A Study of Credit Management Policies at Co-Operative Bank Limited

Contents for Tables:-

S.R.No.	Contents	Page No.
1	Introduction	3-3
2	Co-Operative Bank	3-4
3	History of Co-Operative Bank in India	4-5
4	Features of Co-Operative Bank	6-7
5	Profit Allocation	8-8
6	Structure of Co-Operative Bank in India	9-9
7	Urbon Co-Operative Bank	10-10
8	Rural Co-Operative Bank • State Co-Operative Bank • Dist. Central Co-Operative Bank • Primary Agriculture credit Society • State Co-Operative and Development Bank • Primary Co-Operative Agriculture and Rural Development Bank	10-12
9	Function of Co-Operative Bank	12-12
10	Problem of Co-Operative Bank	13-19
11	Working of District Co-Operative Bank	20-24
12	Research Problem	25-25
13	Credit Risk Management	26-51

Introduction

Financial sector plays an indispensable role in the overall development of a country. The most important constituent of this sector is the banking system which acts as a conduit for the transfer of resources from net savers to net borrowers, that is, from those who spend less than their earnings to those who spend more than their earnings. It is fundamental to the economy of a nation, as it meets the credit needs of all sectors of society. The bank is a financial institution that performs various functions, such as accepting deposits, leading loans, financing and leasing, cash credit, letters of credit, routine transactions, etc. The Indian banking system includes RBI, the country's central bank under which different types of banks such as commercial banks, including public and private sector banks, foreign banks, and regional rural banks as well as Co-operatives are functional. Among the banking institutions in the organized sector, Co-operative banks are very popular. Co-operative banks, which are the blood of life in the Indian economy, play a fundamental role in the rural sector dominated by agriculture and the strengthening of the common individual and by financing their commercial and personal needs. Even the activity of Co-operative banks in urban areas has increased phenomenally in recent years due to the sharp rise in the number of popular Cooperative banks. Co-operative banks in India are registered under the Co-operative societies Act. The Co-operative bank is also regulated by the RBI. The powers were delegated to the National Bank for Agricultural and Rural Development (NABARD) pursuant to Article 35A of the Banking Regulatory Act to carry out inspections at state and central Cooperative banks.

1.1 Co-operative Banks

Co-operative banks are small units organized in the Co-operative sector that work in urban and rural area. These banks traditionally focus on communities, locations and work place groups and, in essence, provide loans to small borrowers and businesses. Co-operative banks in rural areas finance mainly agricultural activities for example, farming, animals, drain, rearing, individual back, and so on, alongside some little scale ventures and exercises driven independent from anyone else business. Co-operative banks in urban area for the most part back a few classes of individuals for independent work, enterprises, small scale

units and residential fund. Co-operative Bank is financial units belonging to its members, which are at the same time the customers and owners of their bank. Co-operative banks are frequently created by persons belonging to the same local or professional community or who have a common interest. Co-operative banks generally offer their members a wide range of banking and financial services (loans, deposits, bank accounts, etc.).Co-operative banks differ from other banks for their organization, their goals, their values, and their Government. In most countries, they are controlled by the banking authorities and must comply with prudential bank regulations, placing them at a level in the field of concert with the banks. Contingent upon the nation, this control and supervision can be actualized straightforwardly by state elements or representatives to a league or a co-operative central element. Co-operative banking institutions take deposits and lend wealth to most of the world. The cooperation segment includes the retail banking, mutual savings and credit associations, construction companies and co-operatives, as well as commercial banking services provided by manual organizations.

1.2 History of Co-operative Banks in India

For Co-operative banks in India, Co-operatives from the organizing group of people and entrepreneurs manage jointly and respectively democracy. There are services required for the sum of deposits and products that produce benefits for services. Professionalism in Co-operative banks reflects the coexistence of a high level of skills and quality in execution, fiduciary duties to an individual. Co-operative banks have achieved 100 years of presence in India. They assume an exceptionally basic part in the monetary framework. The Co-operative banks in India frame a vital piece of our money market today. Along these lines, a concise resume of their development should to be considered. The past of Co-operative banks backpedals to the year 1904.In 1904; the Co-operative credit society act was established to empower Co-operative development in India. Nonetheless, the advancement of Co-operative Bank from 1904 to 1951 was the most impervious one. The main phase of Co-operative banks development was the arrangement and direction of Co-operative society. The authentic changes which prompted the death of the Government of India Act in 1919 exchanged the subject of "Participation" from Government of India to the Provincial Governments. This has prompted the foundation of the following period of the historical

backdrop of credit establishment collaboration. There was the regular perception that urban banks have an imperative part to play in financial development. Various boards have said this. The Central Banking Enquiry Committee of India (1931) trusts that Urban Banks have an obligation to help business and middle class business. The Mehta-Bhansali Committee (1939) prescribes organizations to meet the criteria that banks should to have the capacity to fill in as banks and to suggest an association for these banks. The Co-operative Planning Committee (1946) announced that Urban Banks were the best organizations for small individuals, where banks' standard offers for the most part not concerned. The Rural Banking Research Committee (1950), affected by the minimal effort of foundation and activities, recommended the making of these banks even in residential communities, for example, Taluka. The Board of Governors of the Cooperation Council has been approved by the All India Rural Credit Survey Committee (AIRCSC), which comes with the consent of the assistant and the creation of the Co-operative Banks. The Co-operative banks are probably going to play a few obligations, to be specific, broaden a wide range of credit offices to clients in real money and kind, propel utilization advances, expand managing an account office in rural areas, mobilize deposits, supervise the use of loans etc. The necessities of Co-operative Banks are extraordinary. They have confronted a considerable measure of issues, which has influenced the advance of Co-operative Banks. Subsequently it was basic to think about this issue. The essential investigation of Urban Co-operative Banks was taken up by Reserve bank of India in the year 1958-59. The Report distributed in 1961 recognized the across the board and fiscally solid casing of Urban Co-operative Banks; accentuated the need to set up essential Urban Co-operative banks in new focuses and proposed that State Governments loan dynamic help to their development. In 1963, the Varde committee recommended that bank desks be prepared so that urban centre with a population of 1 lakh or more otherwise are not just a community or a caste. The Committee will introduce the idea of minimum capitalization requirement and commitment criteria to define the urban center from where it incorporates Urban Co-operative bank.

Features of Co-operative Bank

1) The Co-operative banks carry out all the major banking functions of deposit, mobilization, the provision of credit lines and the provision of remittances.

2) Co-operative Bank is perhaps the first government-funded agency in India. Get financial and other helps from Reserve Bank of India, NABARD, Central Government and State Government. They constitute the "most favored" banking segment with the risk of nationalization. For Commercial Banks, the Reserve bank of India is the ultimate lender, but the Co-operative Bank is the first bank to provide financial sources for initial capital (through the Government), working capital, refinancing.

