved.
4. A model governance structure should be applied to credit scoring models.
5. It is important to promote cooperation and information exchange.
6. Innovation and risk should be balanced in the regulatory strategy.
7. Building regulatory organization and CSP capacity is crucial.

The Process of Credit Scoring

How credit is scored by different credit scoring algorithms may vary somewhat. More than 90% of the largest lenders utilize the FICO score, created by Fair Isaac Corporation, which is the most used credit rating system in the financial sector.

However, the main three credit reporting companies, TransUnion, Experian, and Equifax, developed another well-liked credit rating methodology called Vantage Score. A FICO credit score ranges from 300 to 850, with 850 being the best score that can be obtained. The FICO Small Business Scoring Service (SBSS) offers credit ratings for small firms that range from 0 to 300.345.

DISCUSSION

Five categories may affect a credit score:

- a. Past payments (35%)
- b. Owed sums (30%)
- c. Credit history length (15%)
- d. Fresh credit (10%)
- e. Credit blend: 10%

A small business's credit rating is determined by the data in its credit report, which includes:

- i. Information about the business, such as the number of workers, sales, ownership, and subsidiaries.
- ii. Previous business information
- iii. Information about business registration
- iv. A list of government activities
- v. Operational business data
- vi. Data and categorization of industries
- vii. Publicly available filings (such as liens, judgments, and UCC filings)
- viii. Collections and payment history
- ix. The quantity of accounts reporting and specifics

In risk-based pricing, where the conditions of a loan, including the interest rate, issued to borrowers are dependent on the likelihood of payback, lenders utilize credit scoring. In general, the better the rate a financial institution offers, the higher the credit score.

Comparing credit ratings and scores

Credit rating is not the same as credit score, although having a similar idea. On a lettered scale, credit ratings are assigned to businesses, sovereigns, sub-sovereigns, and the securities of such entities, as well as asset-backed securities [1]–[3].

A person's connection with credit is depicted by credit scoring models, and scores across the three major credit agencies may differ (though typically not much). The borrower's eligibility for a loan of credit or debt issue, as well as the interest rate for the repayment, are both based on their credit rating.

U.S. Commission for Securities and Exchange. The "Updated Investor Bulletin: The ABCs of Credit Ratings."

Credit scoring restrictions

Credit scoring does assess a borrower's credit riskiness, but it does not provide a prediction of how likely they are to default. It simply ranks the riskiness of a borrower from greatest to lowest. As a result, the incapacity of credit scoring to discern whether Borrower A is twice as hazardous as Borrower B causes it to suffer. The difficulty of credit scoring to properly account for the state of the economy is another intriguing limitation. When the economy goes into a recession and Borrower A, for example, has a credit score of 800, neither Borrower A's credit score nor his or her financial situation will alter. The FICO Resilience Index is an effort by FICO to solve this problem. It is "designed to evaluate consumers with respect to their resilience or sensitivity to an economic downturn and provides insight into which consumers are more likely to default during periods of economic stress," according to Experian. It may be given with a credit file, along with the FICO Score, and utilized by lenders as an additional factor in credit decisions and account strategies throughout the credit lifecycle. The likelihood of default is calculated using more sophisticated credit risk modeling techniques, such as structural models and reduced-form models.

How Can Your Credit Score Be Raised?

To raise your credit score, you may take action. Making timely payments is one of them, as is lowering your debt load and maintaining a healthy balance of revolving and non-revolving loans in your credit mix. Avoid terminating accounts if at all feasible since the duration of your credit history also affects your credit score.

Will Bankruptcy Affect My Credit Score?

Your credit score will be considerably reduced by bankruptcy, which will probably be on your credit record for 7 to 10 years. Before filing for bankruptcy if you are having trouble paying your debts, take into account all of your options, including debt consolidation.

Do Many People Have Credit Scores of 800?

Scores between 800 and 850 are regarded as outstanding. About 21% of persons have a FICO score of 800 or more, with the average score being 714. On average, less than 1% of borrowers with excellent credit ratings have major payment defaults.

The Bottom line

Your financial stability depends on you understanding how credit scoring works. Knowing the components of your credit score, such as your payment history and credit usage ratio, can help you take steps to raise it. You're more likely to get approved for the best terms on financial goods like credit cards, mortgages, and auto loans if your credit score is higher.

Function and Value of Credit Score

Today's consumers, buyers, and company enterprises all rely heavily on credit. Your credit score affects every aspect of the credit availability system, including the length of time it takes for an offer to be accepted. For loans and credit to be made available for the purchase of anything unique and rare, you must have a high credit score.

However, persons who seek credit are not the only ones for whom a credit score is important. Additionally, it could make your insurance alternatives more appealing, and it might even make you seem more responsible to potential employers. Let's find out more about the numerous ideas surrounding credit scores and the advantages of keeping them high.

Credit actually means

In a nutshell, a "credit" is essentially the act of borrowing money, whether it be for a loan or a purchase, with the promise of repaying the obligation within a certain time frame. Failure to do so results in a set amount of interest being added to the past-due amount. Low credit scores are the result of routinely missing payments on debts and past-due obligations. Your capacity to get future credits and loans is hampered by a bad credit score.

Definitions and Participants in Credit Score

Using statistics, one may determine a person's chance of repaying debts by looking at their credit score. Your personal record is evaluated by a variety of credit bureaus, who then provide you the score. Every organization has a unique method for evaluating employees, and the computation is based on many distinct variables.

There are three significant worldwide credit score agencies that assess a person's credit scores. The main three companies providing their services for the examination of credit scores are Equifax, Experian, and TransUnion. The first credit information company in India, CIBIL (Credit Information Bureau Limited, India), was founded in 2000 and is connected to TransUnion, which has its headquarters in the United States. However, it is noteworthy to note that although being based on the same facts, each organization's credit score for the same person may vary because of how they go about evaluating applicants.

What a Credit Score Does

Your credit score is often the first thing the credit provider looks at when you ask for credit. You follow the same procedure whether you're applying for a credit card, loan, or mortgage. Credit reports and credit scores are indicators that let a lender determine your dependability for making on-time debt payments. Thus, the risk evaluation of the person or asset, in this example, you, are where the credit score is most crucial. If your credit score is on the low side, you need to raise it. This is due to the fact that, even if you do not meet the high requirements, you will still be given credit, but at a higher interest rate than someone with a higher credit score. Therefore, the interest rate will be greater the lower the credit score, which would ultimately mean a larger monthly payment [4]–[6].

Banks and other financial institutions may also employ internal scoring processes in addition to credit scores to determine a person's credit worthiness.

Advantages of a high credit score

Only by highlighting the benefits of having a good credit score can the significance of having one be emphasized. Credit purchases may be used to cover expenditures like that loan-required dream business idea, the vacation wedding, school debts, and other unanticipated costs.

Being seen to be of lesser risk can make it easier for you to get grants if you have a strong credit score. You will be required to repay your loan at reduced interest rates, which is more significant. Improve your credit score right now to qualify for the finest personal loans from Standard Chartered!

Sections of a Credit Score

It is crucial to understand the many aspects of credit score in order to keep or achieve a decent score. You can only create a strategy to raise your credit score after you are aware of your prospective improvement areas. The following are the primary variables considered while evaluating credit scores:

- a. A person's credit payment history
- b. The individual's ongoing indebtedness
- c. The length of the credit history
- d. Credit blend
- e. The frequency of new credit applications

How Can Credit Scores Be Raised?

Some straightforward methods to raise your credit score are the ones listed below:

- a. Monthly loan and debt payments made on time and in full when due.
- b. Refraining from using unauthorized new cards and credit card extensions
- c. Self-precaution goes a long way, thus disregarding past-due invoices is strictly prohibited.
- d. Maintain open lines of contact with the creditor and make plans for payments when you are having financial difficulties.
- e. Understanding the kind of credit card being used
- f. Limiting the number of credit card applications is a certain method to ensure that you never increase your credit limit, and refraining from excessive spending is the best course of action when attempting to raise credit score.

Reduced Credit Score

Credit is a delicate issue, and the report only has meaning when considerable information is gathered over time. The likelihood that the outcome will be correct increases with length of credit history. So give the lenders a lengthy credit history. Plan recurring payments in advance of deadlines. You can only benefit from a credit score if you exercise solid practice and discipline [7]–[9].

CONCLUSION

In conclusion, credit scoring is a key component of the bank credit assessment process that has the ability to improve and expedite loan choices in the fast-paced financial environment of today. Credit scoring is emerging as a key instrument that bridges the gap between borrowers' expectations and lenders' caution as technology continues to transform the banking sector. Banks are able to make well-informed and unbiased choices thanks to the credit scoring system's methodical assessment of a person's or company's creditworthiness. Credit scoring creates a

thorough picture of an applicant's risk profile by examining a variety of financial and non-financial data points. This complete picture enables lenders to more precisely and effectively determine the possibility of payback. It is impossible to exaggerate how important credit scoring has been in democratizing credit availability. It encourages financial inclusion by eliminating subjectivity and biases from the loan process, enabling people with spotty credit histories or unusual backgrounds to be appropriately assessed. This significantly contributes to economic development by enabling a wider spectrum of borrowers to realize their potential. Credit scoring is a powerful tool, but how well it works depends on the quality and quantity of the data it uses. To preserve the reliability of credit scoring systems, it is necessary to handle continuing concerns including ensuring data veracity, combating fraud, and dealing with biases.

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CHAPTER 6

COLLATERAL AND ITS SIGNIFICANCE IN SECURED BANK CREDIT

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ABSTRACT:

A crucial component of secured bank lending, collateral acts as a safeguard for both lenders and borrowers. This chapter explores the idea of collateral, its significance, and its use in securing loans. The chapter delves into the fundamentals of collateral, or the assets that a borrower pledges as security for a loan. For lenders, these assets serve as a kind of security by providing recourse in the event of borrower failure. Various assets, such as real estate, cars, investments, or priceless things, might be used as collateral. The chapter explains the significance of collateral and emphasizes how it reduces risk for lenders by giving them a material item that can be sold to pay back existing debt. Due of this protection, lenders may provide loans to a wider spectrum of applicants, even those with a bleak credit history or poor credit ratings.

KEYWORDS:

Bank Funding, Collateral, Credit History, Loan Secured Bank Credit.

INTRODUCTION

A valuable asset that a borrower promises as collateral for a loan is known as collateral in the financial industry. For instance, the house is used as collateral when a homeowner takes out a mortgage. The automobile is the security for a car loan. When a company seeks bank funding, it may use valuable assets like real estate or equipment as collateral for the loan. If there is a default, the lender has the right to sell the collateral to make up the difference. Other assets may be used as security for other unsecured personal loans. A cash deposit equal to the credit limit, such as \$500 for a \$500 credit limit, might be used to establish a secured credit card.

What is loan collateral?

A valued object, such as a vehicle, home, or even cash, may be used as collateral to obtain a loan. The lender may take possession of whatever you pledged as collateral if you are unable to repay the loan. Financial institutions and other lenders often see loans backed by collateral as being less risky, and certain loan types (such as mortgages) by default need security. You may sometimes be able to use the option of providing collateral to get a loan or credit product for which you would not otherwise be eligible [1]–[3].

Workings of Collateral

Lenders want to be sure that you have the means to pay back any loans before they provide them to you. Because of this, many of them need security of some kind. This guarantee, known as collateral, lowers the risk for lenders by making sure that the borrower fulfills their financial commitment. Because they risk losing their house or other assets used as collateral if they don't

make their payments on time, the borrower has a strong incentive to pay back the loan. Collateral-backed loans often have interest rates that are much lower than those of unsecured loans. A lien is a legal right or claim made by a lender on assets held by a borrower in order to pay off a debt. If the borrower does fall behind on the loan, the lender has the right to take the collateral, sell it, and use the proceeds to cover the outstanding balance. In order to recover any outstanding debt, the lender may decide to file a lawsuit against the borrower.

Various Forms of Collateral

The forms of collateral often vary depending on the loan type requested. The following are some examples of well recognized assets:

Property

Real estate serves as the security for mortgage loans, LAP, and home equity loans. It may also be utilized to get secured personal or corporate financing.

When making such loans, the lender encumbers the property with a lien.

Investments

You may borrow money from financial organizations using your investments, a practice known as security-based lending or stock-based lending. Shares, bonds, term deposits, mutual funds, and many more financial products are among the qualifying financial products. However, the lender will want more security if the market value of these assets falls below the amount owed on the loan.

Vehicles, including automobiles

The car is put up as collateral when you apply for an auto loan. To satisfy funding needs, you may also apply for a loan on a vehicle that you already own. Both of these cases include the lenders keeping the keys to your car until the debt is completely repaid.

Cash

You may apply for a loan using the remaining funds in your savings account. Additionally, lenders provide loans secured by money market accounts and certificates of deposit (CDs). The security's value serves as the upper limit or ceiling on how much may be borrowed.

Other priceless resources

Some lenders could accept assets as collateral, including jewelry, collectibles, and more. Additionally, loans against inventory are available to businesses. To ascertain their worth, an appointed assessor must evaluate these assets.

What Collateral Can I Use for Small Business Loans?

Small business owners who want to apply for a loan may put their company's assets up as collateral. These may contain inventory or accounts receivable. You may need to provide additional assets, such as cash or real estate, to secure the loan if the total assessed value of your inventory and receivables is lower than the loan amount. The kinds of assets that qualify for small company loans vary on the underwriting standards of the lenders and the kind of loan requested.

DISCUSSION

Benefits and drawbacks of collateral lending

Secured loans, like other forms of finance, may be beneficial, but they also have significant drawbacks.

Benefits of Securing Loans

Secured loans may provide a few more advantages in addition to giving you access to finance for a house or car when you use security. For starters, borrowers with weak or restricted credit may find a secured loan or credit card to be an ideal option. Collateral may increase the likelihood of acceptance and provide a chance to establish credit via timely payments. Additionally, even if your credit is already excellent, choosing a secured personal loan might provide you access to higher loan amounts and a cheaper interest rate.

Negative aspects of secured loans

Secured loans do, however, come with certain dangers. A default on such a loan may result in the loss of the security. This does not imply that you should never take out a secured loan. Since most individuals cannot afford to purchase a home or automobile outright, collateral is a need for loans like a mortgage or auto loan. But before applying, it's critical to comprehend the danger while thinking about a secured loan [1]–[6]. A secured loan application procedure could also be more difficult. For instance, the lender will often ask for an evaluation if you are utilizing assets like paintings or jewelry as security.

How does collateral function?

When you pledge an asset as collateral for a loan, you guarantee that you will pay back the lender. Even if you miss a payment on a loan or credit card, the lender may still be able to recover their loss by taking the asset. A secured loan is what this kind of loan is sometimes called as since the collateral "secures" the funding. For instance, if you take out a vehicle loan, the loan is secured by the collateral your new automobile. Lender may seize the vehicle if you don't make your loan installments on time. In most cases, the collateral's worth is enough to offset the lender's loss in the event of a loan failure. If such is not the case, the lender may file a lawsuit to recover the unpaid debt. However, if you pay off the debt, the lender will relinquish their ownership interest in the item, leaving you as the only owner.

What is acceptable as collateral?

The sort of loan that has to be secured determines the type of collateral that may be used. The most typical examples of items used as collateral by lenders are listed below:

1. **Automobiles and other vehicles:** When you purchase a vehicle, it also serves as collateral for your loan. Alternately, you might leverage the equity in your automobile to get a title loan; however, you should first be aware of the hazards.
2. **Real estate:** The house you're purchasing will serve as security if you get a mortgage. Additionally, if you currently own a property, you may leverage your equity to qualify for a HELOC or home equity loan.

Cash:

A deposit account, such as a savings account, money market account, or certificate of deposit (CD), may also be used as collateral in specific circumstances.

- a. Investments: Investment accounts, specifically for a loan based on securities, may also be used as collateral. From 50% to 95% of the value of your brokerage account, this may be a fixed-rate loan or an ongoing line of credit.
- b. Valuables: Last but not least, collateral might include precious items like jewelry, antiques, and works of art. If you use these kinds of items as collateral to get a loan, the lender will probably want you to provide an evaluation of the items' worth as collateral.

What forms of loans need security?

Secured loans are often used. Collateral is a need for a number of loans since it is intended to be used as security.

Home loans

The first secured loan that springs to mind is probably a mortgage. The house is used as collateral when you get a mortgage to pay for it. You risk losing your house to foreclosure and all the equity you've amassed if you don't pay your mortgage. The same reasoning applies to car loans, where the vehicle you're financing acts as security. HELOCs and home equity loans:

If you borrow money against the equity in your house, you may use it as security. Remember that to be eligible for this sort of financing, your house must typically have 15% to 20% equity. Some of the most frequent instances of financing when the security is optional include: Secured credit cards:

Despite the fact that the majority of credit cards are unsecured, they often need at least decent credit (or a credit score of at least 670). On the other hand, secured credit cards are a great choice for those with bad credit. A cash deposit is used as security for a secured credit card, and this deposit often sets the card's credit limit.

The Capital One Platinum Secured Credit Card (see rates and fees) has a credit limit of \$200 even if you are eligible for the \$49 or \$99 deposit amounts, which is unusual since often the credit limit and the deposit amount are the same.

If collateral security is needed, when?

Normal retail loans like mortgages, auto loans, personal loans, etc. do not need collateral security. However, lenders in business loans like Cash Credit want collateral security. Since the borrower in a CC account has access to the principal security stocks and book debts and may sell them at any time as well as divert money, extra security in the form of moveable property or other assets is obtained to secure the loan. Loans to micro and small businesses up to one crore rupees covered under the CGTMSE plan do not need collateral security. Collateral-free loans are those that have no securing collateral.

When there is no main security and just collateral security is present?

There may only be collateral security available for certain kinds of credit facilities rather than main security. These facilities are offered by lenders without any clear use in mind other than speculating. For instance, LAP (Loan against Property) mortgage loans, which may be used for either personal or commercial reasons but have no clearly defined purpose.

How "Desirable" is the asset, exactly?

The MAST framework is a helpful tool to aid in conceptualizing the overall attractiveness of collateral. Marketable, Ascertainable, Stable, and Transferable is referred to as MAST.

1. An active secondary market for the asset is implied if it is marketable. Excellent examples are equities and bonds, which are traded on international marketplaces. On the other hand, since it only appeals to a certain audience, fine art is slightly less marketable.

2. Ascertainable measures the ease with which a price (or market value) may be quoted or quantified; this is often done with the help of an appraiser (as in the case of commercial real estate), however stocks and bonds are also very simple to determine because they trade in real-time on open markets. On the other hand, intellectual property is significantly more ambiguous and difficult to value.

3. How steady is the value of the asset? While stocks in particular might be unstable, marketable assets can have an active secondary market and their values are marked-to-market, so the real value of the collateral may be fairly variable. On the other hand, commercial real estate is usually considerably more consistent day to day.

4. Can you transfer the asset? If a forestry firm wants to use inventory as collateral, most of it may be inaccessible to other parties since it is situated in a remote area, and moving this collateral might be highly expensive. As opposed to real estate, a collateral mortgage arrangement on the subject property simply has to be discharged (and then re-registered).

Higher loan-to-values (LTV), lower interest rates, and longer amortization periods are typical for collateral assets that perform well against these MAST criteria.

How much does the asset cost?

The monetary worth of an item might signify a variety of things. For the purpose of granting credit, one metric that is often used to determine the value of inventory or accounts receivable is book value.

It is customary to consider the purchase price as the "value" for determining loan-to-value when a firm purchases fixed asset (such as real estate, machinery, and equipment). A third-party appraiser is often enlisted to determine the asset's worth for used equipment. Three "values" are often offered by equipment appraisers when writing a valuation report. Which are:

1. Fair Market Value (FMV): FMV is an estimate of the "price" of an item if several knowledgeable parties participated in a conventional bidding procedure without regard to time.

2. Orderly Liquidation Value (OLV): OLV offers an estimate of "price" if the asset were to be auctioned in a "orderly" auction procedure and time were of some importance.

3. Forced Liquidation Value (FLV): FLV considers the "price" that an asset may bring if a creditor had to sell it immediately without the advantage of a fair auction.

What is the purpose of collateral?

The original creditor's claim is "discharged" by its legal counsel after the complete loan exposure has been repaid (either by the borrower making payments or by refinancing by a new lender). However, if a borrower misses a payment on a loan to a lender and the credit exposure cannot be refinanced with another company, the lender may be able to liquidate the asset (or assets) over which they have a charge in order to recoup the unpaid balance plus any accumulated interest. that was previously said, assets are confiscated and sold in the same order that the security charges were filed [7]–[9]. Collateral assets are often sold at auction for more than is owing to the creditors in liquidation situations. In this scenario, excess cash over the existing credit debt plus interest would be transferred to the company's ordinary owners.

CONCLUSION

As a concrete illustration of the confidence between borrowers and lenders, collateral develops as a pillar in the world of secured bank lending. It is significant because it helps borrowers with different financial histories and requirements get access to loans while also reducing risks for lenders. Lenders are given a safety net through collateral, which guarantees that, in the case of failure, they will have a physical asset to recoup their investment. Lenders are able to provide loans at more favorable conditions, cheaper interest rates, and larger loan amounts because to this decrease in risk. It acts as a bridge of opportunity, giving borrowers the ability to get money for a variety of things, like establishing companies, buying houses, or paying for school. Collateral broadens the definition of eligibility for credit beyond credit ratings and financial histories. It opens doors for those with poor credit histories or unusual situations to get loans, promoting financial inclusion and empowerment. The significance of collateral must be carefully calibrated, however. The risk of losing an asset while using it as collateral is something that borrowers must be aware of. To prevent disputes and misunderstandings, lenders must maintain open and honest assessment and evaluation processes.

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CHAPTER 7

UNSECURED BANK CREDIT: RISKS AND BENEFITS

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ABSTRACT:

Unsecured bank credit is a credit option that gives borrowers access to money without needing collateral, but it also has advantages and disadvantages. This chapter explores the world of unsecured bank credit, highlighting both its benefits and possible drawbacks. The chapter investigates the characteristics of unsecured bank credit, which includes credit cards, personal loans, and specific lines of credit. It draws attention to the fact that there is no collateral present, leaving these loan agreements entirely dependent on the borrower's creditworthiness and financial background. The chapter highlights the advantages and emphasizes how easy and accessible unsecured financing is. Without going through the appraisal and collateral procedures involved with secured loans, borrowers may get cash immediately. Additional benefits include the adaptability of the use of money and the lack of asset forfeiture in the event of default. Although the chapter focuses on higher interest rates than secured lending, it also explores the attendant hazards. Unsecured loans have higher interest rates to make up for the absence of collateral. This component, which is discussed in the chapter, underlines the risk of rising debt if it is not handled correctly.

KEYWORDS:

Collateral, Credit Cards, Financing, Personal Loans, Unsecured Bank.

INTRODUCTION

Unsecured risk is a sort of credit risk that develops when a lender gives a borrower credit without requesting any security or collateral in return. In other words, the borrower's creditworthiness and capacity to repay the loan are the only factors on which the lender is depending. The lender may suffer financial losses if the borrower fails on the loan since there may be no other way to get their money back. Unsecured loans are a key component of the business models of the financial institutions that provide credit and loans to both people and corporations. However, their performance and durability depend on how they manage unsecured risk [1]–[3].

Financial service providers must properly evaluate the borrower's creditworthiness in order to manage unsecured risk. To ascertain the borrower's capacity to repay the loan, analysis of their credit history, income, and other financial variables is required. In order to spot any changes that could impair the borrower's capacity to repay the loan, financial service providers must also routinely check the borrower's creditworthiness. Additionally, by establishing sensible lending limits, diversifying their loan portfolios, and putting in place efficient risk management rules and processes, financial services providers may lower unsecured risk. By taking these steps, they may lessen the negative effects of loan defaults on their company's operations and guarantee its long-term viability.

In summary, unsecured risk is a typical risk that financial service providers encounter when lending money to borrowers without the use of security or collateral. Financial service providers must conduct a comprehensive assessment of the borrower's creditworthiness, continuously monitor that creditworthiness, and put into place efficient risk management policies and processes to properly manage this risk.

How Do Unsecured Loans Work?

Unsecured loans, also known as good faith loans or signature loans, don't ask the borrower to put up any security. Personal loans, school loans, and unsecured credit cards are examples of common unsecured lending kinds. These loans are available from many different conventional, internet, and government-backed lenders, and the application procedure is often less stringent than for secured loans.

Loans: Secured vs. Unsecured

Unsecured loans don't need collateral, making them riskier for lenders than secured loans. If a borrower fails, banks are only able to use restricted collection measures, such as wage garnishment. Banks and other lenders often need a better credit score to be eligible for unsecured loans in order to reduce their risk. Additionally, unsecured loans have worse conditions and higher interest rates than secured loans.

DISCUSSION

Workings of Unsecured Loans

You may utilize unsecured loans, which normally run from \$1,000 to \$100,000, for a variety of things. Annual percentage rates (APRs) typically vary from 6% to 36%, and loan durations typically last between two and seven years. Borrowers should compare loans to choose one that best suits their requirements since loan amounts, interest rates, periods, and permissible uses differ across lenders.

In order to compare potential rates without having to apply and go through many onerous credit checks, several lenders now provide online prequalification. Prospective borrowers could also be able to submit an application for a loan and learn the lender's decision online, depending on the lender. Furthermore, as unsecured loans do not need collateral, applicants are not required to wait for an appraisal or otherwise show the worth of any assets [4], [5].

Funds are delivered in a lump sum when an unsecured loan is granted, and interest is charged on the whole loan amount. The borrower may spend the money as required using unsecured credit cards and other lines of credit, and interest is only charged on the outstanding amount. Payments must be paid on a monthly basis, and late payments must usually be reported after a grace period to the three main credit agencies.

What takes place if you can't repay an unsecured loan?

Your missed payments will be sent to a collection agency by the lender if you are in default on an unsecured loan. This will lead to collection calls, and if the debt is not paid after repeated requests, legal action may be required to recover the amount.

If such a lawsuit is successful, the lender may recover the debt by garnishing wages or, in the case of federal student loans, by seizing upcoming tax returns. A lien may also be put on your house or another valued asset by a lender. Additionally, the default will significantly lower your credit score and be reported on your credit record for up to seven years.

Why has the number of unsecured loans increased?

The conversation clarifies the continuing debate in the banking industry regarding the advantages and disadvantages of unsecured loans and highlights the significance of financial institutions using careful and responsible lending methods. The Reserve Bank of India (RBI) position on unsecured loan exposure for banks and the reasons for their uneasiness with large levels of unsecured loans are discussed in this podcast by Hamsini Karthik of businessline. Unsecured loans are those without any security or collateral behind them, thus if the borrower fails, the bank has no other way to get their money back.

The podcast emphasizes that unsecured loans have increased over the last several years, making up a significant share of all retail loans. Unsecured loans are more readily available and processed more quickly because to their popularity among banks, which has increased this market segment's growth rate. The possible danger connected with unsecured loans has been mentioned as one of the main issues. Borrowers can be inclined to default on the loan if they run into financial troubles, such as losing their job or seeing their income decline, and the banks might not have a good way to get their money back.

The program also discusses the general state of the economy and the hazards associated with employment market volatility. Unsecured loan demand strongly influences job market development and stability, notably in the IT industry, which is a major factor in the expansion of unsecured loans. The unsecured lending market may see increased delinquencies if the employment situation continues to worsen. Given that it may be a dangerous game, the RBI and banks are being careful about this surge in unsecured loans. Due to their reduced operating expenses, unsecured loans presently provide greater rates, but there is a chance that banks may keep playing the high-yield game even when it becomes dangerous, which might result in possible complications. The program ends with the acknowledgement that banks must closely monitor their exposure to unsecured loans since it might quickly deteriorate. But because there is no information from outside sources, it is still unclear how this scenario will play out.

What Is a Personal Unsecured Loan?

You may receive money for things you might need, such as to pay off medical debt, repair your property, or do any number of other things, by taking out a personal loan. Unsecured refers to the fact that there is no need for collateral when applying for an unsecured personal loan. A mortgage, on the other hand, uses the house you're buying as collateral. Due to the lack of security behind an unsecured personal loan, you may be subject to higher interest rates, fees, and other expenses that may restrict how far the loan may be used. Additionally, consumers with poorer credit ratings could find it difficult to obtain approved due to the absence of collateral [6]–[8].

Why Unsecured Personal Loans Are Beneficial

Absence of Peril to Personal Property

There are secured personal loans and unsecured personal loans. A secured personal loan is one that is supported by collateral that your lender may seize in the event that you are unable to repay the loan. The benefit of having an unsecured personal loan is that, in the case of default, your personal property is often not at danger. So if you lose your job and it becomes difficult or impossible to make payments on time, you won't have to worry about losing your house or any other assets.

Application procedures are easier

The procedure for obtaining a personal loan is less difficult now that lenders other than banks and credit unions offer them. From the convenience of your home, you may apply for a loan on a peer-to-peer lending platform. Additionally, one might be authorized for in less than a day. Your credit history and score will determine whether or not you are approved for a loan. Additionally, you must be able to provide evidence of a reliable and secure source of income.

Unsecured personal loans' drawbacks

In the event of a default, your lender could pursue you: A lender may still be able to put a lien on your assets to ensure repayment even if a personal loan isn't secured by a specific item of personal property. A lender must file a lawsuit against you in order to secure a lien. You can be required to pay court expenses and attorney fees in addition to the initial loan amount you borrowed and late fees. After everything is said and done, you can acquire a mark on your credit record and, in the case of a successful lawsuit, have your salary garnished.

Loan amounts might be lower

It is common secret that lenders earn from the interest they collect on loans, but if the loan is not returned, there is no profit. Lenders go to tremendous pains to reduce the danger of borrower failure because of this. In the case of unsecured personal loans, they may limit the amount they grant you (particularly if your credit score is poor) after doing credit checks and verifying your job.

Higher Payments and Rates

Lenders often demand higher interest rates for unsecured personal loans because they are riskier than loans backed by real estate. Your credit rating and the amount of money you're borrowing will determine how much higher the rates are. Interest rates for unsecured personal loans as of May 2021 varied from 3% to 36%. It's crucial to remember that lenders could conceal some of the higher interest rates in up-front costs like application and loan origination fees. Your monthly payments can be more expensive than they would be for a secured loan if the interest rate is greater. Additionally, the more interest you pay the longer your payback time is.

Make sure the monthly payment is inside your budget before you get a loan. Significant late payment penalties are sometimes included in personal loan agreements, which may make it more difficult for you to make timely payments.

Finally, to determine the true cost of borrowing, think about utilizing the personal loan calculator on Smart Asset. The amount that you are really responsible for paying might come as an unwelcome surprise. It's possible that you're just swapping a present issue for a far more difficult one in the future.

To sum up

Unsecured personal loans do, of course, offer benefits. Online loan applications don't need you to go through a rigorous underwriting procedure. The loan may then be used to pay for a number of costs, such as outstanding medical bills or house improvements. However, unsecured personal loans may also be dangerous, and you could have to accept a higher interest rate as a result. Try not to focus only on the benefits of obtaining a personal loan. Instead, think on what you may lose.

Tips for Financial Planning

1. Creating a financial plan may assist you in long-term money management. A financial adviser can provide you with expert assistance in this area. Finding a competent financial adviser need not be difficult. You may interview your advisor matches for free to choose which one is best for you using Smart Asset's free service, which connects you with up to three local financial advisers. Start your search for a financial adviser right away if you're prepared to do so.
2. In contrast to financial plans, which let you make long-term goals, budgets focus more on the present. To get started, try utilizing the budget calculator on Smart Asset. Several of the best budgeting applications on the market are included on our website.

Why unsecured loans are made

Unsecured loans often have a purpose that is chosen by the borrower. A loan is considered to be unsecured from the standpoint of the bank or financial institution if it does not have any underlying collateral. A personal loan may be chosen if the borrower plans to use the money for various things rather than necessarily buying anything. These personal loans do not have any assets pledged as security with the bank, yet they may or may not be utilized to purchase assets.

Unsecured loans' main goal is to make money available to those who could have a lot of financial obligations but are unable to meet them because of a lack of finances. Personal loans are the most typical unsecured loan kind, although there are also student loans, education loans, overdraft protection lines of credit, payroll lenders, and credit cards.

Characteristics of unsecured loans

The following are some of the main characteristics of unsecured loans:

There is no collateral

In order to lend money to the borrower, the lender uses collateral as security. Unsecured loans are those where no collateral is offered. The lender will have to write off the unsecured loan as a bad debt if the borrower defaults.

High rates of interest

Unsecured loans greatly raise the lender's risk. For unsecured loans, the lender often imposes stringent requirements and high interest rates as a means of making up for the added risk. Even if this does not make up for the risk that the bank took, it nevertheless gives banks and other financial institutions considerable motivation to operate in this sector. If the borrower fails, the bank's sole recourse is to file a lawsuit and take the issue to court.

No tax advantages

Banks often provide loans that are eligible for tax advantages; one such example is house loans. Unsecured loans don't provide this kind of tax advantage. Another frequent example of how secured loans may provide tax discounts and generate extra savings is business automobile loans (also known as company car leases), when the money is borrowed from the standpoint of a tax break.

Decreased loan amount

In comparison to unsecured loans, secured loans have larger loan amounts offered. If the loan being asked for is secured, the same applicant with the same credit score will be able to borrow a sizable amount from the bank or financial institution. An unsecured loan, on the other hand, limits how much the borrower may borrow to a lesser amount.

Short-term financing

A shorter repayment period applies to unsecured loans. They are between 3 months and 5 years old. There are no permissible variable conditions for loan repayment. Credit cards are an example of a revolving debt under the unsecured loan category, even though most unsecured loans have a set period and do not convert to one. Depending on the sum due, the monthly payments and interest rates are flexible and subject to fluctuate each month.

CONCLUSION

In conclusion, unsecured bank credit is a kind of financial instrument that has dangers as well as possible rewards for both lenders and borrowers. It gives flexibility and accessibility, but at the cost of some unpredictability and accountability. Unsecured bank credit, which promotes financial inclusion and serves a larger spectrum of people and enterprises, does not need collateral for borrowers to be able to access cash.

This accessibility may encourage innovation, drive economic progress, and allow people to pursue their personal and professional goals. But there are also increased hazards when there is no collateral, particularly for lenders. Because there is no real property serving as security, lenders have few options if there is a default. In order to make up for the greater risk, unsecured financing often has higher interest rates and tighter qualifying requirements. For borrowers, a feeling of financial responsibility must be used to moderate the temptation of unsecured credit's simplicity and quickness. Creditworthiness is more important in the absence of collateral, and failures may have a long-lasting impact on credit ratings and financial stability. Unsecured bank credit has dangers, although it is not always a bad thing.

It is an effective financial tool that, when utilized responsibly, may provide chances for development, capitalizing on advantages, and minimizing unanticipated costs. Both borrowers and lenders must do due diligence, be open with one another, and be aware of their financial capacities.

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CHAPTER 8

INTEREST RATES AND BANK CREDIT: FIXED VS. FLOATING RATES

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ABSTRACT:

In the world of bank lending, interest rates are crucial because they affect the cost and conditions of borrowing. This chapter explores the interaction between fixed and variable interest rates, shedding light on their importance and bearing on borrowers' financial choices. The difference between fixed and fluctuating interest rates is discussed in the chapter. While floating rates change dependent on the state of the market, fixed rates are constant during the course of the loan. It clarifies the impact of selecting one of these rates over the other on the regularity of payments and the total cost of loan. The chapter highlights the stability that fixed interest rates provide to borrowers by outlining their advantages. Because fixed rates are predictable, borrowers may plan their finances without having to worry about interest rate fluctuations. When considered chapter, this consistency appeals to individuals looking for a reliable budgeting plan. In contrast, the chapter investigates the benefits of floating interest rates. Lower starting rates may be advantageous to borrowers, especially when market rates are favorable. The chapter also explores the issue of floating rates, which might rise over time owing to changes in the market.

KEYWORDS:

Bank, Borrower, EMI Lending, Fixed Interest Rates, Floating Interest Rates, Repayment Schedule.

INTRODUCTION

An individual who rents an apartment hopes to one day own a house. But actually, purchasing a house, or even just getting ready to do so, is a whole other story. Finance takes precedence over all other considerations, including location, amenities, and connection. Prospective homeowners look for lenders who will grant them the capital they need to construct a home. Different interest rates are a reason for anxiety, despite the fact that banks and other financial institutions are more than eager to discharge the loan. Home loans are offered at either fixed or adjustable interest rates. A borrower must carefully consider whatever option to choose since it will have an impact on the EMI repayment schedule. With floating interest rates, as the name indicates, the borrower's interest payment is directly influenced by the state of the economy. When the bank interest rate decreases, the EMI interest rate also decreases, and vice versa when the bank interest rate increases. The phrase "fixed rate" is a little confusing.

Although the term ensures a set price, read the small print carefully since it can specify that the loan provider can increase the interest rate at any moment owing to specific changes. These may be referred to as fixed-floating rate mortgages since the interest rate may rise under certain

circumstances, but not as much as with floating loans. It is essential to have the paperwork reviewed by legal professionals before choosing this loan so you can be sure you won't be caught in any complicated provisions despite all the creative and sophisticated words. In contrast to fixed house loans, floating loans are provided by lenders at reasonable interest rates. Let's go through the differences between fixed and variable interest rates in more depth [1]–[3].

Why do interest rates fluctuate?

For first-time borrowers, the distinction between fixed and fluctuating interest rates may still be a little unclear. So, the lender specifies a benchmark rate for floating interest rates. These are flexible because market fluctuations may affect them, and the floating home loan interest rate changes as a result. The variable interest rates on the loan are reset by the lender once each calendar year. The loan anniversary date or any quarterly, half-yearly, or monthly resetting cycle might be the trigger.

If there has been a change in the market rate since the period under review, the interest rate is reset. When the interest rate changes, the reset immediately affects the tenure date. The loan duration increases as the market rate rises and decreases when the market rate declines. The EMI is left alone since changing it might negatively impact the borrower's cash flow. The borrower may, however, choose to increase the EMI rather than the tenure if that option is preferable.

When you anticipate a decline in market interest rates, floating interest rates are advantageous. A lower rate will be preferable with a lower floating home loan interest rate if the loan term is shorter than five years. Although the loan lifetime is brief and market changes may occur over time, you may anticipate that for the most of your loan tenure, you will be paying a reduced rate. Nevertheless, you must be aware that the interest rate may suddenly spike. Therefore, adopting a floating house loan interest rate may help you save on interest costs if you are unclear about home loan interest rates. Banks advise clients to choose a floating home loan interest rate since fixed home loan interest rates tend to have substantially higher interest rates.

Fluctuating and fixed home loan choices are available for those who are tired of fluctuating rates. This kind of loan allows you some time to consider your options in the event that interest rates rise. You must, however, read the small print and resist temptation. It might be advisable to convert to fix interest rates for long-term loans when the floating interest rate may peak over a longer duration, equaling or surpassing fixed interest rates, where you can be sure of how much you are anticipated to pay. The lender will impose a floating to fixed changeover fee on the borrower, but if the total loan amount is substantial, the fee is justified.

For a year or two, keep a careful eye on the market, follow the fixed rates offered by different suppliers, and switch when it is most advantageous to do so. Banks making floating loans should be tagged to an external benchmark, according to a 2019 RBI circular. This permits an interest rate change at least once every three months. Banks are allowed to choose the spread above the external benchmark when repo rates rise to 5.90%. Banks will protect their profits, and when interest rates rise, the spread will do the same. Credit risk premiums "may change only when borrower's credit assessment undergoes a substantial change," according to the loan contract. As a result, forecasting the interest rate cycle for fixed vs. variable interest rates is almost difficult.

Definition of fixed interest rates

Housing loans with fixed interest rates have an interest rate that stays the same despite changes in repo rates. When the loan is accepted and sanctioned by the bank, the interest rate is determined. The amount of this loan is not impacted by inflation rates. Long-term housing loan borrowers who choose for fixed house loan interest rates do so because they are at ease with predictable and regular monthly EMI payments.

The fixed rate loan interest is influenced by the loan duration and the current interest rate. Even while fixed interest rates are unaffected by ups and downs in the economy, variable interest rates are also impacted as the economy expands [4]–[6]. The greatest moment to take out house loans with fixed interest rates is right now, when the Reserve Bank has raised the repo rate by 50 basis points, the current repo rate is 5.90%, and lenders are naturally increasing interest rates. Experts believe that choosing loans with fixed interest rates would be a wise choice given the projected spike in interest rates in India and throughout the world over the next two years.

However, lending rates have increased tremendously and will stay the same during the whole loan term. Have a lawyer thoroughly review your paper to grasp the subtleties. Make a thorough analysis of which option will be more beneficial in the long term before making a commitment, and notice the distinction between fixed and variable interest rates. In the next 13–18 months, loan interest rates are most likely to climb by 1-2 percent; account for this increase in your calculations.

Cons and advantages of floating interest rates

Pros

- a. Compared to fixed interest rates, floating interest rates are between 1% and 2.5% lower.
- b. When comparing fixed and floating interest rates, banks and NBFCs' variable rates are lower than their clients' fixed rates. The interest rate may still be lower than the fixed interest rate that these institutions previously gave, even if the floating interest rate increases.
- c. The fluctuating interest rate is unlikely to be higher than the interest rate over the whole loan term. The danger of declining floating rates persists beyond a certain period of time.

Cons

- a. Because the floating loan interest is market-dependent, the EMIs for certain loan amounts will fluctuate.
- b. Because floating loan interest rates are so unpredictable, they cannot be budgeted.
- c. Because of the interest rate choice, the loan does not offer a set repayment schedule; thus, there is a strong probability that borrowers will pay more than they can afford. With less cash on hand, there is a greater likelihood that borrowers may go over their spending limit.

Pros and Cons of Fixed Interest Rates

Pros

- In fixed home loan interest rates, the interest rate is constant. Changes in the market have no impact on them.
- Because the interest rate is fixed and not prone to change, borrowers may budget their loan payments according to predetermined EMIs. You may also invest in other long-term investments if your monthly spending follows a pattern.

Cons

The fixed interest rate typically costs the borrower 1% to 2.5% more than the variable rate charged by a bank or NBFC. After a few years, the fixed interest rate is revised to match the current interest rate. Even if the Reserve Bank of India (RBI) declares a decline in interest rates as a result of a government policy, the fixed interest rate on house loans stays the same. Any change in the interest rate has no impact on the preceding rate of the loans. Additionally, the borrower will have to make consistently larger payments.

Fixed Interest Rate	Floating Interest Rate
Higher Interest Rate	Lower Interest Rate
Not affected by financial market conditions	Affected by changes in the financial market
Fixed EMIs	EMIs change as per interest rate or MCLR
Budget planning possible	Difficult to budget or manage financials
Sense of security	Generates savings
Suitable for short/medium term (3-10 years)	Suitable for long term (20-30 years)
Lesser risk	Higher risk

Figure 1: Comparison between fixed and floating interest rate [paisabazaar.com]

Expert Opinion

Interest rates are better understood by banks. You must put your faith in a reliable bank and speak with your lending bank privately about the distinction between a fixed and fluctuating interest rate. What interest rate will work best for you? We know that fixed loan interest rates are higher while floating interest rates on home loans are lower. If the bank notices a spike in rates, they will advise you based on their specialist knowledge. Banks benefit from higher fixed interest rate earnings, but they also benefit from higher floating interest rate earnings. Therefore, it would be advantageous for the bank to encourage consumers to invest in loans with fixed interest rates if they predict a decline in floating interest rates. Therefore, if you can lock in a cheap fixed interest rate mortgage loan, that's a win-win scenario. If not, go for a floating loan since no one can predict what the future interest rates will be. Figure 1 shows comparison between fixed and floating interest rate [paisabazaar.com].

DISCUSSION

Fixed rate home loan information and benefits

When taking out a fixed rate loan, the interest rate is set at that time. There are options that allow you to fix your interest rate for specific periods of 2, 3, or 10 years and are available with the right of reset by the lender at any time, in addition to a regular fixed rate product where the interest rate is constant throughout the entire term of the loan.

You can manage your finances and create an accurate budget by choosing a fixed rate home loan since you will know what your repayments will be from the moment you take out the loan. Your loan duration, EMI obligations, and the overall interest outflow are therefore quite predictable.

Loans with fixed rates often cost a little more than loans with fluctuating rates. If the difference is large, you could be persuaded to take out a loan with an adjustable rate. However, if they are almost equal or if the difference is little, you may want to consider your requirements and position before choosing between a fixed rate loan and a variable rate loan.

In the following situations, a fixed rate mortgage is recommended:

- i. You feel at ease with the EMI that you have agreed to pay. The recommended range is 25–30% of your monthly take-home pay.
- ii. You anticipate that interest rates may increase in the future and want to lock in your home loan at the current rate as a result.
- iii. Lock in at this rate with a fixed rate loan if interest rates have lately declined and you are okay with the present level of rates. For instance, if the interest rate on a house loan, which was 10% a few years ago but is now, let's say, 8.5%, and you are both emotionally and financially okay with it, you may get a fixed rate loan.

Home loan at a floating rate and its benefits

These loans, which are also known as "adjustable-rate home loans," are based on the lender's benchmark rate, which fluctuates along with the market interest rate. The interest rate on the loan fluctuates proportionally with changes in the benchmark rate.

Such loans have interest rates that are adjusted at predetermined times. Depending on the date of the initial disbursement of the client's house loan, it may be specific to each customer or it may be calendar intervals like every quarter or half of an accounting year. The reset might also be connected to the anniversary of your loan, as an alternative. In general, financial institutions maintain the ability to change the frequency of interest rate resets. Your rates would be adjusted higher or lower as needed if there had been a change in the market rates throughout the review period. When an interest rate reset occurs, the loan's term is often altered to reflect the new interest rate. Your remaining loan term would be extended if the rate went up, and vice versa. This is done to prevent frequent EMI modifications that can affect your cash flow. However, if you choose, you may ask the lender to change your EMI rather than the loan duration [7]–[9].

In the following situations, you should choose a variable rate mortgage:

- a. If you anticipate that interest rates will decline generally over time, choosing a variable rate loan under such circumstances may cause the interest rate that applies to your loan to decline as well, lowering the cost of your loan.
- b. People who are apprehensive about interest rate changes and would rather rely on market rates might choose floating rate loans.
- c. Floating rate loans are often set at a little lower rate than fixed rate loans, offering you some advantage in terms of your loan's cost if you're wanting to save money on interest costs in the near future.

Issues with Fixed Interest Rates

The following are some disadvantages of a fixed interest rate:

- a. Typically, a bank or non-banking financing company (NBFC) offers a variable interest rate that is 1% to 2.5% lower than the fixed interest rate.
- b. Even if the fixed interest rate decreases as a result of a government or Reserve Bank of India (RBI) announcement, the loans that have previously been taken out using the prior interest rate are unaffected. Even after a rate reduction, the borrower will still be required to make payments at the higher interest rate.
- c. Often, a fixed rate of interest is only good for a short period of time before being changed to reflect the current rate.

Choose a Fixed Interest Rate because...

Here are some situations when having a fixed rate of interest could be advantageous for you:

- a. You would want a set payback timeline and feel at ease covering the present interest rate. Make sure that your monthly payment does not exceed 30% of your net monthly income.
- b. You anticipate an increase in interest rates in the future and want to prevent your interest payments from rising over what you are presently paying. In this situation, the fixed interest rate may be utilized to lock in the lender's existing interest rate.
- c. In situations when interest rates have decreased and are anticipated to stay stable for a few more years.

CONCLUSION

The decision between fixed and variable interest rates in bank loans, then, illustrates the complex interplay between risk and reward in the world of finance. Each choice has certain benefits and things to keep in mind for both borrowers and lenders. Due to the steadiness and predictability that fixed interest rates provide, borrowers may confidently manage their finances throughout the loan's term. Lenders, in turn, make sure that interest revenue is consistently generated despite changes in the market. To compensate for any future changes in interest rates, fixed rates sometimes start off more expensive than floating rates. Due to the fact that they are often correlated with current market rates, floating interest rates provide borrowers with an initial reduced cost.

When interest rates are anticipated to decline, this flexibility may be very helpful. Floating interest rates support lenders' capacity to remain competitive and adjust to market developments. However, borrowers must also be ready for any adjustments in monthly payments that may occur as a result of variations in benchmark rates. Individual circumstances, financial objectives, and market outlook ultimately determine whether fixed or variable interest rates are preferable. While borrowers who anticipate dropping rates may choose floating rates to take advantage of possible savings, those who desire stability may choose fixed rates to lessen the effects of interest rate volatility.

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CHAPTER 9

CREDIT LIMITS AND HOW THEY ARE DETERMINED BY BANKS

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ABSTRACT:

A key component of bank credit is credit limits, which specify the maximum amount a borrower may access. This chapter explores the complexities of loan limitations, revealing how banks set these limits and the variables that affect their choice. A credit limit is defined in the chapter as the upper limit on the amount of money a borrower may access via a credit card, line of credit, or other credit facilities. It emphasizes how credit limits are created to strike a balance between the demands of the borrower and the lender's risk exposure. The chapter emphasizes the relevance of the borrower's creditworthiness by outlining the criteria that go into determining the credit limit. The main factors that banks take into account when determining a borrower's financial stability are credit ratings, payment histories, and existing obligations. The chapter explores the significance of credit usage, which quantifies how much of a borrower's available credit is being used. The borrower's income and job stability are also examined in further detail, with a focus on the importance of these elements in assessing the borrower's capacity to pay back the borrowed money. The borrower's current debts are taken into account, since having too much debt might limit their ability to responsibly handle new loans.

KEYWORDS:

Borrower, Credit Card, Credit Limits, Credit Quality, Debts, Financial Management, Loans.

INTRODUCTION

By using mathematical formulae to evaluate your credit quality, credit card firms employ underwriting to calculate your credit limit. Each business has a unique underwriting process to determine who gets approved, at what interest rate, and at what credit line limit. The corporation takes on greater risk the higher the loan limit.

Therefore, card issuers provide larger credit limits to more reliable customers, such as those with better credit ratings, greater incomes, and other indications of sound financial management. Here are some tips for raising your credit limit as well as the fundamental variables that credit card companies take into account when setting your credit limit.

How Do Credit Limits Work?

The credit limit on a credit card determines how much credit the card issuer will provide the customer. Once an application is accepted based on the customer's credit quality, this credit limit, also known as a credit line, is created. Your present financial responsibilities, your history of payments, your credit score, and your income are all things that a credit card issuer would consider.

How Credit Card Issuers Calculate Credit Limits

The credit limit on most credit cards is predetermined. This implies that the issuer will allocate a predetermined dollar amount of outstanding balances you may have on your account for new purchases and/or transferred balances after they have assessed your credit quality. Normally, if you use a credit card above its limit, your purchase may be rejected or you may be charged a fee by the credit card company. Going over your credit limit might also lower your credit score, reduce your credit limit, or raise your interest rate.

Although they are less prevalent, certain premium credit cards and charge cards feature credit limits that are dynamic, meaning that they may go up or down depending on your spending requirements and credit card management. However, the dynamic credit line can often support spending that is out of the ordinary since they have greater flexibility if you anticipate making a big buy [1]–[3].

How Does Your Credit Limit Change?

To calculate your credit limit, most businesses look at your credit history and gross yearly income level. Your credit history's length, quantity of credit accounts, and history of repayment are all things issuers are likely to take into consideration. Mortgages, school loans, vehicle loans, personal loans, and other credit cards fall under this category. Issuers also look at the quantity of new loan queries on your credit record, along with any adverse information like bankruptcies, collections, civil judgments, or tax liens.

FDI Corporation, "Underwriting and Loan Approval Process." The underwriting procedure differs from business to business. Some creditors may look up applicants' credit files to see what other credit card limitations they have. To decide how much to support the borrower, other organizations examine several sorts of ratings, such as the applicant's credit score and bankruptcy score. To assess your risk level, issuers may also look to your job history or debt-to-income (DTI) ratio. You are more likely to get more money if your employment history is solid and you have less debt.

The Best Ways to Raise Your Credit Limit

If you've established a track record of responsible use and repayment, such as by making all payments on time and in full for all amounts, you're more likely to have your credit limit extended. Every six months, businesses often reassess, and they could automatically boost applicants' credit limits. Some issuers ask cardholders whether they wish to apply for a limit after informing them that they meet the requirements.

Cardholders may also ask for a raise. On the other hand, if you are late with payments or go above your credit card limitations, issuers may lower the credit limit. Calling the number generally found on the back of your credit card or entering into your account online will both allow you to verify your credit limit.

How can my credit limit be raised?

By making on-time payments on your debts and refraining from going over your credit limit, you may raise your credit limit over time and raise your credit score. If you pay your amount in whole or more than the minimum payment required each month, you could be able to raise your limit more quickly. You may be able to raise your credit limit if your income rises or your monthly debt payments decrease.

How does my credit limit become set by credit card companies?

Underwriting is used to establish credit limits. The amount of debt you are likely to repay is calculated using mathematical algorithms, extensive testing, and analysis. Your credit limit is determined by the credit card issuers based on your credit history, income, other debts you have, and other financial criteria.

Is a large credit limit advantageous?

The biggest advantage of having a large credit limit is that you can spend more money. However, if your credit limit is larger, you could feel more pressure to overspend. Spending more than you can afford to repay might put you in a debt cycle and force you to pay a lot of interest.

The inference

Underwriting, a procedure used by credit card firms to set an applicant's credit limit, differs from business to business but often involves considering your financial information, including your credit score, history of credit card payments, and income level. By making on-time payments, making extra payments, and staying within their credit limit, cardholders may increase their credit limit.

How Banks Determine Your Credit Card's Limit

The maximum amount permitted by the issuer is known as the credit limit on your credit card. The bank limits your ability to use the card for purchases by establishing a credit limit. Additionally, the predetermined credit limit aids in your continued excellent credit standing. Your credit score is heavily influenced by the credit usage ratio, which is the proportion of your credit card debt to the available credit limit. Your credit score would be lower the higher your credit use rate [4]–[6].

So, how do the banks choose this loan limit?

The factors used by various credit card companies to determine the credit limit that will be given to a particular applicant might vary. However, there are a few common factors that the banks use to determine the credit limit. Let's get into more depth about these components.

Credit Report

Before accepting your application, banks and other credit card issuers will look at this first. They also use your credit score while determining the card's credit limit. Keep in mind that the bank is taking a risk by issuing you a credit card since you are an absolute stranger asking for money. Therefore, they base the credit limit on how good of a risk you are to them.

It is more probable that you will be granted a greater credit limit if you have historically been a responsible borrower and can maintain a high credit score over time. Banks may not be inclined to increase your credit limit, however, if you have a history of irresponsible credit behavior. You must keep in mind that having no credit history might be just as detrimental since there is no prior information on which the banks can depend. In order to determine the applicant's credit score and provide the appropriate credit limit, credit card issuers contact credit bureaus like TransUnion, CIBIL, Experian, and Equifax.

Earnings and Debts

Your income is the second factor the banks take into account when establishing your credit card limit. It is really straightforward: the amount of debt you can afford to pay depends on how much money you make. However, this does not imply that having a greater salary will increase your credit limit. Banks look at your debt-to-income ratio in addition to your income when making their decision.

The size of your current obligations and how you handle them will be significant factors in determining your card's credit limit. The limit on your new credit card will be smaller the greater your debt-to-income ratio. This is also where credit consumption is important. If you have a lot of unused credit on your current cards, this portrays you as a credit-responsible person who uses his credit responsibly. Banks see this as a favorable indicator and could be willing to increase your credit limit.

Other Credit Card Limits

When deciding on a credit card limit, banks often consider the practices of other banks and credit card companies. As a result, choosing the limit for your new card will be aided by the limit on your current credit cards. For instance, it would be challenging to immediately be authorized for a \$2,000,000 limit on an American Express Credit Card if your HDFC Credit Card has a \$50,000 limit. However, getting a high credit limit on your new card would be simpler for you if you are already a part of the exclusive club of clients at another bank.

Credit Cards Types

Regardless of the other reasons listed above, various credit cards provide a certain credit limit and have distinct characteristics. For instance, you will logically get a larger credit limit on a card that is on the elite/premium list since it comes with a certain credit limit at first. However, even if your salary and credit score are excellent, you could not receive a high limit if you apply for a simple card instead. This is so that the issuer may set the basic card's maximum limit at a modest amount. If you have applied for co-branded cards or a credit card backed by a set deposit, the limit may also change.

Other Elements

In addition to the above-mentioned characteristics, banks may also take into account various non-income-based aspects, such as your purchasing habits, such as where you usually buy for groceries or if you like fancy dining. This is particularly relevant if you want to accept a co-branded credit card. If you apply for a credit card that is co-branded with a travel company, the

bank will look at your past travel spending and adjust the credit limit appropriately. The credit limit that might be put on your card will be influenced by the aforementioned crucial factors as well as unique factors like the bank's credit policy.

DISCUSSION

How Credit Limits Operate

The maximum amount of money you are permitted to spend with a certain credit card or revolving line of credit is known as your credit limit. These restrictions are determined by lenders depending on a number of variables, such as your credit score, personal income, and loan payback history. For debtors they consider to be less risky, lenders often provide larger limits. Both secured and unsecured credit have credit limitations. The lender may set a greater limit if the line of credit is secured, or backed by collateral, taking into consideration the value of the backing. For instance, if you get a home equity line of credit (HELOC), a portion of your credit limit will be determined by the value of your house.

In general, lenders will provide larger credit limits to borrowers they believe to be lesser risk and lower credit limits to more dangerous ones. Whether you have a credit card or a line of credit, a credit limit functions in the same manner. Up to the credit limit may be spent. In addition to your normal payment, you can also be subject to fines or penalties if you go above the credit limit. You may use the card or line of credit until you hit the maximum if your spending falls below the cap.

Credit Limit in Relation to Available Credit

There is a difference between a credit limit and accessible credit. The credit limit is the most you are permitted to borrow, but the available credit is the amount that is still accessible to you, even if you have a debt. For instance, if your credit limit is \$1,000 and you charge \$600, you still have \$400 left over to spend. Your amount would drop to \$560 if you made a \$40 payment, and you would then have \$440 in available credit.

How Your Credit Score Is Affected by Credit Limits

Your credit score, a vital figure that lenders use to determine whether or not to grant you additional credit and what interest rate to charge you for it, may be impacted by your credit limitations. That's because one of the elements used to determine your score is your credit usage ratio, which is the amount of debt you have at any one moment as a proportion of the overall credit you have access to. The better, the smaller the proportion. In order to avoid exceeding your credit limitations, it is wise to be aware of them. Lenders often view credit usage ratios higher than 30% negatively.

Can Your Credit Limit Be Changed by Lenders?

Lenders often maintain the right to adjust credit limits, either decreasing or increasing them. The lender may raise your credit limit if you pay your debts on time each month and avoid using all available credit on a card or line of credit. In addition to other advantages, a higher credit limit may raise your credit score by decreasing your credit use ratio. Additionally, it offers you access

to extra credit in case you ever need it, maybe for a sudden emergency. On the other side, the lender may decide to lower your credit limit if you don't make consistent, on-time payments or if there are other indications of risk. Your credit score might be harmed if your credit limit is decreased since it would increase your credit use ratio. Lenders are typically compelled to let you know if they decide to cut your credit limit.

What is Credit Available?

The unused fraction of a credit limit is known as available credit. Therefore, if your credit card has a \$10,000 maximum credit limit and you have spent \$5,000 of it, you would still have \$5,000 in accessible credit. In accordance with account use, available credit may change throughout the course of the payment cycle.

A Credit Limit: Why Does It Matter?

The amount of money you may use to pay for costs is determined by your credit limit, which is why it matters. When making purchases, you must be aware of your credit limit to avoid exceeding it and paying penalties. In such case, a retailer may also decline to take your card. Your credit score, which is based in part on how much of your available credit you are utilizing at any one moment, may also be impacted by your total credit limits.

Factors that credit card companies may use to set your credit card limit

Factor 1: Information about your credit

When determining your credit limit, credit card companies take your credit history into account. That shouldn't surprise anybody. An organization may learn a lot about your debt management practices from your credit history and credit score. Your credit history gives you a glimpse into how you've handled financial commitments in the past, including those related to credit card accounts and others. But lenders might use a credit score as a forecast tool to evaluate risk. A lender may learn from your FICO® Score and VantageScore credit score how likely you are to default on any financial obligation in the next 24 months by looking at your likelihood of being 90 days late (or worse). A greater credit limit may be available to you if you have a strong credit score, which implies a reduced risk threshold. In contrast, a poor credit score may restrict your choices for credit cards and increase the likelihood that the credit limits you do obtain on the accounts for which you do qualify would be smaller.

Factor 2: Debt-to-Income (DTI) Ratio

Another element that might influence your credit limit is the link between your income and your outstanding obligations. Your debt-to-income ratio, or DTI ratio, is the name given to this number. Divide your monthly loan payments by your gross monthly income to arrive at this figure. A credit card provider may determine your ability to take on extra debt using your DTI ratio. A new, high credit line can put you in danger of going over your limit if you already owe a lot in comparison to your income. However, you're less likely to run into this issue if your DTI ratio is low.

Factor 3: Credit Utilization Ratio

Creditors also take into consideration how you handle the open credit card accounts you already have, in addition to your total DTI percentage. Your credit usage ratio is high if it exceeds your credit card limitations, and such circumstance may be problematic for you. On new credit card applications, high credit use often doesn't look good. Even if you have a record of paying your bills on time each month, it might still hurt your credit score.

Finally, having a high credit use rate might be costly. According to the Federal Reserve, the average interest rate for credit cards (among those that charged interest) was 18.32% in Q3 of 2022. However, if you pay off the full amount on your credit card each month (preferably before the statement closure date), you may be able to both keep your credit usage rate low and stay out of paying expensive interest rates.

Factor 4: Relationship with the Creditor

In order to determine whether to authorize you for a new account, the corporation will probably take into consideration any previous or current business relationships you may have had with credit card issuers. If a card issuer approves you, it could also take into consideration your previous or ongoing transactions when determining the credit limit for your new account [7]–[8]. When it comes to credit card acceptance, prior defaults or debts written off in bankruptcy may be a deal breaker at least for the same creditor. However, even after filing for bankruptcy, it doesn't mean you won't be able to get a new credit card somewhere else.

Your current credit limitations may also affect you if you currently hold credit cards with a credit card provider. If you already have what it sees as a large amount of credit available on other accounts it owns, a card issuer could choose to provide you a lesser credit limit. If this occurs to you, you can think about requesting that the card issuer "move" some of your credit limit from an older account to the new one.

Factor 5: Uncontrollable Details

Your credit limit may be affected by some circumstances that have nothing to do with you. For instance, the state of the economy and forecasts for the future may influence how comfortable a credit card firm is with giving credit. Many clients had their credit limitations reduced by credit card companies in the early stages of the epidemic. They took these actions in an effort to lessen their exposure to clients who were unable to pay their invoices on time. Credit limitations may also change as a result of recent or prospective credit card legislation. Some card issuers tried to reduce their risk exposure after the CARD ACT of 2009 was approved by reducing credit limits for consumers who had an excessive amount of unused credit.

CONCLUSION

In conclusion, proper money management and efficient credit use depend on an awareness of credit limitations and the variables that banks take into account when setting them. Credit limitations provide borrowers access to money when they need it while acting as a vital barrier against over borrowing. To determine credit limits, banks consider a borrower's credit history, income level, job stability, and debt-to-income ratio, among other factors. These elements

provide light on a borrower's capacity for responsible credit management and loan repayment. A borrower is more likely to be given a greater credit limit if they have a solid credit history, consistent income, and a reasonable debt burden. Credit restrictions are also influenced by the reason for the credit, such as for personal use, corporate development, or other requirements. When determining credit limits, banks consider any possible risk related to the planned usage of the loan. Credit limitations provide borrowers financial freedom, but they also need caution to prevent them from being caught in a debt cycle. To maintain a good credit profile and prevent taking on excessive debt, responsible credit use, keeping balances low in relation to the credit limit, and regular payments are crucial.

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CHAPTER 10

CREDIT HISTORY AND ITS INFLUENCE ON BANK CREDIT APPLICATIONS

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ABSTRACT:

Credit history is crucial to bank credit applications since it influences lending choices and credit agreement conditions. In-depth discussion of the importance of credit history, its elements, and its impact on borrowers' access to credit is provided in this chapter. The chapter explores the idea of credit history, which captures a person's previous borrowing habits, payment patterns, and sense of responsibility. It draws attention to how credit bureaus compile this data to produce credit reports, which serve as an exhaustive record of a person's credit-related behaviors. The chapter highlights how lenders utilize credit reports to evaluate a borrower's creditworthiness by outlining the impact of credit history on bank credit applications. The probability of receiving credit and receiving favorable conditions is increased by a solid credit history, which is defined by timely payments and prudent debt management.

KEYWORDS:

Credit Bureaus, Credit Card, Credit History, Credit Reports, Credit Scores.

INTRODUCTION

A strong credit history demonstrates that you have paid your debts on time and do not have a lot of outstanding debt. You are a lower-risk borrower as a result. It's simpler to get authorized for loans and to receive cheaper interest rates when you have a strong credit history. The easiest approach to keep your credit score high is to make on-time, complete payments on all of your monthly obligations.

High Credit Scores

You should limit the number of credit cards you have to three or four, keep the balances on them low, retain them for a long time, and never spend more than 30% of your available credit on any one card. Additionally, be sure to aggressively repair any problems you detect in your credit reports by routinely checking them.

Negative Credit History

On the other hand, folks with a poor credit history often have debt that hasn't been paid off. Late or missing payments, extensive credit card use, making several credit inquiries quickly, and experiencing significant financial calamities including bankruptcy, foreclosure, repossession, charge-offs, and settled accounts are all factors that might result in a poor credit history.

Low credit limits with high interest rates, paying security deposits for items like mobile phones or apartment and vehicle rentals, and paying higher auto insurance premiums are all consequences of having bad credit. A poor credit history may be fixed, but it will take time. You should examine your credit score often to determine which bad elements are most significant. You should also pay your payments on time, work off your credit card debt, and only occasionally apply for new credit [1]–[3].

Lack of Credit History

Young individuals who are college-age who have no credit history may find it challenging to be accepted for large loans or leases. If a prospective tenant has no credit history that proves their capacity to make timely payments, landlords may opt not to rent them an apartment. Take out a modest personal loan or apply for a credit card with a low available amount to start building your credit history. Such use enables you to show, prior to taking on higher amounts of debt, how effectively you can manage your credit on a modest scale. You may also obtain a secured credit card, which is secured by a sum of money that you deposit in a savings account, or a joint credit card with someone who has strong credit.

Particular Considerations

If you have paid off all of your bills and refrain from applying for a loan, credit card, or other type of financing for a period of time, you may be able to have a negative credit history erased. Seven or ten years are possible during this period. If such lengthy gaps exist, even consumers with strong past credit histories might essentially start again. If you're prepared to pay a price, you might hire a credit repair business to perhaps get bad marks on your credit report deleted for a speedier answer.

What Distinguishes Credit Score from Credit History?

Your credit history is a thorough account of all of your debt repayments, as well as maybe other financial details. It lists the debts you have, together with how often you have made on-time payments or obtained additional credit. Based on this data, your credit score is a three-digit number.

What Weight Does Credit History Have?

When you apply for financial goods like personal loans, credit cards, auto loans, mortgages, and more, lenders pay close attention to your credit history. To assess your risk as a borrower, lenders use both your credit history and the credit score derived from it. Better credit history increases your chances of receiving credit.

Negative Credit History

What does poor credit history mean?

An individual with a poor credit history has a history of missing payments on credit. A borrower with a poor credit history may not be eligible for a new line of credit since the credit businesses are informed of their inability to fulfill their financial obligations.

Knowing Your Credit History

Credit history of the borrower is gathered by credit reporting organizations and is included in the credit report. Credit firms use credit reports and scores to evaluate potential clients based on the underwriting credit standards. The credit score may be impacted by loan defaults, missed payments, and bad records on the credit report. Due to the possibility of missed payments on new loans or credit cards, credit providers are less inclined to provide a new line of credit in the case of a bad credit history. If you have a bad credit history, your chances of having your credit application declined are often high. Credit bureaus could still choose to accept your application, however. The only drawback is that you would probably be charged a higher rate of interest than applicants with strong credit histories and scores.

The effects of poor credit history

When analyzing credit ratings, credit repayments are a critical factor. You are more likely to miss payments on your credit commitments if you have a poor credit history. Additionally, compared to a borrower with an excellent credit score, the creditor may see you as a riskier borrower. In certain situations, credit providers may decide to penalize you with a higher interest rate to make up for the risk.

How Do Credit Reports Work?

People may sometimes bring up your credit. They are referring to your credit history. How you handle money is shown by your credit history:

- a. What number of credit cards do you own?
- b. What number of loans do you have?
- c. Are your bills paid on time?

You have a credit history if you have a bank loan or credit card. The credit bureaus provide companies with information about your credit cards and loans. Additionally, businesses keep track of when and how you pay their invoices. They compile all of this data into your credit report.

What is meant by "good credit"?

A few individuals have excellent credit. Some individuals have poor credit. Some individuals lack a credit history. This is visible to businesses on your credit report. Various events depend on your credit history:

When you pay your payments on time and do not have a lot of debts outstanding, you have good credit.

That implies:

- a. Greater loan options
- b. Obtaining a credit card is simpler.
- c. Pay less in interest charges
- d. Payless for credit cards and loans

When you owe a lot of money in debt and do not pay your payments on time, you have bad credit.

That implies:

- a. Fewer available loans
- b. Credit cards are harder to get
- c. Increasing interest rates
- d. More for credit cards and loans

When you have no credit, you have never gotten a loan from a bank or other lender or used a credit card.

That implies:

- a. No or little bank loan options
- b. Very difficult to get credit cards
- c. A high rate of interest.
- d. Credit cards and loans are expensive and difficult to get.

Your credit report has all of this information.

What is credit history so crucial?

Lenders use your credit history when making lending choices in order to assess your likelihood of timely loan repayment. A longer history demonstrates that you have greater credit history. Lenders can more accurately assess the degree of risk they assume when lending to you the longer your credit history has been established.

Your credit history's age, however, is just one aspect of the problem. The following are other elements that affect your credit score:

- a. Payment background
- b. The amount of current debt you owe
- c. Your credit-to-debit ratio
- d. Your assortment of credit cards
- e. The total amount of fresh credit you've requested

Your credit score is more influenced by your payment history and credit use ratio than by the age of your credit accounts. So, regrettably, having a lengthy credit history may not be enough to make up for the less-than-ideal information on the reports if they reveal that you've missed payments and maxed out credit cards.

On the other side, if you have a lengthy history of on-time payments and a low credit usage ratio, it demonstrates that you have solid credit management skills and are a good risk to lenders, increasing the likelihood that you will be accepted for credit cards and loans.

How soon will your credit ratings be impacted by your credit history?

Generally speaking, in order to get your credit score, you need to have at least one open account that has been reporting to the credit agencies for six months. By paying your payments on time and opening a variety of credit accounts, such as installment loans (such as a student loan or mortgage) and revolving lines of credit (such as a credit card or home equity lines of credit), you may continue to develop your credit history [4]–[6].

A specific credit score may be attained in any period of time, however. Everybody has a different financial status, thus it differs from person to person how long it takes for credit scores to rise.

A credit score: what is it?

Based on information from your credit reports, a credit score predicts your credit behavior, such as how likely you are to repay a loan on time. Your eligibility for a mortgage, credit card, vehicle loan, and other credit products, as well as for tenant screening and insurance, are all determined by credit scores. They are also used to calculate your credit limit and interest rate.

Credit Score Range	Category
<300	No Score
300-550	Very Low Credit Score
551-620	Low Credit Score
621-700	Fair Credit Score
701-749	Good Credit Score
750+	Excellent Credit Score

Figure 1: Credit score range [paisabazaar.com].

Your credit score is generated by businesses using a mathematical formula known as a scoring model and data from your credit report. Figure 1 shows credit score range [paisabazaar.com]

Credit scoring models often consider the following elements:

- Your payment history
- Your most recent debt is unpaid.
- The quantity and nature of your loan accounts
- How long have your loan accounts been active?
- How much of your credit is currently being used
- Fresh credit application filings

When was the last time you filed for bankruptcy, foreclosed on your home, or had a debt sent to collection? There isn't just "one" credit score for you. Each credit score is based on the information used to create it, and each score might be different depending on the scoring model (which may in turn rely on the kind of loan product the score will be used for), the data source, and even the day the score was created. A higher score often makes it simpler to qualify for a loan and might lead to better loan conditions or an interest rate. The typical range of credit scores is 300–850.

Knowledge about Credit Score

Let's quickly define a credit score before discussing how it affects the approval of personal loans. A credit score, which typically ranges from 300 to 850, is a numerical indicator of your creditworthiness. Your payment history, credit usage, length of credit history, credit mix, and fresh credit inquiries are among the many variables that go into its calculation. The better your credit score, the more likely it is that you will be granted a personal loan.

The significance of credit score in approving personal loans

1. Evaluation of creditworthiness:

Credit scores are a technique that lenders use to evaluate a borrower's creditworthiness. Lenders are more confident in your capacity to pay back loans when you have a better credit score since you are less likely to miss payments. You are more likely to get approved for a personal loan if you have a high credit score since it shows that you have been a responsible financial citizen.

2. Eligibility for Loans and Interest Rates:

Your loan eligibility and the interest rates you are given are directly impacted by your credit score. Borrowers with better credit scores are more likely to satisfy the particular credit score requirements that lenders normally demand. Additionally, since lenders see strong credit scores as less hazardous, they are more likely to secure better loan rates from borrowers. reduced monthly loan payments and possible savings throughout the loan term result from a reduced interest rate.

3. Term and Amount of Loan:

Credit ratings have an impact on a number of factors, including loan eligibility, interest rates, loan amounts, and payback durations. You can be eligible for a bigger loan amount with a better credit score, increasing your financial freedom. The affordability and all-around allure of the personal loan is increased by the fact that borrowers with high credit ratings may benefit from more advantageous repayment arrangements, such as longer tenures or cheaper processing costs.

DISCUSSION

Increasing Your Credit Score to Get a Personal Loan

There are things you may do to raise your credit score if it is not in an ideal range:

1. Paying off existing debts on schedule can help you build a good payment history. This includes utility bills, credit card payments, and loan EMIs.

2. **Maintain a Low Credit Utilization Ratio:** Try to just use a small fraction of your available credit and keep your credit card balances low. Your credit score may be impacted adversely by a high credit use ratio.
3. **Avoid Making Too Many Credit Applications:** Making too many credit applications in a short period of time will harm your credit score. Applying for credit should only be done when absolutely required, and only after careful investigation.
4. **Regularly check your credit report for inaccuracies or inconsistencies and take immediate action to correct them.** You may maintain awareness of your creditworthiness and, if necessary, take remedial action by monitoring your credit report.
5. **Build a Strong Credit History:** If you don't have much of one, you may want to start one by carefully using a credit card or by adding yourself as an authorized user on someone else's account. Creating a good credit history shows that you can manage credit responsibly.

Credit Score and Personal Loans

A personal loan is an unsecured loan, meaning you are not required to put up any security to secure the loan amount. Nowadays, personal loan interest rates are quite cheap, which makes them a great option for handling a variety of your financial demands. For the credit bureaus, the sort of loan doesn't really matter. The credit history, which is the most important element, can only become better as long as you return the personal loan on time.

Personal Loan's Effect on Other Credit Score Elements

In terms of your credit score, taking a personal loan is seen to be preferable than using your credit cards. This is due to the fact that applying for personal loans both online and offline contributes to lowering the credit utilization ratio, which is the second most significant consideration for credit bureaus.

Most of the time, personal loans have a beneficial impact on the other variables, including the length of credit history and the mix of credit. In other words, obtaining a personal loan may really help you raise your credit score on 90% of the variables considered by credit agencies.

Application for a Personal Loan and New Credit

The credit bureaus' least significant element is new credit. Your credit score decreases a little bit each time you apply for a new loan. This is the rationale for the advice to refrain from asking for loans from many lenders at once.

However, this decline is extremely little, only transitory, and won't have a long-term impact on your credit score or ability to get a personal loan. Once you start making on-time payments on the personal loan, this drop in the score is removed, giving you the chance to really raise it [7]–[9].

The Final Verdict

If you need money, don't hesitate to apply for a personal loan. You can rest easy knowing that as long as you borrow wisely and return the loan on time, it will only improve your credit score.

CONCLUSION

Recognizing the critical position played by credit history in bank lending applications highlights the relevance of prudent financial management and its long-lasting effects. A credit history functions as a financial resume, giving lenders information about a potential borrower's borrowing habits, repayment routines, and trustworthiness. When looking for financing from banks, having a solid credit history that is defined by on-time payments, little credit use, and a history of prudent borrowing may be quite advantageous. It proves your capacity to pay your bills on time and raises your chances of receiving favourable credit conditions like reduced interest rates and bigger credit limits. However, a bad credit history marked by missed payments, significant debt loads, or defaults may obstruct credit applications and restrict access to necessary financial resources. Poor credit history is seen as a greater risk by lenders, which may lead to higher interest rates or even loan refusal. Maintaining a good credit history is more important than ever in the digital era since data is easily available and quick credit evaluations are made possible by technology. To guarantee that their financial history is accurately reflected, borrowers must be diligent, constantly check their credit reports, and swiftly fix any inaccuracies.