3) Co-operative banks offer constrained managing an account items and pros are practically identified with rural items. However, Co-operative Bank likewise offer home credits.

4) Co-operative banks belong to both the capital market and the wealth market. Primary Agricultural Credit Societies offer medium-term and short term loans.

5) Co-operative banks are only partly financial intermediaries.

6) Co-operative banks work on principles of cooperation that is the reason why Co-operative banks get financial assistance from Reserve bank of India at concessional rate.

7) The sources of your funds (sources) are:

a. The Central and State Government,

b. The Reserve bank of India and NABARD

c. Other Co-operative institutions,

d. Ownership funds and,

e. Deposits or Bond Issues

8) Some Co-operative Banks are programmed banks, while others are unplanned banks. Co-operative banks are subject to CRR liquidity requirements and other banks, as planned and not programmed. However, their requirements are lower than commercial banks.

9) In the current the Indian Central bank has made changes in the interest rates of Co-operative Banks, along with changes in the interest rates of Commercial Banks. The structure of interest rates of Co-operative Banks are quite complex. The rates charged by them rely upon the sort of bank advance and differ starting with one state then on to the next.

10) Since 1966 the rate of credits and deposit of Commercial Banks has been managed straightforwardly by the Reserve Bank of India. Despite the fact that the Reserve Bank of India had the power to adjust the Co-operative banks rate, but this was only exercised after 1979 for non-agricultural progress they were free to apply any commission at their discretion. Although the primary goal of the Co-operative banks is to offer a cheaper credit to members and not maximize profits, they can access the wealth market to improve their income so they remain vital.

11) Co-operative Banks (COBs) play a key role in the growth of the short-term and long-term rural credit structure over India over the years. The Co-operative credit effort is said to be the first attempt to provide microcredit in India.

1.3.1 Co-operative bank shares some common features for their customer benefit: The rules of organization of Co-operative banks may differ according to their national legislation; Co-operative banks share common features as follows:

Customer-owned entities

In Co-operative Banks, the needs of clients meet the needs of the owners, as Cooperative banks members are both. Consequently, the first objective of Co-operative banks is not to maximize profits but to offer the best products and services possible to its members. Some Co-operative banks run with their members, but most of them also allow non-members clients to benefit from their banking and financial services.

Democratic member control

Co-operative banks are owned and controlled by their members, who electively elect the board of directors. As a general rule, members enjoy equal voting rights in accordance with the principle of cooperation of "one person, one vote".

Profit allocation

In a Co-operative Bank, a significant portion of annual benefits, benefits or surpluses is usually allocated to build reserves. Part of this benefit can also be distributed to members of the Co-operative, with legal or statutory limitations in cases mainly. The benefit is usually assigned to members through a profit dividend, which is identified with the utilization of the items and administrations of the co agents by every part, or through an intrigue or a profit, which is identified with the quantity of shares bought in by every part. Co-operative banks are to a great degree established inside local areas and communities. They are associated with local development and add to the maintainable advance of their communities, as their individuals and administration board ordinarily have a place with the groups in which they apply their exercises. Co-operative banks play an important role on the monetary development in the nations in which they work in and increment the productivity of the overall budgetary framework. Their specific type of enterprises, depending on the previously mentioned standards of association, has demonstrated effective both in developed and developing nations.

Structure of Co-operative Banks in India

The structure of Co-operative system in India can be divided into two broad segments

1. Urban Co-operatives Banks
2. Rural Co-operatives Banks Some Co-operative banks are scheduled banks, while others are nonscheduled banks. For instance, State Co-operative banks and some Urban Co-operative banks are scheduled banks but other Co-operative banks are non-scheduled banks.

Scheduled banks are those banks which have been included in the second schedule of the Reserve bank of India act of 1934.

Structure of Co-operative Banking in India

(As at End-March-2015)

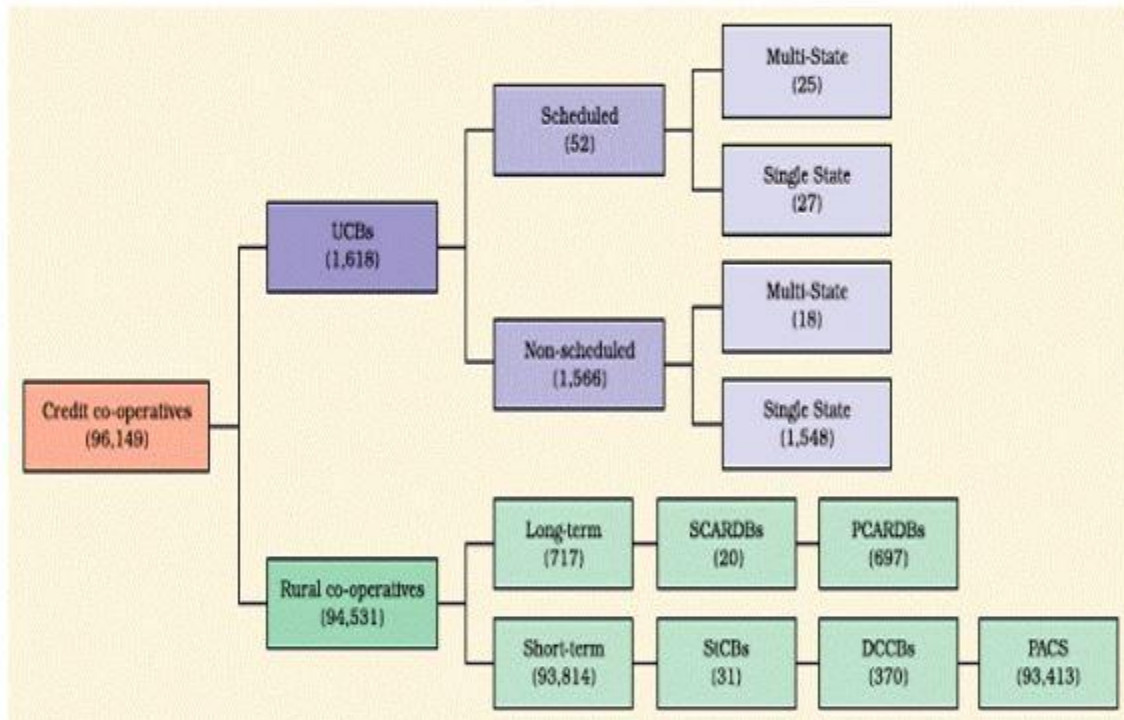

Figure: 1.1 Structure of Co-operative credit Institution of India. (Source: www. Reserve Bank of India.org) SCBs: State Co-operative Bank, DCCBs: District Central Co-operative Bank; PACS: Primary Agricultural Credit Societies; SCARDBs: State Co-operative Agriculture and Rural Growth Banks; PCARDBs: Primary Co-operative Agriculture and Rural Growth Banks. Notes:

1. Figures in parentheses indicate the number of institutions at end-March 2016 for UCBs and at end- March 2016 for rural co-operatives.

2. For rural co-operatives, the number of co-operatives refers to reporting co-operatives.

Urban Co-operative Banks

Credit unions based in urban areas are known as Urban Co-operative Banks. Urban Cooperative Bank also called the Primary Bank Co-operative Bank (PCB) by the Reserve
Bank of India. The Reserve Bank of India defines the PCB as small, Co-operative, organized banking units operating in metropolitan, urban and semi-urban areas to primarily meet the needs of small borrowers, that is to say, owners of small industrial units, retail traders and the salaried classes. Urban Co-operative Banks mobilize medium and low income savings groups and provide credit to small borrowers, among the weaker sectors of society. These banks are organized on a limited liability basis, generally extending their area of activity over a city. The main functions of these banks are promoting savings deposits that attract members and non-members and make loans to members. The management aspects of these banks continue to belong to the State Governments under the respective law of Co-operative societies. These multiplepresence banks are regulated by Central Governments and are registered under the law of multi-state Co-operative societies.

Rural Co-operative Banks

Rural Credit Co-operatives are the oldest and most extensive form of rural institutional financing in India. The main thrust of these Co-operatives in the agricultural sector is the prevention of the exploitation of peasants by the moneylenders. Rural Co-operative structures are divided into short and long term. Co-operative Bank is operating on three levels in different states. These are –

Short term Co-operative bank structures:

a. State Co-operative Banks- They function at the apex level in states.

b. District Central Co-operative Banks-They function at the district level.

c. Primary Agricultural Credit Societies-They function at the village or grass-root level.

Likewise, the long-term structures are further divided into –

a. State Co-operative Agriculture and Rural Growth Banks (SCARDS) - These function at state-level. b. Primary Co-operative Agriculture and Rural Growth Banks (PCARDBS)-They function at district level.

State Co-operative Banks

The State Co-operative Banks is a federation of the Central Co-operative Banks and acts as custodian of the Co-operative banking structure in the state. It monitors the 9 functioning of central banks and finances them, and through them helps primary Cooperative societies. It also acts as a link between the Reserve Bank of India, which lends central banks and primary societies.

District Central Co-operative banks

District Central Co-operative banks form the middle tier of Co-operative credit institutions. These are the independent units in as much as the State Co-operative banks have control or supervise their affairs. The bank's funds are made up of share capital, deposits, and loans and uncovered by State Co-operative Bank and joint ventures. These banks give wealth to societies within the limits of the ability to hire social loans. They also carry out all the activities of a bank of shares .

Primary Agricultural Credit Society

These are organized at the village level. These societies generally advance credits just for beneficial purposes. The main objective of a PACS is to raise capital to give advances and supporting the fundamental exercises of the individuals such as supply of agriculture contributions at minimum cost, enhancing water system ashore possessed by individuals, energize different salary expanding exercises, for example, cultivation, creature farming, poultry and so forth. In India, around 99.5 percent of towns are secured by PACs.

State Co-operative Agriculture and Development Banks (SCARBDs)

SCARBDs constitute the upper-tier of long term co-operative credit structure. Though long term credit co-operatives have been permitted to get public deposits under specific conditions, such deposits constitute a relatively small extent of their aggregate liabilities. They are mostly dependent on borrowings for on-lending. The main objective of the Co-operative State Agriculture and Rural Development bank is to finance primary agriculture and rural development banks. The bank issues long haul and medium term credits towards rural and unified exercises like development of godowns, cows shed, cultivate house, buy of grounds and so on.

Primary Co-operative Agriculture and Rural Development Banks (PCARDBs)

Primary Co-operative Agriculture and Rural Development Banks are the most lowest layer of long term credit Co-operatives. It is primarily dependent on the borrowings for their lending business. They give credit to formative purposes like minor water system, development of estate crops and for expanded purposes like poultry, dairying and sericulture on schematic premise. They get essential money related help from the Co-operative State Agriculture and Rural Development Bank. Keeping in mind the end goal to enlarge their extent of loaning to contend with other money related associations, the Primary Co-operative Agriculture and Rural Development Banks have been allowed to fund craftsman, create men and small scale business entrepreneurs.

Functions of Co-operative Bank

Co-operative bank also perform the vital banking functions of banking but they differ from Commercial Banks in the following respects:

A. Commercial banks are joint stock companies under the companies act 1956, or public sector banks under a separate parliamentary law, while Co-operative banks have been established under the deeds of the Co-operative society of several states.

B. Co-operative banks do banking business generally in agriculture and rural segment. However Urban Co-operative Bank, State Co-operative Bank and Central Co-operative Bank in semi urban, urban and metropolitan areas.

C. Only some of the sections of the 1949 Banking Regulation Act (fully applicable to Commercial Banks) are applicable to Co-operative Banks, which results only in partial control by the RBI ,Co-operative banks and

D. Co-operative banks function on the principle of cooperation and not totally on commercial parameters.

Problems of Co-operative Bank

The essential link in Co-operative finance system i.e. Co-operative Bank itself remains
very poor. They are too small to operate property and some of them are available only on the paper.

a. The NPLs of the Co-operative Bank are higher than those of Commercial Banks in NPLs to asset ratios.

b. They are playing out the untrustworthy practices by the groups of executive.

c. They are to a great extent relies on Government capital than the investors commitments.

d. The laborers cooperation in the working is substantially lesser than anticipated.

e. They are facing infrastructural weakness and structural laws. They do not have potentials in members, deposits and borrowers.

f. Co-operative Bank till now needs to depend intently on renegotiating offices from the Government RBI and NABARD. They are not ready to wind up selfsubordinate through their sources of deposits.

g. They have a large number of political and official interventions in their work. In addition to that government interventions that are also coming to their path of progress and preventing them from becoming self-sufficient. Large of the banks are governed or managed by politicians.

h. They are faced with a poor quality of loan assets and a poor recovery.

1.7 Co-operative banks and NABARD

It is the apex banking Institution to provide finance for agriculture and country development National Bank for Agricultural and Rural Growth was built up on 12 July 1982 with the paid up capital of Rs.100 cr. by 50:50 commitment of legislature of India and Reserve bank of India. NABARD has been sharing with the Reserve bank of India certain supervisory functions in respect of Co-operative banks and Regional Rural Banks (RRBs).

Objectives of NABARD NABARD

works for the progressive institutionalization of rural credit and ensures that agricultural credit claims are met, including new and future areas, such as tissue culture, bio-fertilizers, rain irrigation, irrigation drop etc. It also has the responsibility to promote and integrate rural development activities through refinancing.

Functions of NABARD

A. It is an apex institution which has power to deal with all matter concerning policy, planning as well as operations in giving credit for agricultural and other economic activities in rural area.

B. It is a renegotiating agency for those institutions that provide investment and production credit for advancing the several growth programs for rural growth. It prepares rural plans, annually, for all districts in the economy.