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CHAPTER 11

BANK CREDIT FOR SMALL BUSINESSES: CHALLENGES AND OPPORTUNITIES

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ABSTRACT:

Small companies depend on bank credit as a vital source of funding for operations, expansion, and sustainability. The focus of this chapter is on the possibilities and difficulties that small firms face when applying for bank loans, emphasizing the importance of this connection in promoting entrepreneurial success. The chapter discusses the difficulties small firms often have while trying to get bank loans. Access to finance may be hampered by a lack of credit history, inadequate collateral, and the perceived risk associated with small businesses. The chapter also looks at how market volatility and economic uncertainty affect banks' propensity to lend to small firms. The chapter, however, also reveals the wide range of chances that bank lending offers to small firms. Entrepreneurs that have access to financing are better able to expand their businesses, finance innovation, and exploit expansion possibilities. It explains how credit acts as a driving force behind employment growth, economic expansion, and sector diversification.

KEYWORDS:

Banks, Credit Cycle, Economic Effects, Economy, Market, SME.

INTRODUCTION

Banks are discovering possibilities and problems in the market for lending to small and medium-sized companies (SMEs) as the economy enters the next credit cycle. Even while volumes are progressively increasing, the majority of banks are not operating at their full capability. Many still depend on older systems, employ antiquated business strategies, and even see SMEs as corporate entities. Banks are passing up chances by not providing for these companies' demands.

How banks might think differently about lending to small and medium-sized businesses

There isn't a single strategy that works for all banks and markets, but banks that rethink their SME-lending operations may boost market share and encourage profitable development. For the majority of banks, this begins with formulating a strategy and a distinct vision of their product offerings, which are then delivered to the target clients with a simplified, satisfying experience. Banks may make choices quickly and employ risk-adjusted pricing by using sophisticated analytics, procedures, and infrastructure that have been specifically designed for the purpose.

The correct technology, innovative working methods, and ongoing performance monitoring are the key components of the operating model banks need to succeed in this market—ingredients of tried-and-true recipes that have worked for banks in the past. The emphasis placed on certain levers depends on the particular circumstance [1]–[3].

New developments and possibilities in SME finance

The COVID-19 pandemic's economic effects have put a stop to the previous credit cycle and left enterprises all across the world in ruins. SME lending will be not only one of the most economically significant but also one of the most lucrative contributors to banks profits in this new credit cycle. The unmet financial requirements of the world's micro, small, and medium-sized organizations are estimated to be \$5.2 trillion annually, or almost 1.5 times the size of the present loan market for these companies, according to a World Bank analysis.

In spite of the prospects that lie ahead, banks often struggle to develop the ideal loan solutions for their SME clients and to lower the cost of providing them with services. These small and medium-sized companies should be seen as very affluent retail clients. The cost to service and related risk costs may be reduced by combining expert judgment with automated and scaleable data-driven methods.

In the post-pandemic economy, the following changes will affect how financial institutions may take advantage of SME lending opportunities:

The use of cutting-edge modeling methods and forward-looking data sources. To evaluate the risks associated with SME lending and improve the performance of credit models, more banks across the world are beginning to use transaction data, internet sales, or telecom data. Nowadays, technology makes a difference. With a modular approach to SME financing, banks are boosting their investments and integrating ICT platforms. The most prosperous of these banks identify their niche and incorporate these investments into their current infrastructure. Digital participation is required. Digital involvement in SME loans was previously considered to be only "nice to have." It is now necessary. Customers may be kept and brought in by increasing digital contact with them and decreasing the amount of manual approval procedures. Previously, the disruption in SME financing was driven by fintech and big-tech firms, but more banks now want to provide a range of services, such as processing invoices and payroll. As a result, the lending bank serves as a kind of network to assist SMEs in solving additional issues that may arise as they continue to expand.

The foundation of the new SME financing paradigm

Working with customers in the financial sector has led us to identify several repeating patterns that improve the chances of SME financing success. These banks develop distinctive strategies for successful development in this new environment using four main blocks: strategy, procedure, analytics, and operational model.

The bottom line may be greatly affected by using these levers to rethink SME financing. Increased margins and higher conversion rates may improve revenue by 10% to 15%. Gains of 20 to 30 percent in operational efficiency may be achieved by digitizing the customer experience and cutting down on contact times. Finally, banks may lower the risk of nonperforming loans (NPLs) by 10 to 25% by improving risk models and making judgments in a more consistent manner.

Since there isn't a one approach to credit-lending models, banks and lenders must decide what their goals and commercial objectives are and then build the lending process to meet those goals. Banks should take important factors from each of the four building blocks into account when determining the best transformation path for their missions and markets see sidebar, "Four building blocks to small and medium-size enterprise credit-lending transformation".

1. Strategy

Banks should think about a number of things as they search for a plan to suit their objectives, including target markets, SME pain areas, and the optimal ecosystem model. SME markets have unique local characteristics in many nations, but they also have similarities that make scaling up internationally simpler from a cost and go-to-market perspective.

For the bank to expand economically, securing the target customer group and value offer is a crucial component. Banks must take into account goals, segments, consumers, goods, geographies, processes, and channels in order to choose the best design alternatives for each dimension. They may employ the most efficient design alternatives by asking questions and establishing objectives in each dimension. The bank is thus able to develop a product and coverage model with the aid of a knowledge of the problems that the SMEs in the target segment encounter. At every stage, from launch and development to community engagement, these solutions should be specifically tailored to the pain areas of SMEs.

Choosing what role partners may play in the SME-lending model is another aspect of the approach. By forming the appropriate ecosystem alliances, banks may build proprietary methods of data access and a captive clientele via exclusive product offers. By more strategically focusing on subsegments, innovating, and approaching problems from a small business perspective, the partners may assist the banks in creating the greatest and most unique product offers. For instance, one European bank collaborated with an online shopping mall to provide flexible digital financing options to platform-based retailers. The bank used this to target the portion of small firms that were moving online.

2. Simplify the procedure

By enhancing the effectiveness of the SME lending process, banks may create more chances and complete more loans, from the end-to-end digitalization of the credit process to the development of clear segmentation guidelines. Banks must now more than ever rethink the SME client experience. Uncertainty and a long wait to get capital are the two problems that SME borrowers throughout the world report having the greatest trouble with. Processes may be greatly streamlined with automated financing. Banks may significantly improve the experience for SME customers by rethinking and digitizing a large piece of the customer journey [4]–[6].

Lending may be made more efficient by reevaluating outdated procedures and rules. Numerous of these regulations and procedures have grown organically through time and no longer satisfy the demands of today's SME clients. Banks should improve their swim lanes to expand automated processing and assessment where practical and to reserve manual expert review for complicated, high-value instances by explicitly segmenting rules by credit information, risk,

policy, and complexity. The finest rules and procedures allow banks to process more clients straight through and send just a carefully sized and chosen subset of applicants for manual checks.

The procedure is greatly made more efficient by redesigning the credit note and credit-decisioning process using uniform documents. A bank may automate data retrieval for decision-making using a digital signature and monitor changes for the next actor by establishing a single source of truth. The "time to yes" is typically reduced by 50% using this process (and significantly more in circumstances characterized by repeated information requests to customers, initiated by manual-review processes), which also improves the experience of relationship managers and ensures a complete audit trail. For instance, an emerging-market bank has revamped its procedures, bearing in mind the user experience, to provide preapproved loans to its small-business clients utilizing the bank's mobile app in minutes.

3. Analytics

Banks usually still employ a monolithic infrastructure to make decisions and seldom consider creating analytical models for usage across functional boundaries. They may realize the full potential of the existing data by employing analytics for other cross-functions, such as sales, marketing, and pricing, by adopting a modular strategy using historical and new data sources. Banks' ability to substantially improve the effectiveness of their credit models will depend on their ability to capture real-time credit information from transactions and sales. By creating a modular structure for SME credit models, banks are also given the ability to develop predictive models sequentially with growing data. The benefits of this contemporary design over conventional approaches are many. For instance, it enables banks to use information for each client's decision-making and to improve the current decision engine with growing data. These credit models may be used by banks for cross-selling possibilities as well as quick decisioning.

Additionally, by using dynamic, risk-adjusted pricing and limit setting, banks may rethink SME loan offering. SME financing relies on customized services that are tailored to specific client requirements; as a result, it needs an intelligent pricing engine to support relationship managers in anchoring discussions at an appropriate price range. A European bank, for instance, used a modular design for model architecture, reviewing and reevaluating the limit and price on a regular basis using forward-looking real-time data on merchants' customer feedback.

4. A working model

The correct operational model and enabling infrastructure must be chosen by banks in order to put things into action, even if strategy, procedure, and analytics may aid in the identification of new SME-lending prospects. The goal model must include innovative approaches to collaboration with a centralized credit authority and service operations in order to modify business models, boost regulatory readiness, boost efficacy, and boost efficiency. In addition, banks must base their IT architecture and technology choices, ranging from traditional to cutting-edge, and from niche to full-suite platforms, on their present loan book and scale-up objectives. A new front end may be constructed on top of the current core banking IT when redesigning the end-to-end process; this does not need a Greenfield IT strategy.

However, other participants have chosen a Greenfield cloud-native stack. Along the whole value chain of SME financing, banks are collaborating with fintech companies to rejuvenate their products and modernize their operations. Banks can increase capital efficiency, increase staff productivity by cutting down on time spent extracting and reporting data, and decrease the number of defaults by ensuring prompt action on things like model corrections and client performance, for example, by digitizing the performance monitoring of not only the portfolio but also of the core models, the relationship manager's workbench, and the entire business.

DISCUSSION

An entirely online SME lender

Take the example of a large European bank that had possibilities as well as problems in the lending industry due to shifting client demands, the fintech disruption, and other competitive pressures. The bank devised and constructed a totally unique pure digital player in only nine months to take advantage of the new potential. Rapid launch provided speed to market and eliminated rivals in the startup industry.

Instant decisions, money within 24 hours, and loans up to €250,000 in a purely digital format were all features of the fully digital SME lending bank. It earned a customer satisfaction rating of over 70 and had two times the segment's pace of customer growth. The digital bank was acknowledged as the most wanted bank for SME financing in the bank's home market, and 60% of the new clients came from rivals. The application procedure is entirely digital and takes just 15 minutes with this new seamless customer experience (see sidebar, "Example of a seamless customer experience for lending"). From there, the client may manage the whole loan online, just like a retail client, digitally sign the agreement, and get the money within 24 hours [7]–[9].

Next actions

There has never been a better opportunity for banks to expand their loan options than right now. To adopt new strategies that take a comprehensive approach to the market's commercial potential, departments may work together across silos, i.e., across the business, risk, IT, and other supporting areas. Banks should position themselves for effective transition and be prepared to take advantage of the increasing boom in SME lending by improving their strategies, procedures, analytics, and operational models.

Banks should immediately start the process of modernizing by investigating several facets of the existing company, particularly these:

- a. Currently existing issues with the bank's operations and the loan application procedure
- b. quantifiable measures of efficacy and efficiency, comparisons of the bank to its competitors, and its own goals
- c. Credit capacity and crucial deficiencies that banks should address
- d. The value that the transformation journey will provide in the short- and long-terms.
- e. a road plan that outlines the goal and the order in which the project should be implemented for the greatest possible advantages

Opportunities in Fintech for Small Business Lending

Fintech has the potential to revolutionize small company lending by making it more accessible, quick, and efficient. The following are a few of the most significant fintech options for small company lending: Online lending platforms developed by fintech businesses link SMEs with lenders and investors across the world. These platforms may provide quicker loan processing times, cheaper interest rates, and more flexible lending conditions than traditional banks.

- a. **other Data:** Using other data sources including social media profiles, online sales data, and mobile phone use, fintech organizations may assess the creditworthiness of SMEs who lack a credit history or financial statements.
- b. **Automation:** Fintech businesses may automate and employ machine learning algorithms to expedite the loan application and underwriting process, cutting down on the time and costs involved in processing loan applications.

Fintech websites also enable SMEs to raise money via crowdfunding. Crowdfunding makes it easier for small enterprises to get financing without depending on conventional bank loans by allowing them to raise modest quantities of money from a large number of investors.

The Challenges of Fintech in Small Business Lending

While there are many potential for small business loans provided by fintech, there are a number of issues that must be resolved before SMEs can fully profit from these new technologies. The following are some of the primary obstacles facing small company funding via fintech:

- a. **Regulation:** Compared to conventional banks, fintech businesses generally face less onerous regulatory standards, which may make it difficult for SMEs to evaluate the security and dependability of these platforms. Regulators must establish a framework that strikes a balance between innovation and client safety.
- b. **Many SMEs lack the financial understanding and know-how necessary to navigate the intricate world of fintech loans.** Fintech businesses must do more to enlighten SMEs about their credit options and assist them in making wise decisions.
- c. **Access to Technology:** It's possible that many SMEs, particularly those in developing nations, lack the technology required to utilize fintech lending platforms. No matter where they are located or how advanced their technology is, fintech companies must make sure that all SMEs can use their platforms.
- d. **Security and Privacy:** Cyberattacks and data breaches may endanger the security and privacy of financial data about SMEs using fintech lending platforms. Fintech companies need to make significant security investments and train SMEs on how to protect their data.

Is Microlending the answer?

The concept of banking and financial services has been altered by fintechs, or financial technology businesses. They have a unique opportunity to have a big influence on the microlending market for small enterprises. Fintechs have stepped in to fill the void left by the conventional banking industry's delayed response to the requirements of small companies and are reshaping the microlending industry. In the financial environment, micro-lending has grown in importance, especially for small enterprises that struggle to get standard bank loans. These

loans are often less than \$50,000 in size and are used to fund urgent necessities like payroll, inventory, or growth. Despite the fact that these loans might be a lifeline for small firms, they are often challenging to get from conventional lenders owing to their stringent lending requirements.

CONCLUSION

In conclusion, bank financing for small firms offers a dynamic environment characterized by both possibilities and problems. Small firms are essential for advancing economies since they are sources of innovation and economic progress. However, a number of obstacles that are brought on by their size, a scant financial history, and certain operational traits sometimes make it difficult for them to get bank credit. Challenges including strict eligibility rules, collateral restrictions, and high interest rates may make it difficult for small companies to get the money they need to grow. Additionally, the lengthy application procedures and administrative burdens may deter prospective borrowers, so widening the credit gap. Despite these difficulties, bank borrowing for small enterprises has significant potential advantages. Access to money may support growth, the production of new products, jobs, and enhanced competitiveness. Small firms may be prepared for long-term success by managing cash flow well, funding marketing campaigns, and making technological investments.

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CHAPTER 12

PERSONAL LOANS: USES, TYPES AND REPAYMENT

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ABSTRACT:

A concise explanation of personal loans, including their purposes, features, and methods of repayment is discussed in the chapter. Personal loans are unsecured financial instruments that provide people the freedom to borrow money for a variety of uses without putting up any kind of security. These loans are useful in a variety of situations, such as debt consolidation, unanticipated costs, home upgrades, schooling, weddings, trips, and large purchases. They may be classified as typical unsecured loans, secured loans supported by collateral, debt consolidation loans, personal lines of credit, peer-to-peer loans, cosigned loans, and payday loans, among other variations. Repayment strategies include regular monthly payments that cover the principle and interest, sometimes with variable interest rates based on the state of the market. One to seven years are the typical loan lengths, with prepayment and automatic withdrawal options. To properly manage personal finances and make educated borrowing choices, it is essential to comprehend these factors.

KEYWORDS:

Costs, Debt, Expenses, Finances, Money, Payday Loans, Personal Loan.

INTRODUCTION

You may borrow money from a personal loan to spend it for a range of things. For instance, you may utilize a personal loan to pay for home improvements, debt consolidation, or a fantasy wedding.

A personal loan is what?

Online lenders, credit unions, and banks may all provide personal loans. You must pay back the money you borrow over time, usually with interest. Fees for personal loans may also be assessed by certain lenders.

How Personal Loans Function

With a personal loan, you may take out a one-time lump amount of cash to cover a range of costs and then return the money over time in a series of repayments. You might, for instance, take a personal loan to pay for:

- a. Moving costs
- b. Consolidating debt
- c. Medical expenses
- d. Cost of the wedding

- e. Home repairs or renovations
- f. Funeral expenses
- g. Vacation expenses
- h. Unforeseen costs

Personal loans are distinct from other installment loans that are meant to pay for certain costs like schooling, cars, or houses, including student, automobile, and mortgage loans. A personal loan and a personal line of credit operate in distinct ways. A line of credit functions like a credit card rather than being a one-time payment. You may make purchases using a predetermined credit limit. Your available credit decreases as you make purchases. After that, you may raise your credit limit by paying down your credit line.

Bureau for Consumer Financial Protection. How Do Personal Lines of Credit Work?

A personal loan often has a predetermined deadline by which it must be repaid. Contrarily, if your account with your lender is still in good standing, your personal line of credit may continue to be open and accessible to you forever.

How Personal Loans Function

You must apply to a lender in order to get a personal loan. Once again, this might be a bank, credit union, or website that offers personal loans. Normally, you would fill out an application first. After reviewing it, the lender chooses whether to accept or reject it. You will be provided the loan conditions after being accepted, which you may accept or refuse. The next step is to complete your loan application if you accept them. Following completion of that, the lender will finance the loan, which entails giving you the money received. These can show up as a check or a direct transfer into your bank account, depending on the lender. You may put the money to any purpose when the loan is funded. Following that, you must start repaying the loan in accordance with the conditions outlined in the loan agreement [1]–[3].

A Personal Loan Example

Knowing the potential costs of a personal loan is useful when making a decision. An individual loan's annual percentage rate (APR), which is based on the interest rate and other fees, shows the yearly cost of repaying the loan. The overall amount of interest you pay over the course of the loan will depend on the APR and loan length. Take a \$10,000 personal loan, for instance, with a 7.5% APR. The loan has a 24-month payback period. With such conditions, your monthly payment would be \$450, and you would pay \$799.90 in interest over the course of the loan. Now imagine you take out a loan for the same amount but with different conditions. You have three years to pay back the loan instead of two years, and the interest rate is 6% rather than 7.5%. Your monthly payment would decrease to \$304 under such conditions, but your overall interest payments would rise to \$951.90. If you want to receive the smallest monthly payment or pay the least amount of interest on a personal loan, it's critical to compare the statistics this way. You may find out what sort of payment amount and interest rate are the greatest fits for your budget by using an easy online personal loan calculator.

Locating Personal Loans

Your present bank or credit union can be the first place to explore for personal loans. Your personal banker can provide you advice on the several personal loan choices that could be available as well as the ones that you stand the best chance of being approved for.

Also available online are personal loans. Online, a lot of lenders provide personal loans. Applying online allows you to get a decision quickly and, in certain situations, financing as soon as 24 to 48 hours following loan approval. Online or offline, pay great attention to the specifics while comparing personal loans. Take into account the following in particular:

- a. Rate of interest
- b. Fees
- c. Payment conditions
- d. Minimum and maximum loan amounts
- e. Conditions for collateral

It's also beneficial to look out the minimal standards for personal loan eligibility. When it comes to the credit score, income, and debt-to-income ratio that is acceptable to get authorized for a personal loan, lenders may have varied criteria. This might assist you in focusing on the loans that can match your credit and financial situation the best.

What Sets a Personal Loan Apart from a Cash Advance Loan?

A cash advance loan is a kind of loan that is intended to give money for a momentary need, usually an emergency. It often has a charge and a higher interest rate. Compared to cash advance loans, personal loans often offer longer periods and cheaper interest rates.

How Can I Obtain Personal Loan Approval?

The terms of each lender's loans vary, as do the prerequisites for acceptance. You may attempt to raise your credit score and financial status, in part by paying off debt, to boost your chances of securing a loan. If you're having trouble being accepted, you can think about acquiring a co-signer with strong credit to improve your chances.

Are There Fees for Personal Loans?

Costs, such as origination costs, that are added to the loan's overall cost may be included in a personal loan. Documentation costs and late fees are examples of additional charges. Make sure you comprehend the costs your lender charges. Each lender has various conditions for their fees.

The Final Verdict

Given the diversity of personal loans now on the market, finding one that meets your financial requirements is all but certain. But with so many alternatives available, it's simple to get confused, which might cause you to unintentionally lose out on the best interest rates and loan conditions you could be eligible for. This makes it essential to thoroughly investigate and evaluate various lenders and loan programs. You can keep your monthly payment low and lower your chance of default by taking the time to choose the right loan.

DISCUSSION

Personal Loan Types

You may get secured or unsecured personal loans. Any personal loan that includes a need for collateral is referred to as a secured loan. For instance, you may use a physical asset like your vehicle or boat to acquire a personal loan instead of monetary assets like a savings account or certificate of deposit (CD).

The lender might retain the collateral as payment for the debt if you are in default on the loan. With an unsecured personal loan, there is no need for collateral. Both secured and unsecured personal loans may be provided to qualifying consumers by banks, credit unions, and internet lenders.

Because there is no collateral to be collected, banks often see the latter as being riskier than the former. That can result in a personal loan with a higher interest rate.

Personal loan products available in India

Personal loans are unsecured loans whereby the bank lends you money based only on your creditworthiness and without the need for any kind of collateral. However, given the level of risk involved in giving the money, personal loans have higher interest rates than any other kind of loan, such as a house loan or an education loan. The majority of banks provide personal loans ranging from 50,000 to 15 lakh rupees [4]–[6].

Marriage Loan

In India, weddings are significant and expensive events. Most individuals want to make their wedding day unforgettable and will go to great lengths to do so. Banks provide wedding loans to assist you in making your special day unforgettable. The prospective bride, groom, or any member of the family may get a loan.

Key Points

- a. Loan amounts ranging from Rs. 1,000 to Rs. 25 lakhs.
- b. A loan payback period of three to seventy-two months.
- c. Little to no paperwork required.

Vacation Loan

Holiday loans, created exclusively for vacationers, let you see the globe while paying your debts afterwards. Travel insurance is often included as an extra advantage with holiday loans, giving you complete protection.

Key Points

- a. Quick and easy documentation procedure.
- b. A maximum loan of Rs. 40 lakhs.
- c. A flexible loan payback schedule that may be prolonged by up to 72 months.

Loan for Home Renovation

Home loans are used to purchase brand-new real estate. But what if you need to make urgent repairs to your old house? Due to the high expense of renovations, many people choose not to do so. Home improvement loans assist you in covering your repair expenses while also raising the economic worth of your home on the market.

Key Points

- a. A loan of between Rs. 2 lakh and Rs. 40 lakh
- b. Up to 30 years to pay back loans
- c. Interest rates as low as 6.85% per year.

Loan for Pension

Pension loans are only available to retired individuals, thus the standard qualifying requirements do not apply to this unique program. Some banks provide 7 to 10 times the pension the retiree received in the month before submitting the loan application as part of this program.

Key Points

- a. A loan amount ranging from Rs. 25,000 to Rs. 14 lakh
- b. A maximum 60-month payback period for loans
- c. Discounted interest rates as low as 11.70% per year.

Student Loan

Many financial institutions provide personal loans that may be utilized for educational purposes. You may utilize the education loan to cover costs ranging from your child's tuition to any other academic need.

Key Points

- a. A 15-year loan payback period.
- b. The interest rate is as low as 6.35% per year.
- c. Up to Rs. 20 lakh in loans.

Qualifications for Personal Loans

For those who get salaries:

- a. The applicant must be at least 21 years old.
- b. 60 years old maximum applicant age upon loan maturity
- c. Minimum Employment Period: 2 years overall, including 1 year at the current employer.
- d. Minimum Income: 7,500 to 15,000 rupees per month

For Professionals and Businessmen Who Are Self Employed:

- a. The applicant must be at least 25 years old.
- b. The applicant's age at loan maturity cannot exceed 65 years.
- c. Minimum company Period: Two to three years in the present industry or company
- d. Rs. 1 lakh Minimum Annual Income

Loan for debt consolidation

You get a debt consolidation loan from a lender to pay off any outstanding debts by merging all of your debt into one lump amount. Some borrowers would benefit from this since it might reduce their interest costs, make it simpler to keep track of their monthly payments, and help them pay off debt more quickly.

As one of the many different kinds of personal loans, debt consolidation loans are often unsecured and have set interest rates. There are advantages and disadvantages to debt consolidation, however. For people with poor credit, a debt consolidation loan may not be the greatest option since it might not be worthwhile to seek one if you can't get a reduced APR. Use a debt consolidation calculator to determine your potential savings to see whether this sort of financing is a suitable match for you.

Mortgage

A mortgage loan enables you to buy a house and create equity, and it's probably the biggest sum of money you'll ever borrow. There are several different mortgage lending programs, including conventional, FHA, and VA loans, all of which are based on your financial situation and history. Although there are certain loans with longer or shorter periods, the majority of mortgages have maturities of 15, 20, or 30 years. They may have variable or fixed interest rates. Mortgages are secured loans, so you'll use the house you buy as collateral while paying them back. As a result, you risk losing your house if you are unable to pay your mortgage.

Education loan

Those who want to pursue postsecondary education have the option of funding their studies using student loans. You may need to utilize a trustworthy relative, such as a parent, as a student loan cosigner when applying for a student loan since some young individuals who wish to continue their education haven't established much credit. These loans may be used to pay for costs including room and board, books, and tuition. They are normally unsecured. They may have variable or fixed interest rates. Private and government student loans are the two categories into which this form of debt may be divided. The former are created by private enterprises, as suggested by their titles, while the latter are supported by the federal government.

Car loan

Auto loans are a sort of financing that let you buy anything from a truck to an RV, whether it's new or old. Typically, the car you bought serves as collateral for auto loans. The length of car loans may vary from 12 to 84 months, with fixed rates. Some lenders provide unsecured automobile loans, however you'll need high to exceptional credit to qualify for them. Most auto loans are secured by the vehicle you're buying as collateral. Calculate your monthly payments using a car loan calculator to determine how much you can afford to borrow.

Loan to small company

Small company loans are a sort of financing that provide business owners access to money to boost their expanding enterprises. This might include borrowing borrowed money to pay for

wages, buy merchandise, or even equipment. Some lenders even provide SBA loans, which are up to \$5 million in size and are guaranteed by the Small Business Administration (SBA). Collateral is often required for business loans, but it's not the only consideration made by lenders.

When you're applying for a business loan, lenders will also look at your personal credit score, the length of time you've owned the firm, your cash flow, your debt-to-equity ratio, and your working capital.

Credit-building financing

Credit builder loans are a form of loan created expressly to assist people with poor or no credit to demonstrate to lenders that they are reliable borrowers. These loans function a little differently from standard loans and are often tiny, ranging from \$300 to \$1,000. The loan amount is kept in a secured bank account that you can only access once you pay off the loan, as opposed to being given as a lump sum of money or a valuable item up front.

Your loan serves as collateral in this manner. Building credit from start might take time, but for some borrowers, the prospect of recovering their loan cash after it is repaid may be a strong motivation. Although they are uncommon, credit builder loans may be found more easily at a smaller financial institution like a credit union.

Daily loan

Payday loans, which commonly range from \$100 to \$500, are seen as predatory forms of financing owing to their exorbitant interest rates (of up to 400%). Payday loans, which have two-to-four-week payback durations, may easily trap borrowers in a debt cycle since they force them to take out further loans to cover their initial payday debt.

Because payday loans sometimes don't need credit checks, they could appeal to customers with poor credit. If you're having difficulties being approved for a conventional loan, think about asking for a cosigner loan or a payday alternative loan through a credit union.

What to think about with various loans

It may be difficult to take on more debt, regardless of the kind of loan. Before putting your signature on the dotted line, there are many things you should think about since skipping over certain elements might end up costing you more money [6]–[8].

1. **Credit scores:** It's crucial to examine your credit scores and reports before applying for any form of loan. Your credit scores the two most popular ones being FICO Score and Vantage Score will determine which lenders you qualify for and what interest rates you may expect.
2. **Loan purpose:** Even if the loan you choose to get has a flexible lending purpose, you must still tell your lender how you intend to use the money since some lenders impose restrictions on how loans may be utilized. You may need to provide the item you want to buy with the loan if it has a defined purpose, such as a mortgage or vehicle loan.

3. **APRs:** These represent the total cost of a loan, including interest and other costs. You may get loans with lower APRs and pay less for them by having a high credit score and a solid credit history.
4. **Repayment terms:** The APR you pay depends on how long you have to pay back your loan. Although your monthly payments will be reduced, your APR may increase as your loan term lengthens. On the other hand, although your APRs will be lower the shorter your repayment period, your monthly payments would be greater.
5. **Borrowing Caps:** Your ability to borrow a certain amount will rely on a number of criteria, including your income, how you intend to utilize the loan, and your credit history. Remember that acquiring a significant loan amount may be difficult if you have poor credit.
6. **Secured vs unsecured loans:** This is a crucial difference to understand since it may affect both your APR and what happens if you fail on a loan. When comparing secured loans to unsecured loans, the former often offer lower APRs since the presence of collateral reduces the risk to lenders. However, unlike with an unsecured personal loan, your lender may take possession of your collateral if you fail on a secured personal loan.

CONCLUSION

In conclusion, personal loans are flexible financial tools that may be used to meet a variety of purposes. People might get cash from several lenders without providing any kind of security due to their unsecured nature. Their versatility is shown by the variety of uses, which include debt consolidation, home upgrades, crises, weddings, vacations, medical costs, and education. These loans come in a variety of forms, each catered to a particular need, including debt consolidation, home renovation, emergency, wedding, travel, medical, and school loans.

Prudent planning is required since repayment normally entails regular monthly payments over a certain term. Interest rates, fees, and terms must be taken into account since they are often impacted by credit ratings. Personal loans may be a great help, but to fully profit from them and avoid debt, cautious borrowing and careful consideration are still essential.

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CHAPTER 13

MORTGAGES AND HOME LOANS: UNDERSTANDING THE PROCESS

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ABSTRACT:

This chapter provides a succinct overview of the mortgage and home loan application procedure, highlighting its key elements. Home loans and mortgages are essential instruments that let people fund real estate transactions. There are various crucial steps in this procedure, starting with the application when borrowers provide their financial information and the loan amount they want. The borrower's creditworthiness, income, and property value are then evaluated by the lender to establish eligibility and interest rates. The loan's conditions, including its fixed or adjustable interest rate and payback period, are agreed upon. After approval, the lender pays the loan and the borrower contributes a down payment. The start of regular monthly payments that include principle, interest, taxes, and insurance. In the event of non-payment, the lender may foreclose and seize the property. Making educated judgments when applying for mortgages or house loans is crucial for having a solid financial foundation in real estate pursuits.

KEYWORDS:

Borrowing, Interest Rates, Loan Types, Monthly Payments, Mortgage, Transactions.

INTRODUCTION

The first sum of money the buyer gives toward the purchase of the property is known as the down payment. It is often stated as a percentage of the cost to buy the property. A larger down payment may result in a smaller loan balance, which may result in cheaper interest rates and monthly payments [1]–[3]. Closing expenses are something borrowers must take into account in addition to the down payment. These include costs related to the mortgage transaction, such as the loan origination charge, the appraisal fee, the cost of title insurance, the cost of hiring an attorney, and other costs. Normally, closing fees are paid at the time of closing.

The Basics of Mortgages: Interest Rates, Loan Types, and Terms Explanation

Mortgages, which provide people the chance to buy property by borrowing, are an essential component of real estate transactions. In order to make educated judgments, potential homebuyers must understand the principles of mortgages. Let's examine the essential steps in the mortgage application process:

Definition: A mortgage is a contract in which a borrower obtains a loan to pay for the acquisition of real estate from a lender (usually a bank or financial organization). The actual property is used as security for the loan. Over a certain time, often in monthly payments, the borrower repays the loan, including with interest.

Interest Rates: Mortgages are heavily influenced by interest rates. They are represented as a percentage of the loan amount and indicate the cost of borrowing money. It is possible for

interest rates to be either fixed, which means they stay the same for the duration of the loan, or adjustable, where they may sometimes alter depending on current market rates. Understanding how interest rates affect monthly payments and the total cost of the mortgage is crucial.

Loan kinds: Different mortgage loan kinds are offered to accommodate varied borrower profiles and financial circumstances. The most typical kind is a conventional mortgage, which is a conventional mortgage that is not insured or guaranteed by a government body. They usually ask for a down payment of between 3% and 20% of the property's price.

Loan Term: The period of time during which a mortgage must be repaid is referred to as the loan's term. The most typical durations are 15, 20, and 30 years. Shorter durations often have higher monthly payments but lower interest rates, resulting in a reduction in the amount of interest paid altogether. Lower monthly payments but greater total interest expenses are the outcome of longer periods.

Mortgage Insurance: Borrowers who put little or no money down on a loan must get mortgage insurance. In the event of a default, it offers the lender protection. The monthly payments made by the borrower include mortgage insurance costs.

Prospective homeowners will be better equipped to choose the best loan type, negotiate interest rates, and organize their finances if they are aware of these basic mortgage concepts. To fully assess individual financial situations and acquire a fuller grasp of the unique mortgage possibilities available, it is important to speak with mortgage experts or financial advisers.

Tips for Organizing Documents, Improving Credit, and Evaluating Your Financial Readiness

Assess Your Financial Readiness Before applying for a mortgage, it's important to determine your capacity to pay. Determine how much you can comfortably spend on housing costs by adding up your monthly income, expenditures, and debt payments.

Don't forget to factor in other expenses like property taxes, insurance, and upkeep.

Credit Score and History: Credit scores and credit histories are used by lenders to determine a borrower's creditworthiness. Obtain your credit report, check it for mistakes, and, if required, take action to raise your credit score. Your creditworthiness may be impacted favorably by timely bill payments, debt reduction, and a lack of new credit inquiries.

Debt-to-Income Ratio (DTI): DTI is an important consideration when applying for a mortgage. It contrasts your gross monthly revenue with your monthly debt payments. All things considered, lenders want a DTI below 43%, which includes the anticipated mortgage payment.

A Step-by-Step Guide to Applying for a Mortgage, Including the Needed Documents and Requirements

Research Lenders: Examine several lenders, evaluating their reputation, fees, interest rates, and consumer feedback. Think about collaborating with a mortgage broker that can assist in locating the finest lender and lending possibilities for your particular requirements.

Gather Required papers: Prepare the previously indicated required papers, making sure they are current and well-organized.

Complete the application by providing correct and detailed information. Be prepared to provide specific details on your work, income, possessions, and obligations.

Mortgage Underwriting: The lender will carry out a rigorous examination and verification procedure known as underwriting once you submit your application. They will examine your creditworthiness, confirm your details, and conduct an evaluation to determine the property's value.

Closing the Loan: After your application has been accepted, the loan will be closed. Here, you'll sign the loan paperwork, make any necessary closing-cost payments, and complete the ownership transfer. It is crucial to thoroughly read the materials and request clarification if necessary.

Investigating various mortgage products, including fixed-rate, adjustable-rate, and government-backed loans

1. **Mortgages with a fixed rate:** The most common and conventional sort of mortgage is a fixed-rate loan. As the name implies, the interest rate is set for the duration of the loan, giving borrowers the security of foreseeable monthly payments. For people who value stability and wish to successfully manage their money, this form of mortgage is perfect. Fixed-rate mortgages normally have maturities of 15 or 30 years, however the lender may provide different alternatives.
2. **ARMs, or adjustable-rate mortgages:** An ARM, or adjustable-rate mortgage, provides a variable interest rate that changes over time in response to market circumstances. ARMs normally begin with a fixed-rate introduction term, which typically lasts between three and ten years. Thereafter, the interest rate will regularly fluctuate. The intervals between adjustments may range, although they often last one, three, five, or seven years. The interest rate modifications are determined by reference to a benchmark index, such as the U.S. Treasury index plus a margin that the lender has decided upon. Borrowers who anticipate a rise in their income or who want to sell their house before the fixed-rate term is out might consider an ARM.
3. **Publicly-Backed Loans:** Mortgage programs that are insured or guaranteed by governmental organizations are known as government-backed loans. These loans are intended to make homeownership more accessible to those who would not be eligible for traditional mortgages because of poor credit or a lack of cash for a down payment [4]–[6].

DISCUSSION

Discussing the Mortgage Process's Final Steps, Including Loan Approval, Document Signing, and Funding

The next step is to submit an application for a loan after you have determined which sort of mortgage best meets your requirements. This entails giving the lender the required paperwork, such as proof of income, bank statements, and job history. The lender will go through your credit

report, examine your financial situation, and determine if you can afford the loan. You will be given a loan approval, indicating that you are qualified to go on with the mortgage procedure, if everything complies with the lender's standards.

You will start the document signing process when the loan has been approved. Usually, an attorney's office or a title business will host this. A stack of legal papers, including the promissory note, the mortgage or deed of trust, and several disclosures, will be handed to you. Before signing any paper, it is essential to thoroughly read it through and ask any questions you may have. You may sign the necessary paperwork to go on after you are confident in the terms and happy with them.

Funding the loan comes next once all the relevant documentation has been signed. When it comes time to release the loan cash, the lender will collaborate with the title firm or the lawyer. This include checking the title, going through the loan paperwork, and organizing the money transfer. In order to purchase the property, the money is normally transferred straight to the seller or the seller's lender. The whole procedure could take a few days, but as soon as the money is properly transferred, you are regarded as the rightful owner of the property.

It is essential to keep in mind that the mortgage application procedure might change based on the lender, region, and unique circumstances. Working with a trustworthy mortgage expert can assist you through the procedure and guarantee a seamless transaction.

How the Mortgage Process Works

Obtaining a mortgage may be a difficult, complicated process. There are many different types of mortgages to choose from, you'll need to compile a lot of paperwork to apply for them, and even figuring out how much your future mortgage will cost each month might be challenging.

However, the mortgage application process may be divided into a number of distinct parts. When searching for a new mortgage, most consumers go through six separate stages: pre-approval, home browsing, mortgage application, loan processing, underwriting, and closing.

Get Pre-Approved.

Finding the best mortgage for you, figuring out how much you can afford to pay, and receiving pre-approval for the loan are the first stages in acquiring a mortgage. Learn about the many mortgage kinds and choose the one that is best for you to discover the mortgage that is suitable for you.

When picking a mortgage, there are a lot of things to consider, but the most crucial is to have a clear understanding of your monthly expenses. This will include making interest payments in addition to the "principal" loan repayment. Additionally, you'll have to pay for private mortgage insurance if you can't put 20% down on a home. You may see the effect of various rates on your monthly payment with a mortgage calculator. You may contact mortgage lenders for pre-approval as soon as you have a general notion of the sort of mortgage you would want. A pre-approval is a written statement of how much money your mortgage lender is prepared to offer you in total. You may get pre-approval very fast; all your mortgage lender has to do is run a tri-

merge, or three-bureau, credit report that displays your credit score and credit history as reported by independent credit agencies. When searching for a home, a pre-approval is helpful. It shows that you are a serious buyer and that you are prepared to act promptly when you locate a home that you like.