C. It inspects RRB and Co-operative banks under the provisions of the 1949 Banking Regulation Act.

D. Undertakes inspection of State Co-operative Agriculture and Rural Growth Banks (SCARDBs) and apex non-credit Co-operative Societies on a voluntary basis.

E. Provides recommendations to Reserve Bank of India on opening of new branches by State Co-operative Bank.

F. Administering the Credit Monitoring Arrangements in Co-operative Bank.

G. NABARD will receive such statements and other information regarding Regional Rural Banks and State Co-operative Banks, which would facilitate NABARD's close monitoring of the institutions' performance, health and viability.

Core Functions of NABARD for Co-operative Banks

NABARD has been entrusted with the statutory responsibility of conducting inspections of State Co-operative Bank (SCBs), District Central Co-operative Bank (DCCBs) and Regional Rural Banks (RRBs) under the provision of the Banking Regulation Act, 1949.

A. To serve as an apex financing agency for the institution proving investment and production credit for promoting different growth actions in rural area.

B. To coordinate the rural financing activities of all organization occupied with advancement work at the field level and association with the Government of India, The State Government, Reserve Bank of India and other national level Institution concerned with policy formulation; and

C. To undertake monitoring and evaluation of scheme refinanced by it. 13

D. NABARD also gives guideline for promotion of group activities under its programs and provides 100% refinance support for them.

E. It also supports Vikas Vahini volunteer programs which offer credit and growth activities to poor farmers.

F. It is also inspect and supervises the Co-operative Bank and RRB to periodically ensure the growth of the rural financing and farmer’s welfare.

G. NABARD also recommends about licensing for RRBs and Co-operative Bank to RBI.

District Central Co-operative banks in India

District Central Co-operative banks are a federation of primary societies and other functional societies, the members are the affiliated District Central Co-operative Banks. The District Central Co-operative banks fills in as an association between State Cooperative Bank and Primary Agricultural Societies. In a couple of cases, they draw in the surplus assets of certain essential social orders, to supply the same to others. Hence, District Central Co-operative Bank Act as adjusting focuses to the

essential social orders. District Central Co-operative banks are enrolled under the Banking Regulations and are under the administrative control of the Reserve Bank of India. It is normal that the banks will take after the different significant arrangements of the Banking Act and will be liable to intermittent supervision so they will act as indicated by the laws and with reasonability. In the event of District Central Co-operative Banks, NABARD has been designating as under the RBI. The District Central Co-operative banks are considered as a nerve center to control all the Co-operative activities in a specific area of operation, usually a district. District Central Co-operative banks play a very significant role in the growth of agriculture and the rural people. The performance of the District Central Co-operative banks is determined by the recovery, quantum of loans and advances issued, profitability, repayment to the higher financial institutions etc. At present, District Central Co-operative banks are reluctant by the poor performance of their credit portfolio recovery, which has led to greater delinquency and NPL.

History of District Central Co-operative banks in India

The Co-operative Societies Act was passed in 1904; there was no provision for the formation of central bank. The sponsors of the Co-operative progress expected that the rural credit societies would be able to attract substantial deposits from the members and well to do sections of the village community and their savings would be available to meet the needs of the needy in the villages. It was also contemplated that any deficiency in the funds would be made good by loans from the government. But these expectations of the promoters did not materialize. They could not augment their own capital base by encouraging thrift and self help among their members. The advance picked up notoriety; the social orders began expanding in number significantly. In any case, the money related plans visualized did not yield enough riches to meet their developing necessities. The Co-operative Societies Act was, along these lines, corrected in 1912 with a view to allowing enrollment of primary societies. It might hold any importance with take note of that even before the alteration; some national banks had been built up to oblige the monetary needs of the essential social orders. The main national bank was enlisted in Uttar Pradesh

in 1906 as an essential society. In any case, the primary ideal national bank in the present sense saw the light of the day in the rancher central territories and Berar. In Rajsthan, the Central Cooperative Bank was began in 1910 at Ajmer. In any case, there was no arrangement for development of Central Co-operative banks preceding 1912. It was in the year 1912 that an Act, identifying with Co-operative social orders accommodated the development of District Central Co-operative banks. The all India Rural Credit Survey Committee embraced the perspectives communicated by this Reserve Banks standing warning council on rural credit, that there should to be just a single national bank for each region, yet in the event that, nonetheless, different conditions, defended, the arrangement of a bank for an area littler than a region, there should to be no complaint to that. In perspective of the presence of more than one national bank in a locale which did not fit in with the standard, the advisory group unequivocally prescribed that plans of amalgamation must be presented in all states nearly on an obligatory premise and the base benchmarks as to possessed capital and working capital of the region national banks 115 were additionally consented to paid up share capital and holds about Rs.3 lakhs and working capital of Rs.20 to 25 lakhs. The Central Bank has gone through a few periods of development, stagnation and restoration from their origin to the beginning of the arranging time. Their advances made amid the war time frame Central Co-operative banks in numerous parts of the nation were powerless and required defense. The all India Rural Credit Survey Committee brought up that, "The focal Co-operative banks in many states are to great degree unsuitable foundations. It is hence, essential to draw up for each state gets ready for the legitimization and fortifying of Central Co-operative banks in a few of their viewpoints including budgetary and the regulatory in a few phases. Be that as it may, the banks have gained fast ground with dynamic help of the legislature and the Reserve bank of India and State Co-operative bank. Presently, they have investor of Central Cooperative banks and such goes about as loan specialist of final resort.

1.10 Objectives of District Central Co-operative Bank

The objectives of the DCCBs are:

1. To finance the primary societies for agricultural purposes.
2. To attract local deposits.
3. To develop and extend banking facilities in rural areas and make the people banking minded.
4. To provide a safe place for investing the reserves of the primary societies.
5. To supervise the working and management of the affiliated societies.

Functions of District Central Co-operative Bank

The District Central Co-operative banks are expected to render the following functions:

a. Raising sources and attaining self-sufficiency of sources is one of the important objectives of District Central Co-operative banks. The bane of the Co-operative progress is that of excessive and continuous dependence on Government for their resource. Even after decades of existence they are not able to stand on their own legs. District Central Co-operative banks provide a solution to this, in that sense they alone can mobilize the much needed sources.

b. The District Central Co-operative banks are expected to guide the Primary Agricultural Credit Societies and other member societies in all respects. By being this extreme financing agency they have the responsibility to supervise the functioning of Primary Societies. In addition to the financial help the District Central Co-operative banks can help the ultimate to maintain proper accounts, disseminate the values of cooperation for the transformation of the rural economy.

c. Growth of rural banking is one of the important tasks of District Central Cooperative Banks. Among the co-operatives, the District Central Co-operative banks alone are armed with necessary infrastructure to extend banking facilities to rural areas through branch banking.

d. In perfecting and popularizing the crop loan system the role of the District Central Co-operative banks needs no emphasis. The crop loan system with a

17 decade of service to the farmers needs certain modifications. To take its benefits to the entire farming community long term strategy is to be formulated and this could be done only by District Central Co-operative Banks.

e. In the program of revitalization of the primary agricultural societies the central banks are expected to initiate and function with the Co-operative societies. Feasibility among primary societies could be attained only with the help of the District Central Co-operative Banks.

f. It is the duty of the District Central Co-operative banks to see that all.

g. Primary Credit Societies are having full time paid secretaries. In this respect, if circumstance permits, they can organize the management cadre to man the village credit societies with qualified personnel.