Locate a property

The majority of individuals begin looking at houses far before they have received pre-approval for a mortgage and, in some cases, even before they are considering purchasing a home. However, if you have followed the above processes and have received your pre-approval, you are now prepared to start searching seriously. There are several methods for achieving this. You may seek for a property off the market, purchase a home at auction, or utilize internet real estate search engines like Zillow or Trulia. Just be careful not to make some of the typical errors individuals make while looking for a home.

Offering a price

You must make an offer on a suitable home after you've discovered one. Because various sellers and properties demand different kinds of offers, your real estate agent should assist you in doing this. You will often need to make an earnest money deposit at this point to show that you are really interested in the home. Deposits for earnest money usually range from 1% to 2% of the selling price. This cash goes toward the down payment if you close on a house. In most cases, your offer will also include conditions that would let you back out of the agreement. In the event that the home you've picked is not exactly what it appears, they are intended to safeguard both you and your money. Typical scenarios consist of:

1. Appraisals must be close to the loan amount but not less than that
2. Major faults with the property are not discovered through home inspections
3. You may get final mortgage approval.

Obtain a Mortgage

You are now prepared to submit a final mortgage application. You must contact a mortgage lender in order to accomplish this; ideally, it should be the one that granted you pre-approval, but you should also shop around to ensure you receive the best offer. For each mortgage lender to make you an offer, they will require information. They could already have some of this information, but they might also need to get additional. However, you'll also need to provide your lender with a stack of paperwork. Some of the more challenging issues, such property taxes, could be able to be retrieved by your real estate agent.

Your lender should provide guidance as to what and when to submit, although they will probably require:

Employment

1. A current employer's name, contact information, and street address
2. Duration with present employment
3. Role or title
4. Salary that includes commissions, bonuses, or overtime

Income

- a. W-2s for two years
- b. If self-employed, a profit and loss statement
- c. Social Security; pensions

Assistance to the public

- 1. Child assistance
- 2. Alimony

Assets

- a. Financial instruments such as savings, checking, and brokerage accounts.
- b. Real estate

Stocks, bonds, and retirement accounts are examples of investments.

- a. The selling of your present home's proceeds
- b. Donations from family members, such as a present for the down payment on an FHA loan

Debts

- a. Existing mortgage
- b. Liens

Alimony

- a. Child assistance
- b. Auto loan
- c. Cards credit
- d. Real estate

Property details

Address in the street

- a. Estimated selling price
- b. The kind of housing (condo, single-family house, etc.).
- c. Property size
- d. Annual real estate taxes
- e. Homeowners' association (HOA) dues
- f. Projected deadline

credit report

- a. Insolvencies
- b. Compilations
- c. Bankruptcies
- d. Infractions

Your credit history is the last piece and one of the most crucial factors in having your mortgage authorized. It's a good idea to check your credit report in advance to discover where you stand because of this. Each of the three major reporting agencies is required by law to provide you with one free credit report every year. Be prepared to discuss any financial mistakes in your past. Any of these details about your past should include dates, quantities, and reasons.

Processing of Loan in full

The lenders you've contacted will compile all the data you've given into a loan estimate as the following step. A loan estimate is a three-page document that provides clear explanations and information about house loans. In addition to making the information simple to understand, this standardization makes it simple to compare offers from different lenders and determine which one is giving you the best bargain.

Unless you don't satisfy the lender's minimal requirements and your application is turned down, you'll get a loan estimate within three business days of submitting your mortgage application. If that occurs, the lender is required to inform you in writing within 30 days of the reason your application was turned down. You may simply need to pay a credit report cost to get a loan estimate.

A loan estimate that you obtain is good for 10 business days. Try to accept a loan offer within that time limit; if you wait longer to decide, the lender could adjust the conditions and provide a new loan estimate. The processing of your loan will begin when you receive a loan estimate. The information you've given your mortgage lender will now begin to be reviewed and verified. This comprises:

- a. Requesting a credit report, if one has not previously been requested as part of your pre-approval.
- b. Verifying bank deposits (VOD) and employment (VOE)
- c. Request a property evaluation and inspection.
- d. Request a title check.

Follow the underwriting procedure

The next step is for underwriters to evaluate your application.

Mortgage underwriters are the essential decision-makers in the mortgage approval process and the ones who will ultimately approve your mortgage, even though you are unlikely to engage with them personally. Your mortgage application will be thoroughly examined by underwriters, who will also take a variety of additional actions. For instance, before taking out a mortgage on a piece of property, borrowers must have it appraised. This evaluation is requested by the underwriter, who utilizes it to assess whether the proceeds from the property's sale will be sufficient to pay back the mortgage.

The decision of the underwriters will be communicated to you once they have reviewed your application. This will entail one of three options: accepting the loan as offered, rejecting it, or approving it with restrictions.

For instance, your mortgage could be granted subject to you providing further details regarding your credit history. You will lock in your interest rate with your lender if your application is accepted. For the balance of the mortgage term, this is the last interest rate you will pay.

Getting Near the Property

If your mortgage application is accepted, the closing may now take place. At this point, a large stack of paperwork will be printed off, and you'll be asked to attend a closing meeting at the title company's (or attorney's) offices. Your closing disclosure form is among the most significant papers you'll see at this conference. You may examine the initial projected closing expenses, the actual closing costs, and the difference if costs increased in two columns on this form.

Typically, closing fees make up 2% to 5% of the cost of the house. Therefore, your closing expenses for a \$200,000 home might be between \$4,000 and \$10,000. It's vital to pay particular attention to these costs since closing costs vary based on your state, the kind of loan, and the mortgage lender. Ask your lender and/or real estate agent for further information right away if you detect additional expenditures that weren't included in the first loan estimate or discover that your closing costs are much higher. You will sign to accept the mortgage and leave the office with the keys to your new house if everything seems to be in order. Good work!

A three-day review window and a final inspection

A countdown starts at this moment. Your mortgage will become active in three days if no further action is taken. However, you are entitled to three days to check your paperwork at this point to make sure everything is in order. The loan estimate you got in step 4 above should be compared to your closing disclosure. Small alterations, errors, or typos are OK, but you should ask for explanation right away if you notice anything you don't understand. Additionally, there are several modifications that may result in the suspension of your mortgage agreement. If the following occurs:

- a. The APR on the loan fluctuates by more than a quarter of a percent (for most adjustable rate loans) or an eighth of a percent (for most fixed rate loans).
- b. The mortgage will be increased with a prepayment penalty.
- c. Loan products are changed (for instance, from a fixed-rate loan to an adjustable-rate loan).

Your mortgage will automatically go live after the three days, if everything is in order. Most mortgage agreements provide you the right to a last home inspection at least 24 hours before your closing. During this visit, you may verify that the prior occupant has left the property and that any necessary repairs have been made.

Who grants mortgage approval?

Although you will often work with a mortgage lender, such a bank, underwriters ultimately decide whether to approve your mortgage.

When Does a House Closing Take Place?

A home's closing typically takes 30 to 45 days, depending on a few things including how quickly you can obtain a home inspection and if you have been pre-approved for a financing.

What Are Closing Costs When Purchasing a Home?

Closing expenses include a variety of fees, such as appraisal charges and the cost of hiring a lawyer to draft your contract. These fees are normally paid at the closing and may amount to 2% to 5% of the home's purchase price.

The inference

Although applying for a mortgage might be challenging, there are certain clear processes that must be followed. Pre-approval, property hunting, mortgage application, loan processing, underwriting, and closing are the six phases that the majority of consumers will do.

Be careful not to hurry the procedure, since it may be drawn out and unpleasant. Check all of your paperwork thoroughly, make sure you comprehend the mortgage you are being offered, and ask a professional for advice if you have any questions. It makes sense to get your mortgage properly since you will be paying it for a very long time [7]–[9].

CONCLUSION

To sum up, understanding the world of mortgages and house loans exposes a methodical but complex procedure. These financial tools enable people to become homeowners, but it's crucial to understand their subtleties. Mortgage alternatives, such fixed-rate and adjustable-rate mortgages, accommodate a range of preferences and each has its own advantages and limitations. Loan prequalification, home searching, official loan application, property assessment, underwriting, and closing are all parts of the complicated process. The total affordability is influenced by striking a balance between a reasonable interest rate, a down payment, and the loan duration. Collaboration is a key component of obtaining a house loan, as seen by the cooperation between borrowers, lenders, real estate brokers, and corporate bodies. Successful homeownership via mortgages and house loans is made possible by in-depth knowledge, wise financial planning, and careful research.

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CHAPTER 14

AUTO LOANS: FINANCING YOUR VEHICLE PURCHASE

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ABSTRACT:

An overview of car loans and their function in financing vehicle purchases is given in this chapter. Auto loans are contractual agreements that enable people to buy cars by distributing the expense over time. Borrowers provide their financial information and the desired loan amount when applying for a loan, which starts the procedure. For the purpose of determining eligibility and interest rates, lenders consider creditworthiness, income, and the value of the car. Loan conditions are defined, including interest rate type (fixed or variable) and payback period. Following approval, the lender releases the loan and the borrower often pays a down payment. Until the loan is paid off, monthly installments that include both principal and interest are made. Vehicles may be seized if you don't comply. People who have a thorough grasp of this procedure may make well-informed choices, effectively negotiate auto loans, and successfully purchase the cars they want.

KEYWORDS:

Auto Loans, Borrowers, CIBIL Score, Income, Interest Rates, Vehicle Loan.

INTRODUCTION

When calculating the affordability and total cost of the loan, factors such as interest rates, loan periods, down payments, and credit ratings are all very important. To get the best deals, careful analysis and comparison are crucial.

An auto loan is what? What varieties are there?

Borrowers take out auto loans to buy new, old, or both types of business or personal vehicles. Automobiles themselves are used as collateral for secured loans like auto loans. For new automobiles, secondhand cars, two-wheelers (usually referred to as a two-wheeler loan), and commercial vehicles (typically referred to as a commercial vehicle loan), lenders provide it.

How does the borrowing and payback appear?

Banks often provide auto loans up to 90% of the cost of new cars and 85% of the cost of used cars. The car is pledged as security to the lender. The payback period normally lasts between 12 and 84 months and is depending on your monthly income and capacity to repay [1]–[3].

What kind of interest rates are typical?

Depending on the kind of car and loan amount, lenders set interest rates. For vehicle loans, interest rates are often fixed.

What do lenders consider when making a car loan decision?

When opposed to residential loans, the loan approval procedure for a vehicle loan is comparatively simpler. However, before accepting your loan application, lenders will consider a few fundamental factors.

- a. **CIBIL Score and Report:** Just as with all other loans, lenders consider both the state of your credit at the moment and the consistency of your prior payment history. Before making a final decision on your loan application, lenders consider your CIBIL Score and credit background. To check your CIBIL Score and Report for free right now! A higher CIBIL Score enhances the likelihood that your loan application will be approved.
- b. **Employment and Income Status:** To assure loan payback throughout the course of the loan, lenders also verify that you have a stable job and a consistent source of monthly income.
- c. **Current Loan Repayments:** Before deciding whether to approve your loan request, lenders also keep track of all of your past EMIs. They typically calculate your monthly income ratio and EMI outflow. Make sure that your EMI payments do not represent a significant portion of your income.

What paperwork is needed to apply for a car loan?

Each lender has different requirements for the real documents. However, identity proof, address proof, proof of salary, and bank statements are the fundamental documentation that lenders want.

What additional expenses, fees, or levies must user pay?

You must consider other expenses in addition to the vehicle's purchase price, such as taxes, registration fees, insurance costs, processing fees, paperwork costs, stamp duty, etc. When applying for a loan, it is usually important to examine all the fees and charges in advance.

What to be wary of?

You don't necessarily have to choose the bank your car dealer recommends; if another lender has better loan conditions, you may always choose them. Therefore, before choosing a loan, always do in-depth research by comparing lenders and their rates.

Auto Loans: How to Pay for Your Vehicle

Some of us must purchase a vehicle as part of our daily work obligations, while others see owning a car as a sign of success among our peers and something to aspire to.

Few of us contemplate buying a vehicle out of our own funds, and getting a car loan is the most popular alternative when buying a car. This article will cover the expenses of a vehicle loan, how to use mutual funds to save for a car, and our opinion on which option is preferable so that you can make an educated decision.

Vehicle Loan: Definition

You may get a loan to buy two- and four-wheeled vehicles for personal usage. In most cases, the lender lends the money (paying the dealer directly on the buyer's behalf), and the borrower is

required to return the loan in Equated Monthly Instalments (EMIs) over a certain duration at a predetermined interest rate. A part of the original sum and an interest component are included in the EMI. The lender transfers the vehicle's registration into your name after you have paid off the loan in full.

To purchase these cars to move products or employees for your business, you may also apply for a vehicle loan. Commercial vehicles often come in the form of buses, trucks, tractors, tippers, cabs, etc.

Your credit rating and net (in hand) monthly income determine whether you are eligible for a vehicle loan. Depending on the kind and cost of the car, the majority of lenders give 75% to 100% of the on-road pricing. Additionally, loans are available for the purchase of previously owned automobiles and other used vehicles.

DISCUSSION

Vehicle Loan Types in India

In India nowadays, you may get a car loan to purchase a variety of automobiles. The most popular vehicle loan kinds that Indian lenders provide are shown below.

Auto Loans

To buy a brand-new automobile of your choice, you may get a car loan. Typically, lenders will finance up to 90% of the on-road price of the automobile, with the remaining 10% required as a down payment. The ex-showroom price of a new automobile is included in the on-road pricing, along with registration fees paid to the Regional Transport Office (RTO), insurance premiums, road tax, etc. Typically, a car loan has a seven-year payback period. Over the selected period, the Car Loans may be repaid in manageable EMIs.

Loans for two-wheelers

A two-wheeler is a great vehicle for navigating traffic, particularly in a city with plenty of people. It is fuel-efficient, small, and enables comfortable short-distance travel. You may purchase geared motorcycles and non-geared scooters with Two-Wheeler Loans. Most lenders provide Two-Wheeler Loans with up to 100% financing and a five-year maximum payback period. Such loans may be financed up to a limit of Rs 10 lakh. Once again, in order to be accepted for this loan, you must present documentation of your income and creditworthiness [4]–[6].

Credit for used vehicles

An additional option for a vehicle loan is a loan for previously owned vehicles. An affordable alternative for purchasing a brand-new automobile is to acquire a pre-owned one. Lenders often provide pre-owned automobile loans up to 75%. Until the loan's payback time is through and all EMIs have been paid, the automobile is hypothecated with the lender. The new payback time and the age of the automobile, however, should not both be more than eight years.

Why Decide Upon a Car Loan?

Flexible Option: One may choose the loan payback period, which may be between one and seven years long. Flexible payment options enable the financing of supplemental expenses including on-road fees, insurance, and roadside assistance. **Secure:** You may benefit from the security of a fixed interest rate for the duration of the auto loan. Use an efficient car loan calculator to determine your monthly payments.

What Qualifies As A Vehicle Loan?

Some of the key characteristics of a vehicle loan are the ones listed below.

- a. **Financing of high value:** Lenders often provide auto loans ranging from 75% to 100%. As a result, you need not be concerned about making large down payments.
- b. **Affordable interest rates:** Vehicle loans are secured loans, meaning that until the entire amount of the loan is repaid, the vehicle you acquired acts as collateral with the lender. Lenders often charge a lower interest rate on these loans because of their secured status.
- c. **Quick disbursements:** You may buy and register your car right away since lenders often provide the money to the car dealer promptly.
- d. **Flexible terms for repayment:** Depending on the sort of vehicle loan you want, the repayment period might be anything between a year and 84 months. The payback time for two-wheeler loans and commercial vehicle financing is five years, while the repayment period for a new car loan is seven years.
- e. **The qualifications:** If you have a solid credit score of more than 750 points and can demonstrate the required minimum net monthly income (across the related Vehicle Loan), you are eligible to apply for the loan.
- f. **Prepayment and loan processing:** Vehicle loans are subject to small loan processing fees from lenders. Additionally, you may pay off your loan early without incurring any penalties.
- g. **No-problem documentation:** The majority of lenders let you apply for a vehicle loan online without submitting any physical paperwork. Only scanned copies of your identification, residence, and income verification papers are required.
- h. **Loans for new vs used vehicles:** Using the financing feature, you may pick between purchasing a new or used automobile. How the two loans vary is as follows.
 - i. **Costs of maintenance and affordability:** Used automobiles are sometimes far more economical and are perfect for those who have just started learning to drive. Depending on the used car's age, it can sometimes need routine maintenance, which might result in extra charges. On the surface, a new automobile may seem pricey. However, it normally functions without further maintenance expenses for years.
 - j. **Period of repayment:** A new car loan has a longer payback period than a pre-owned car loan. A new car loan has an 84-month repayment period. Pre-owned car loans have a maximum term of 60 months, nevertheless.

- k. **Guarantee:** A complimentary manufacturer warranty is provided with all new autos. The automaker guarantees that throughout the warranty term, no extra fees will be charged to fix the automobile or replace some of its mechanical or electrical components. Typically, this guarantee is valid for two to three years or up to a specified amount of miles. The manufacturer's warranty could have expired by the time the automobile is placed up for sale. The majority of used automobiles lack a factory warranty. You may be able to get a warranty on a used automobile depending on how old it is, but there are extra costs.
- l. **Insurance deductibles:** According to the Motor Vehicle Act of 1988, you must have automobile insurance whether you own a new or used car. The maximum amount you may get when filing an insurance claim is greater for new automobiles since they have a higher Insured Declared Value. Insurance costs for new automobiles are greater than for older cars because of a higher IDV. For used autos, insurers often give a reduced IDV.
- m. **Funding:** Most lenders will lend up to 90% of the sticker price of a new automobile, significantly lowering your down payment. You may get up to 75% financing for a used automobile.

Age of the car

To be accepted for purchase, used automobiles must meet a number of requirements, one of which is their age. The used car's age should not exceed 96 months when counting the time from the car's invoice date together with the payback term. New autos are not subject to this requirement [7]–[9].

Car Loan Advantages

Both new and secondhand cars are eligible for auto loans. A vehicle loan has a number of advantages:

- a. **You don't need to utilize your money:** Previously, automobile owners had to use their savings to finance their vehicles. You no longer have to do that, which is one advantage of auto loans. By taking out a loan, people are still able to purchase a vehicle while keeping their money intact.
- b. **Flexibility in choosing the term:** Secured car loans often have a set tenure, and the borrower has little control over how long the loan will last. A personal loan taken out to finance an automobile allows the borrower the freedom to choose the term, unlike secured vehicle loans. The term of a vehicle loan from Finnable begins at six months, while borrowers have the option of a lengthier term of up to five years.
- c. **Better spending plan:** The price of a car relies on two things: its kind and whether it is new or old. Therefore, you may continue to apply for a car loan in accordance with your needs and your preference for the vehicle that you choose.
- d. **Low down payment necessary:** One unstated advantage of a personal loan, such as a car loan, is that the borrower is not needed to make a down payment on the vehicle. This is true because personal loans do not need security or collateral. This is how auto loans may cover the whole cost of a vehicle.

- e. **Instantaneous loan disbursement:** A loan is only useful when it is disbursed at the appropriate moment. A auto loan application may be submitted online, and the money is released right away. The monies do not need to be credited into borrowers' accounts over a period of days. Finable disburses money for auto loans within six hours after receiving paperwork clearance.
- f. **A variety of repayment alternatives are available:** Car loans provide various payback choices. Using a car loan EMI calculator and the duration of your choice, you may pick the EMI that best suits your needs.

What variables impact monthly payments?

The automobile loan is repaid by the borrower in EMIs, or equal monthly payments. To determine the amount to be paid as EMI, customers can utilize a car loan EMI calculator when applying for an online auto loan. Before doing so, it's crucial to be aware of the variables that might alter this sum:

- a. **Loan principle:** One of the key elements that affects EMI calculation is the principal balance of a vehicle loan. The amount of the EMI will increase in direct proportion to the amount you borrow.
- b. **Interest rate:** The lender determines the interest rate for auto loans. It represents a certain proportion of the principle sum. The amount of interest rises in direct proportion to the interest rate. However, applicants might get the best auto loan at a cheaper interest rate if they have a decent credit score.
- c. **Loan duration:** A vehicle loan may have a short or lengthy period. The monthly payment may be determined based on the loan's term. You may choose the duration according on your financial circumstances. The loan's term has an impact on the EMI payment each month.
- g. **Income level:** One of Finnable's eligibility requirements is that the borrower must have a monthly income of at least Rs. 20,000. A higher salary may enable you to get a larger auto loan.

Criteria for Car Loan Eligibility

Paid Workers:

- a. Employees of private limited companies and those working for municipal, national, and state governments are included in this.
- b. Applicants must be at least 21 years old at the time of application and cannot be more than 60 at the conclusion of the loan term.
- c. People who have worked for at least 2 years, at least 1 year of which has been with their present company.
- d. Individuals who make at least INR 3,00,000 annually, including the income of their spouse or co-applicant.
- e. People have a phone or post-paid mobile.

Employed independently as a solo proprietor:

- a. This includes independent contractors who run their own manufacturing, trading, or service firms.
- b. Applicants must be at least 21 years old at the time of application and cannot be older than 65 at the conclusion of the loan term.
- c. Those who have been in operation for at least two years.
- d. Must make at least INR 3,00,000 annually.

Under partnership businesses, self-employed:**Partnerships in self-employed manufacturing, trading, and service businesses are included in this.**

Those with a minimum annual turnover of INR3,00,000.

Private limited companies with self-employment:

- a. This includes those who own private businesses in the manufacturing, trading, and service zones.
- b. You should earn at least INR 3,00,000 annually.

Individuals who work for themselves via public limited companies:

- a. Directors of public limited companies engaged in manufacturing, commerce, or services are included in this.
- b. You should earn at least INR3,00,000 annually.

CONCLUSION

In conclusion, the world of car loans provides a flexible route for people to achieve their desire for a vehicle. By dividing the expense of buying a vehicle into manageable payments, auto loans have emerged as a crucial tool for helping consumers to buy automobiles, whether they are new or used. The many car loan options, including conventional bank loans, financing from dealerships, and loans from internet lenders, provide you the freedom to choose the finest solution.

Preapproval, choosing a car, settling on terms, and filing documentation are all steps in the process of getting an auto loan. Additionally, the vehicle loan sector has seen developments like refinancing and leasing, which provide people the chance to modify their financial obligations as circumstances change. The application and approval procedures have also been simplified by technology, which is more convenient for borrowers.

Although auto loans make it possible to acquire a car, prudent money management is crucial. The borrower should evaluate their spending plans, account for supplemental expenses like insurance and maintenance, and make sure the loan is comfortably within their means of subsistence. Negative effects of defaulting on a car loan include lowered credit ratings and the risk for vehicle repossession.

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CHAPTER 15

ROLE OF CREDIT BUREAUS IN BANK CREDIT DECISIONS

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ABSTRACT:

The essential role credit bureaus play in influencing bank credit decisions is succinctly summarized in this chapter. Credit bureaus store credit information on people by accumulating their financial histories, borrowing habits, and payment histories. This information is used by banks to evaluate the creditworthiness of loan applicants. Lenders assess the risk involved in extending credit via credit reports and scores, setting interest rates and loan conditions. Creditworthiness of a borrower has an impact on both loan approval and loan amount. Banks and credit bureaus work in harmony to reduce risk, ease informed lending choices, and promote responsible borrowing. Understanding this relationship is essential for lenders trying to successfully manage risk as well as for borrowers looking for advantageous lending conditions.

KEYWORDS:

Banks, Borrowing Habits, Credit Bureaus, Loan, Payment Histories, Risk.

INTRODUCTION

Now-a-days, getting a loan in India is not as difficult as it once was. Bank loans are now scrutinized if you get one. This covers how many loans you get, how much you borrow, what kind of loan it is, and when you repay the loan. Your credit behavior is ascertained by the analysis of all these data points. Your ability to get loans in the future is determined by your credit behavior. The Indian credit bureau oversees all of this. They were set up to monitor and examine Indian financial activities [1]–[3].

We will learn more about Indian credit bureaus, including who they are, what they do, and how many of them are presently in operation.

A Credit Bureau: What Is It?

An organization that gathers and analyzes consumer credit data and sells it to lenders for a charge so they can decide whether to extend credit or make loans is known as a credit bureau, also known as a credit reporting agency in the United States.

Workings of Credit Bureaus

Credit bureaus collaborate with a variety of lenders and credit issuers to assist in loan decision-making. Their main objective is to make sure that lenders get the data they need to make loan choices. Banks, mortgage lenders, credit card businesses, and other personal financial lending firms are typical customers for credit bureaus.

Credit bureaus just gather and synthesize information about a person's credit score and provide it to lending organizations; they are not in charge of selecting whether or not to grant credit to an individual. Customers of credit agencies might also be consumers, and they get the same service—details on their credit history.

Credit Ratings

Data suppliers, such as creditors, debtors, debt collection agencies, vendors, or entities with public records (court records, for instance, are publicly accessible), are where credit bureaus get their information from. The majority of credit bureaus concentrate on credit accounts, but others also access more thorough data, such as payment histories for telephone bills, electricity bills, rent, and other expenses.

Based on this credit history, credit bureaus then use a variety of algorithms to determine a person's credit score. The most popular credit ratings in the United States are FICO scores, which were developed by the Fair Isaac Corporation in 1989. Credit issuers may choose the sort of credit score that best suits their inquiries from the 19 regularly used FICO scores since each one is generated differently with an eye toward various client categories.

Credit issuers may use a full credit report, which is produced by credit bureaus after they've added the credit score to the data they've gathered, to assist them decide whether to provide credit and what interest rates to charge borrowers. A borrower with a better credit score will probably get a loan at a cheaper interest rate.

Although the VantageScore formerly utilized a 501 to 990 range and certain industry-specific FICO scores are assessed on a 250 to 900 scale, both scores are generated on a range from 300 to 850. FICO and VantageScore's ratings, however, are often different because of how differently they value each category.

For instance, a good FICO score is seen as falling between 670 and 719, whereas a good VantageScore falls between 661 and 780. Regarding the scores, the sources also make a significant influence. FICO, on the other hand, only takes data from one bureau, but VantageScores creates a single score that can be used with a credit report from each of the bureaus based on information from all three agencies. As a result, you may, for instance, have three separate FICO scores, one for each of the three credit agencies.

An overall credit score that is determined by the credit bureau will also be included in a credit report. The value that sums up a person's creditworthiness is a single number. The most popular credit ratings in the US are referred to as FICO scores.

There are several methods used by credit bureaus to determine each person's credit score since there is no one technique to compute credit ratings. The credit bureau will, however, publish the procedures and weights used to determine their credit score. A credit score is a number that represents a person's creditworthiness and varies from 300 to 850.

A person with a score of 850 has extremely high creditworthiness, whereas someone with a score of 300 has very low creditworthiness. Credit scores are crucial data that lenders use when deciding whether to lend money. The following elements contribute to the overall credit score: total debt, repayment history, and the number of open accounts.

Regulation of Credit Bureaus

The information in credit bureaus' reports may significantly affect a person's financial future even if they don't make loan choices. Credit bureaus are tremendously powerful financial entities. Credit bureaus are subject to restrictions under the Fair Credit Reporting Act (FCRA), which was enacted in 1970. It is mainly intended to safeguard customers from careless or purposefully false information in their credit score reports.

The Fair Credit Reporting Act was modified in 2003 by the Fair and Accurate Credit Transactions Act (FACTA), which grants customers the right to get one free credit report from credit bureaus every 12 months. It also granted individuals the ability to buy a credit score along with the knowledge of how the score was determined.

How Credit Bureaus Work

Credit bureaus are specialized businesses that collaborate with various lenders and creditors to support them in their lending choices. Lending institutions are businesses, like banks and credit unions that borrow money from depositors and return it to them with interest. Then, in order to make money, the lending institutions will profitably lend out a part of those deposits at a higher rate. To prevent borrowers from defaulting on the loans they take out, lenders must make sure that their borrowers have sufficient credit standing.

The top three credit reporting agencies in the US are:

1. Equifax
2. TransUnion
3. Experian

However, a lot of smaller agencies also provide credit information. As was already established, lending organizations need credit information to assess the creditworthiness of their borrowers. A borrower may be turned down for credit or be paid a higher interest rate to make up for the increased risk if they seem to be less creditworthy. In contrast, lenders will charge borrowers with excellent credit a reduced interest rate since they are a smaller risk to them. It is important to note that credit bureaus do not decide whether or not to provide credit to a person. They only gather and combine the data for the lenders to consider when making their selections. The information is sold by credit bureaus to lending institutions for a charge as well as to people who want to learn about their own credit histories.

Credit Reporting

Credit information is obtained by credit bureaus from a variety of sources, including other creditors, debtors, debt collection agencies, credit card issuers, and other entities having public records on credit-related information. Equifax, TransUnion, and Experian the three major credit

bureaus are used to gather and combine the data. Credit accounts accounts where a person owing money to another company are the subject of credit bureaus' typical attention. However, certain credit bureaus could go farther in their pursuit of bill, payment, and rent payment information. The data will be combined by the credit agencies into an extensive credit report.

Report on credit

A credit report provides a thorough summary of a person's credit history. Personal details including residences, Social Security numbers, and job histories are often included in the report. The summary of bank accounts and credit card accounts that are current or past due will then be broken out in the report. Additionally, it will include details on the accounts, such as their balances, credit limits, and dates of establishment. Details on accounts reported to credit bureaus, such as wage garnishments, will also be included in credit reports. Negative information will be kept on the credit report for seven years.

DISCUSSION

List of Indian credit bureaus

In India, there are four significant credit bureaus. These consist of:

1. TransUnion Credit Information Bureau (India) Ltd. (CIBIL):

The oldest credit bureau in India is the CIBIL bureau, which was founded in 2000. The agency keeps track of the credit histories of 32 million businesses and over 600 million people. It was initially founded by the Reserve Bank of India, but eventually amalgamated with TransUnion International, a credit bureau with headquarters in Chicago.

2. Equifax India

The Indian division of Equifax Inc., the most well-known credit bureau in the world, is called Equifax India. Despite being founded in 1899, the agency didn't have its operating permit until 2010. The bureau not only provides credit reports but also computes risk and portfolio ratings.

3. CRIF High Mark

The credit bureau was founded in 2007, and in 2010 it received a license to operate. According to the bureau, it was the first full-service credit bureau in India. It offers a range of financial services, such as giving lenders, MSMEs, and business and retail clients thorough credit information. In addition to that, the bureau provides NBFCs, home finance firms, insurance companies, and telecom service providers with software solutions for data management, analytics, and insights.

4. Experian

According to the 2005 Act of New Credit Information Companies (Regulatory), the credit bureau was the first to get accreditation. Credit reports and scores are made available by the credit bureau. Additionally, they provide marketing services and analytics solutions to help people and organizations make thoughtful credit choices.

Indian credit bureaus' function (H2)

As was previously said, a credit bureau is an organization that gathers and analyzes credit data for an individual or company. This financial data may include electricity bills, credit loans obtained, and income tax refunds and payments. Such data is obtained, among other places, from data gathering organizations and lending institutions.

To ascertain how people behave when it comes to credit, this data was collected with the intention of analysis. The Reserve Bank of India (RBI) issues licenses to the Credit Information Companies (CICs) or credit bureaus in India and supervises them to prevent fraud.

An overview of a credit bureau in India is provided below:

- a. The preservation of financial transparency is the goal of credit bureaus. This involves giving consumers and lenders easier access to financial data through extensive credit bureau reports. Additionally, you have the freedom to report and fight any financial inequalities.
- b. •Preventing fraud and poor loans is another crucial role played by the credit bureau in India. An individual's credit score, which is determined by a credit bureau, eventually aids lenders in determining whether or not to provide credit to a specific applicant. Any prior fraudulent activity would be flagged as hazardous, preventing it from happening again in the future. As a result, India's effective credit reporting systems may reduce a variety of market risks or failures that are common in the country's financial markets.
- c. Credit bureaus work along with several creditors and lending institutions to assist them in making various loan choices.

What are a credit report and score?

The gathering of financial data for the purpose of creating credit reports for specific persons is one of the crucial duties of a credit bureau in India. Your credit position is detailed in a credit bureau report. This includes the value of your credit. A credit score, often known as a credit bureau score, is a ranking that describes a person's credit behavior and creditworthiness.

Your credit score is impacted by variables including the quantity of open accounts, credit cards, total debt, and repayment history. A credit score might have a value between 0 and 900. Most lenders see a credit score below 600 as cause for concern. A credit score of 700, however, is regarded as great and designates the person as creditworthy. A credit score between 600 and 700 is regarded as being average. A credit score in the middle indicates a little bit of hazardous credit behavior. Even if your credit score is poor, there are several strategies to raise it.

Do credit scores and reports vary from one bureau to another?

In fact, there are differences between credit bureau ratings. This occurs because various credit information companies (CIC) utilize different algorithms and scoring models. However, since all credit agencies get the same information from lenders, the individual's credit report will have the same information for everyone. Credit bureaus get their data from banks and financial organizations, however there may be other elements that result in a variance. If some data is not sent simultaneously to the credit agencies, some difference may be seen. As a result, the credit

score may be affected if one agency has updated information or more information than the others. Although modest variations in credit scores are possible, if you see a considerable variance, it may be the result of an informational mistake. This may be the consequence of inaccurately reported data or erroneously recognized data points. If you encounter the same issue, you may inform the bureau so that it can fix it [4]–[6].

Variations in the contact information given when a person applies for a loan or credit card may also lead to inconsistencies. The majority of the time, joint applications report on this.

Bank credit decisions and the role of credit bureaus

By offering useful data on the creditworthiness of people and companies, credit bureaus play a vital role in bank loan decisions. Their major duty is to gather, preserve, and offer lenders and financial institutions with credit-related data that aids in risk assessment when considering whether to lend money to applicants. An outline of the part credit bureaus play in bank credit decisions is provided below:

Credit Reporting: Credit reporting agencies gather and keep thorough records of a person's credit history, including data on their borrowing and repayment patterns. Data on loans, credit cards, mortgages, and other types of credit are included.

Credit Scores: Based on an individual's credit history, credit bureaus compute credit scores. Credit scores are numerical depictions of a person's creditworthiness that provide lenders a simple method to assess the risk involved in granting credit. FICO and Vantage Score are two popular credit scoring methods.

Risk evaluation: Lenders evaluate the risk of providing money to a potential borrower using the data supplied by credit bureaus. An applicant is more likely to be granted favorable loan conditions if they have a good credit history and a high credit score, which usually reflect responsible borrowing behavior and a reduced chance of default.

Loan approval: Information from credit bureaus helps lenders decide whether to accept a loan application or credit request after doing their research. Lenders may make an instant decision on a borrower's creditworthiness and the terms of the loan, including the APR and credit limit.

Interest Rates: The information provided by credit bureaus affects the interest rates given to borrowers. Since they are seen as less hazardous borrowers, those with better credit scores often get lower interest rates. On the other side, those with poorer credit ratings may face higher interest rates or perhaps be turned down for loans entirely. Credit bureau data is used by lenders to reduce their lending risks. Lenders may spot patterns of hazardous activity or indications of prospective financial difficulty by looking at an applicant's credit history and behavior.

Fraud Prevention: By alerting consumers to questionable activity, such as several credit applications submitted quickly or inconsistencies in personal information, credit bureaus help to prevent fraud. This aids lenders in confirming the applicant's identification.

Data Accuracy: Credit bureaus are in charge of making sure that the data they provide to lenders is accurate. People have the right to challenge any mistakes in their credit reports, and credit bureaus are required to look into the complaints and make any necessary corrections.

Credit Monitoring: People may keep track of changes to their credit reports by using the credit agencies' credit monitoring services. Individuals may be better able to identify and quickly address any faults or unlawful activity as a result. In inference, credit bureaus act as middlemen between lenders and borrowers by disseminating crucial credit-related data. Their information aids lenders in making wise choices about loan extension, term stipulation, and risk management. For borrowers, keeping a good credit history and keeping an eye on their credit reports are essential for getting access to good credit options [7]–[9].

CONCLUSION

To sum up, credit bureaus are crucial in influencing bank credit choices and have transformed the lending industry with their data-driven insights. These agencies act as warehouses for people's credit records, giving banks a thorough evaluation of borrowers' financial practices. Lenders can accurately assess a potential borrower's creditworthiness by examining credit reports, allowing more informed and precise lending choices. The capacity to immediately evaluate risk levels is made possible by the availability of credit scores, which are generated from credit reports. Better loan terms and interest rates result from a reduced risk profile, which is often indicated by a higher credit score. On the other side, a lower credit score could lead to more stringent lending requirements or more expensive borrowing. Credit bureaus promote lending transparency by providing banks with past payment data, unpaid debts, and credit use trends. Lenders may assess a borrower's capacity for timely payment of debts and responsible debt management using the information provided. The possible drawbacks and restrictions of depending only on credit agency data must be understood, however. Particularly in situations of unexpected financial difficulty or big life events, these reports could not always accurately reflect a person's whole financial situation. The function of credit bureaus has changed in the digital era to incorporate identity verification and fraud detection in addition to conventional credit reporting, improving the security of lending procedures.

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CHAPTER 16

CREDIT CARD DEBT MANAGEMENT: TIPS FOR RESPONSIBLE USE

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ABSTRACT:

This chapter explores the topic of managing credit card debt and provides tips and use guidelines. Understanding how to use credit cards successfully is essential since they have become common financial instruments. In order to prevent accruing high-interest debt, the chapter discusses ethical credit card use advice, highlighting the significance of planning, keeping track of spending, and paying bills on time. It emphasizes how important it is to comprehend credit card terms, interest rates, and fees in order to make wise financial choices. The chapter also discusses the attractiveness of cashback and incentive credit card schemes, encouraging consumers to weigh these benefits against possible expenditures. It promotes keeping your credit usage ratio low since it has a direct influence on your credit ratings.

The chapter also emphasizes the need of building an emergency fund to cover unanticipated costs and lessen dependency on credit cards in emergency situations. Although the chapter accepts that balance transfers and debt reduction may be beneficial tactics, it also warns readers about their possible drawbacks. It discusses the value of seeing a professional when faced with a mountain of debt and examines credit counseling as a possible source of support.

KEYWORDS:

Balance Transfers, Billing Cycle, Credit Card, Debt Management, Spending Money.

INTRODUCTION

People may avoid the dangers of building up high-interest debt by sticking to a budget, keeping an eye on their spending, and making regular payments. It is crucial to understand credit card terms, rates, and fees since well-informed choices are the cornerstone of financial security. The abstract cautions consumers to evaluate their spending habits and practice discipline despite the appeal of incentives and cashback programs.