Funds Management of District Central Co-operative Bank

The success of any financial institution depends upon its resource mobilization, its deployment of funds and its recovery performance. The funds needed by a DCCBs depends on such factors as volume of business, type of service it provides, kind of physical facilities needed, nature of competition it faces and degree of risk it takes in the conduct of day to day business.

Sources of Finance

The sources of DCCBs are classified in to two categories; namely owned funds & borrowed funds. The main components of owned funds are share capital and reserve fund. The borrowed funds consist of deposits, borrowings from Reserve Bank of India , NABARD and SCBs.

Share Capital –

The share capital forms an integral part of owned funds. An individual or a primary level society has an obligation to buy at least one share of the bank for enjoying the rights of membership. The PACS/PLS, the State Government and other special Agencies like SFDA are ‘A’ class members, while the individuals are ‘B’ class members.

State Government Participation –

The Reserve bank of India has set up a fund called National Agriculture Credit (Long Term Operations) for the purpose 18 of making advances to State Governments for enabling them to contribute the share capital to DCCBs. The NABARD has been entrusted with the above function.

Deposits –

Deposits are an important tool for resource mobilization. Higher deposits will enable the banks to reduce the dependence on external capital. At present it is more important because of the fact that the NABARD has linked the concessional finance to banks to deposit mobilization performance of the District central cooperative Banks.

Borrowings –

It is a normal feature of the bank to borrow funds as and when internal funds are not sufficient. The volume of borrowings depends upon the deployment of funds and repayment performance. Further the volumes of borrowings are limited to 10 times the paid up share capital + RF or as permitted by the RCS from time to time. The banks are borrowing regularly from NABARD.

Cash Credit Limits –

The DCCBs are permitted to draw the advances from the SCBs, as and when the demand for loans arises from the members. This is termed as cash credit facility. Reserve Bank of India also provides rediscounting facility or making advances against 'Co-operative papers'.

Working of District Central Co-operative Banks

The area of Function:

It varies from the taluka to district and tahsil in some states to a district, of several talukas or tahsils other states. A District Central Cooperative Bank should cover as large an area as compatible with convenience and efficiency, the present policy is that there should be only on central bank for each revenue district.

Membership:

It is confined both to individuals and societies. Membership is open not only to rural co-operative credit societies but also to marketing societies, consumer's stores, farming societies and urban co-operative credit societies. Individuals are no longer taken as members on grounds of safety.

Borrowing Power:

It is generally related to their own funds. In practice a ratio of 1.10 between owned funds and deposits is generally considered as the norm. The borrowing power of these banks is generally fixed at 12 to 15 times of their paid up share capital and reserve fund. These loans come from external agencies, ie the State 19 Co-operative Banks, the Government, R.B.I, NABARD, State Bank of India and jointstock banks

Loan policy:

Loans are generally, advanced to primary credit societies for financing agriculture such as cultivation expenses, purchase of seeds, manure and other requirements for seasonal agricultural operations for a short-term (say for 12 months) and reclamation, building of cattle sheds, digging and repairing of wells, purchase of cattle and carts for medium term (ranging from 1 to 3 years) ; for purchase and installations of pumps and oil engines for a medium term (for periods not exceeding 5 years) and for refund of deposits (not exceeding one year). Credit are allowed on appropriate security, for example, landed assets, house mortgage, cattle, agricultural produce, gold, or ornaments, fixed deposit receipts, life insurance policies, Government promissory notes and promotes executed by the borrowing societies. At the general public level, the credits are secured by individual security for dissolvable individuals other than mortgage of lands. The rate of interest on loans and advances charged by these banks on the advances in respect of funds obtained by borrowing from the apex bank varies between 1 to 3 percent.

Management:

The Management of the DCCBs generally vests in the Board of Directors, consisting of 12 to 15 members. These banks supervise the primary societies. At least one

supervisor looks after 20 societies and one senior supervisor manages 80 supervisors.

Loan facilities available through District Central Cooperative Banks

a) Loan to salaried members up to Rs. 2.00 lakh marking.

b) Loan up to Rs 1.00 lakhs to provide domestic durable goods.

c) Mortgage / visionary loan up to Rs 10.00 lakhs for small businessmen.

d) Loan upto Rs. 6.00 lakhs for purchase of vehicles under SRTO scheme.

e) Loan uptoRs 2.00 lakh against receipt of Warehousing Corporation.

f) Under the Deendayal Upadhyay Co-operative SwarozgarYojana, maximum marking for agriculture and non-agricultural purposes is Rs. 2.00 lakh loan. 20 g) Loan upto 85% of the actual value of agricultural machinery under agricultural mechanization. h) Maximum marking for house building / repair / up gradation etc. Loan up to Rs 10.00 lakh i) Loan against KisanVikas Patra, NSC and Fixed Deposits.

Achievement of District Central Co-operative Banks

Major achievements of the year 2010-11, 2011-12 and 2012-13 1)

1)In the year 2010-11, 2011-12 and 2012-13, short-term crop loan distribution of 3262.34, 3818.87 and 4872.88 crore respectively.

2) The share of the bank was 121.40, 143.85, 171.33 crore mark in the 2010-11, 2011-12 and 2012-13 mark respectively.

3) Working capital of the bank, in the year 2010-11, 2011-12 and 2012-13 respectively marking the mark is 7221.93, 8027.69 and 8907.87 crore.

4) Deposits of the bank were marked as 4343.48, 4630.72 and 4905.85 crore respectively in the year 2010-11, 2011-12 and 2012-13.

5) For the distribution of crop loan to the District Co-operative Banks, the bank has made refinance of Rs. 1970.52, 2541.85 and Rs. 3051.16 crore respectively in the year 2010-11, 2011-12 and 2012-13.

6) The Capital Adequacy of the Banks is 17.63, 14.32 and 13.25 percent relative to the standard set by the Reserve bank of Indiain the year 2010-11, 2011-12 and 2012-13 respectively.