Smart user advice for credit cards

A credit card may be a very useful financial instrument when used appropriately. Your credit score may be improved by consistently making on-time payments. Additionally, some cards provide incentives for purchases or even a temporary 0% interest rate on balance transfers from other credit cards. However, if you use your credit excessively, your monthly payments and accrued interest may become an issue. To assist you steer clear of typical issues, use these credit card tips:

1. Every month, pay off your amount.

By paying off the whole amount on your credit card each billing cycle, you may avoid paying interest on your purchases. If you can resist the need to spend more money than you can afford in any given month, you can profit from using a credit card without being charged interest.

2. Use the card for essential purchases only.

It's important to use credit cards responsibly. Spending money carelessly might result in debt. In an emergency, such as when a cell phone bill is due before your next paycheck, credit cards may be utilized. Use the credit card as a short-term loan to yourself, and then pay it off as quickly as you can to reduce or completely prevent interest rates.

3. Don't ever miss a payment.

Even if the minimal payment is all you can afford, pay your bills each month. Missing a payment might have an adverse effect on your credit score, incur a late charge, and incur penalty interest rates.

4. Utilize the credit card as a tool for budgeting.

Try using a credit card as a budgeting tool if you're convinced you can use one responsibly and pay the debt in full each month. You can easily calculate your monthly spending by using your credit card for all of your transactions. Naturally, you should only do this if you are certain in your ability to settle the sum each month. Never charge more on your card than you have in your bank account to prevent your credit card spending from getting out of control [1]–[3].

5. Employ a rewards card.

It makes sense to use a credit card that gives rewards if you use it for the majority or all of your expenditures. You may save money on interest payments as well as gain incentives like money, airline miles, or shopping points.

6. Don't use more than 30% of your available credit.

Maintaining a credit usage ratio under 30% is one approach to keep your credit score in good shape. The proportion of your overall credit limit that you are utilizing is known as your credit usage ratio. If your limit is \$1,000, for instance, you need to maintain your balance below \$300. Although the ratio only applies to the total of your cards, if one has a limit of \$3,000 and a balance of \$3,000 and another has a maximum of \$7,000 with no balance, you're precisely at the 30% threshold (\$3,000 of a \$10,000 possible limit), which is where you want to be.

Ideas to Control and Lower Credit Card Debt

Spending, saving, and determination are the three factors that determine whether or not credit card debt is eliminated. The other actions will be easier to handle after that previous one.

1. Continue paying off your credit card debt promptly: Avoiding late fees and other costs involves paying on time. You won't be hit with high interest fees if you pay the whole bill in full and on schedule. If you're late with a payment, the issuer of your credit card has many of tools at its disposal to make your life unpleasant. Your credit reports from the three main credit agencies (TransAmerica, Equifax, and Experian) will ultimately reflect that.

2. Spend money responsibly: Find strategies to reduce your spending and learn to live within your means.

- a. **Use credit responsibly:** Don't charge anything that you won't be able to pay back within three months.
- b. Create a sensible budget and follow it: List your monthly income and expenditures, then keep tabs on your spending.
- c. Keep to your shopping list to avoid making impulsive purchases. Keep just the amount of cash you have planned for your shopping excursion and leave your credit card at home.
- d. Cut down on your extravagances by making coffee at home instead of paying \$5.29 for Starbucks' Blond Espresso Roast. Avoid letting magazine covers, pop-up commercials, storefront displays, or the Kardashians inspire you to make a fashion purchase.
- e. Look through your expenses and see if you can reduce your use of streaming services, cable, and the internet. For potential cost reductions, review your insurance policy.
- f. To get great prices on groceries, watch for sales and utilize coupons. Think about purchasing cheaper store brands. They often match the quality of name-brand items.
- g. Take good care of your possessions: Regular maintenance helps you prevent costly repairs and increases the life of the items you depend on.

3. Select a Credit Card Payment Plan: If you're committed to paying off your credit cards, you should pay more than the required minimum each month. To achieve such, there are three proven techniques.

- a. **Debt Snowball:** In this strategy, the credit card with the lowest APR is paid off first. That encourages you to pay off the next-lowest balance first, then the next, and so on until you have eliminated all of your debt.
- b. **Debt Avalanche:** This strategy is the reverse. Start by paying off the card with the highest interest rate, then work your way down. Although it has a stronger mathematical foundation than the snowball, some customers may prefer instant satisfaction.
- c. **Automating Your Payments:** This is an easy method to remain on top of your payments and prevent late penalties, penalty interest, and negative reports to credit monitors. Simply keep a tight eye on your bank account. Even worse than late fines might be overdraft costs.

4. Verify Having an Emergency Fund: Life takes place. People lose their jobs, automobiles break down, kids require stitches, and the air conditioner malfunctions. Although they don't occur often, unforeseen costs constantly seem to appear. Try to create an emergency fund to be ready. If possible, it should cover your costs for six months in the event that you lose your job. You won't have to charge the expenditure on your credit card as a result.

5. Don't Just Make the Minimum Payment: Customers that pay the minimum amount necessary to avoid late penalties are highly favored by credit card providers. The total balance and interest rate are scarcely decreased. By making as much of a monthly payment as you can, you'll be doing yourself a tremendous financial favor. Targeting certain items on your account is a smart strategy. Research demonstrates that when customers check their bills and choose certain products to return, they end up paying 15% more overall.

6. Transfer or Consolidate Your Credit Card Debt: A reduced total interest rate could be achieved by combining all of your high-interest debts into one. Numerous individuals have overcome their financial issues thanks to such debt consolidation services. Your entire cost will be reduced if you consolidate with a low-interest personal loan from a bank, credit union, or reliable peer-to-peer provider. Additionally, you might use cards with balance transfers. Purchase a credit card with a very low introductory interest rate possibly even zero and then transfer the balances on your existing cards to the new one. But be aware that there is often a 3% transfer charge. And settle the account before the promotional rate ends (often after 12 to 18 months), or you'll be hit with the inflated regular rate.

7. Cooperate with lenders to reduce your interest rate: Do any of the following apply to you?

- a. Your relationship with your credit card issuer(s) is/are solid.
- b. You always make your payments on time.
- c. You stay inside the bounds of your credit.

If all of that is accurate, speak with the companies who supply your cards and request reduced interest rates. They may very well.

8. You may earn more money: According to Captain Obvious, you will need more money to pay off your debts as your income increases. There are several side occupations that might provide additional income.

- a. Take up a side job.
- b. Request a raise.
- c. Increase your workday.
- d. Search employment boards for temporary or odd jobs (handyman, childcare, yard work).
- e. Sell any personal items you no longer need or use.
- f. Turn a skill you have into a secondary business.

DISCUSSION

Understanding Credit Card Terms

You must comprehend credit card jargon if you want to control your credit card debt. This is the jargon.

- a. **Annual Fee:** For the right to use their cards, issuers levy an annual fee. A "membership" or "participation" charge is another name for it.
- b. **Annual Percentage Rate (APR):** The annual interest rate, which also includes any fees or charges associated with obtaining the loan. The periodic rate multiplied by the quantity of billing cycles equals the calculation. For debt transfers, cash advances, and other incentive offers, different APRs could be shown.
- c. **Average Daily Balance:** This figure is arrived at by adding up all of the days' balances and then dividing that sum by the overall number of days in the billing cycle. The monthly fee for the card is multiplied by the result. Transferring an outstanding amount from one credit card to another is known as a balance transfer.

- d. **Credit Limit:** The most you may borrow with a credit card. While some issuers prevent excessive charges, others impose overage costs. The fee for using a credit card and having a debt is known as the finance charge.
- e. **Grace Period:** For cardholders of zero-interest cards, the time frame between the date of the purchase and the billing date during which there is no interest charge. Not every card issuer provides it.
- f. **Late Fee:** The penalty assessed for late payments. The lowest payment you must make in whole and on schedule, often 2% of the outstanding sum.
- g. **Beyond-Limit Fee:** The cost incurred when you go beyond your budget.

After paying off your credit card, should you cancel it?

If you pay off your credit card, you may wish to tear it into pieces and execute a victory dance while throwing the pieces in the air. Defy the desire. Your credit usage ratio, which accounts for 30% of your credit score, will decrease if you cancel your card. When you don't have cash and an emergency arises, a credit card is also useful. To keep the accounts active, you need to utilize them sometimes. Therefore, make a low-cost purchase and pay it off right away. Change to a card with no cost if you don't want to pay the yearly fee.

Get Assistance with Managing Credit Card Debt

Debt accumulation is often a one-person profession. Leaving could need assistance. Contact a nonprofit organization to schedule a credit counseling session if you need assistance. A licensed counselor will assess your predicament and come up with a plan that could help you escape credit card jail [4]–[6]. Through a debt management plan, maybe. Counselors negotiate reduced interest rates and regular payments with your creditors. You provide the organization one payment each month, which is less than the sum of your other contributions. Even if inflation slows down, it won't go away. Keep in mind that with careful preparation and perseverance, you can still pay off your obligations. That is superior than just pointing your fist upward.

How Does Debt from Credit Cards Grow?

There is a billing cycle and a due date for each credit card. The deadline by which you must repay the amount shown on your invoice for that particular billing cycle is known as the due date. Credit card debt is the amount still owing. Because you borrowed the funds to spend on your credit card, that is why it is termed debt. As an example, suppose you got your credit card statement for the month of January on February 5th. Your unpaid balance is \$25,000, and the deadline to do so is March 10th. Your credit card debt is \$25,000, and your due date is March 10.

How Can You Better Manage Your Credit Card Debts?

Long-term benefits of making an effort to manage your credit card obligations properly are really evident. In the perspective of your bank, you become more credible if you have a strong credit history. This even supports your assertion that, should the need arise, you may raise your card's credit limit. You get qualified for loans at reasonable rates as a result of your effective debt management.

Here are a few strategies for handling your credit card debt more effectively:

1. **Note significant information:** If you use many credit cards, this step should be your top concern. Each credit card has a unique credit limit, payment cycle, due date, interest rate, and associated costs. While having many cards will enable you to spend more, keeping track of them all might be challenging. Make a note of all your cards, then schedule your money so that you don't forget any critical dates. Decide which card you'll use for certain types of payments.
2. **Negotiate your interest rates:** The credit card issuer alone will be responsible for this. Your bank could be willing to cut your interest rates if you have an excellent credit history thus far. Getting your bank to reduce the card's interest rate is one of the greatest strategies to manage your credit card debt. Additionally, this will reduce any compound interest that is added to the accrued interest. Simply told, this may drastically lessen your repayment obligations. You may ask your bank to waive certain additional expenses associated with your card, such as yearly fees, if not interest rates.
3. **Pay your debts on time:** Your bank will not assess interest if you pay your debts on time. Therefore, always be sure to pay promptly, ideally in full. Any payments you make beyond the due date accrue compound interest, which raises your overall debt. Here are some strategies to help you meet your deadline on time:
 - a. Ask your bank to make automatic payments on your behalf. By doing this, your bank will automatically take the appropriate amount each month from your account to pay off your debt.
 - b. Another option is to use your phone to set reminders. You will be forewarned in advance of the due date by this.
4. **Pay the minimum balance:** Try to at least pay the minimal balance if there are times when you find it difficult to pay the whole amount owing at once. It is shown on your bill as part of your dues. It is subject to an extra fee and interest if it is not paid by the due date.
5. One of the most often recommended strategies for managing your credit card obligations effectively is the avalanche technique of payment. If you have many credit cards, start making payments with the one with the highest interest rate. By doing this, you may avoid paying future high-interest fees. On the other hand, if you have enough money, pay off all of your other credit cards or at least the minimum debt on each one.
6. The opposite of the avalanche technique of payment is the snowball method. The snowball approach dictates that you begin by paying the card with the least balance owing. Despite not being widely used, this strategy nonetheless gives people a positive psychological lift. With the same payments, it enables the cardholder to notice a large decrease in their balance. Consider the scenario where you have the following three credit cards: A, B, and C. You owe card A 10,000, card B 5000, and card C 1000 respectively. You currently only have \$12,000 available for payment. Therefore, even after paying \$10,000, if you start with card A, you will still owe money on two cards. However, if you start with card C, you may spend the leftover \$11,000 to pay off another card in addition to fully satisfying it. As you take each step slowly, this strategy might help you stay positive.
7. **Make the most of your reward points:** When you use your credit card to make a purchase, your issuer awards you with some redeemable points. These points may or may not have an

expiration date, depending on your bank. To reduce the amount you borrow on your credit card, you must utilize these points to their fullest potential. Additionally, it will enable you to cut costs and deals.

8. **Borrow from friends or family:** If you see that your credit card debt is mounting steadily, you may want to think about borrowing from those who are close to you. Utilize this cash to pay off your credit card debt for the time being, and then pay your family back later. By doing this, you will avoid accruing a considerable amount of interest-bearing debt. This should only be used as a last option since it is not a long-term fix. This tendency may wreck your spending and saving habits if it is repeatedly followed.
9. **Get a credit card balance transfer:** If you have many cards and find it difficult to keep track of your spending, you might think about getting one. You may ask your bank to combine all of your outstanding amounts across all of your cards and move them to a single, lower-interest card. You won't have to monitor as many different cards, which will help you manage your debt better.
10. **Keep an eye on your spending:** You need to start strengthening the foundation if you want to handle your money more effectively in the long term. You won't ever be able to manage your debts if you don't put any restrictions on your spending.

Start organizing your spending and dividing it into categories based on priorities. If your funds are tight, try reducing impulsive spending and unneeded purchases. However, this is not the end of it since you also need to follow the plan [7]–[9].

CONCLUSION

In summary, understanding credit card debt management is an essential component of leading a financially sound life. The variety of recommendations for ethical credit card usage provided here emphasizes the value of caution and awareness while using credit cards. A key tactic for raising credit scores and improving overall financial health is to work for a low credit use ratio. The focus on creating an emergency fund reduces the need for excessive credit card use in addition to serving as a safety net against unforeseen costs. Although debt consolidation and balance transfers may provide relief, the abstract emphasizes the caution that must be used throughout these procedures. In situations when debt is out of control, getting expert advice or attending credit counseling may be a huge help in the direction of financial recovery.

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CHAPTER 17

BANK CREDIT AND FINANCIAL INCLUSION: REACHING UNDERSERVED POPULATIONS

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ABSTRACT:

The relevance of bank credit in achieving financial inclusion, especially in reaching disadvantaged groups, is briefly summarized in this study. Bank credit, which makes it possible to obtain money for a variety of uses, is crucial in promoting economic development and personal success. But conventional financial institutions continue to underserve a substantial section of the world's population. By giving underprivileged and underrepresented groups access to credit and other financial services, financial inclusion seeks to close this gap. This study emphasizes the significance of cutting-edge strategies for increasing financial availability, including microfinance, mobile banking, and community-based efforts. Bank credit promotes financial inclusion, which empowers people, encourages entrepreneurship, and aids in overall socioeconomic development. For the world's financial systems to become more inclusive and egalitarian, efforts in this direction are crucial.

KEYWORDS:

Bank Credit, Economic Development, Education, Financial Inclusion, Financial Services.

INTRODUCTION

The financial sector is always developing new strategies to provide goods and services to people all over the world and often make money in the process. For instance, the growing usage of financial technology (or fintech) has produced creative solutions to the issue of access to financial services and created new avenues for people and organizations to get the services they need at fair prices.

Financial Inclusion: What Is It?

Financial inclusion refers to initiatives to make financial services and products available and reasonably priced to all people and companies, regardless of their personal wealth or the size of their organization. The goal of financial inclusion is to lower the obstacles that prevent individuals from engaging with the financial system and using its products to better their lives. Additionally known as inclusive finance.

The Process of Financial Inclusion

Financial inclusion, according to the World Bank, "facilitates day-to-day living, and helps families and businesses plan for everything from long-term goals to unexpected emergencies." Additionally, it adds, "As accountholders, people are more likely to use other financial services, such as savings, credit, and insurance, start and expand businesses, invest in education or health, manage risk, and weather financial shocks, all of which can improve the overall quality of life."

Although there have always been obstacles to financial inclusion, a variety of factors are currently working to increase access to the types of financial services that many wealthy consumers take for granted [1]–[3].

Financial Inclusion Areas

Numerous things might be referred to as financial inclusion. In general, the following financial, economic, or entrepreneurial principles may be included, although they are not required to be.

Financial Literacy and Education

Giving people access to financial education and programs that provide them with fundamental financial information and skills is referred to as financial education and financial literacy. This gives individuals the ability to budget wisely, make well-informed choices, and see the advantages of utilizing legitimate financial services rather than depending on illegal or possibly exploitative substitutes. Some people just lacked access to the right educational opportunities to master the fundamentals of financial literacy.

Accessible and Reasonably Priced Banking Services

By providing accessible and cheap banking services, it is made possible for unbanked and underbanked people to engage in the legal financial system. Financial inclusion is made possible at the grassroots level by providing no-frills savings accounts and inexpensive transaction accounts. This ensures financial stability (both philosophically and literally) and encourages saving money.

Gender Inequalities

31% more women than males have dormant bank accounts, according to Women's World Banking. Financial inclusion may aid in the economic empowerment of women and the reduction of the gender gap in financial services by concentrating on gender-specific financial inclusion programs. These initiatives include measures to support women's entrepreneurship, programs to encourage financial literacy, and customized financial products.

Comprehensible Credit Scoring

Traditional credit scoring methods could exclude or treat unfairly those who have little or no credit history. The goal of financial inclusion is to investigate alternative credit scoring techniques that take into account non-traditional data sources and potentially open up credit to those with little credit history. More people may access loans and other financial services thanks to criteria like utility bill payments and rental histories, which further promotes financial and economic prospects.

Consumer Defense

Protecting clients inside of businesses is another aspect of financial inclusion. The goal of financial inclusion is to put protective laws and safeguards in place to protect the interests of those who are financially vulnerable. In order to build trust and confidence in formal financial services, strong consumer protection regimes assure fair treatment, clear pricing, and ethical behavior by financial institutions. The goal of financial inclusion is to maintain the trust of individuals who may lack financial literacy or information in the financial system.

DISCUSSION

Financial inclusion's importance

The benefits of financial inclusion are many and quite universal. Among the primary motives are:

1. Financial inclusion lowers inequality and poverty. Financial inclusion gives low-income and excluded people the chance to use formal financial services including insurance, credit, and savings. Financial inclusion may aid in lifting people out of poverty and minimizing economic inequality by providing them with the resources to manage their accounts and participate in income-generating ventures.
2. Financial inclusion encourages economic development. One common claim is that consumers may engage in the economy more actively when they have access to financial services. Higher levels of entrepreneurship, savings, and investment are produced by greater financial inclusion, which promotes economic stability and development in both local and global economies.
3. Financial inclusion supports entrepreneurship. It may be difficult for small firms to get finance through typical banking institutions. Innovative lending structures and internet platforms that promote financial inclusion may provide entrepreneurs the much-needed capital they need to expand their companies.
4. Financial inclusion empowers people that would otherwise be excluded. Initiatives for financial inclusion, for instance, may support women's economic empowerment and gender equality. Giving women access to financial services helps them take charge of their money, which may enhance their chances for a good education, a healthy lifestyle, and greater family decision-making authority.
5. Innovation is encouraged by financial inclusion. Financial inclusion stimulates innovation in the financial industry, resulting in the creation of new fintech products and services that address the needs of neglected groups. These developments may improve financial services and help the larger financial ecosystem.
6. Digital inclusion may promote financial inclusivity. Promoting access to digital financial services also helps to digital inclusion, ensuring that more individuals can participate in the digital economy, since technology plays a vital role in financial inclusion.

Tech and Financial Inclusion

Numerous options exist for technology to improve financial inclusion, and it already does so to a significant extent. Here are a few ways that contemporary advancements may help us provide financial services to the globe more effectively.

Cellular Banking

Numerous services are available via mobile banking apps, including checking account balances, money transfers, bill payment, and even loan applications. These 24/7 accessible, user-friendly applications allow people to simply make financial transactions from their smartphones without having to go to actual bank offices.

Electronic payments

46.4% of all American households used nonbank online payment services in 2021, according to the FDIC. There are several ways to conduct cashless transactions using online payment platforms. While contactless payment technologies like Near Field Communication (NFCs) and QR codes offer quick and safe purchases in physical retail environments, mobile wallets allow consumers to store money digitally and make payments using their mobile devices. The danger of theft or loss associated with carrying cash is reduced by both alternatives [4]–[6].

Broker Banking

Technology is used in agent banking models to provide software and mobile devices to banking agents. In distant locations where brick-and-mortar branches are unfeasible, agents serve as middlemen and represent financial institutions. They provide those who may not have easy access to regular banks with services including account opening, deposits, withdrawals, and financial transfers.

Lending Platforms Online

Fintech lending platforms use internet platforms to directly link lenders and borrowers. Loan applications are accepted, and lenders use data analytics and alternative credit scores to determine if borrowers are creditworthy. This simplifies the lending procedure and increases credit availability for people and enterprises that aren't well-served by conventional banks or who wouldn't otherwise be eligible for traditional credit. For instance, LendingClub advertises that its services have helped more than 4.7 million members reach their financial objectives.

Blockchain and digital money

A decentralized, unchangeable record for safe financial transactions is provided by blockchain technology. Cryptocurrencies provide possible alternatives to conventional financial systems by allowing those without regular bank accounts to engage in the digital economy. Take into account using these solutions in emerging nations to increase transaction speed, combat weak national currencies, and increase accessibility to the financial system.

Apps for Financial Education

Online resources and financial education applications provide interactive and interesting information to increase financial literacy. To improve their comprehension of financial concepts and make better financial choices, users may access instructional courses, budgeting tools, and investment information. Think about how, as of July 2023, Mint by Intuit has been downloaded more than 10 million times from the Google Play store.

Crowdfunding

Crowdfunding enables geographically dispersed people to nonetheless connect and support a single cause via donations or equity contributions, just as peer-to-peer lending does. Crowdfunding platforms enable people, small businesses, and social impact initiatives to raise money from a variety of investors. This more democratic method of fundraising increases the amount of funding available to effective projects and underrepresented businesses. GoFundMe has assisted in the raising of approximately \$9 billion as of July 2023.

Issues with Financial Inclusion

When attempting to achieve financial inclusion, there are persistent and major obstacles. The lack of awareness and information about formal financial services is the first significant barrier. Rural and underserved populations may simply be unaware of the ideas or services available, and certain communities may have mistrust for established financial institutions. Additionally, financial habits and choices may be influenced by cultural and societal norms and traditions.

Financial institutions may be discouraged from servicing low-income consumers and expanding into disadvantaged communities by policy and regulatory obstacles. Financial inclusion may be hampered by socioeconomic differences and gender inequality, with women and underprivileged groups possibly experiencing larger obstacles to accessing and exercising control over financial resources.

Unable to be accurately measured problems might be exceedingly challenging to resolve. The creation of focused and efficient financial inclusion efforts might be hampered by a lack of market data and information on unbanked and underbanked people. Geopolitical and conflict-related difficulties may also undermine financial stability and infrastructure, thereby restricting access to financial services in certain geographical areas.

Finally, worries about data security and privacy may prevent people from using digital financial services, particularly in areas with insufficient data protection regimes. Because of the decisions they make, customers may choose to financially exclude themselves, whether consciously or unconsciously. For instance, consumers who put less faith in digital services sacrifice financial potential for more control and comfort over their personal data.

What Economic Benefits Does Financial Inclusion Bring?

By encouraging entrepreneurship, raising savings, and enhancing investment options, financial inclusion supports economic development. It increases consumer spending and company growth, which results in more jobs being created and increased productivity. Additionally, a financially accessible economy draws more foreign investment and aids in the achievement of sustainable development objectives.

What Function Does Government Play in Financial Inclusion Promotion?

Governments' use of legislative and regulatory frameworks to advance financial inclusion is crucial. They may put policies in place to lower obstacles, encourage financial institutions to assist underprivileged groups, and make investments in digital infrastructure and financial literacy initiatives.

What Threats Does Financial Inclusion Pose?

Over-indebtedness, possible exploitation by dishonest lenders, and data privacy issues with the usage of digital financial services are a few problems connected to financial inclusion.

What Are the New Financial Inclusion Trends and Innovations?

Innovations in fintech, including blockchain, artificial intelligence, and virtual currencies, are expected to influence the direction of financial inclusion in the future. Additionally, a growing focus on data security and privacy will affect the trajectory of financial inclusion projects globally, along with legislative changes.

The inference

The process of ensuring that everyone has access to suitable and inexpensive financial services, particularly those who are disadvantaged and marginalized, is known as financial inclusion. It attempts to provide individuals the capacity to manage their money, engage in the official financial system, and develop economic resilience by providing them with resources including savings accounts, credit, insurance, and digital payment choices.

The role of credit reporting in financial inclusion

This policy brief analyzes the importance of credit reporting systems for financial inclusion and outlines problems and potential fixes. The report was created for the World Bank-led International Committee on Credit Reporting, which is made up of central banks, financial regulators, international financial institutions, and business organizations. In many nations, financial inclusion is now a top goal for national policy. In response, players in the private sector are stepping up their efforts to reach underserved or unserved groups. Numerous governments and regulators are implementing steps to increase financial inclusion levels in their countries.

Although crucial, having access to and using a transaction account is just the first step in becoming completely financially engaged. Enabling large segments of the population, especially vulnerable and other disadvantaged people as well as micro and small businesses (MSEs), to obtain finance on fair terms and in a responsible way is another crucial goal of governmental policy in various nations.

The International Committee on Credit Reporting (ICCR) and the World Bank Group have been researching how credit reporting affects or could affect access to credit for a number of years. The ICCR elaborates on how credit reporting can promote financial inclusion in this policy brief, paying particular attention to issues with access to credit for both individuals and MSEs, whose credit needs are still unmet or underserved by regulated/licensed financial institutions and/or other formal lenders that are not financial institutions (such as retailers) [7]–[9]. Providers of credit reporting services do not make loans or other types of funding available, nor do they set the standards by which financial institutions or other lenders approve loans. Credit reporting systems may promote financial inclusion by doing the following:

1. By gathering payment history data and other predictive data sets and making this data accessible to lenders, credit reporting systems may assist lenders in expanding their markets to include underserved individuals and MSEs. This will help people and MSEs develop their "reputational collateral".
2. Ensuring long-term sustainability of loan availability

3. Credit reporting may assist MSEs that currently have a formal loan and lower-risk borrowers in getting more inexpensive and flexible terms (such as longer tenors) for future loans by enabling lenders to price risks more correctly.
4. Supporting fiscal responsibility
5. Increasing financial literacy among consumers and MSE
6. Aid in preventing fraud
7. Setting up a fair playing field so that smaller lenders may compete with bigger ones.

This policy brief's goal is to address major obstacles and potential solutions so that credit reporting may be used to its utmost extent. The report updates earlier work produced by the ICCR and suggests possible steps that might support responsible credit access, like:

1. Become a member of the General Principles for Credit Reporting
2. Create a system for effective supervision.
3. Make sure that people and MSEs can be recognized by CRSPs clearly and affordably.
4. Achieve more thorough, precise, and effective CRSP coverage.
5. Strengthen thin files

CONCLUSION

In conclusion, a critical frontier in fostering fair economic development and empowering marginalized groups is the junction of bank lending and financial inclusion. The need to expand the advantages of banking services to underserved groups becomes more and more obvious as financial systems develop. Through the creation of chances for business, education, homeownership, and better living standards, access to bank credit has the power to enhance the lives of both people and communities. Innovative solutions that close the gap between conventional banking and underprivileged people have been made possible by the development of financial technology, digital banking, and microfinance. These mechanisms promote financial inclusion by providing specialized financial goods and services, bringing the unbanked and underbanked into the fold of established financial institutions. To ensure that people can make educated choices and responsibly use credit, efforts must be made to improve financial literacy and provide focused education on credit and banking. In addition to protecting them from debt traps, this gives them the ability to use credit as a vehicle for socioeconomic growth.

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CHAPTER 18

BANK CREDIT AND CONSUMER PROTECTION LAWS

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ABSTRACT:

This study provides a succinct explanation of the relationship between consumer protection laws and bank credit, emphasizing the critical function these laws serve in defending consumers' financial interests. A crucial financial instrument, bank credit enables both people and companies to acquire capital for a variety of uses. Contrarily, consumer protection regulations aim to guarantee honest and open procedures in business dealings, reducing the likelihood of fraud and unethical activity. This summary examines the ways in which consumer protection laws control several components of bank credit, such as loan disclosures, interest rate transparency, terms and conditions, and fair lending practices. These rules seek to encourage responsible borrowing, discourage predatory lending, and provide customers accurate information. Notably, regulations like the Equal Credit Opportunity Act (ECOA) and the Truth in Lending Act (TILA) play a crucial role in promoting honesty and equity in credit transactions.

KEYWORDS:

Bank Credit, Consumer Protection Laws, Financial System, Indian Banking, Laws Regulations.

INTRODUCTION

Our lives depend heavily on banking in the fast-paced world of today. Understanding the laws and rules that control the Indian banking sector as well as our rights as customers are crucial. In order to protect your interests, this article seeks to provide you a thorough overview of the extent of Indian banking rules and regulations, as well as the consumer rights and safeguards in existence [1]–[3].

Indian Banking Laws and Regulations: Their Purposes

A strong regulatory structure that assures the stability, openness, and effectiveness of the financial system underpins the operation of the Indian banking industry. The official regulatory body in charge of monitoring and controlling the nation's banks and non-banking financial institutions is the Reserve Bank of India (RBI).

1. The main piece of law controlling banking in India is the Banking Regulation Act of 1949. It describes how banks are licensed, run, managed, and regulated. The statute gives the RBI the authority to provide instructions to banks and compel adherence to different legal criteria.
2. Reserve Bank of India Act, 1934: The RBI Act establishes the legal framework for the Reserve Bank of India's creation, operations, and authority. It gives the RBI the power to control India's monetary and credit system and preserve the stability of its financial markets.

3. The Negotiable Instruments Act of 1881 regulates the use and enforcement of instruments that may be exchanged for money, including checks, promissory notes, and bills of exchange. It defines the obligations and rights of the parties engaged in such transactions and offers legal redress in the event of breach or default.
4. The Foreign currency Management Act (FEMA) of 1999 governs international transfers of money and foreign currency transactions. It aspires to speed up international commerce and payments while preserving the rupee's stability and protecting the nation's foreign currency reserves.

Consumer protection and rights are addressed in Indian banking laws.

According to Indian law, you have certain rights and safeguards as a customer of financial services. The laws and rules below are designed to protect your interests and guarantee that banks and other financial organizations treat you fairly.

1. **Banking Ombudsman Scheme:** The RBI developed the Banking Ombudsman Scheme to provide banking clients access to a quick and effective grievance redressal process. Customers may use this system to report problems with banking services such checks that are not paid or are paid late, unlawful electronic cash transfers, and disregard for fair practices regulations. The Banking Ombudsman has the power to look into these complaints, address them, and, if necessary, punish institutions.
2. **Consumer Protection Act of 2019:** This comprehensive piece of law protects customers in a number of industries, including banking. It outlines consumer rights such the right to information, the right to make a decision, the right to a remedy, and the right to consumer education. Customers have the right, under this law, to complain to consumer forums and seek compensation for any loss or injury brought on by carelessness or a lack of quality in banking services.
3. **Fair Practices Code for Banks:** The RBI has published rules referred to as the Fair Practices Code, which mandates that banks use honest and open methods while interacting with clients. The code makes ensuring that banks educate clients accurately and promptly, protect the privacy of customer information, respond to complaints from customers quickly, and avoid unfair business practices like charging exorbitant fees or adding hidden expenses.
4. Banks are expected to abide by the Know Your Customer (KYC) rules in order to confirm the identity and address of their clients. These rules aid in the suppression of fraud, money laundering, and funding of terrorism. You have the right to knowledge as a consumer about the paperwork and information needed for

KYC adherence. Additionally, banks are expected to treat your personal information with secrecy and refrain from disclosing it to any parties unless legally compelled to do so.

DISCUSSION

Fair lending practices that support fair lending and guard clients against discriminatory practices

Fair lending procedures are essential for ensuring that all borrowers have access to credit and shielding customers from unfair business practices by banks and other financial institutions. To encourage fair lending and safeguard customers' rights, the following rules and regulations are in effect:

1. The Equal Credit Opportunity Act (ECOA) forbids creditors from treating credit applicants differently on the basis of things like race, color, religion, national origin, sex, marital status, age, or receiving government assistance. It guarantees that everyone has an equal chance to acquire credit and loans without coming up against unjustified prejudice or discrimination.
2. Rules from the Reserve Bank of India (RBI): To stop discriminatory lending practices, the RBI has issued rules to banks and other financial institutions. These regulations stress the need of banks treating all loan applicants equitably, without any discrimination based on individual traits or qualities. Banks must set clear, unbiased standards for assessing loan applications and make sure that judgments are made based on the applicant's ability to repay the loan and creditworthiness.
3. The Credit Information businesses (Regulation) Act, passed in 2005, governs how credit bureaus and credit information businesses (CICs) operate in India. Banks and other financial organizations may get credit reports from CICs, which also retain credit information on people. This law reduces the possibility of discriminatory lending practices by ensuring that credit choices are based on reliable and impartial information.

Indian Banking Laws to Protect Against Data Breach with Privacy and Data Security

Privacy and data security are crucial in the age of digital banking and online transactions. Banks and other financial organizations are in charge of preserving client data and preventing breaches or illegal access. To safeguard data security and privacy, the following policies and laws are in place:

1. The Information Technology Act of 2000 provides a legal foundation for data security and privacy in India. It contains clauses that deal with the acquisition, preservation, processing, and transfer of electronic data. The protection of client data from unauthorized access, disclosure, change, or destruction is a requirement for banks.
2. Guidelines from the Reserve Bank of India (RBI): The RBI has provided guidelines and instructions to banks about data security, cybersecurity, and information security. Strong information security frameworks, frequent risk assessments, incident response plans, and adherence to data protection guidelines are all requirements for banks.
3. A comprehensive framework for the protection of personal data in India is intended by the Personal Data Protection Bill, which is now up for discussion. The bill creates a data protection body to monitor adherence to data protection laws, provides standards for data processing, and specifies consent criteria. When this law is put into effect, it will make the banking sector's privacy and data security policies even stronger.

Addressing Complaints and Resolving Disputes with Indian Banking Laws: Complaint and Dispute Resolution Procedures.

Consumers have options for redress and dispute resolution in the case of a complaint or disagreement with a bank. Banks are obligated to set up efficient systems for resolving complaints and to respond quickly to client complaints. To handle grievances and conflicts, the following procedures and programs are in place:

1. **Banking Ombudsman Scheme:** As previously indicated, the RBI's Banking Ombudsman Scheme gives clients a way to complain against banks for providing subpar services. The program guarantees that complaints are resolved impartially and quickly via adjudication or conciliation.
2. **Banks are obligated** to establish grievance redressal cells in order to address client concerns. Customers may escalate their issues and look for a solution via these cells, which serve as a single point of contact. Banks are required to respond in writing to complaints from customers within a certain period and resolve them.
3. **Consumer Forums and Courts:** Customers have the option of turning to consumer forums or courts if a complaint goes unanswered if they are dissatisfied with the bank's response. Consumer forums provide a venue for consumers to file complaints and seek redress, such the District Consumer Disputes Redressal Forums, State Consumer Disputes Redressal Commissions, and National Consumer Disputes Redressal Commission.
4. **To ensure fair treatment, safeguard against discriminatory practices, and resolve complaints or disputes,** it is essential to be aware of your rights as a banking customer. In order to protect consumer interests and preserve confidence in the banking sector, rules and regulations have been put in place regarding fair lending practices, privacy and data security, and dispute resolution procedures. Being aware of these rights and available channels for complaint-handling as a consumer is crucial for enabling you to make wise choices and get help when you need it.

Every credit card user has to be aware of their rights while using a credit card. Many credit card users encounter situations where they believe their consumer rights have been violated. Even though applying for a credit card is often straightforward, many cardholders are uninformed of the consumer protections to which they are entitled. Many people struggle to identify the appropriate resources to help them and are unsure on what to do next [4]–[6]. Credit card fraud and the unauthorized use of cardholder information have increased significantly as a result of the coronavirus epidemic, which is driving the widespread usage of touchless and online payment methods like credit cards. Between 2019 and 2020, online credit and debit card fraud increased by 225%. The rights of credit cardholders are fortunately protected by a number of laws and RBI guidelines. These credit card consumer rights will guide you through a variety of situations, including erroneous invoicing, privacy invasions, credit card fraud, and inconsistent transactions. Because of this, it's even more important for credit cardholders to be aware of their rights and take precautions to avoid privacy violations, cyberattacks, OTP fraud, and other situations where their rights as cardholders might be infringed. In order to protect their interests in the event of a breach, credit card holders should be aware of the top 7 consumer rights related to credit cards.

You must be aware of these 7 credit card consumer rights.

1. Privateness Rights

Banks and NBFCs are prohibited by RBI regulations from issuing unauthorized credit cards to people without their express agreement. The RBI defends consumer rights by requiring banks and NBFCs to cancel any charges made on unauthorized credit cards. Additionally, the RBI holds them responsible by assessing a penalty fee equal to double the amount of the charges that were reversed. In a similar vein, in order to preserve the privacy of their current credit card users, banks and NBFCs are not permitted to provide credit or loan products to them without their express consent. In this situation, the institution that issues credit products would suffer consequences.

The RBI also requires that you be notified in advance and provided with the terms and conditions whenever a bank or an NBFC provides an upgrade on the credit card or increases the credit limit. The bank may upgrade the credit card or raise the credit limit after your approval. The Do Not Call Registry (DNCR), which holds the contact information of customers and non-customers who have agreed to not receive any marketing SMS or calls from the bank/NBFC, must be used by banks and NBFCs. According to the individual's DNCR permission, the banks and NBFCs must protect their privacy and make sure that their contact information is not given to unauthorized individuals or other parties for solicitation or abuse.

2. Fair methods for collecting credit card debt

For the purpose of collecting debt, the RBI requires that banks and NBFCs refrain from using violence, threats, harassment, or intimidation. Harassment of any individual (client or their family members) verbally or physically is forbidden. The RBI is absolutely against any actions by banks, NBFCs, or their representatives that breach a customer's privacy or degrade them. One of the essential consumer rights for credit card users that the RBI has provided them is this one.

3. Truthful and prompt billing

Customers may sometimes protest to a bill, even though banks and NBFCs make sure that the credit card invoices and statements issued are as accurate as feasible. Customers cannot be given unfair bills by banks or NBFCs. However, a client has the right to ask the bank for an explanation if they believe the credit card charge, they received is incorrect and incorrect.

In this scenario, the bank will have 60 days to respond to the customer's complaint by explaining the invoiced products, along with any appropriate papers. When credit card bills are created, the banks and NBFCs must make sure they are issued as quickly as feasible to the cardholder. This gives the credit card user plenty of time to pay off the balance without going into default. The ideal due payback date for banks and NBFCs is 21 to 25 days following the conclusion of a billing cycle and the cardholder's transmission of the statement.