1.15.2 Major achievements of the year 2013-14, 2014-15 and 2015-16

a. In the year 2013-14, 2014-15 and 2015-16 respectively Rs. 6180.81, Rs. 7001.24 and Rs. short term crop loan distribution of 7454.05 crore.

b. In the year 2013-14, 2014-15 and 2015-16, on the District Central Cooperative banks of the state, recovery of 71.78, 63.68 and 68.93 percent of the actual demand for interest and interest between the bank and the committee respectively. 21

c. The share of the bank is Rs.10 in 2013-14, 2014-15 and 2015-16 respectively. 202.50, Rs. 247.05 and Rs. 274.43 crores.

d. Working capital of the bank in the year 2013-14, 2014-15 and 2015-16, respectively Rs.9962.35, Rs.12004.55 and Rs. 11950.12 crores. e. Deposits of the bank in the year 2013-14, 2014-15 and 2015-16 respectively. 5267.06, Rs.6830.77 and Rs. 7110.57 crores.

Birth of District Central Co-operative Banks in Meerut Division

The history of the Co-operative progress in this district of Meerut and that of Ghaziabad date back to the year 1904, After passing of the co-operative societies Act in 1904 the first co-operative society of this district was establishment in thesil, a small village of Mawana tehsil. Since under the above act there was no provision for the formation of Primary Societies, hence another co-operative societies Act in India was enacted in the year 1912 for remedying the defect of the Act of 1904. It was in the year 1919 when some corporation of this district having full faith in the philosophy of cooperation, through of organizing a District Co-operative Bank in this district for providing credit facilities to the small farmer artisan and person of limited means who at that time were being exploited by those better placed in the society. Thus the Co-operative progress in this district gained momentum only after 1919, when this bank under the name and style of Meerut District Central Co-operative Bank Ltd. Meerut came in to the existence with the registration no.56 of 19/09/1919. Zila Sahkari Bank Ltd., Ghaziabad was built up in year 1983. Since its origin the bank has been executing lively and sharp civilities to the general

population for the comprehensive fiscal extension of the district by and large and Rural Growth specifically. This bank is in benefit through its Head Office situated at Rajnagar, Ghaziabad, Uttar Pradesh (India) and it has developed as one of the main bank in the State of Uttar Pradesh. In the year 1962, bank opened its first branch office at Baraut a town in the Bagpat tehsil of this District. With a view to attract more deposit and to provide more facilities 22 to our member societies. In order to provide banking facilities to the customers in the evening.

District Central Co-operative banks in Meerut Division

There are three Districts Central Co-operative Bank in Meerut Division consist of Meerut District Central Co-operative Bank, Bulandshahr District Central Co-operative Bank and Ghaziabad District Central Co-operative Bank. [108] 1.18 Functioning of the District Central Co-operative banks in Meerut Division In the beginning is started its working in a small rented building. The working of the bank at its infancy was on a very modest scale. 1.Membership- a Individual b Societies 80

Functioning of the District Central Co-operative banks in Meerut Division

In the beginning is started its working in a small rented building. The working of the bank at its infancy was on a very modest scale

1.Membership- a Individual *b Societies*	80 11
2.Paid up Share capital - a .Individual *b.Societies*	Rs.17300 Rs.1,065
3. Deposit	Rs.1,000
4.Owned Capital	Rs.18365
5.Working Capital	Rs.19365
6.Loan Outstanding	Rs.18182
7.Profit of the Year(1919-1920)	Rs.789

In order to control the increased volume of work and to develop its work, particularly of the banking business, bank got the first position in its building constructed in the year 1957-1958 with a provision for the strong room at the

Meerut branch of the bank for providing locker facilities to its constitutions. Simultaneously with the increases in volume of work bank also started its branch expansion work. In the year 1962, bank opened its first branch office at Baraut a town in the Bagpat tehsil of this district. With a view to attract more deposit and to provide more facilities to our member societies. In order to provide banking facilities to the customers in the evening, bank also opened its two evening branches at Begam Bridge and Budhana Gate in the city in the year 1967 and 1972 respectively. The bank through its branches at Meerut, Ghaziabad was the member of the clearing house for providing quick banking facilities to our constituents. Bank for the attainment of its principle objective has done and is doing very commendable work and is providing full cooperation in accelerating agricultural production in this district of Meerut and Ghaziabad by providing short term and medium term loans in cash and kind for meeting for various needs of the agriculturist, seed, fertilizers, and pesticides. Bank has been providing credit to the landless member of the agricultural credit societies along with the consumption loans for birth education marriage medical aids, death and customary function etc.

Research Problem

Co-operative Bank issued the loan to the borrowers, but the borrowers do not repay the loan to the bank on time. Non recovery of loans along with interest creates credit risk to bank. Credit risk is the biggest problem of Co-operative banks which affect financial health of the Co-operative Banks. At Present, The National Federation of State Co-operative Banks showed absolute Non- Performing loans of District Central Co-operative Banks was Rs. 1678096.17 Crore during 2011-2012 Crore and Rs. 2240604.43Crore in the year 2015-2016. In India the Non-Performing loans of District Central Co-operative Banks increased from 2011-12 to 2015-2016. [107][108]. In Meerut division District Central Co-operative Banks had 3315.6 lakh Non -Performing loan in the year 2015-2016. The foremost among the challenges faced by the banking segment today is the challenge of understanding and serious concerns about how bank manage the credit (loan) they issue out to customer with particular emphasis on the loan they give and how efficiently they manage to

recover such loan when the time is due. The increase of Non-Performing loans caused by lack of proper credit risk management. This study aim to what extent Co-operative banks can manage their credit risks, what tools or techniques are at their disposal and what bank should take proper remedial steps for managing credit risk. This study will delve into these matters comprehensively.

CREDIT RISK MANAGEMENT

Credit

The credit is the supply or assurance to provide money or substitutes for money (both in the balance sheet and off balance sheet) in a secured or unsecured form to a defaulter who is mandatory to pay upon request or at a preset or determinable amount. Future the amount borrowed along with commissions and / or interest on it.

Credit Risk

Credit risk is the risk of financial loss arising from the disappointment of a borrower or other money related counterparty to meet its statutory commitments to the Bank. In the first resort, the risk is that of the lender and includes lost principal and interest, disruption to cash flows, and increased costs. The pursuit of the Bank's development objectives renders substantial credit risk an unavoidable and necessary consequence of its business operations. Credit risk is the most important part of the bank's overall risk, and in ensuring that the establishment remains financially sustainable and is in this manner ready to accomplish its targets, dealing with this risk takes inclination.

Features Responsible for Credit Risk

The basic parts which cause credit risk and have hostile impact using a credit quality featured in various examinations led by master groups/bunches are: Internal and External factor influence credit risk like deficiencies in evaluation of credit proposals and in the assessment of credit estimation of money related quality of borrowers, Inadequately described crediting methodologies and systems, High prudential presentation limits for people and social event of borrowers, Absence of

credit center points of confinement for various ventures/business segment, Inadequate estimation of pledges acquired by the banks to secure the advance offices, Liberal advance authorizing powers for bank administrators without checks and adjust, Lack of information and abilities of authorities handling advance recommendations, Lack of information on functioning of various industries and performance of economy, Lack of proper coordination between branches of banks exploring credit limits, Lack of all around characterized authoritative structure and clearness regarding responsibilities, specialists and correspondence channels, Lack of appropriate arrangement of credit 51 chance rating, measuring and overseeing crosswise over land and product offerings, Lack of consistency of information being utilized for overseeing acknowledge and hazards related for crediting, Too much pestering staff responsibility and thus, demotivating staff and not looking credit judgment from information of the past.