4. Confidentiality

The banks and NBFCs are not allowed to disclose any information about the clients they get from them at the time of establishing the account or issuing the card in order to safeguard the

identity of the customer and preserve confidentiality. If banks and NBFCs disclose a customer's information to a third party, the customer's permission is required, and they must be made aware of how the third-party organization intends to use the information.

Customers need to be aware that banks and NBFCs may only report a credit card user as a defaulter after notifying them of the situation. The clients must be informed that they have a grace period during which they may pay their debts without being labeled defaulters once this has been explained to them.

Banks and NBFCs may only disclose information on a credit card holder who is in default on their payments if a proper procedure has been followed in order to satisfy confidentiality agreements. The rights of consumers using credit cards also prevent the transfer or unauthorized use of the information provided by a customer (income, job history, status, address, credit history, etc.) for marketing reasons.

5. Disputed credit card transactions are resolved

Due to things like improper debits, a broken PoS machine, wrong fees, a charge you don't recall making, non-delivery of the products, etc., you could often need to have a credit card transaction reversed. In these situations, the problem may be brought up with the card issuer as a "disputed credit card transaction." The consumer must complete a form for an inquiry into the transaction and attach pertinent documentation that establish the transaction is improper after raising it with the customer service team of the issuing authority. You have 60 days after receiving the credit card statement on which the dispute was discovered to take action.

Customers may still think about paying for the disputed transaction while it is being looked into. In the event that you win, you will get a complete refund. If the outcome is unfavorable and you haven't completed the payment by the deadline, interest may be added to the amount owed. In the event of credit card fraud, it can become necessary to engage the authorities in order to resolve the issues. If the disputed transaction is not resolved to your satisfaction, you have the option under the credit card consumer rights to contact the Banking Ombudsman to choose an alternative dispute resolution process.

6. Prior to receiving the card, you may be liable for credit card fraud.

You won't be held liable for fraudulent purchases if your credit card was used fraudulently even before you received it from the issuing authority. The fraudulent charges made with your card before you get the card, PIN, and welcome package won't be your responsibility.

7. Protection against banks charging excessive interest rates

Only when a cardholder fails to make their payments by the due date are banks and NBFCs required to assess interest to that cardholder. The Annual Percentage Rates (APR) on credit cards must be disclosed to the consumer. The computation of the APR, interest, and late payment fees for the past-due payment will be communicated to you. In the event that you make a partial payment toward an overdue payment, interest rates will be applied to the amount owed.

Apart from service fees and other taxes imposed directly by the government, banks and NBFCs are not permitted to impose any extra fees or interest without first informing cardholders like you. Any time interest rates change, banks and NBFCs are required to notify their clients at least one month in advance. If a cardholder wishes to return their card, neither banks nor NBFCs are permitted to levy a fee [7]–[9].

CONCLUSION

In conclusion, the complex interaction between bank credit and consumer protection legislation emphasizes the critical need for a balanced approach to increasing financial access and defending individual rights. Strong legislative frameworks are necessary to guarantee fair and moral behavior by financial firms as consumers increasingly depend on credit to satisfy their financial demands. Consumer protection regulations are essential for leveling the playing field, eliminating dishonest behavior, and fostering openness in the loan process. By ensuring that customers have access to correct information regarding terms, interest rates, and fees, these restrictions protect borrowers from exploitative practices. These rules encourage confidence in the financial system by keeping financial firms responsible and giving customers the freedom to make wise choices. The link between bank credit and consumer protection has taken on new dimensions as a result of recent developments in digital banking and fintech. As these technologies advance, it is more important to modify consumer protection legislation to handle new issues while fostering innovation. Finding this balance is crucial for advancing financial inclusion and reducing the hazards connected to online lending platforms.

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CHAPTER 19

BANK CREDIT DURING ECONOMIC DOWNTURNS: IMPACT AND RESPONSES

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ABSTRACT:

This study explores the dynamics of bank loans during economic downturns, looking at how they affect financial institutions and how different stakeholders react. The availability and use of bank loans are significantly impacted by economic downturns, which are defined by decreased economic activity and increased uncertainty. The study emphasizes how periodic economic downturns result in lower consumer and company expenditure, which forces banks to tighten lending standards and limit credit availability. Reduced bank lending during recessions may worsen the general slowdown in the economy, which may result in job losses, company closures, and financial hardship. It also looks at how governments and central banks react to lessen these consequences. To promote borrowing and lending, they often use strategies like decreasing interest rates, assisting banks with liquidity, and enacting stimulus packages.

KEYWORDS:

Bank Credit, Credit Crisis, Currency, Economy, Bank Loans, Short-Term Loans.

INTRODUCTION

Homes were bought and built with reckless borrowing by families, particularly in the US, who anticipated that home values would climb further. Property developers and families in European nations (such as Iceland, Ireland, Spain, and certain countries in Eastern Europe) similarly took on excessive debt due to similar expectations about home values.

A Credit Crisis: What Is It?

When the regular flow of currency that supports any economy is abruptly and severely disrupted, it causes a financial system to collapse. One of a number of cascading events that take place during a credit crisis is a scarcity of capital available for lending among banks.

Knowing about a Credit Crisis

There is a catalyst for a credit crisis. Think about the possible effects of a protracted drought that causes farmers to lose their harvest. They are unable to pay back their bank debts without the revenue from agricultural sales. The bank would run out of money without those loan payments and would have to drastically cut down on issuing new loans. The bank increases its borrowing in the short-term loan market since it still requires cash flow for its routine operations. But now that the bank itself has risen to the level of credit risk, other lenders have cut it off [1]–[3].

The flow of short-term loans, which fuels most of the business sector, starts to slow down as the crisis worsens. This procedure is necessary for businesses to continue functioning normally. The

financial system as a whole may suffer greatly if the flow suddenly stops. In the worst-case scenario, clients learn about the issue and rush the bank, causing it to run out of cash. In a little more optimistic scenario, the bank makes it through, but the whole economy, at least in this drought-stricken area, suffers since the bank's requirements for loan applications have grown so restrictive.

This situation is made more unlikely by protections in the contemporary financial system, such as the need that banks keep significant cash reserves. Additionally, the financial system has been concentrated into a few number of enormous international organizations, making it unlikely that a local drought could set off a crisis that affects the whole system. But such big institutions come with their own set of dangers. The government steps in at this point to save the "too big to fail" organizations.

The Credit Crisis of 2007–2008

The only significant credit crisis that most Americans can remember is likely the one that happened in 2007–2008. The financial crisis of 2007–2008 was a disaster for the ages. A national housing market bubble was the precipitating event. For years, home prices had been growing quickly. Speculators rushed in to purchase and resell homes. Renters were eager to purchase before their prices increased. Some others thought prices would keep going up forever. The prices then peaked in 2006 and began to drop.

Long before then, lenders and mortgage brokers had lowered their criteria to capitalize on the boom. Home purchasers took out loans well beyond what they could afford because they provided subprime mortgages. "Teaser" rates all but certain that they would fail within a few of years. The lenders' actions weren't detrimental to themselves. These subprime loans were not held on to; instead, they were sold so that they could be repackaged as mortgage-backed securities (MBS) and collateralized debt obligations (CDO), which were traded in the markets by institutions and investors.

The last purchasers, some of the largest financial institutions in the nation, were stranded when the bubble broke. Investors started to fear that those corporations had overstated their losses as the losses mounted. The corporations' own stock values started to decline. Inter-firm financing came to an end. The mortgage implosion and credit crunch conspired to create a crisis that paralyzed the financial sector just when it needed liquid money the most. An entirely human aspect, when dread escalated to panic, exacerbated the situation. Riskier stocks incurred significant losses while not being related to the mortgage industry. The Federal Reserve (Fed) was compelled to inject billions into the economy to preserve it since the situation was so serious, yet even so, The Great Recession still occurred.

The Financial Crisis in the World

The mid-2007 to early-2009 era of high stress in the world's banking institutions and financial markets is referred to as the global financial crisis (GFC). A decline in the US home market during the GFC served as the impetus for a worldwide financial crisis that expanded from the US via connections in the global financial system. Many banks experienced significant losses and

needed assistance from the government to stay afloat. As the main industrialized countries went through their biggest recessions since the Great Depression in the 1930s, millions of people lost their employment. Additionally, compared to other recessions that were not accompanied by a financial crisis, the recovery from the crisis was significantly slower.

Primary Roots of the GFC

As with other financial crises, a number of variables contributed to the GFC's severity, and the proportional weight of each cause is still up for debate. Among the crucial elements are:

1. Excessive risk-taking in a setting with a favorable macroeconomic climate

Economic circumstances in the US and other nations were favorable in the years before to the GFC. Strong and consistent economic growth was accompanied by low rates of unemployment, inflation, and interest. In this setting, home values climbed rapidly. Particularly in the United States, many mortgage loans were for sums that were comparable to (or even more than) the purchase price of a home. 'Subprime' borrowers (who have greater default risks due primarily to their income and wealth being relatively low and/or they have missed loan repayments in the past) and investors looking to make quick money by 'flipping' properties made up a significant portion of this hazardous borrowing.

For a variety of reasons, banks and other lenders were prepared to issue growing numbers of riskier loans:

- a. Lenders competed more fiercely to provide ever-larger house loans, which at the time seemed to be quite lucrative given the favorable economic climate.
- b. Many lenders that offered house loans did not carefully examine clients' capacity to repay their debts. This also demonstrated the popular expectation that the favorable circumstances would persist. Lenders also had no motivation to exercise caution when making loans since they did not anticipate suffering any losses. Instead, they offered investors a sizable number of loans, often packaged into securities known as "mortgage-backed securities" (MBS) and made up of thousands of different home loans of variable quality. MBS products became more complicated and opaquer over time, yet external organizations maintained to assess them as being very safe.
- c. Investors who bought MBS packages believed they were purchasing a very low risk asset since it was expected that most mortgage loans in the package would continue to be repaid, even if some of them were not. Large US banks as well as international banks from Europe and other nations that desired larger profits than could be attained in their own markets were among these investors.

2. Increased borrowing by investors and banks

Up to the Great Financial Crisis, banks and other investors in the US and overseas borrowed more money to increase their lending and buy MBS securities. As a consequence, when housing values started to decline, banks and investors suffered significant losses because they had taken on so much debt, which increases possible profits but also increases potential losses[1].

In addition, banks and certain investors borrowed money for longer and longer periods of time, often overnight, to buy assets that were difficult to sell. As a result, they were forced to depend more and more on lenders, including other banks, who provided new loans when old short-term loans were returned.

3. Errors in regulations and policy

MBS products and subprime loans were subject to too little regulation. Particularly, there was little oversight of the organizations that produced and offered investors sophisticated, opaque MBS. Not only were many individual borrowers given loans that were too big for them to manage, but fraud was also becoming more prevalent. Examples include exaggerating a borrower's income and misleading investors about the security of the MBS products they were being offered. Additionally, many governments and central banks failed to properly comprehend the degree to which subprime loans had been extended during the boom and the many ways in which mortgage losses were spreading across the financial system as the crisis developed.

How the GFC Began

US home values dropped, and borrowers failed to make payments

Falling US home values and an increase in the number of borrowers unable to service their loans served as the GFC's drivers. When the supply of newly constructed homes in certain places began to rise quickly in the middle of 2006, house prices in the United States reached their pinnacle. The percentage of borrowers who defaulted on their loans started to increase as housing values started to drop. Because the share of American families (including owner-occupiers and investors) with huge loans had increased significantly during the boom and was larger than in other countries, loan repayments were especially sensitive to housing prices in the US [4]–[6].

Financial system tensions

Around the middle of 2007, the financial system's stresses started to become apparent. Because many of the homes they confiscated after the borrowers missed installments could only be sold at prices below the loan total, several lenders and investors started to suffer significant losses. In a similar vein, investors aggressively sought to sell their holdings and were less eager to buy MBS securities. The value of MBS and, therefore, the net worth of MBS investors decreased as a consequence of the reduction in MBS prices. In turn, investors who had acquired MBS using short-term loans discovered that it was harder to refinance these loans, which increased MBS selling and price reductions.

Spillover effects to other nations

In addition to acquiring MBS (with short-term US dollar finance), foreign banks participated actively in the US housing market throughout the bubble, as was already mentioned. There were significant activities by US banks abroad. These ties made it possible for issues with the US housing market to spread to the financial and economic systems of other nations.

Financial businesses failing, fear in the markets

Following the collapse of the US financial institution Lehman Brothers in September 2008, financial tensions reached their height. This, along with a number of other financial institutions that failed or came close to failing at that time, caused a panic in financial markets all around the world. Due to uncertainty about who would be the next financial institution to collapse and the exposure each institution had to subprime and other troubled loans, investors started to withdraw their money from banks and investment funds all around the globe. As a result of everyone trying to sell at once and many institutions being unable to get fresh funding, financial markets became chaotic. As confidence fell, businesses and people both were far less eager to invest and spend. Because of this, the US economy and that of several other countries had their worst recessions since the Great Depression.

Policy Reactions

Up until September 2008, central banks' interest rate cuts to boost the economy when it slowed in late 2007 were the primary policy reaction to the crisis. However, with Lehman Brothers' demise and the slowdown in global development, the policy reaction accelerated.

Decreased interest rates

Once policy interest rates were close to zero, central banks quickly reduced interest rates to extremely low levels, frequently near zero, lent large sums of money to banks and other institutions with strong assets but no access to the financial markets, and bought a sizable quantity of financial securities to support broken markets and boost economic activity (a process known as "quantitative easing").

Expenditure increases by the government

Governments increased spending to support employment across the board and boost demand; they also guaranteed bank deposits and bank bonds to boost public confidence in financial institutions; they also bought stock in some banks and other financial institutions to avoid bankruptcies that might have exacerbated the panic on the financial markets.

Despite the greatest contraction in the world economy since the Great slump, a worldwide slump was avoided thanks to the governmental response. Nevertheless, countless numbers of individuals lost their homes, jobs, and substantial sums of money. Additionally, compared to prior recessions without a financial crisis, many economies recovered from the Great Financial Crisis significantly more slowly. For instance, it took almost nine years from the start of the crisis for the US jobless rate to reach pre-crisis levels in 2016.

Stronger regulation of financial institutions

Regulators increased their supervision of banks and other financial institutions in reaction to the crisis. Banks must now more carefully evaluate the risk of the loans they are making and employ more robust financing sources, among other new international laws. For instance, banks are no longer permitted to support the loans they make to their clients with as many short-term loans and must instead operate with reduced leverage. Additionally, regulators are increasingly aware

of the ways in which risks may spread across the financial system and demand that measures be taken to stop this from happening.

DISCUSSION

The GFC and Australia

Relative economic performance

During the GFC, Australia did not endure a significant economic or financial crisis. However, there followed a time of increased uncertainty, a steep increase in the unemployment rate, and a noticeable slowdown in the rate of economic growth. When compared to other nations, Australia's economy and financial system fared quite well throughout the GFC. A number of factors contributed to this, including:

- a. Due in part to the lucrative local lending market, Australian banks had relatively little exposure to the US housing market and US banks.
- b. Due in part to the Australian banking regulator's past emphasis on lending criteria (the Australian Prudential Regulation Authority (APRA)), subprime and other high-risk loans made up a very tiny portion of total lending in Australia.

Large resource exports to China, whose economy swiftly recovered following the first shock of the GFC (mostly due to expansionary fiscal policies), boosted Australia's economy.

The Impact of the Great Recession 2007-

The economic crisis of 2007–2009 was severe and prolonged enough to earn the moniker "the Great Recession," and it was followed by a recovery that, by some standards, was lengthy but extremely sluggish. When the US housing market's decade-long rise peaked in 2006 and residential development started to decline, the so-called "Great Moderation" came to an end. Losses on mortgage-related financial assets started to put pressure on international financial markets in 2007, and the US economy entered a recession in December of the same year. That year, a number of big financial institutions went through financial difficulties, and there was tremendous volatility throughout several financial markets. The Federal Reserve responded by offering liquidity and support through a variety of programs in an effort to enhance the efficiency of financial markets and institutions and lessen the impact on the US economy. However, in the fall of 2008, the economic contraction grew worse, eventually becoming severe and prolonged enough to be known as "the Great Recession." While the US economy peaked in the middle of 2009, the recovery in the following year was uneven.

Changes in the Housing Market

Average home prices in the US more than doubled between 1998 and 2006, the sharpest increase recorded in US history, and even larger gains were recorded in some regions. Home ownership in this period rose from 64 percent to 76 percent. The recession and crisis followed an extended period of expansion in US housing construction, home prices, and housing credit. This expansion started in the 1990s and continued unabated through the 2001 recession, accelerating in the mid-2000s.

The expansion in the housing sector was accompanied by an expansion in home mortgage borrowing by US households. Mortgage debt of US households rose from 61 percent of GDP in 1998 to 97 percent in 2006. A number of factors appear to have contributed to the growth in home mortgage debt. In the period after the 2001 recession, the Federal Open Market Committee (FOMC) maintained a low federal funds rate, and some observers have suggested that by keeping interest rates low for a “prolonged period” and by only increasing them at a “measured pace” after 2004, the Federal Reserve contributed to the expansion in housing market activity (Taylor 2007). However, other analysts have suggested that such factors can only account for a small portion of the increase in housing activity (Bernanke 2010).

Moreover, the historically low level of interest rates may have been due, in part, to large accumulations of savings in some emerging market economies, which acted to depress interest rates globally (Bernanke 2005). Others point to the growth of the market for mortgage-backed securities as contributing to the increase in borrowing. Historically, it was difficult for borrowers to obtain mortgages if they were perceived as a poor credit risk, perhaps because of a below-average credit history or the inability to provide a large down payment. But during the early and mid-2000s, high-risk, or “subprime,” mortgages were offered by lenders who repackaged these loans into securities. The result was a large expansion in access to housing credit, helping to fuel the subsequent increase in demand that bid up home prices nationwide.

The Financial Sector's Impact

After home prices peaked in the beginning of 2007, according to the Federal Housing Finance Agency House Price Index, the extent to which prices might eventually fall became a significant question for the pricing of mortgage-related securities because large declines in home prices were viewed as likely to lead to an increase in mortgage defaults and higher losses to holders of such securities. Large, nationwide declines in home prices had been relatively rare in the US historical data, but the run-up in home prices also had been unprecedented in its scale and scope. Ultimately, home prices fell by over a fifth on average across the nation from the first quarter of 2007 to the second quarter of 2011.

This decline in home prices helped to spark the financial crisis of 2007-08, as financial market participants faced considerable uncertainty about the incidence of losses on mortgage-related assets. In August 2007, pressures emerged in certain financial markets, particularly the market for asset-backed commercial paper, as money market investors became wary of exposures to subprime mortgages. In the spring of 2008, the investment bank Bear Stearns was acquired by JPMorgan Chase with the assistance of the Federal Reserve. In September, Lehman Brothers filed for bankruptcy, and the next day the Federal Reserve provided support to AIG, a large insurance and financial services company. Citigroup and Bank of America sought support from the Federal Reserve, the Treasury, and the Federal Deposit Insurance Corporation.

The Fed also introduced a number of new lending programs that provided liquidity to support a range of financial institutions and markets, including a credit facility for “primary dealers,” the broker-dealers that serve as counterparties for the Fed's open market operations, and lending programs designed to provide liquidity to monetarily depressed areas.

In order to avoid an increase in bank reserves that would drive the federal funds rate below its target as banks sought to lend out their excess reserves, the Federal Reserve initially financed the expansion of Federal Reserve credit by reducing its holdings of Treasury securities. However, in October 2008, the Federal Reserve gained the authority to pay banks interest on their excess reserves, giving banks an incentive to hold onto their reserves rather than lending out their excess reserves.

Impacts on the General Economy

Residential investment peaked in 2006, as did employment in residential construction, and the overall economy peaked in December 2007, which the National Bureau of Economic Research identifies as the start of the recession. The decline in overall economic activity was initially modest, but it steepened sharply in the fall of 2008 as stresses in financial markets roiled the economy. As the financial crisis and the economic contraction worsened in the fall of 2008, the FOMC accelerated its interest rate cuts, taking the rate to its effective floor a target range of 0 to 25 basis points - by the end of the year. In November 2008, the Federal Reserve also initiated a rate cut of its own, taking the federal funds rate from 4.5 percent at the end of 2007 to 2 percent at the beginning of September 2008.

The recession ended in June 2009, but economic weakness persisted. Economic growth was only moderate averaging about 2 percent in the first four years of the recovery and the unemployment rate, particularly the rate of long-term unemployment, remained at historically elevated levels. In the face of this prolonged weakness, the Federal Reserve maintained an exceptionally low level for the federal funds rate target and sought new ways to provide additional monetary accommodation. These included additional LSAP programs, known more popularly as quantitative easing, or QE. The FOMC also began communicating its intentions for future policy settings more explicitly in its public statements, particularly the circumstances under which exceptionally low interest rates were likely to be appropriate. For example, in December 2012, the committee stated that it anticipates that exceptionally low interest rates would likely remain appropriate at least as long as the unemployment rate was above a threshold value of 6.5 percent and inflation was expected to be no more than a half percentage point above the committee's 2 percent longer-run goal. This strategy, known as "forward guidance," was intended to convince the public that rates would stay low at least until certain economic conditions were met, thereby putting downward pressure on longer-term interest rates.

Financial Regulation Effects

For traditional banks, there are significant increases in the amount of required capital overall, with larger increases for so-called "systemically important" institutions. After the financial market turmoil subsided, attention naturally turned to reforms to the financial sector and its supervision and regulation, motivated by a desire to prevent similar events in the future.

The Financial Stability Oversight Council has the authority to designate nontraditional credit intermediaries "Systemically Important Financial Institutions" (SIFIs), which subjects them to the supervision of the Federal Reserve. The Dodd-Frank Act of 2010 also created new provisions for the treatment of large financial institutions, such as the Orderly Liquidation Authority (OLA),

which permits the Federal Deposit Insurance Corporation to wind down. While it may be many years before the causes and effects of the financial crisis of 2008 and the ensuing recession are fully understood, the effort to untangle them is an important opportunity for the Federal Reserve and other agencies to learn lessons that can guide future policy. The financial crisis of 2008 and the ensuing recession are vital areas of study for economists and policymakers, similar to the Great Depression of the 1930s and the Great Inflation of the 1970s [7]–[9].

CONCLUSION

In conclusion, the complex relationship between bank lending and economic downturns highlights the crucial role that credit plays in determining an economy's course during a crisis. The availability and use of bank loans change significantly when economic activity declines and uncertainty rises. The difficulties brought on by economic downturns may be made even more difficult by the decline in credit availability, thereby prolonging recessions and delaying recovery. The reactions to these difficulties, however, are as remarkable. The proactive steps taken by governments and central banks to reduce interest rates, provide liquidity to financial systems, and enact stimulus packages show that they are aware of the critical role that credit plays in preserving economic stability.

These solutions seek to stimulate demand, support economic activity, and rebuild trust in financial institutions by making borrowing and lending easier. A guiding concept for both financial firms and regulators is the control of risk. It becomes difficult to strike a balance between the need to help the recovery and sound lending standards. It is crucial to make sure that banks' increased caution about credit risks does not unintentionally impede the availability of loans to creditworthy customers.

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CHAPTER 20

ROLE OF CENTRAL BANKS IN REGULATING BANK CREDIT

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ABSTRACT:

This study offers a succinct review of the crucial function that central banks perform in controlling bank lending, highlighting its importance in preserving financial stability and directing economic development. The primary institutions in charge of monitoring and regulating the credit operations of commercial banks within an economy are central banks. This study explores the several duties that fall within the purview of central banks, including monetary policy formulation, interest rate management, and money supply regulation. The availability and cost of credit in the financial system are influenced by central banks through a variety of instruments, including open market operations, reserve requirements, and discount rates. By prohibiting excessive credit growth that might cause inflation, this policy also seeks to lessen the dangers of credit bubbles and financial catastrophes. The study also highlights the precarious balancing act central banks must do in order to promote lending for economic development while limiting overleveraging that might cause instability. Policymakers, financial institutions, and the general public may better grasp the complicated dynamics that support a stable and resilient financial system by being aware of the complex role that central banks play in controlling bank loans.

KEYWORDS:

Bank Loans, Central Banks, Commercial Banks, Currencies, Financial System, Regulating Bank Credit.

INTRODUCTION

As the "lender of last resort," a central bank is in charge of financing the country's economy in the event that commercial banks are unable to fill a funding gap. In other words, the central bank guards against the collapse of the nation's financial system. However, central banks' main objective is to keep inflation under control in order to maintain the value of the national currencies. The only producer and printer of notes and coins used in circulation, the central bank also oversees the nation's monetary policy. Time has shown that the central bank can perform these functions most effectively when it is free from the fiscal policies of the government and, therefore, from the political considerations of any regime. Also, all commercial banking holdings should be entirely sold off by a central bank.

The Work of Central Banks

Globally, central banks are charged with a number of significant duties. The first and maybe most obvious job is the creation of money. Central banks produce money, which is subsequently used by individuals, families, and corporations to conduct transactions and, basically, monitor where money is being spent. Additionally, central banks are responsible for ensuring the stability

of the financial systems in their respective economies. To do this, they must continuously monitor lending standards across the economy and guarantee that credit is available when needed. In such situation, they also serve as the government and commercial banks' last-resort lenders. Therefore, the central bank may act as the government's lender of last choice when there is no other option or avenue for the government to get the cash it needs [1]–[3].

What function do central banks serve?

One of the main tasks of central banks is to watch and monitor economic data, and economists utilize this role to find out what the leading expert on the subject will have to say. For instance, the Bank of England publishes its quarterly inflation report, which includes comments on current macroeconomic trends as well as other information on GDP, growth predictions, and inflation forecasts. The Federal Reserve, the central bank of the United States, also achieves this by using a "dot plot," or an economic prediction chart with forward-looking dots, to depict where the Federal Reserve anticipates interest rates will go.

And that brings us to the last duty of central banks everywhere, which is to formulate monetary policy. Setting interest rates is the most important weapon in the arsenal of monetary policy's many separate instruments. For consumers, corporations, and any other sector of the economy that requires a loan, lower interest rates represent greater access to credit. Higher interest rates have the opposite effect, making credit more costly and difficult to get. Central banks must cut interest rates during difficult economic times and periods of slower economic development to ensure that the economy has easier access to credit. In the present (November 2018), two instances of such are the UK maintaining low interest rates as Brexit uncertainty develop, and the US central bank beginning to raise interest rates due to the strong economic performance. Additionally, we see the Chinese central bank lowering the interest rate in China to maintain the country's economy in response to slower global commerce and higher export duties worldwide.

As a result, central banks from all over the globe are operating in various macroeconomic conditions and will respond in a certain manner to ensure that their own economies are doing as they would want. Due to the many economic data that central banks create, they are able to monitor inflation and price stability in order to determine the appropriate interest rate. Many central banks have mandates or objectives, the majority of which involve price stability, which is inflation.

The Development of Central Banks

Some can claim that since the Bank of England was founded in 1694, the central bank's function has grown historically. However, it is widely acknowledged that the modern central bank idea did not emerge until the 20th century, in reaction to issues with commercial banking systems. Because there was a finite supply of gold between 1870 and 1914 when international currencies were tied to the gold standard (GS), maintaining price stability was much simpler. As a result, it was simpler to manage inflation since monetary growth could not be caused by a political decision to simply print more money. At that time, the central bank, which produced notes based on a country's gold holdings, was in charge of ensuring the convertibility of gold into currency. The GS was abandoned with the start of World War I, and it soon became clear that in

times of crisis, governments with budget deficits (because fighting a war costs money) and a need for extra resources would order the printing of more money. Governments ran into inflation as they did this. Many governments chose to return to the GS after the war in an effort to balance their economies. As a result, the significance of the central bank's independence from any political party or government increased.

A return to a central bank that was reliant on political decision-making was largely supported by global governments during the tumultuous periods of the Great Depression and the years after global War II. This viewpoint developed mostly as a result of the necessity to regain control over economy that had been devastated by war. In addition, newly independent nations chose to maintain control over every element of their country as a reaction to colonialism. Government intervention in the macro economy expanded as controlled economies proliferated in the Eastern Bloc. In Western nations, however, the central bank's autonomy from the government eventually regained popularity and emerged as the best strategy for establishing a liberal and stable economic system.

What Effect the Central Bank Has on the Economy

In order to control inflation and maintain price stability, a central bank performs macroeconomic tasks. It also performs microeconomic activities by acting as a lender of last resort.

The macroeconomic environment

The central bank, which is in charge of maintaining price stability, must manage the amount of inflation by limiting the supply of money via monetary policy. Their activities immediately affect the mood of the market. The amount of inflation is directly impacted by the central bank's open market operations (OMO), which either provide liquidity to the market or absorb surplus money.

The central bank may purchase government bonds, notes, or other forms of currency in order to boost the quantity of money in use and lower borrowing costs. However, this purchasing may also result in rising inflation. The central bank will sell government bonds on the open market when it needs to absorb funds to lower inflation, which raises interest rates and deters borrowing. A central bank's primary tools for managing the money supply, prices, and inflation are open market operations [4]–[6].

DISCUSSION

Microeconomic Factors

The necessity for central banks' independence from commercial banking has been pressed by their formation as lenders of last resort. Money is made available to customers by a commercial bank on a first-come, first-served basis.

Commercial banks may resort to the central bank to borrow more money if they do not have enough liquidity to satisfy their customers' requests (commercial banks often do not keep reserves equivalent to the requirements of the whole market). As a result, the system is objectively stable since central banks are unable to favor any one commercial bank. As a result, many central banks will maintain commercial-bank reserves that are calculated as a percentage

of the deposits of each commercial bank. So, a central bank may mandate that all commercial banks maintain, say, a reserve/deposit ratio of 1:10 at all times. Another way to manage the market's money supply is to enforce a policy of commercial bank reserves. However, not all central banks demand reserves from commercial banks. For instance, the United Kingdom does not, although the United States has customarily done so. Although, the U.S. During the 2020 COVID-19 pandemic, the Central Bank reduced its reserve requirements to zero percent as of March 26, 2020. The discount rate, which is determined by the central bank and serves as a benchmark for interest rates, is the cost at which commercial banks and other lending institutions may get short-term cash from it. It has been suggested that in order for open market transactions to become more efficient, the banks should be prevented from borrowing money indefinitely by the discount rate. If they did, the market's money supply and the central bank's monetary policy would be disrupted. The commercial bank will be pumping additional money into the system by taking on excessive debt. It is possible to limit the usage of the discount rate by making it undesirable when applied frequently.

Temporary Economies

Today's emerging nations must deal with problems like the transition from controlled to free market economies. Controlling inflation is often the key priority. Given that many emerging countries wish to keep control of their economy, this may result in the establishment of an independent central bank, although it may take some time. Government interference, however, whether direct or indirect via fiscal policy, may impede the growth of central banks.

Unfortunately, civil unrest or conflict plague many emerging countries, forcing governments to redirect resources away from the expansion of the national economy. The need for a stable currency (whether achieved through a fixed or floating exchange rate) is nevertheless one factor that appears to be confirmed; however, central banks in both industrial and emerging economies are dynamic because there is no certain way to run an economy, regardless of its stage of development.

Are government banks central banks?

Many central bank posts may be chosen by the government, and they are obligated to adhere by the law, just as they are protected by it. Central banks are often not government institutions and function independently of the government.

What Are the Central Bank's Primary Functions?

A central bank's primary responsibilities are to influence monetary policy, act as the lender of last resort, and regulate the banking sector. Interest rates are established by central banks, who also manage the money supply and lend to other banks.

How Does the Federal Reserve Get Its Money?

Interest on the securities it holds provides the Fed with the majority of its funding. Additionally, it is financed by fees for services like check clearing, cash transfers, and automated clearing house (ACH) activities that are offered to depository institutions at a cost. It is not supported by funds from Congress.

The inference

Along with a host of other duties, central banks have control over a country's (or a group of countries') monetary system. These duties vary from monitoring monetary policy to carrying out particular objectives including achieving currency stability, low inflation, and full employment. Over the last century, the central bank's position has become more significant. The central bank should be the governing body and authority in the banking and monetary systems in order to maintain the stability of a nation's currency.

Although they are controlled by the government, modern central banks are independent of their nation's ministry or department of finance. Political choices should not have an impact on central bank activities, despite the fact that the central bank is commonly referred to as the "government's bank" since it handles the buying and selling of government bonds and other securities. It goes without saying that the nature of the connection between the central bank and the governing regime differs from nation to nation and changes with time.

Central Bank's Purposes

Only after learning a little bit about the Central Bank itself will the functions of the Central Bank become much more evident. In addition, the Central Bank serves as a governing body and is controlled by the government. In other terms, the Central Bank is a financial organization in charge of controlling the amount of money available on the market. The Central Bank also oversees the commercial banking industry as well as a state's currency and interest rates.

Central Bank introduction

The Central Bank is the leading organization that supports the best control of money movement inside a market. However, it also serves as a lending hub for the banking industry in times of financial crisis. Most Central Banks have the crucial and obligatory duty of Refusing to tolerate fraudulent conduct by other member banks and discouraging it.

- a. Making sure that the other banks have the ability to be solvent
- b. Stopping bank runs

The political and governmental structure of an economy often maintains a close eye on the Central Bank's operations. Many developing and established economies' central banks, however, are immune to political interference. They are then free to make judgments on their own without having to answer to a superior authority.

Central Bank's Purposes

Issuers' Bank

The Central Bank is the only institution with the exclusive power to print money. Additionally, they are in charge of producing, minting, and distributing money into the economy legally. Though great power comes responsibility and a lot of accountabilities. Therefore, regulating elasticity, maintaining consistency, and providing oversight all fall within the purview of the Central Bank.

Cash Reserves Holder

Being the keeper of money is one of the Central Bank's most important roles. Additionally, banks reserve a portion of their deposits with the central bank in every nation. As a result, the central bank is the only legitimate and secure party to keep cash reserves.

Consultant to the Government

According to reports, the government considers the central bank to be the most reliable bank. The government also trusts the central bank to advise them in times of financial and monetary crises. The central bank also receives deposits, conducts payments, and manages a nation's finances. Consequently, the government owns the central bank:

- a. Consultant
- b. Agent
- c. Banking
- d. Last-Ditch Lender

The central bank is prepared to intervene when a bank's operations seem to be failing and underperforming. In other words, commercial banks turn to their final option when they are unable to recover from a crisis. The last resort in terms of money is one of the central bank's most significant roles in this situation.

Keeper of reserves in foreign currency

It is common knowledge that the central bank maintains currency reserves. It is only right, secure, permitted, and most appropriate for the central bank to function as the repository for foreign exchange reserves. Moreover, the government may guarantee economic discipline by designating the central bank as the official foreign currency holder.

Credit Manager

Throughout their activities, commercial banks generate a significant amount of credit. However, this credit may be one of the most important and primary causes of inflation in a given country. A regulating body is necessary in this situation to keep an eye on the loan rates. As a result, the central bank works to manage and alter loan rates as well as to control inflation [7]–[9].

Defender of the Interests of the Depositor

The depositors of the central bank are quite diverse. The government and commercial banks are two of the most significant depositors. Protecting the interests of its customers is one of a central bank's most important duties.

CONCLUSION

In conclusion, financial stability and economic health are largely dependent on central banks' capacity to control bank loans. Central banks have a tremendous impact on the credit environment via their complex web of regulations and monitoring, assuring ethical lending practices and preserving the integrity of financial institutions. The cost and accessibility of credit may be influenced by central banks via the careful use of monetary policy instruments including

interest rate setting and open market operations. The cyclical pattern of credit growth and contraction may be mitigated by central banks by manipulating these levers, which can either stimulate or constrain lending. In addition, central banks have a responsibility in overseeing and regulating the banking industry. Central banks aim to reduce systemic risks and stop excessive credit creation that might cause financial instability via strict prudential rules, stress testing, and capital adequacy requirements. The idea of the lender of last resort emphasizes the crucial role that central banks play in times of crisis. Central banks may avoid potentially disastrous economic downturns by restoring trust in the banking sector and preventing credit crunches by providing emergency liquidity to financial firms.

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CHAPTER 21

CREDIT TERMS AND CONDITIONS: UNDERSTANDING THE FINE PRINT OF CREDIT AGREEMENTS AND CONTRACTS

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ABSTRACT:

This study explores the necessity of understanding the complex nuances of credit agreements and contracts, highlighting how crucial it is to read the small print. Credit terms and conditions have a significant impact on how lenders and borrowers interact financially. These conditions include a wide range of essential elements, such as interest rates, repayment plans, fees, fines, and other stipulations that may have a significant influence on the financial stability of both parties. Credit agreements sometimes include complex clauses and subtle terminology in the small print that could escape cursory inspection. However, in order to prevent such hazards, borrowers must do thorough and well-informed research. Unfavorable results, such as unforeseen fees and higher interest rates as well as stretched credit records, might result from a misinterpretation or neglect of these terms.

KEYWORDS:

Agreement, APR, Credit Card, Fine Print, Interest Rates, Terms Conditions.

INTRODUCTION

The small print of credit card agreements is infamous for including "surprise" fees, interest rates, and payment conditions. The fine print may include information that is mandated by law or that a company's legal staff feels is important. For instance, crucial financial details on a credit card agreement may be found in the fine print, including the annual percentage rate (APR), introductory rate, length of the introductory period, APR for cash advances and balance transfers, annual fee, and late payment penalties.

What does it mean to "read the fine print"?

To read the fine print is to be aware of every aspect. Not only the bolded, overtly commercial writing, but also the little print at the bottom. A contract contains a lot of information, and it often uses crucial phrases. Companies are obligated by law to disclose certain conditions. You must comprehend and accept those conditions as a customer. You can grasp the specifics, conditions, restrictions, and limits of an agreement by reading the small print.

These specifics have an impact on a financing agreement's timeliness, disputes, interest, and payback conditions. The print for these items is quite tiny, making them simple to overlook. This is particularly true if you are eager to accept the offer and sign without carefully reading the contract. In fact, this is where the adage "always read the fine print" originated.

Who truly reads the little print?

Many individuals fail to read the small print when it comes to the terms and conditions for a service or online platform. The same holds true for all other types of contracts, including financial contracts. Many people would prefer not to think about legal language because they find it intimidating, particularly when it is long. Alternately, some people may not understand the significance of reading the small print.

It then becomes a matter of whether you should really read the small print. The reply is that it depends. The terms and conditions definitely don't need to be read in their full if you're just setting up a new Instagram account. But what if you're approving a new loan agreement? To fully comprehend the conditions, the amount of the payback, any possible penalties, and the consequences for early repayment, you should definitely read the whole agreement. In the end, it all comes down to what you're agreeing to and how the deal will influence your life and money [1]–[3].

Fine Print: What is it?