Aim of credit risk management

The factors and objectives that shape up the bank's policies towards credit risk management are:

1. To make available sufficient liquidity to meet credit a ailments, interest, operational and other costs and losses;
2. To maximize profits; and
3. To support broad national policy of liquidity, interest rate stability, financial stability and above all, allocation of scarce financial resources efficiently to foster economic growth.

Difficulties face to credit risk management

Banks in emerging markets like India face intense challenges in managing credit risk. These may be determined by factors external/internal to the bank. The external factors include:

a) Regular instability in the business environment

b) Wide swings in commodity and interest rates

c) Legal framework less helpful of debt recovery

d) Financial restrictions

e) Government policies and controls

f) Economic sanctions

g) Natural disasters, etc

These may be aggravated by internal factors in the management of credit risk within the bank like:

a) Inadequacy in credit policies / administration

b) Lack of portfolio concentration limit

c) Deficiencies in appraisal of financial position of the borrowers

d) Poor industry inquiry 52

e)Inadequate risk estimating

f) Poor controls on credit documentation

g) Infrequent customer contact

h) Inadequate post-sanction surveillance

i) Lack of explained credit review instrument

j) Failure to enhance collateral position as credits fall apart

k) Absence of stringent resource grouping and credit loss provisioning guidelines

l) Inadequate governing rules in the credit procedure

m) Failure to control and review the credit procedure adequately

n) Poor recovery performance

o) Delay in sanction and disbursement

p) Lack of cooperation of leading bank

q) Sanction of credit in excess of the need /capacity These insufficiencies can prompt credit portfolio shortcomings including over centralization of credits in a single industry or segment, substantial arrangement of non-performing credits and credit losses. These may additional lead to miss liquidity and ultimately insolvency. The fact that the banks operate in an economic environment that poses objective difficulties for good credit management.

Managing of credit risk

Credit risk implies decrease of credit risk in an introduction by a wellbeing net of unmistakable and feasible securities including outsider endorsed

ensures/protection. Banks utilize various systems to moderate the credit dangers to which they are uncovered. Exposures can be secured by need shares in entire or to some degree with cash or securities, the presentation of a credit can be ensured by an outsider, or a bank can buy a credit additional to balance different types of credit risk.

A. Every bank employs risk mitigating techniques to hedge credit risk exposure. The acknowledgment of credit hazard relief is liable to various components like legitimate conviction of enforceability, viability and valuation of the collateral of the borrower. Credit risk mitigation techniques used by banks tend 53 to vary with the size, business strategy, credit granting policy and administration process.

B. Potential credit losses from a particular record, client and portfolio are mitigated by utilizing a scope of instruments for example collateral, credit insurance and other guarantees. The trust that can be placed in these mitigators is carefully assessed in the light of issues such as the certainty and applicability of the law, the correlation between the market valuation and the counterparty risk of the guarantor.

C. For Banking, these policies set out the clear criteria that must be satisfied if the mitigation is to be considered effective.

D. Risk mitigates should not be corresponded with the fundamental resources to such an extent that default would harmonize with a bringing down of the constrained deal estimation of the insurance.

E. Legal opinions and documentation must be in place.

F. Ongoing survey and controls exist where there is a maturity mismatch between the protection and exposure.

G. For all credit risk mitigates that meet the approach criteria, a reasonable arrangement of methods are connected to guarantee that the estimation of the fundamental protection is properly recorded and updated regularly.

H. Collateral composes that are qualified for risk mitigation include: money, business and trade property, fixed assets for example, engine

vehicles, airplane, plant and hardware, attractive securities, products, bank assurances, and letters of credit. Standard Chartered additionally goes into collateralized invert repurchase agreements. The guarantees and settlements along with collaterals are highly used to mitigate the credit risk by cooperative bank. Uses of credit covenants are considered as one of the most important credit risk mitigating techniques by banks. Basically, collaterals/guarantees are acknowledged just to help credits and may not serve the banks as a substitute for the borrower's capacity to meet the commitments. It is found that banks have the policies in place covering the suitability of different forms of collateral as a mitigating method, valuable procedures for the valuation of insurance, 54 and operational procedure to guarantee that security is, and keeps on being, enforceable and achievable. In case of guarantees and settlements banks calculate the level of exposure provided by the guarantor in relation to the credit quality and lawful capacity of the guarantor.

The administration of credit risk should get the best administration's consideration and the procedure should envelop

a. Measurement of risk through credit assessment/scoring

b. The quantification of the risk by estimating the expected losses on credits i.e. the amount of credit losses that the bank will experience in a specific time horizon (through the monitoring of portfolio behavior for 5 or more years) and unexpected credit losses, is to say, the amount by which through the standard deviation of losses or the difference between probable credit losses and a certain quantity of credit loss.

c. Risk pricing on a logical basis; and

d. Implementation of KYN policy

e. Focus on weak and/Problem credit

f. Internal Audit

The credit risk administration process should to be enunciated in the bank's credit policy, appropriately affirmed by the board. Each bank should constitute an abnormal state Credit Policy Committee, additionally called Credit Risk Management Committee or Credit Control Committee and so on to manage issues identifying with credit approach and

techniques and to investigate, oversee and control credit chance on a bank wide premise. The Committee should be led by the President / CEO / ED and should involve the heads of the Credit Department, the Treasury, the Credit Risk Management Department (CRMD) and the Chief Economist. Committee should, inter alia, formulate clear arrangements on norms for introduction of credit recommendation, money related contracts, rating standards and benchmarks, appointment of credit endorsing powers, prudential points of confinement on huge credit exposures, resource fixations, norms for advance guarantee, portfolio administration, loan review mechanism, hazard focuses, risk monitoring and 55 assessment, valuing of advances, provisioning, administrative/lawful consistence and so on. In the meantime each bank must set up a credit risk management department (CRMD), independent of the credit administration department. he CRMD must approve and select the consistency of the risk parameters and the prudential confinement points established by the CPC. The CRMD should also establish risk assessment frameworks, examine the nature of the early portfolio, recognize issues and gaps in rights create MISs and accept a credit survey / review. Banks may believe a separate arrangement for credit review / revision. The Department should conduct portfolio assessments and conduct comprehensive environmental studies to assess the resilience of the credit portfolio.

Credit Risk Strategy

A credit risk strategy or plan establishes the objectives that guide the bank's credit granting activities and its credit risk management functions. Strategies or directives:

A. The first reason for bank's credit system is to decide the risk appetite of the bank. When it is resolved the bank could build up an arrangement to improve return while keeping credit risk within predetermined limits..