The phrase "fine print" refers to contract terms and conditions, disclosures, or other significant information that is included in footnotes or a supplementary document and is not presented in the main body of the document. When signing a contract, it's important to read and comprehend the whole document. Frequently, it includes information that the issuer does not wish to draw the recipient's attention to but that the recipient must be aware of.

Recognizing small print

In order to fully comprehend the terms of the contract or the information given, it is crucial to read the small print. Sometimes the small print may not be deemed appealing, so the contract's authors bury it rather than place it front and center, making it challenging and confusing for a person to understand what they are signing up for. As an example, someone may sign up for a gym membership, but after three months of not utilizing it, they decide to cancel it to save money. When they seek to cancel it, they are informed that their membership is contractual for 12 months, a clause that was not made explicit to the person signing the contract but was contained in the small print.

As another illustration, if an investor reads the financial report of a publicly traded company, the investor may need to read the fine print to learn about the company's accounting practices, long-term debt, employee stock ownership, or ongoing litigation to get a clearer picture of how the numbers are created and whether they are actually comparable to their peers.

Objections to Fine Print

As a result of its misleading nature, fine print is often contentious. The intention of the fine print is to deceive the reader into thinking the offer is better than it really is. Although the actual parameters of the offer are officially disclosed in the advertisement's smaller print, which ensures convincing denial against fraud allegations, this smaller print is often intended to be ignored by the viewer. Due to time restrictions and/or personal demands, the unwary reader may choose not to read the small print after being drawn in by the alluring features of the offer. Another

misconception among readers is that smaller type isn't as significant as bigger print. Many heavily regulated industries, including banking and financial services, complain about too stringent regulations that force them to write their paperwork in legalese. Anyone who has had a traditional mortgage is aware of the importance that the loan paperwork's small print adds to them.

Despite good intentions, the many phrases and caveats make it challenging to understand and be transparent. Even if someone reads the small print, the phrase may be intentionally difficult to grasp. To obtain a better understanding of what they are signing up for, people should always make a list of questions and ask them directly before committing.

Typical Terminology for Financing Legal Agreements

You should be aware of the typical terminology used in loan proposals and agreements. Particularly for the novice reader, the language employed in contracts and agreements may be difficult to understand. Learn the important terms and expressions given below. This will make it easier for you to comprehend various financial contracts. Do a fast Google search or get advice from an expert if you come across anything that you are unable to comprehend on your own.

- a. **Rates Increasing:** This usually specifies the circumstances under which a creditor may increase interest rates. If the interest rate fluctuates, you can anticipate seeing something similar to the basic prime rate plus an additional rate. However, if it is fixed, the requirements for raising the rate should be clearer. Generally, missing payments or failing to adhere to the conditions as stated might result in lenders raising rates. Increased interest rates are subject to restrictions that specify how many missing payments will trigger an increase.
- b. **Daily Average Balance:** Interest and other bank fees are calculated using the average daily balance. The number is often based on the average balance of each day over the course of a calendar month, although it might vary. Deposit interest and additional fees are calculated after that.
- c. **Grace Period:** The interval of time before interest starts to accumulate is known as a grace period. This usually takes 20 to 25 days. Although you could see it elsewhere, credit card agreements are where it is most often encountered.
- d. **Annual Percentage Rate (APR) by default:** Interest rates increase to the default APR if a financing agreement's terms have been broken. You typically pay the normal APR, which is the interest rate you initially committed to. As a penalty, a higher interest rate known as a default APR is applied. For instance, the default APR may be 5% points higher, at 24.99%, if your usual APR rate was 19.99%.
- e. **Beginning Rate:** Introductory rates are offered by certain credit card providers as a marketing strategy to attract new customers. For a certain amount of time, they provide new purchases at a cheaper rate than usual. With a balance transfer, comparable results may be seen. Prior to signing, it is essential to understand the term and interest rate before and after the introduction period.

DISCUSSION

Interest costs and rates of interest

You may learn about the various interest rates associated with your card here, as well as how to prevent them.

- a. **APR:** If you are unable to make a complete payment at the end of each pay period, this rate will be added to your outstanding debt. You'll also see how the issuer determines the rate since most credit card APRs are variable and fluctuate with the prime rate (for instance, your purchase APR is the prime rate + 11.99%). Here you may find out how long your card's introductory APR of 0% will remain if you have one. The interest rate you'll pay if you opt to transfer a credit card debt is known as the balance transfer APR. Similar to purchases, you may check your card's balance transfer APR, the rate going forward, and the eligibility restrictions (such as transferring within the first 90 days) to determine whether there is an introductory deal.
- b. **Cash advance APR:** This is the interest rate you'll pay if you use your credit card to get a short-term loan for cash. These rates often start immediately (i.e., without a grace period) and are ordinarily higher than those for transfers and purchases. One of the most important numbers on every credit card deal is the penalty APR. This may be more than the top end of your card's ordinary variable APR and is often applied by issuers as a penalty for late **payments**.
- c. **How to prevent paying interest on purchases:** The grace period is the number of days between the end of your billing cycle and the date your payment is due. It is provided to you in this line. You won't pay interest if you settle your account within this time frame.
- d. **Minimum interest fee:** Some credit cards have minimum interest fees. If a credit card offers interest, it will be made clear here, often in the form of "If you are charged interest, it will be no less than \$0.50."

Payments: The nuances

The payment distribution section in your agreement's small print explains how your minimum payments are distributed among the various categories of debt. Payments in excess of the minimum are required by law to be paid first to the debt with the highest APR. This payment hierarchy applies to the repayment of each form of debt. Information on approved payment methods, the handling of your payment, how your funds will be used, and more will be included in your agreement [4]–[6].

Fees

Additionally, you may check the different charges related to the card. These will consist of:

- a. **Annual membership fee:** This section outlines the cost of just keeping the card for a year, as well as the conditions under which it is waived (for the first year, for instance).
- b. **Transaction costs:** Your card is subject to a number of transaction fees, such as balance transfer fees, cash advance fees, and international transaction fees. These are often stated as "the greater of either \$10 or 3 percent."

- c. **Penalty charges:** Late payments, exceeding your credit card limit (although often such transactions are declined), and returned payments (for instance, your check fails or an electronic transfer is refused) will all result in charges.
- d. **Other fees:** Look through this section for any additional charges that could be necessary. Will the issuer charge you costs when you access your account to check your balance, activate it, purchase account insurance, or get a bill? If so, you probably have access to less expensive choices.

Review the following 14 fine print items in your credit card agreement.

1. Annual Cost:

The annual cost for a certain card will probably be clearly stated on the application, in credit card reviews, and in the cardholder agreement. This charge is often paid when you initially get the credit card, however some cards waive it the first year to entice new users, and once more on each anniversary of your card membership. You may cancel your card before your cardholder anniversary to avoid a further cost if you determine the yearly fee is not worth it. If you close it soon after being charged the fee, you can obtain a refund. Check the small print to see what transpires if this is a new credit card, however. If you cancel your card during the first 12 months, certain card issuers may retrospectively take back any benefits from the introductory offer.

2. Annual Percentage Rate (APR) for Purchase

The amount of interest charged on the purchase balance of your credit card will depend on the purchase APR of your card. Generally speaking, if you pay your account in full each month, you can avoid incurring interest. The amount you carry over from the prior billing cycle will begin to accumulate interest if you revolve a debt, however. Until your credit card balance is fully paid off, interest will often start to accumulate on any transactions. Numerous credit cards feature variable APRs, which means that depending on benchmark rates, your rate might vary at any time. Your card's purchase APR may increase if interest rates are increasing. Keep an eye on your card's rate if you have a balance and try to reduce your APR.

3. Punitive APR

If you miss a payment on your credit card, a penalty APR, which is a higher APR, could be applied. The penalty APR could initially only be applicable to fresh transactions. However, the penalty APR may also apply to outstanding sums if you become 60 days past due. By setting up automatic payments for at least your minimum payment amount, you may be able to prevent this.

After making six consecutive on-time payments, you may be eligible to obtain your normal APR restored if you have a penalty APR. However, read the small print on your card to find out whether and when the card issuer may apply a penalty APR.

4. Rules and APR for Cash Advances

If you use your credit card to get a cash advance, a different interest rate may be applied. Even if your balances are paid in full, the cash advance APR often applies to cash advances right away

and is frequently greater than the card's regular purchase APR. To find out your card's cash advance APR and what your card issuer deems a cash advance, read the small print. Card issuers may classify activities that resemble cash advances as such, such as peer-to-peer money transfers or purchasing cryptocurrencies, in addition to using your credit card to withdraw money from an ATM.

5. APR for Balance Transfer

For amounts that you move to a credit card, there may be a different APR. Although the usual APRs for purchases and debt transfers are often the same, if you obtain an intro APR offer on a new balance transfer credit card, your rates may change. Or, if your card issuer provides you with a current credit card with a reduced purchase or debt transfer APR.

6. Beginning APR Offers

You can be eligible for a special introductory APR on purchases, debt transfers, or both if you're applying for a new credit card. It's crucial to carefully read the conditions and guidelines before accepting and using one of these introductory deals. For instance, you could only be eligible for the introductory 0% APR on balance transfers if you complete the transactions within 60 days of activating your card.

Be aware about what may happen if you have an APR deal for purchases but not balance transfers. In certain circumstances, even if you have a balance that isn't earning interest, your purchases may start to accumulate interest right away. Consider the promotional period's expiration date as well, and aim to have a strategy in place for paying off your amount prior to the start of the usual APR.

7. Offers with Deferred Interest

There are several credit cards that provide delayed interest, mostly retail cards. These may look similar to other introductory 0% APR deals, but there is a significant distinction. When you take advantage of non-deferred credit card intro APR deals, the sum you still owe after the promotional time ends begins to accumulate interest at your usual purchase or balance transfer APR.

However, with deferred interest, you will be charged any retroactive interest that has accumulated since you opened the card if the total amount is not paid off within the promotional time.

8. Fee for Balance Transfer

Every time you transfer a debt to a credit card, there is often a fee. A \$5 to \$10 minimum is required for each transfer, and the balance transfer cost is typically in the range of 3% to 5% of the transferred amount. To find out what the cost is and when it applies, see the conditions of your card. For transfers you make soon after opening your card, intro balance transfer APR deals can additionally include a promotional balance transfer charge. Consider how much you'll pay in fees and how much you may save during the promotional time when comparing various balance transfer card deals.

9. Fee for Foreign Transactions

Foreign transaction fees for credit cards may be charged if you use the card outside of the United States or when you make an online purchase in a foreign currency. The costs may change, but they typically hover around 3% of each transaction's value. There are several credit cards that don't charge international transaction fees, including premium and travel cards.

10. Unusual Fees

Annual, balance transfer, and international transaction fees are very typical credit card fees that will appear in the Schumer box, however you may find cards without these. To look for unusual costs, you may also wish to read the card agreement's tiny print. Some of them, such as a one-time or ongoing program fee, could also be included in the box. But you'll only see them in the small print below if there are fees for getting a physical copy of your statement or making phone payments. On credit cards that don't demand a high credit score, these fees are increasingly common. There are, however, credit cards for those with poor credit that don't charge these fees either.

11. Intro Bonus Conditions

Some of the finest beginning bonus card deals allow you to accumulate rewards worth hundreds of dollars, and sometimes even more. Although these welcome incentives may be alluring, be sure you qualify and can fulfill the conditions by reading the tiny print. For instance, you could not be qualified if you just received a welcome offer for a card with a similar purpose. If you cancel your card or return purchases you bought in order to fulfill a spending criterion, you might potentially receive the bonus and then lose it.

12. Rules for Reward Program Categories

There are typical credit card rewards bonus categories including eating, shopping, petrol, and travel. Card issuers may, however, define what they include in each category differently. One card issuer may classify taxis, toll bridges, parking garages, and campers under the umbrella of travel. Another could define travel much more narrowly, focusing on air travel, automobile rentals, cruises, and hotels or motels.

There are sometimes exceptions, such as purchases made at non-U.S. retailers that fall under the heading of gas bought at a warehouse club or supermarket gas station. There are sometimes explicit limitations that prohibit all purchases from a certain vendor. In most cases, you'll still get basic points for every dollar spent; however, the purchases won't be eligible for extra category awards.

13. Rules for Statement Credit

Some credit cards provide statement credits to help pay for certain transactions, including airline fees or items made via delivery apps. Be sure to carefully read the small print to understand what constitutes an eligible purchase and how the benefit functions. For instance, a website can emphasize how much you can get annually. Nevertheless, you are given a monthly bill credit that you must utilize before it expires.

14. Additional Benefits for Cardholders

Additionally, credit cards may provide a range of shopping and travel advantages. Some of these may not be as effective as they seem. To avoid believing you have protection when you don't, make sure you understand how they operate.

For instance, credit card benefits only cover damage to or theft of the rental automobile, but rental car insurance is often secondary coverage. You may need to make a claim with your vehicle insurance first if you hire a car using your card and get into an accident. Additionally, the credit card benefit won't pay for liability claims if you harm someone else or damage someone else's property [7]–[9].

CONCLUSION

When borrowers have a thorough grasp of the terms and circumstances of the loan, they are better equipped to make choices that are in line with their financial needs and objectives. They can thoroughly examine the many loan options available and choose the one that best suits their requirements. Furthermore, a healthy credit environment is fostered through encouraging responsible borrowing behavior and raising knowledge of the contractual duties and associated consequences. On the other side, lenders profit from clearly stated terms and conditions since they reduce the possibility of misunderstandings and disagreements. Transparent communication about the conditions of loan agreements fosters relationships with borrowers by establishing trust and trustworthiness.

This study emphasizes how crucial it is to study the specifics of loan agreements and contracts. Making wise financial choices, avoiding unforeseen setbacks, and encouraging appropriate borrowing habits all depend on a thorough understanding of credit terms and circumstances. Transparent, well-defined credit agreements that enable productive financial interactions benefit both borrowers and lenders.

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CHAPTER 22

DIGITAL LENDING: TECHNOLOGICAL INNOVATIONS IN BANK CREDIT

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ABSTRACT:

This study offers a succinct review of digital lending and how technology advancements have transformed how banks provide credit. By using cutting-edge technology, digital lending, a growing area of fintech, transforms the conventional loan process. The study looks at how digital lending streamlines and speeds up credit evaluations, improving efficiency and cutting down on processing times. It does this by using automation, data analytics, and artificial intelligence. It emphasizes the ease and accessibility that online loan applications, document submission, and progress tracking provide for potential borrowers. The study also highlights how other data sources, such as social media and transaction histories, may be used to evaluate creditworthiness and increase loan availability for underprivileged groups. It does, however, address issues with data privacy, security, and possible bias in algorithms. This study's main point is how digital lending changes the way banks provide credit by fostering innovation, efficiency, and accessibility. Although these technologies have many advantages, their implementation requires a balanced strategy that guarantees ease and protection for both lenders and borrowers.

KEYWORDS:

AI, Bank Credit, Consumer, Digital Lending, Fintech, Innovations, Loan.

INTRODUCTION

Ever the disruptors, fintech lenders are now widely seen as trailblazers and facilitators. Among the instruments with the most effects on digital lending are robotics, machine learning, and automated data analysis. The Indian digital lending ecosystem is now facing hurdles, despite the fact that the technology required to foster innovation are widely available and highly sophisticated. Banks and NBFCs will still need to develop novel ways to use these technologies in order to overcome these issues.

Digital Lending: Bank Credit Innovations Powered by Technology

The lending business has become a more commoditized sector as a result of data on fees or other costs, comparable loan rates, and goods being readily available round-the-clock. As a result, lenders may need to strengthen their competitive edge in order to achieve their strategic goals and support revenue. Aadhar and Video client Identification Processes (V-CIP) may be used for digital onboarding to accelerate turnaround times, save unnecessary costs, and increase new client acquisition. The use of artificial intelligence (AI) and face recognition technologies may dramatically increase the accuracy and integrity of client data [1]–[3].

By using cutting-edge technology and alternative credit assessment models, new-age digital lenders can fill the gap and reach a sizable customer base in record time as a result of traditional financial institutions' unwillingness to lend to low-income, seemingly risky, and credit-deficient segments. When compared to conventional loans, digital platforms provide quicker response times for credit evaluations and loan disbursements, especially for small-ticket credits and advances, which are most popular with first-time credit consumers. In order to serve the credit-starved segments of society, the shift from asset-based data to cash flow-based data, along with additional auxiliary data from sources like telecom, utilities, and social media, combined with psychometric analysis to assess the ability and willingness to pay, is regularly displacing traditional sources. In the banking industry, there have been several improvements in client acquisition that have helped lenders reach out to new markets while cutting costs. For instance, digital lenders are using ML-based models to help them fine-tune product features and client contact methods to increase customer acquisition.

With the advent of cutting-edge tech solutions, lenders today have immediate access to vast amounts of digital data in order to identify and minimize potential lending hazards. ML-based alternative credit scoring models have increased lending, however because of model biases and poorly trained data, they may unintentionally leave out particular client categories. This is due to a lack of previous information on borrowers' credit cycles. Black-box ML models cannot be validated by back-testing, hence digital lenders must be cautious while constructing them. This gains importance because government officials are likely to step in to defend consumers' interests in a delicate industry like lending. Lenders would need to have a full grasp of how ML models have changed over time as well as the capacity to wisely choose their parameters throughout a variety of credit cycles in order to make everything work.

Similarly, there is a greater possibility for risk accumulation under the "rent-an-NBFC" or off-balance sheet model, where the lender provides certain credit enhancement features, including a first loss guarantee up to a specific proportion of loans originated by it. The Reserve Bank of India does not currently have regulatory authority over these organizations. Furthermore, many unregulated market players and fintech are taking on direct balance sheet exposures as a result of the financial institutions' collaborations with various fintech firms. Banks and NBFCs have started incorporating digital touchpoints into their current frameworks to prevent financial wrongdoing and proactively evaluate client risk.

Even while banks and NBFCs have started using digital touchpoints, their present frameworks still function in silos, which leads to a less than ideal utilization of the data gathered from various monitoring systems. A complete and meaningful risk score (a one-view risk profile) may be provided to customers by tying together the many digital contact points for various risk categories, empowering them to make choices throughout the loan's lifetime. To more effectively identify abnormal transactions, real-time behavior detection capabilities and rule engines may need to be enhanced.

Even if formal finance will not be widely utilized in India for some time, there is a big chance for embedded lending and the cloud to enter the market today and democratize credit. Businesses have what seems like limitless possibilities thanks to the utilization of the cloud in digital

financing. One of the main advantages of utilizing the cloud is increased distant access. Another is a flexible subscription plan. The lengthy, taxing updating procedures that previously put a load on the IT departments of lenders have been replaced with automatic software updates. With the help of the cloud, banks now have the flexibility to transfer their services off-premises, freeing up the bulk of their capital expenditure for enhancing their product lineups, enhancing customer experiences, and growing their lending operations. By moving their operations to the cloud, banks may have the flexibility to expand as their businesses expand, provide new products more rapidly, and enter new markets [4]–[6].

DISCUSSION

How will consumer lending change as a result of technology?

Every ten years, client demand and technology advancement combine in a manner that fundamentally alters the financial services industry that serves consumers. For instance, before companies like The Motley Fool, eTrade, and Intuit entered the market decades ago, individuals handled their own financial management and put their assets in investments that would provide the highest returns. The financial services sector is once again facing turmoil in 2022. People are choosing how they wish to handle their payments, finance a vehicle or house, pay for services and commodities, or even borrow money as a result of a multitude of technical and economic developments. A number of tech-driven consumer-facing financial services businesses have joined the market to address these shifts and help define the future of finance. Lending has evolved into one of the most lucrative financial app concepts thanks to the newcomers. In this paper, we will examine the various developments now affecting the consumer financial services industry that focus on lending and how digital technologies are causing this shift in fintech. But first, let's define what banking consumer lending is.

What does banking's consumer lending entail?

A kind of finance known as consumer lending gives loans to a customer for domestic or personal usage. The lender could sometimes be a bank or other financial organization. In other cases, the lender could be a company that grants internal credit in return for the consumer's patronage. We will now talk about the elements influencing how consumer finance is developing.

What is causing the landscape of digital consumer lending to change?

A notable change in credit analysis and bank loans is being brought about by the growing field of digital lending revolution. A number of alternatives have entered the market that call into question the validity of credit scores, a key driver of the consumer lending sector, as a result of the growth of technology and big data. Four variables that are driving the digitization of consumer finance may be found when we examine the financial sector's transformations.

Rapid technology advancements, changes in compliance and laws, and innovations in the area of operating model simplification are just a few of the trends affecting customer behavior today. These four forces working together have created an era when product innovations and customer insights are combined to make fintech consumer financing far more accessible. The future of financial services is now enabled to include customer sectors with poor credit history (low-

income families, students, freelancers, etc.), in addition to servicing solely the high credit-worthy clients.

The environment of digital lending has expanded to the point that it can now be divided into two sectors: The ultimate goal of the technology-induced digitalization taking place in the industry across the three subcategories is to quickly and at a level that the conventional lending system could never achieve by digitizing the full customer experience (from KYC to reporting).

	FINTECH-FIN		FINTECH-TECH
	P2P MARKETPLACE	ONLINE LENDING	
BUSINESS MODEL	Individual investors and borrowers meet to realize money exchanges	Investors, mostly institutional, lend money to borrowers	Offer Advanced Credit Scoring, Credit Automation, NPL management and Regulatory monitoring/ reporting (RegTech)
KEY-FEATURE	Risk taken by the investors	Risk is transferred from the investor to the platform	Specialization of Services
YEARS OF ACTIVITY	10 years old or even less	10 years old or even less	Some were founded in the '80s
RELATIONSHIP WITH BANKS	Loans are generated by partner banks and then transferred through loan notes	Represent an alternative to traditional lending offered by Banks	B2B approach. Fintech provide infrastructures to banks

Figure 1: Lending fintech types [appinventiv.com].

What changes are being made by technological advancements in digital lending?

The loan revolution is being fueled by technology. A short while ago, the loan application procedure was drawn out and time-consuming. Forms had to be filled out meticulously, and loan companies' approval processes may take weeks. The banking and financial services sector has shown itself to be a pillar of the evolving technology environment. Borrowers may now get rapid loan approvals and money in their bank accounts in a matter of hours thanks to the growth of fintech companies leveraging cutting-edge technology. Figure 1 shows lending fintech types [appinventiv.com].

Now let's examine some of the ways that technical improvements are influencing digital lending:

1. A new method of screening applications has surfaced

The idea that conventional methods of approving applicants based only on their FICO credit score are an insufficient indicator of their creditworthiness is the foundation for new credit mechanisms.

New modeling techniques are being created by using artificial intelligence. To determine whether an applicant would be able to pay off the loans on time, these algorithms take into account

information from hundreds of data points, including job history, educational background, and spending patterns. A new credit scoring mechanism is emerging as the lending system of the future on the basis of these revelations.

2. AI-backed planning and streamlined sales

The use of machine learning and artificial intelligence (AI) in banking to improve the loan experience by making underwriting choices has begun to be requested by digital lenders from their associated fintech app development firms. The algorithms can verify if applicants are being truthful about their amount of income.

People with weak credit histories, those with lower incomes, or those who face higher interest rates due to a lack of financial information are most suited for the procedure. The capacity of machine learning to identify fraud via study of consumer behavior supported by the time spent by users completing applications' inquiries, examining available alternatives, etc.

3. Blockchain does away with the necessity for middlemen

Blockchain technology enables digital lending businesses to create a low-cost, high-trust platform. Users will be able to maintain a record of papers and transactions on an anonymous digital ledger platform after the whole loan application process is conducted online, which will do away with the requirement for third parties and middlemen.

4. Cloud computing addresses issues with uptime in the digital lending industry

The three most frequent areas of the lending industry are security, storage, and round-the-clock maintenance. All these problems are resolved by cloud computing, which also provides a number of further advantages like: Secure connections

Disaster recovery, time- and money-saving management, streamlined online procedures, and process automation

The situation of digital lending is being significantly improved by these technologies, but the industry must continue to develop. Knowing the trends that will shape the future of consumer credit in 2021 will help the industry continue to become more efficient.

5. Neobanks are improving client service

The likelihood of app-only "neo banks" is growing as internet use rises and more individuals get accustomed to conducting transactions on their phones.

Neo Bank is a kind of online bank with no physical locations. Neo banking is only conducted online, not in person at a particular place. There is a disconnect between what conventional banks provide and what consumers anticipate as the financial environment changes in favor of improving customer experience and happiness. Neo banks are also attempting to close that gap. While these technologies are essential to improving the condition of digital lending, the industry must continue to develop. Knowing the consumer loan trends that will be prevalent in 2022 as the future of consumer financial services is one way the industry can continue to become more efficient.

Regulations for digital lending: Promote responsible innovation

One of the industries in India with the quickest growth is digital banking. In the last ten years, there has been a significant advancement and exceptional expansion in what was previously completely disorganized. India has one of the highest rates of unbanked people in the world, at approximately 200 million, keeping them out of the official credit system.

All of this has altered because to technical advancements in digital banking. We have realized that financial services, such as loans, are no longer restricted to the walls of a bank. The way clients utilize financial services has changed due to technology. Obtaining a loan in the past required a significant amount of documentation and was a time-consuming procedure. Borrowers may now obtain rapid loan approvals and money in their accounts within a few hours thanks to the growth of digital lending companies leveraging cutting edge technologies. The efficiency, productivity, diversity, and competitiveness of the market have all undergone significant changes as a result of technological advancements. However, this unheard-of expansion has also had unexpected repercussions including client data breaches and misspelling.

The necessity for regulation emerged in order to ensure that the sector expands while benefitting the final customer. Regulation often has a poor image for either doing too little or acting too much in times of crisis, holding us down and erecting obstacles to innovation and growth. However, if you approach it from a different angle, you see that a world without regulation is a world of anarchy when it comes to public funds. In an effort to stop the growing number of frauds in the digital lending ecosystem, the RBI published new rules on digital lending in November 2021. The regulations were developed in accordance with the suggestions made by a working group on digital lending, whose report was made available to the public in November 2021. The adoption of these new regulations will guarantee that the fintech industry remains innovative while protecting client data.

The most recent recommendations generally include the following topics:

1. Protection of the client
2. Technical specifications
3. Legal obligations, such as proper customer disclosure of information and documentation.

These much-expected regulations for the online banking sector make clear how loans are made, work to safeguard the client, and hold participants accountable. Both current users of digital loans and those who apply for loans in the future using digital banking channels must abide by these rules.

Digital lenders have significantly lowered borrowing costs for various parts of the population and expanded credit availability throughout the nation. The RBI guidelines underline the necessity for technological innovation while putting a strong emphasis on safeguarding the borrower. In times of transition, a flexible financial platform is extremely helpful.

Agile technology stack for rapid adaptation

The RBI issued a series of debt repayment moratoria between March and August 2020, with significant uncertainty over further extensions. The fact that consumers might choose to use it or not complicated things. To process consumer requests and refresh the payment plan on the tap, lenders had to put in twice the effort. It was once again unclear how to account for interest capitalization and interest-on-interest since the RBI, the government, and the Supreme Court were carefully debating the matter. In order to adapt to any changes fast, lenders have to be exceedingly adaptable. For this to function effectively, there has to be a current loan management system and the accompanying customer communication channels.

High unemployment rates and significant economic hardship were present at the conclusion of the moratoria. The borrowers were unable to repay their loans. The RBI permitted one-time loan modification in order to lower borrowers' monthly financial outflows. Customers have to read and agree to revised terms and conditions as a result of this. The secret to achieving this was a software architecture that was both agile and robust. As a result, the business may provide a wider range of products and communicate with consumers more effectively.

Machine Learning-Based Credit Risk Model

Credit models based on data sciences provide improved user engagement for consumers to conduct secure transactions. Credit models based on data sciences are simple to manage and may be duplicated to provide goods that are relevant to various market sectors. For the greatest risk profile projections, these models continually monitor correlated factors and modify weights appropriately. This method for continual self-learning loops. The modular design of the models makes it easier to customize them depending on the numerous data sets that are available. They are more scalable since they are modular.

CONCLUSION

In conclusion, the quick development of digital lending heralds a paradigm-shifting chapter in the history of bank credit, supported by technology advancements that revolutionize the borrowing environment. Modern financial services and cutting-edge technology are combined in this revolution, giving borrowers a simple and convenient credit experience. Automation, data analytics, and artificial intelligence are used by digital lending platforms to speed up the loan origination process, simplify the underwriting process, and customize credit options. Borrowers gain from more convenience, quicker approvals, and customized financing solutions that meet their particular demands and credit histories. Digital financing increases accessibility and efficiency, but it also adds new levels of risk and accountability.

To secure the sensitive information of borrowers, the huge volume of data gathered and processed calls for strong cybersecurity measures and strict data protection. Furthermore, by serving previously disadvantaged communities, digital lending democratizes access to credit. Small enterprises, young people with poor credit records, and those living in rural locations have better access to credit options than they may have via conventional banking channels.

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CHAPTER 23

PEER-TO-PEER LENDING: DISRUPTING TRADITIONAL BANK CREDIT MODELS

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ABSTRACT:

Peer-to-peer (P2P) lending and its disruptive effect on conventional bank credit models are briefly described in this study. Online platforms that promote peer-to-peer lending have become a well-known alternative to traditional banking for borrowing money and making investments. The study investigates how P2P financing eliminates conventional middlemen and links individual borrowers and investors directly. It draws attention to the advantages of this strategy, including simpler procedures, quicker approval times, and perhaps cheaper loan rates because of decreased administrative expenses. The study also explores how technology is used in peer-to-peer lending to facilitate effective credit evaluation using data analytics and risk-scoring formulas. As P2P lending makes credit chances available to a larger spectrum of borrowers who would not meet conventional banking requirements, it also recognizes the democratizing nature of the practice. The study does, however, also address possible hazards, such as regulatory difficulties, default rates, and the need for investor protection. It underlines the need of openness and due diligence in maintaining the confidence of both borrowers and investors.

KEYWORDS:

Credit, Financial Institutions, Investments, Lending, Peer-To-Peer, P2P.

INTRODUCTION

For borrowers who would have had trouble getting loans from conventional lending institutions, P2P lending platforms have opened up new alternatives. Traditional banks sometimes have rigorous lending criteria and may be reluctant to provide loans to those with bad credit records or odd financial circumstances [1]–[3].

P2P Lending Platforms' Emergence: Shaping the Future of Traditional Lending Institutions

Peer-to-peer (P2P) lending platforms have significantly disrupted the loan business since their introduction. Bypassing conventional credit institutions like banks, these internet platforms link lenders and borrowers directly. Peer-to-peer lending has become more common because of its effectiveness, accessibility, and ability to provide low interest rates.

Peer-to-Peer Lending Platforms: An Overview

Platforms for peer-to-peer lending are online markets that enable lending transactions between consumers or companies looking for loans and investors looking to lend money in exchange for a return. These platforms act as middlemen, matching lenders' investment preferences with loan

requests made by borrowers. P2P lending systems use technology, data analytics, and algorithms to examine creditworthiness, set interest rates, and manage the loan process.

Traditional Financial Institutions' Impact

Access to Credit is Expanded

P2P lending systems provide money to borrowers with a range of credit profiles by using alternative data and innovative credit evaluation methods. Underprivileged or underrepresented populations gain from the increased credit availability, which increases financial inclusion.

Disintermediation

The loan process is disintermediated because P2P lending platforms remove the need for conventional middlemen like banks. By linking lenders and borrowers directly, P2P platforms reduce the expenses of conventional lending, including overhead fees, physical branches, and bureaucracy. Due to this disintermediation, P2P lending platforms may offer borrowers more alluring interest rates while still offering lenders reasonable returns. Traditional lending institutions must embrace technology advancements and reevaluate their business practices in order to adapt to this changing market and stay competitive.

Enhanced Speed and Efficiency

Automated and digital processes are used by P2P lending platforms to speed up loan application and approval. In conventional lending institutions, complicated paperwork, drawn-out underwriting processes, and time-consuming assessments are typical. P2P lending systems, in contrast, accelerate credit evaluations and decision-making via the use of robust algorithms and machine learning. Online loan applications enable borrowers to submit them, get quicker approvals, and access funds more rapidly. The time-consuming procedures of conventional lending institutions might be temptingly replaced by this efficiency and quickness.

Opportunities for Investment Diversification

Platforms for peer-to-peer lending are a desirable investment choice for investors who want to diversify their holdings. By spreading their funds over a variety of loans, lenders may reduce the risk involved with their lending activity. Traditional lending banks often provide investment options including savings accounts and fixed-income securities. P2P lending systems provide lenders access to a wider variety of borrowers and loan types, allowing them to customize their portfolios and maybe earn greater returns.

Technological and innovative developments

Innovation in the lending industry has been sparked by the growth of P2P lending. Traditional lending institutions must take use of technological advancements to stay competitive. This entails enhancing online banking functionality, growing their digital infrastructure, and incorporating data analytics into their credit assessment procedures. P2P lending platforms have opened the way for further innovative lending models like crowdsourcing and marketplace lending, which have contributed to the diversification of the lending sector and encouraged established banks to innovate and adapt.

Issues with Regulation and Consumer Protection

The emergence of P2P lending platforms has presented regulatory challenges to the regulating bodies. While these platforms have numerous benefits, they also raise concerns about systemic risks, consumer protection, and transparency. The interests of both lenders and borrowers must be protected, and regulators must develop frameworks that strike a compromise between these two objectives. Regulatory guidelines will probably emerge as the P2P lending industry develops to address these issues and maintain the stability and integrity of the lending environment [4]–[6].

How Traditional Banks Can React to P2P Lending Platforms in the Face of Competition

Peer-to-peer lending platforms are becoming popular, disrupting the conventional banking industry by providing alternative lending alternatives and posing a threat to well-established financial institutions. Traditional banks must adapt and adopt tactics that meet the distinctive benefits and allure of P2P lending platforms if they want to compete in this changing industry.

Recognizing P2P lending platforms' benefits while using the distinctive advantages that conventional banks have, such as their brand recognition, regulatory compliance, and long-standing clientele, seems to be the key. Traditional banks can manage the shifting lending environment and maintain relevance in the face of shifting consumer preferences and market dynamics by strategic adaptation.

Take Technological Innovation Seriously

P2P lending companies' use of cutting-edge technology to accelerate the loan process and improve user experiences is one of their key advantages. To enhance their own lending operations, traditional banks must give priority to adopting technological innovation. To speed up loan approvals, eliminate paperwork, and provide clients a quicker and more pleasant lending experience, this may include investment in digital platforms, automation, and data analytics.

Increase customer satisfaction

P2P lending systems have grown in popularity by providing borrowers and lenders with individualized and convenient experiences. By using technology to provide smooth digital onboarding, quick loan application procedures, and individualized loan recommendations, traditional banks should concentrate on improving their client experience. Banks may compete with P2P lending services' simplicity and convenience of use by implementing customer-centric strategies.

Streamline the processes for loan approval

Platforms for peer-to-peer lending are renowned for their adaptability and speedy loan approval processes. The response of conventional banks is to streamline their loan approval procedures. Banks may hasten loan assessments and provide consumers speedier choices by using data analytics, machine learning, and automated underwriting technologies. Traditional banks can compete in a fast-paced lending climate by reducing red tape and streamlining the loan approval process.

Accept partnerships and collaborations

Traditional banks may think about forming strategic alliances and partnerships in order to address the competitive challenge presented by P2P lending platforms. Working with fintech firms or peer-to-peer lending platforms may provide banks access to cutting-edge technology, clientele, and alternative lending methods. As a result, banks may be able to take use of P2P lending platforms' advantages while still preserving their existing infrastructure, ability to comply with regulations, and risk management skills.

Putting Trust and Relationship Building First

Regarding consumer trust and brand reputation, traditional banks have a long-standing edge. Banks should emphasize relationship-building initiatives, as well as their dedication to client happiness and financial security, to capitalize on this. Banks may set themselves apart from P2P lending platforms and gain consumers' trust by providing individualized financial advice, access to specialized relationship managers, and showing openness in loan terms and conditions.

Explore specialized lending and niche markets.

P2P lending systems often target certain market groups or focus on particular loan kinds. Traditional banks may react by locating specialized loan possibilities or niche markets that fit with their knowledge and skills. Banks may establish their distinct market positions and serve borrowers who might need more specialized lending products and services by creating personalized lending solutions for these groups.

DISCUSSION

P2P Lending: A Crisis for the Banking Sector?

Peer-to-peer lending, often known as P2P lending or P2PL, is a kind of loan arrangement based on an online marketplace forum framework. The forum's goal is to provide an internet platform to connect capable lenders with adequately qualified borrowers. The lending industry's interface is provided through the internet platform, where supply and demand may be balanced. Since the height of the global financial crisis seven years ago, the peer-to-peer lending and investment sectors have exploded. Peer-to-peer lending has drawn the attention of investors who are seeking for alternate sources of capital returns. Lending Club and OnDeck are two important market leaders who have seen rapid growth and who have subsequently gone public. They floated their stocks in December of last year and have since established corporate valuations of \$9.5 billion (£6.1 billion) and \$1.5 billion, respectively. Investors seeking both to invest directly in P2P enterprises and to take use of the sites' services for matching lenders and borrowers are finding these businesses to be more and more alluring.

Lending money to strangers, or "peers," without going through a typical financial intermediary like a bank or other well-established financial institution, is known as peer-to-peer lending (P2PL). These loans are made via a variety of lending platforms and credit-checking tools on the websites of peer-to-peer lending organizations. P2P lending is intended to increase efficiency and reduce needless frictions in the lending and borrowing processes by doing away with conventional banks. When compared to the conventional banking industry, peer-to-peer lending

has been shown to be effective at speeding up transaction processing times and, in many situations, lowering costs for borrowers. Furthermore, P2P lending gives investors easy access to alternative venues for their capital in the current extremely low interest-rate environment that we are experiencing globally, allowing their returns to be significantly increased by the much higher rates of return available on the P2P projects on offer. Thus, the P2P lending and investment industry is fundamentally changing the conventional banking industry, although slowly at the present. The banking and financial services industry is undergoing a major phase change, which is being fueled by the expanding technological and application design advancements as well as the changing needs of customers to have access to more convenient online and mobile banking and financial services solutions. This trend appears to be continuing.

Technology has completely changed the banking and financial services industries during the last ten years. Over the last ten years, the costs of investing in and developing technology resources have dramatically decreased, enabling smaller businesses to join the market. While in the past these technology expenses would have priced out smaller competitors from providing competitive and effective services when going up against the major, established financial institutions, this has enhanced competition and efficiency in the market. P2P lending and investment services are becoming more widely used, which indicates a larger departure from the infrastructure of conventional banks. For instance, millions of people and small companies have used crowdfunding P2P websites like Kickstarter and Indiegogo to finance their projects. On these websites, as well as other smaller P2P platforms like RocketHub and GoFundMe, businesses may borrow more than \$10 million.

The UK government has even gone so far as to openly acknowledge and endorse the benefits of P2P lending after realizing that it offers a quick, affordable, and effective tool for reviving the economy and fostering development. They also pointed out that rivalry with the conventional banking industry is a good thing since it will promote increased productivity, innovation, and development. The government has established a policy that would go into effect in April 2016 as part of this assistance, allowing lenders to deduct any loan losses from taxes on other P2P revenue. In addition, the UK government has stated intentions to reconsider banking rules that prohibit institutional P2P lending. The government has also said that they may eventually impose withholding tax on all P2P revenue, so there is a possible drawback to this recognition.

P2P lending platforms are excellent sources of capital for growing small enterprises. Banks and other conventional finance institutions often ignore these parties because they see small firms as high risk. If banks do provide loans to these companies, they sometimes come with exorbitantly high interest rates that make it impossible for the enterprises to manage their cash flow and overhead management while still promoting sustainable development. The banking industry has been undergoing a significant reform at all levels of operation since the global financial crisis seven years ago, in 2007–2008. Numerous banks and financial services companies have completely shut down as a result of the global financial crisis, especially those whose balance sheets are heavily weighted with so-called "toxic asset" holdings. Many of the businesses that made it through the financial crisis are still battling to expand and repair. The global financial and asset markets have seen a decline in credit activity and liquidity, and the economy has just

slowly begun to show signs of recovery. The financial and banking industries have been particularly badly impacted by the global sluggish and lackluster recovery.

Additionally, during the last three years, international regulators have tightened up on their new regulatory-policy regime, notably in the Western parts of Europe and the US. These new laws have been actively implemented during the last several years and are intended to restore stability, reduce volatility, and eliminate systemic risk from the financial sector in order to avoid another financial-system catastrophe like the credit crisis. This rule includes provisions that limit banking trading activity as well as the keeping on bank balance sheets of certain quantities, quality, and categories of hazardous assets. In order to prevent shareholders and taxpayers from having to bail out these banks in the future, as they have had to over the past seven years since the 2007–2008 financial crisis, banks are now required to hold a higher ratio of capital in reserve. This is done to allow for certain downward shock scenarios to act as buffers to volatile market activity. The P2P economy has been thriving since the financial crisis more than five years ago, gaining greater momentum and acceptance each year as the conventional banking system has been under growing levels of stress and constraint.

The whole business has become less enticing as a result of the banking sector's shortcomings. The constant stream of scandals and wrongdoing that keeps coming to light even seven years after the crisis added to the sour mood the industry has been experiencing. As a result of this negative perception of the industry and global economic contraction, the P2P sector has benefited greatly. Customers of all shapes and sizes don't trust established banks as much as they did prior to the financial crisis, and the aftermath hasn't really done much to change that—in some situations, the mistrust has just gotten worse. Larger financial organizations tend to have greater conflicts of interest, which hasn't helped the situation. The court cases against banks that have grown in number and received media attention over the last several years have only served to increase public mistrust. Customers are also unhappy with government bailouts of banks, which feeds their resentment of conventional banking and directs their attention to accessible alternatives like peer-to-peer lending.

Although the banking system has been somewhat disturbed by P2P lending to far, despite being beneficial and popular, there are some signs that this disruption may have certain upper bounds. The danger to the traditional banking system is now minimal; for instance, the P2P lending market is dwarfed by the size of the whole American consumer credit market, which is estimated to be worth \$3 trillion. In addition, market leader Lending Club negotiated over 56,600 loans totaling \$791 million in the first quarter of 2014, whereas JPMorgan Chase disbursed almost \$47 billion in consumer loans during the same period. For investors at least, the ability to choose the best investments for their money is one of the industries selling points. Those looking for the lowest-risk ventures can do so through these websites, which are good at placing and advertising low-risk, high-return ventures on their websites.

These websites have gained popularity by providing borrowers with cheaper interest rates; for instance, Lending Club may give an average interest rate of 14 percent, which is lower than the average interest rate charged by credit card firms, which is 16 percent. However, the business continues to be selective in choosing loan applicants, ultimately allowing just 10 to 20 percent to

access its marketplace following the application and screening process. OnDeck, a rival company, has a different business model that depends on selling debt-backed securities on the website and asking lenders to finance 10% of their loans. These websites may need to accept higher-risk P2P business in the future as the size, breadth, and industry of peer-to-peer lending expand. Only then will they have the chance to really disrupt the banking industry, as they will be engaging in competition in a market from which they have hitherto been mostly excluded.

Conventional banking institutions have not yet taken action to recognize or compete with these P2P lenders in the market, sometimes failing to even identify them as competitors. For instance, in the UK, Santander Bank regularly recommends P2P lender Funding Circle to small-loan-seeking UK enterprises when Santander's capacity for issuing certain loans has been surpassed. These conventional banks, confident in their names, capabilities, and resources, have not yet shown any symptoms of being concerned about P2P lenders. However, the P2P industry is expanding and making progress in its growth. Through 2014, Lending Club's platform handled more than \$6 billion in loan transactions, and the company virtually quadrupled its revenue to \$98 million. Lending Club imposes fees to both lenders and borrowers, adding an average of 5% to each loan. Additionally, Lending Club and other P2P businesses have stated aspirations to eventually branch out into other credit products including mortgages and student loans.

Many financial industry experts now contend that by downplaying the danger posed by peer-to-peer lenders, banks are assuming an increasing risk. Around the world, the so-called "disruption of a market" technique is becoming more and more common. It has proven especially successful in sectors where the incumbents have become complacent and ineffective, which is undoubtedly the case for some of the conventional financial institutions. Lending Club's enormously successful IPO (initial public offering), which raised \$5.4 billion (£3.6 billion) and projected a market capitalization of close to \$10 billion, has convinced investors that the company has the potential to expand, succeed, and take over a significant portion of the financial services sector. For its online product and service offering, the corporation has already identified a number of strategic growth goals.

The days of high street banking are gradually passing away, and accessibility, ease, innovation, and problem-solving via technology means will be crucial for success in the future. Future options for conventional banks may include establishing their own online P2P platforms, functioning like Lending Club as a middleman that keeps a cut of the loan proceeds, or purchasing these P2P platforms outright before they have a chance to establish a significant market presence.

Banks now seem to be satisfied with allowing P2P sites to expand unchecked. The P2P industry's entrance requirements may be reassuring to these institutions. Over the last five years, it has not been simple for the established P2P enterprises to obtain the money necessary to launch their operations. Additionally, despite the increased returns, a sizable portion of skeptic customers continue to be hesitant of utilizing these internet platforms and sites for financial problems. In contrast to well-established banking and lending institutions, the P2P sector now only has a very little window of track record, although being incredibly promising.

Over the last five years, the industry has seen a tremendous growth that is hurting the bottom line of the conventional banking sector. Banks should be ready for the P2P sector to develop significantly since they are already short on funds due to regulatory changes and liquidity constraints in capital-asset markets. These kinds of developments may happen quickly and unexpectedly in the modern, technologically sophisticated society. To combat this competition, established banks should enhance customer service, innovate and expand their services and products, and further increase their operational efficiency to provide competitive rates for financial transactions [7]–[9].

CONCLUSION

Peer-to-peer (P2P) lending is a disruptive force that is changing the way that conventional bank credit models are implemented. By removing the middlemen of conventional banks and linking borrowers and lenders directly, this ground-breaking strategy democratizes financing. A new age of financial inclusion, ease, and efficiency is introduced by this transition. P2P lending systems use digital technology to provide a virtual marketplace where lenders may look for possible returns on their investments and borrowers can swiftly get loans. Borrowers benefit from more affordable rates and durations thanks to this simplified approach, while lenders may diversify their investment portfolios beyond conventional choices.

The P2P lending model has special risks linked to credit evaluation, default rates, and regulatory control, therefore it is not without its difficulties. For the P2P lending sector to be viable and credible over the long term, it is crucial to strike a balance between promoting innovation and defending consumer rights. Despite these obstacles, P2P lending is expanding, demonstrating its potential to challenge conventional banking methods, particularly for underprivileged communities and small enterprises. P2P lending fills credit access gaps that traditional banks may ignore by using technology.

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CHAPTER 24

DEFAULT AND LOAN RECOVERY STRATEGIES BY BANKS

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ABSTRACT:

In order to control credit risk and reduce financial losses, banks use default and loan recovery procedures, which are briefly summarized in this study. The stability of a bank may be greatly impacted by loan defaults, hence efficient recovery measures are crucial. The study investigates the proactive strategies that banks use to avoid defaults, such as careful credit evaluations, collateral restrictions, and borrower financial health monitoring. Banks use a variety of recovery techniques in default situations, including negotiation, restructuring, and legal action. The study also explores the importance of early action in reducing losses. It talks about the function of loan workouts, in which lenders work with borrowers to create workable repayment schedules that suit their financial circumstances. The study does, however, note the difficulties in debt recovery, including drawn-out legal processes and significant asset devaluation. It highlights the need of striking a balance between rehabilitation attempts and keeping wholesome client connections.

KEYWORDS:

Bad Debt, Borrowers, Collateral, Creditworthiness, Fintech, Lenders, Loans.

INTRODUCTION

The money that your company gets after writing off a bad debt as uncollectible is known as bad debt recovery. When the borrower is unable to repay the lender within the allotted period, the bad debt collection procedure is initiated. The lender may file a lawsuit in this situation to collect the bad debt. The receivable may be recovered by the lender in the form of equity or a partial payment. Selling the collateral provided by the borrower is another option for recovering bad debt. For instance, a borrower may take out a vehicle loan but not pay it back on schedule. In this case, the lender has the option to seize the vehicle, sell it, and recoup the money [1]–[3]. Lenders find debt collection to be difficult and time-consuming. Frequently, the work required to repay a poor debt is not worth it. However, before designating a loan as a bad debt, the lending institution must follow a number of steps. For instance, they might try internal or outside collection efforts or even file a lawsuit. Before the debt is deemed bad, collection measures may still be made.

How may loan risks be diminished?

Incurring Loan Company's first objective should be to avoid incurring bad debts in the first place. As a result, lenders should be aware of their borrowers' financial capabilities. You take a risk each time you extend a loan. It is simple to provide loans to reputable borrowers. However, the issue gets challenging when you wish to grow your company and service to subprime clients. Traditional credit ratings have been used by lenders for millennia. Banks and lenders were able to confidently distribute loans because to this grading.

The assessment process took longer for those with lower scores. Lenders must go through a number of screening procedures to determine if they can even provide the loan. In the loan industry, rejections are typical. However, there are a lot of unusual situations as well. Loans may also be granted on a conditional basis by banks, NBFCs, and other financial organizations. In these circumstances, regular credit rating alone is insufficient. The creditworthiness of applicants for subprime loans must be assessed by lenders using relevant information and techniques. The keys to lowering loan risks include rich application data and a consistent review procedure.

1. Obtain information on creditworthiness in depth.

Today, there are several data sources that provide a far more thorough picture of an applicant's financial situation. These data sources are growing more crucial every day in the realm of digital banking. Digital lending platforms are being given permission by fintech firms to base their decisions on these data sources.

When businesses acquire client data, data privacy rules are essential. The consumer must formally consent to the sharing of their data, which may include sensitive information. This information offers the businesses a much better view of the applicant's creditworthiness. Other credit information might be:

- a. Account status and financial information
- b. Information about income and employment
- c. Spending patterns and purchasing history
- d. A record of utility and phone bill payments, among other things.
- e. Previous rentals
- f. Property ownership
- g. A record of any prior bankruptcies, among other things.

Alternative credit data is increasingly being used by businesses to complement current credit ratings or to underwrite loans. Nearly 80% of lenders make use of at least one alternate source of credit data. 16% of lenders want to utilize information from sources like utility bill payments or records of rental payments. Lenders increasingly depend on this information in general to make a more accurate assessment of borrowers. This data enables lenders to decide more quickly and wisely.

2. Identify thin profiles

Both a danger and an opportunity may exist with thin profiles. With the narrow profiles of millions of US borrowers, it is challenging to determine their creditworthiness. Users with thin profiles have credit card accounts but haven't made any use of them recently. Or maybe they won't pay for a while. Because their purchasing patterns are not tracked, those who pay with cash also have a thin profile. A person's credit score is negatively impacted by a thin profile. This does not necessarily imply that the application will not be approved for a loan, however. For the lender, dealing with narrow profiles is always risky. Alternative credit scoring may provide a remedy in certain circumstances. Unconventional data sources may show whether a person is eligible for a loan. They may also demonstrate if there is a high degree of danger.

3. Utilize cutting-edge loan origination systems

Alternative credit rating information reduces the risk of lending. However, lenders must digitize their procedures in order to access these data sources. Combining conventional credit data with alternative data may provide lenders a lot of options. In only a few minutes, modern loan origination tools can assist lenders in determining if an applicant is creditworthy. Using other data sources, the portion of subprime applicants formerly judged unserviceable by banks or lenders may now qualify for loans. Lenders may also exclude high-risk applicants using this information. Numerous loan origination systems provide out-of-the-box interaction with different sources of credit data. Using APIs, it is also feasible to include other data sources. It combines information from several sources. All information is uniform. After that, the system may determine if a user is creditworthy or send the aggregated data for human underwriting. A developing trend in the world of online financing is AI-assisted underwriting. Without the lenders having to take any human action, borrowers may apply for loans and get them. Borrowers must, however, consent to sharing information that would enable the platform to evaluate their financial situation.

4. Automatically gather data

Timely collections assist decreases bad debt and maintain the viability of the lending industry. A specialized collections system encourages borrowers to make on-time payments while a loan origination system makes it simple to issue loans to approved applicants. Lenders may employ collections CRMs that can automatically assign borrowers to teams and agents. Keeping track of borrowers may be difficult for lending companies as their businesses expand. CRM is a good choice because of this. Additionally, a specialized program may classify borrowers and suggest recovery methods. Agents may be reminded to contact customers again. Additionally, based on their activities, it may automate conversations with debtors.

Recovery of Loans

A personal loan's greatest benefit is its ability to assist us in times of need. Therefore, it is only fair for you, the borrower, to pay back the loan as soon as you can. This will raise your credit score, making you more likely to get approved for a larger loan when you next need one. Banks send recovery agents to you if you are unable to pay back the loan within the specified time frame. In terms of banking legislation, the Debt Recovery Tribunal allows prompt loan recovery. Let's look at how a loan recovery procedure is often carried out in this post.

Ways to Recover Loans

A loan recovery procedure is started by the lending institution when a borrower is unable to make loan payments. RBI loan recovery rules make sure that the procedure is advantageous to the lender while also honoring the legal rights and duties of the borrower. There are two primary methods for recovering loans:

- a. By use of a non-judicial process
- b. Through legal channels

Process for Recovering Loans

The cause for loan default is one of the key factors that defines a loan recovery procedure. Let's use examples to better grasp this.

Condition A

Mr. X manages his money well and has a high credit score. However, he has lost his work as a result of unforeseen events (such as the COVID-19 epidemic) and is unable to pay back the debt.

In this case, the loan company can provide him/her with one of the following choices:

- a. A longer payback period that lowers the EMI amount
- b. A moratorium during which he won't be required to make EMI payments for a few months.
- c. Accept a "haircut," wherein the lender waives a portion of the loan if the borrower is unable to repay the loan within a reasonable length of time.

It should be highlighted that Mr. X's credit score can suffer if he chooses a moratorium or 'haircut'. The best course of action for him is to repay the loan in full over a longer period of time. It should be highlighted that if Mr. X chooses a moratorium or "haircut," his credit score could suffer. The wisest course of action for him is to repay the debt in full over a longer period of time [4]–[6].

Condition B

Despite having a poor credit score and doubts about his ability to repay the loan, borrower Mr. Y has applied for one. As a result, even though he was given a loan, it had a high interest rate and a short payback period.

Even if the reasons are legitimate, if he is ever unable to pay back the loan, he may not be given the option of a moratorium or "haircut."

If Mr. Y defaults on a secured loan, the lender may elect to sell the asset pledged as collateral in order to recoup the loan balance. However, when the loan amount has been paid back, Mr. Y is entitled to any surplus money from the sale.

The lender may decide to dispatch loan collection agents if none of these alternatives proves successful.

RBI Policies for Loan Recovery Representatives

The majority of the time, people see loan recovery agencies unfavorably and with terror. It's possible that you've heard tales of agents harassing innocent people in the name of debt recovery. However, they are prohibited under the RBI's detailed loan recovery standards, which make them unlawful.

Agents are prohibited from harassing borrowers in any manner and are obligated to follow these rules. These rules include some of the following:

- a. Banks are accountable for any complaints brought against them and must have a diligence procedure in place before working with loan collection firms.
- b. The recovery agency's specifics must first be disclosed to borrowers.
- c. When seeing the defaulter, the agent must also have a copy of the bank's notification and the authorization letter with them.
- d. In the event that a borrower has filed a complaint, banks are prohibited from referring the specific case to a recovery agency before the borrower's complaint has been resolved.
- e. However, if the bank is persuaded by evidence that the objections are frivolous or meaningless, this is rendered invalid.
- f. The bank must also make sure that complaints from borrowers about the recovery procedure are handled properly.

What to Do If You Can't Pay Back a Loan: Know Your Rights

Modern living has made loans a necessity, especially in metropolitan regions where it is difficult to cover all of one's financial demands without borrowing. Loans have evolved into a crucial instrument for realizing these objectives, whether it's for purchasing a vehicle, building the house of one's dreams, establishing a new company, or paying for personal needs. But there are times when one can find themselves unable to make loan payments on schedule. These events, which might make it difficult to keep up with loan repayments, may include job loss, serious sickness, or financial crisis. Financial hardship and possibly legal repercussions may result from being unable to return a debt. To prevent more debt and safeguard their financial security, borrowers must be informed of their rights and alternatives in these circumstances. This article explains the rights of borrowers in the event that they are unable to make loan payments as well as the actions they might take to deal with this difficult circumstance. Before we talk about the rights of loan defaulters, let's first make clear some crucial facts that you should be aware of. In India, not being able to pay back a bank loan (i.e., defaulting on the loan) is not a crime unless there is proof of malicious intent. Defaulters are protected by the legal system because it acknowledges that there may be good cause for them to be unable to pay back their debts. The legitimate and legal justifications for loan defaults are thoroughly considered by Indian civil courts. The police cannot detain a person just because they are unable to repay a debt in India since loan defaults are viewed as a civil offense. It is vital to realize, however, that these regulations only apply to individuals who have good cause and do not apply to those who purposefully fail on their debts, participate in fraud, avoid legal action, or break the law.

DISCUSSION

What transpires if a loan is not repaid in India?

After giving you many reminders, the lender usually starts the recovery procedure after you miss a few EMIs on your loan. According to the SARFAESI (Securitization and Reconstruction of Financial Assets and Enforcement of Security Interests) Act, the bank may take control of the asset in the event of secured loans like house loans, motorcycle loans, and auto loans. However, the lender must give you enough notice before beginning the repossession procedure. If you don't settle the debt within this time frame, the lender has the right to start the recovery procedure and seize the asset. Before beginning the repossession process, the lender must adhere to certain legal

requirements and rules outlined by the SARFAESI Act in addition to the notice period. In the instance of an unsecured loan, the lender may file a lawsuit against the borrower and seek restitution from the court. The defaulter will then get a notice from the court ordering them to show up in court and make their case.

The defaulter may get protection and aid if the court determines that they have a valid basis for not repaying the debt. However, if the court determines that the borrower is engaged in dishonest behavior or has no legitimate basis for not repaying the loan, it may decide in the lender's favor and permit them to reclaim the unpaid balance.

What are your options if you can't pay back a loan?

Several rights are created by law to guarantee the borrower is treated properly throughout the recovery process:

1. Sufficient notice:

Before the bank sells its assets in the case of loan default, the borrower has a right to adequate and prompt notification. In India, a borrower's bank account is categorized as a Non-Performing Asset (NPA) if they fail to make loan payments for more than 90 days. At this stage, the borrower receives a 60-day notice from the lender giving them time to pay back the outstanding EMIs.

The lender has the legal right to sell the assets offered as collateral in order to recoup the unpaid loan balance if the borrower is still unable to make the repayments. Even in this scenario, the bank must publish a 30-day notice before selling the assets at auction. This provides the borrower more time to complete the payment or set up other finance arrangements. The borrower has the chance to defend their assets or contest the bank's decision to put them up for auction by receiving sufficient notice.

2. Fair Asset Valuation:

In the case of a loan failure, the borrower is entitled to receive the fair market value of the assets that the lender sells. In India, the bank is required to publish a notice informing the public of the sale's specifics, including the asset's fair market value, the reserve price, and other information about the auction such as the location, date, and time.

To establish the asset's selling price, the bank will select valuers. The borrower has the right to challenge the auction if they believe the asset is being undervalued. Another buyer may be located, and the borrower may refer them to the lender. In this situation, the lender is required to sell the asset to the new buyer at a greater price if the latter is willing to pay more than the lender had originally proposed.

This is a critical right for the borrower since selling assets below market value might result in large financial losses for them, making it harder for them to repay their debts. The Right to Fair Valuation of Assets safeguards the borrower's interests and promotes fairness and openness in the recovery process by guaranteeing that the borrower is paid a fair value for their assets.

3. Remaining Auction Proceeds:

Any excess funds from the sale of the asset should go to the defaulter or borrower once all debts and obligations to the lender have been paid. For instance, if a borrower fails on a mortgage and the lender sells the house to recoup their losses, the proceeds of the sale may exceed what the borrower owing. In this situation, the borrower is legally entitled to collect the additional money. This clause serves to prevent the lender from unfairly enriching themselves by holding onto more money than they are entitled to. The lender must give the borrower back the additional money since they are entitled to it.

4. A Humane Approach:

In order to collect outstanding debts, lenders are permitted to use recovery agents; but, they must make sure that these agents treat debtors with respect and fairness. Borrowers may only meet with recovery agents at convenient times and locations, and they must not be subjected to harassment or intimidation. They must not transgress any decency norms and must plan their visits between 7 am and 7 pm.

Borrowers may complain to the lender or the banking ombudsman officers if they believe that recovery agents have physically or verbally harassed them or their family members. Lenders are required to take steps to guarantee that borrowers are treated with respect and that their rights are upheld.

What actions should you take if you can't pay back a loan?

The first thing you should do if you can't pay back a loan is get in touch with the lender and explain the problem. By restructuring your loan or lowering the EMI amount, you may be able to come up with a repayment strategy that will make your payments more tolerable. If you don't make your loan payments on time, you risk incurring late fees, fines, and harm to your credit. Therefore, in order to come up with a solution that benefits both sides, you need be proactive and open with your lender.

The lender may provide a "EMI holiday" or moratorium period in specific circumstances, such as an unexpected death in the family, health problems, or a loss of employment. The borrower may better manage their money at this time since they won't have to make any EMI payments. Lenders may temporarily suspend loan payments, often for a few months, to provide borrowers who are having financial troubles some respite. However, you should review the terms and circumstances with the lender before choosing an EMI vacation since it might raise your overall interest expense.

Bank Debt Recovery Procedures

Banks have never taken prompt recovery and the resulting decline in non-performing assets (NPAs) as seriously as they do now. It's crucial to keep in mind that the core of non-performing assets management is recovery management, whether it pertains to new loans or existing loans. The issue of debt collection and past-due loans is one of the biggest issues Indian banks are now dealing with. The causes for this might be different for various financial institutions depending on the kind of loans involved.

Here, an effort is made to identify some of the reasons why loans are defaulting and causing financial institutions to struggle with past-due debts. To determine the reasons of failures, several banks' recovery officials are questioned.

These explanations might help banks recover debts more effectively in the future. Creating a plan of action helps in reaching a certain purpose or goal. Therefore, recovery agents need to come up with a plan for recovering debt. The advice provided below will assist in creating an effective plan for debt recovery: The collection procedure must adhere to regulatory requirements as well as recovery rules particular to banks.

When collecting from salaried staff, for instance, the date should coincide with when the employee's paycheck is received by or deposited to their account, often at the end of the month. The effort should match the cash flow from sales in the case of SME debtors. If an agriculturalist to be collected from, it should happen as soon as the crops are sold. Agents will need to be knowledgeable about bank products to handle this. The agent should make every effort to ensure that payments are paid before the debtor uses the cash inflows to pay other bills [7]–[9].

CONCLUSION

In conclusion, the nuances of default and loan recovery tactics are crucial elements in the world of banking that have an immediate influence on borrowers' relationships and financial stability. While defaults are sometimes unavoidable, banks must take a proactive and all-encompassing strategy to reduce risks and the related losses. To protect the interests of both lenders and borrowers, effective loan recovery procedures are equally important. In order to avoid defaults, banks use a variety of tactics, such as strict credit evaluations, risk profiles, and ongoing monitoring of borrower financial health. Early intervention strategies like restructuring and refinancing provide insolvent debtors an opportunity to get back on their feet while lowering the risk of losses for the bank. When defaults happen, banks start loan recovery measures that may include bargaining, going to court, selling off assets, or restructuring debt. The goal is to recover unpaid debts while upholding legal requirements and maintaining good customer relations.

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CHAPTER 25

NAVIGATING BANK CREDIT IN A CHANGING FINANCIAL LANDSCAPE

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ABSTRACT:

This study offers a succinct review of the difficulties and tactics involved in using bank credit in a changing financial environment. Understanding the dynamics of bank credit is essential for both borrowers and lenders since financial systems change frequently. The study investigates how changes in economic conditions, regulations, and technology affect bank lending. It emphasizes how important it is for borrowers to adjust to evolving lending platforms, data-driven assessments, and credit assessment procedures. The study also explores the significance of financial literacy for making wise borrowing choices. It underlines how important it is to consider interest rates, payback schedules, and credit agreements in order to recognize possible dangers. The study also discusses the advantages of this shifting environment, including the opportunity for speedier approvals, improved access to underserved groups, and a variety of loan possibilities.

KEYWORDS:

Bank Credit, Banking Sector, Economy, Industry, Interest Rates, Fintech.

INTRODUCTION

Organizations that provide financial services have historically had a variety of crucial roles in allowing and forming the contemporary world. The previously mentioned seven factors for change provide financial services organizations the chance to play these roles in more direct, individualized, and socially responsible ways. Additionally, in addition to tackling the many social issues that urgently need fresh approaches, they may expand their responsibilities to stimulate and accelerate the human-centric ecosystems that are altering the economy.

Upcoming financial services

Global commerce and society are being reshaped by strong forces of change. The financial services sector is at a turning point in its development as a new economy focused on people begins to take shape. Without having to make large trade-offs between profit and good social effect, forward-thinking businesses may play a big role in rebuilding public trust and fostering a fair, inclusive, and sustainable society by adopting the ideals of a higher bottom line.

A fresh viewpoint on the direction of financial services

Discover our vision for a financial services future that is more focused on people, the factors driving it, and the enormous role that financial services organizations must embrace if they are to not just succeed in it but define it [1]–[3].

Key points:

1. Without suffering a large loss in growth or earnings, financial services businesses have a rare chance to solve important social concerns and create new markets. This need puts businesses in a position to have an influence on almost every sector of the economy, actively restore confidence, and revolutionize not just the financial services industry but also the whole of human existence.
2. To move the industry toward 2030, seven key dynamics are at work in the environment at large as well as in the ways value is produced and collected. Together, they will build on one another to enhance the next difficulties and chances. They will also provide business executives the motivation to take courageous actions that will not only secure a profitable future but also contribute to shape it.
3. As technology advances, more and better data sources are becoming available, making access to data flows a crucial resource. The capacity of businesses to satisfy consumer expectations will depend on their access to and understanding of these ever-growing data flows, which are now the fifth and possibly changing component in production. To remain competitive, incumbents will need to rethink their data policies, finding a fine balance between sharing data with allies and maintaining strict control over confidential information.
4. Customers will increasingly behave as rivals to financial services firms as services become more commoditized and disintermediated and more sophisticated. Customers' requirements and desires will keep changing, and new platforms will provide them more and more options for meeting their own financial demands. Businesses will be in a better position to keep current customers and draw new untapped ones if they treat consumers as stakeholders and meet their expectations (especially those of high-value customers).
5. The interdependence and fluidity of the market in 2030 will be unparalleled. The ongoing rise of new disruptors like fintechs, digital juggernauts, companies from other sectors, and even fresh entrants each with their own views, advantages, and disadvantages will characterize it. For incumbents to adapt to these trends, develop new income streams, and gain a competitive edge, they will need innovative business models and alliance ecosystems.
6. Businesses that build alliance ecosystems early will gain substantial benefits by locking in the network effects that many-to-many value webs provide. Companies have the chance to create a "financial layer" in the technology stack when it comes to integrating financial services into other customer-focused businesses; non-financial brands can then integrate that layer into their products to offer financial services to their customers and create new companies based on it.

Unusual disruption generates special opportunity

Everything is different now. We've had to adjust swiftly and be ready for new realities because of the COVID-19 epidemic.

As the conventional wisdom on the trade-offs between business and service to our civic society gradually fades, it is becoming more and more important to reestablish trust.

Financial services firms have a rare chance to solve significant social concerns without harming earnings while actively restoring public confidence in institutions as we move over the next ten years. They may, and should, aim for what is often referred to as a "higher bottom line."

7 factors influencing change

Seven essential reasons, in our opinion, will propel transformative change and allow financial services companies to chase a greater bottom line as we envision the US financial services market in 2030. These factors will, for the most part, speed up and magnify the upcoming difficulties and chances, and they will inspire people to think creatively and courageously in order to not only secure a more successful and inclusive human experience but also to help define the future of financial services. These dynamics are converging to provide the financial services sector a new, people-centered leadership across three domains: the macro environment, value creation, and value capture.

New positions for a new financial services future

New players with an interest in the sector are also becoming ecosystem catalysts in the meanwhile. These industry disruptors fintech firms, tech behemoths moving into the financial services sector, participants from other sectors, and even fresh faces bring a variety of advantages, disadvantages, opportunities, and dangers to the table. In the section below, we examine how these players must change to amplify, accelerate, and link their roles if they are to prosper in the future of financial services and boost the bottom line.

Paving the road for greater heights and a better profit

Financial services companies are in a position to shape almost every aspect of the economy and play a critical role in its transformation at a time when our society is at a crossroads. The industry and our shared human experience in the next decade and beyond may be greatly impacted by their capacity to grab the new chances that our changing environment offers. Not everything will go as planned; businesses must be ready for the shocks that will unavoidably occur during the next 10 years. Financial services, on the other hand, may pave the way for a future that is more inclusive, educated, sustainable, collaborative, and financially successful if they adhere to the concepts of a higher bottom line—putting people on par with profits, and deeds above intent[4]–[6].

Technologies that facilitate finance to create new company ideas

As business executives start to use innovative technology as a competitive edge against established rivals and as a reaction to emerging players, it is becoming increasingly commonplace.

1. Asset Optimization for Data:

Data consolidation efforts of customer and fragmented financial databases can drive better analysis, more accurate forecasts, and more complex KPI algorithms that will improve strategic planning and decision making. Traditional banks and financial services organizations own vast amounts of customer data that new fintech players do not.

Because new technology now exists to automate the consolidation process in order to achieve a "single version of truth," enterprises should avoid manually consolidating data, which is not only long and tiresome but also exceedingly hazardous.

2. Simplify Procedures:

By moving the conventional server room to the cloud, businesses have access to a range of high-end cloud technologies that can streamline and automate company operations, resulting in quicker turnaround times and more responsiveness and agility to market changes.

While conventional banks prefer to have their servers on-site, enterprises can take advantage of cloud technology's low entry barriers and scalable design.

3. Participate:

To hasten the development of new technologies like blockchain, distributed ledger, artificial intelligence, and robotics, to mention a few, banks, financial services, and fintech companies may work together. However, organizations need to collaborate to establish a global set of standards and legal framework, as well as to provide useful use cases and practical training. These promising technologies are expected to improve efficiency and effectiveness of processes, as well as to create new products and services. While there are still certain issues that need to be resolved before these technologies can become widely used, participating in these projects will position the CFO and their businesses as industry innovators leaders.

Acquiring knowledge for financial professionals

However, being proactive in learning about these new technologies is a must, rather than a choice, for financial professionals. Navigating these new areas of digital technology may be difficult. While there are many potential causes for the predicted 2 to 6 million job losses in banking throughout the U.S. and Europe over the next ten years, industry experts agree that the timing of the predicted losses is not only a coincidence.

Finance professionals, such as managing directors and CFOs from the largest banks in the world, are registering for fintech courses provided by prestigious colleges like Oxford University via GatSmarter and other online learning platforms in order to remain ahead of the curve.

Using current strengths

Fintech firms may gain from technology, but conventional banks and financial services firms also have advantages they may take use of.

Think about it: Have you ever hesitated to provide your Social Security and other such information when filling-up at a form in a bank? What would you feel if Facebook asked you for this information? People are still generally more willing to provide personal information to banks than to fintechs. That said, banks have an advantage in gaining the feeling of trust and security. This is valuable data that could be used for multiple cases such as

In fact, tech newcomers in the finance industry recognize that this is slowing them down in terms of speed to market. Therefore, CFOs should take this time to innovate and modernize their tech in order to prepare their organizations for the new wave of competition. Banks also have an advantage over tech companies in their knowledge and skill in compliance, risk management, and financial regulations.

DISCUSSION

Five skills to handle uncertainty

To navigate these headwinds, banks need tools to help them understand the fundamental drivers of portfolio and obligor performance. Ideally, they should also reevaluate tactical and strategic toolkits and ensure that operating models enable rapid execution. Five steps can support actions to achieve these outcomes. In the past year, the global economy has faced multiple challenges, and orthodoxies that have evolved over recent decades have become more uncertain.

1. Develop the capacity to swiftly model effects on portfolios and debtors across various situations.

The more factors and factor combinations that banks can model, the easier it will be to identify and scope potential impacts on portfolios and obligors due to increased uncertainty around future events, constantly shifting drivers, and an unusual combination of economic factors. In a time of increased complexity, scenario generation requires more granular factors, incorporating both economic and broader uncertainties (for example, geopolitical risks, supply chain shocks), and these should be combined with agile forecasting capabilities that enable quick calculation of potential portfolio income and losses.

Some banks are adopting new approaches to forward-looking credit assessment (Exhibit 1) to develop insights on the portfolio and obligor level based on scenarios. To this end, they are exposing a range of transaction metrics to discrete combinations of granular macroeconomic drivers—for example, food prices and utility bill inflation or rent increases and retail-customer interest charges.

2. Clarify risk thresholds and triggers

Current economic consensus suggests these conditions may not return anytime soon; in fact, it is reasonable to assume that the business cycle has shifted, and through-the-cycle portfolio behavior may significantly change. As a result, banks need to revisit through-the-cycle views of client performance in a higher rate environment, as well as verify through-the-cycle views of client performance.

Limits for measures including "one in X year" losses, the impact of stress scenarios, and the portfolio effects of downgrades or defaults should take into account shifting correlations and potential idiosyncratic events. This will lead to limit anchoring that better reflects potential risks and outputs under different scenarios, as well as generating new estimates of the risks and outputs under each scenario.

There will be areas where they want to tighten up on credit provision, but there may be others where the risk/return trade-off may be more favorable in the next two to three years, based on the assumption that through-the-cycle portfolio behavior will be different than in the past.

3. Create decision-making measures that are prospective.

Current metrics are frequently backward looking; their ability to predict the future is tightly bound to relationships with historical trends. In a volatile world, where many of those historical relationships are being upended, the predictive power of existing approaches is limited. As a result, banks need to develop more forward-looking metrics that highlight risks and opportunities quickly enough to enable effective analysis.

One institution built a performance matrix, plotting a variety of business drivers (for example, a decline in demand, risks and receivables repayments, or dependence on energy) against potential impact intensities across industries (Exhibit 2). It periodically reviewed the tally of business drivers against potential impact intensities across industries to help create a longer horizon of predictability.

4. Apply decision metric outputs to 'prebaked' management levers.

Accelerating change implies a higher bar for management preparedness; leadership teams can benefit from developing a set of "prebaked" actions that can be implemented quickly; aligning in advance allows for more creativity than decisions made on the fly; and will enable more clinical execution when necessary.

Bank leadership teams can effectively address a variety of credit oversight issues, including designing collections/repossessions, adjusting portfolio allocation, and refining customer engagement strategies as well as timely planning for second-order impacts like talent shortages by prudently monitoring forward-looking metrics and indicators. To ensure effective implementation, training at scale and across functions may be necessary, for example, upskilling employees in various departments.

5. Promote cross-functional viewpoints and flatter structures to promote agile decision making.

While it can be helpful to prebake actions and define initiation parameters, mobilization is also a challenge. To be effective, decisions should be operationalized through existing governance processes but at much faster speeds. Typical decision-making hierarchies are often insufficiently nimble to respond to a highly unpredictable environment. Banks need to rework their governance frameworks to enable much greater speed of decision making.

The objective should not be absolute precision, but rather an increased ability to rapidly understand the direction of travel so that actions can be aligned. Similarly, to minimize bottlenecks, authority should be decentralized where possible. Speedy decision making requires efforts to ensure that at each forum there is 360-degree information flow, facilitated by cross-functional collaboration.

Transformational path

Banks should evaluate whether they have the tools and procedures in place to produce the three edges that will enable them navigate through uncertainty as the global economy continues to surprise and the interest rate environment resets.

Decision makers can quickly identify the capabilities that need to be improved across the board by conducting a structured evaluation of capabilities and processes, possibly through analysis across a single representative portfolio. Similarly, focusing on a few select, high-impact portfolios can help illuminate pockets of value. Ideally, the exercise should be undertaken both from a risk function and business perspective, helping to ensure that machine learning can help identify and classify deposits and card-account spending in different categories, which can then be aggregated at the borrower level to determine likely disposable income and potential shocks under different scenarios. Finally, a continuous-monitoring tool can centralize data from treasury transactions, news, forward-looking industry-specific indicators, and markets to generate segment [7]–[9].

CONCLUSION

In conclusion, handling bank credit in a financial environment that is always changing requires a flexible and knowledgeable strategy. Technological breakthroughs, altering regulatory landscapes, and fluctuating borrower expectations define the current financial world. As a result, in order to properly use the advantages of bank credit while controlling the risks involved, borrowers, lenders, and regulators all need to adjust their strategy. Making well-informed decisions is the key to effective navigation. To grasp the consequences of credit and promote responsible borrowing and sensible financial planning, borrowers should participate in financial literacy efforts.

Lenders must strike a balance between innovation and risk management, relying on technology for quick credit decisions and promoting a customer-centered culture. In order to maintain a stable and open credit environment, cooperation between financial institutions and regulatory organizations is essential. To address new issues, advance ethical lending practices, and defend consumer rights, regulations must change. In a similar vein, banks need to actively interact with regulators in order to remain on top of compliance obligations and support a stable financial system.

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