B. It is basic that banks give due thought to their objective market while concocting credit risk strategy. The credit procedures should plan to acquire inside and out comprehension of the bank’s clients, and their organizations keeping in mind the end goal to completely know their clients.

C. The strategy should provide continuity in approach and take into account cyclic aspect of country’s economy and the resulting shifts in work and quality of overall credit portfolio. While the procedure would be assessed intermittently and changed, as

esteemed essential, it should be reasonable in long haul and through different financial cycles.

D. The senior administration of the bank should to create and build up credit strategies and credit organization techniques. Such strategies and methods might give direction to the staff on different kinds of loaning including 56

corporate, SME, shopper, farming, and so forth. At minimum the policy should include

- Detailed and formalized credit evaluation/ appraisal process.
- Credit approval authority at various hierarchy levels including authority for approving exceptions.
- Risk identification, measurement, monitoring and control Risk acceptance criteria
- Credit origination and credit administration and loan documentation procedures
- Roles and responsibilities of units/staff involved in origination and management of credit.
- Guidelines on management of problem loans. In request to be successful these policies must be clear and conveyed down the line. Advance any critical deviation/exception to these policies must be communicated to the top management/board and remedial measures should Managing credit risk be taken. It is the duty of senior administration to guarantee viable usage of these strategies.

Credit policy Credit

policy provides the framework for the entire credit management process. Written credit policies and procedures are the cornerstones of sound credit management. They set the objective standards and parameters to guide bank officers who grant credits and manage the credit portfolio. They also provide the board of directors, regulators, and internal and external auditors with a basis for evaluating a bank's credit management performance. When credit policies are carefully formulated, administered from the top and clearly understood at all organizational levels, they enable the bank management to maintain proper credit standards, avoid excessive risks and evaluate business opportunities properly. Loan policy is one aspect of the general range of policies that guide a bank's

operations. Credit policy must address issues such as target markets, rules for the submission of credit proposals, financial agreements (price and other conditions), qualification rules and criteria for risk acknowledgment, appointment of credit endorsement powers, 57 prudential cutoff points for vast credit exposures, active concentrations, credit guarantee rules, portfolio management, credit review mechanism, risk concentration levels, risk oversight and assessment, credit prices, credit loss provisions, regulatory / legal compliance, exceptional reports, etc. It should also cover other elements such as the availability of funds and the structure of the terms of responsibility. All commercial officials must clearly understand the bank's approach to credit sanctions and must be responsible for compliance with the established policy and procedure. In summary, a bank's credit policy must address total credit risk management. The significance of such approaches and methods that are appropriately created and actualized empowers the bank to

- keep up uniform and sound credit granting standard
- Ensuring operational consistency
- Monitor and control credit risk
- evaluating new business opportunities
- Identify and manage problematic loans Developing credit policy is particularly important when a bank must adapt to a complex and rapidly changing environment. Credit policy by establishing a common credit language throughout the organization helps in determining the level of acceptable risk and expected return.

Credit Approving Authority

Banks usually adopt either a committee or sequential process of credit approval. The former requires ultimate approval of a credit or credit facility by a committee that customarily consists of members of senior management and the heads of the credit departments. The sequential process involves an approval chain of individual credit officers with ascending levels of authority to sanction credit. Most of the Indian banks, especially in the public sector have adopted the sequential system of credit sanction. The proponents of the committee system believe that:

a) The committee has better decision making capabilities, by virtue of the combined experience of its members and

b) There is greater transparency in the decision making process.

Advocates of the sequential system, however, argue that:

a) Majority of the members may follow the preferences of the senior members of the committee.

b) The system may not always help in speedy decision-making.

c) It may be difficult to fix accountability to generate more responsible decision-making.

d) Committee may hence be more risk- prone Ultimately, the size of the bank, the scope of its operations and most important - its credit culture will determine the type of credit approval process to be adopted by it. It may be mentioned that RBI in its recent guidelines has asked banks to consider establishment of the 'Committee' system of credit approval. Banks must also develop an appropriate framework for informing and evaluating the quality of credit decisions made by the various functional groups. The quality of credit decisions must be assessed within a reasonable period of time, for example from 3 to 6 months, through a well-defined credit review mechanism.

Principles of the Assessment of Credit Risk

A) Establishing an appropriate credit risk environment

B) Operating under a sound credit granting process

C) Maintaining an appropriate credit administration, measurement and monitoring process

D) Ensuring adequate controls over credit risk

E) The role of bank management

A. Establishing an appropriate credit risk environment

1. The governing body should to be in charge of supporting and intermittently evaluating the credit risk system of the bank and its critical credit risk arrangements. The technique should reflect the bank's resistance for risk and the level of profitability that the bank hopes to accomplish by causing different credit risk.

2. Credit risk strategy approved by the board of directors and developing policies and creating arrangements and techniques for recognizing the estimation, observing and control of risk. These arrangements and strategies should 59 address credit risk in all saving mone address credit risk in all saving money resources and in the individual portfolio and credit level.

3. The bank must recognize and manage the credit risk characteristic in all things and activities. New items and exercises should be liable to fitting systems and controls before their presentation or execution.

B. Operating under a sound credit granting process

1. Banks must work under sound, all around characterized credit-granting criteria. These criteria should include a thorough an intensive comprehension of the borrower or counterparty, as well as addition the reason and structure of the credit, and its wellspring of repayment.

2. Banks should set up general credit limits at the level of individual borrowers and counterparties, and gatherings of associated counterparties that aggregate in comparable and important way different types of exposures, both in the banking and trading book and on and off the balance sheet.

3. Banks should have a clearly-established process in place for approving new credits as well as the extension of existing credits.

4. All extensions of credit must be made on an arm's-length basis Specifically, credits to related organizations and people must be checked with specific care and other proper advances taken to control or relieve the dangers of associated loaning.

C. Maintaining an appropriate credit administration, measurement and monitoring process

1. Banks should to have set up a framework for the continuous organization of their different credit chance bearing portfolios.

2. Banks must have set up a framework for observing the state of individual credits, including determining the adequacy of provisions and reserves

3. Banks should to create and use inside risk rating frameworks in overseeing credit risk. The rating framework ought to be steady with the nature, size and many-sided quality of a bank's exercises.

4. Banks must have data frameworks and expository procedures that empower administration to quantify the credit risk natural in all on- and off-balance sheet exercises. The administration data framework ought to give satisfactory data on the creation of the credit portfolio, including identification of any concentrations of risk.

5. Banks must have set up a framework for checking the overall composition and quality of the credit portfolio.

6. Banks should take into consideration potential future changes in monetary conditions while evaluating singular credits and their credit portfolios, and should assess their credit risk exposures under distressing conditions,

D. Ensuring adequate controls over credit risk

1. Banks should establish a system of independent, continuous credit review and the consequences of such reviews should be communicated directly to the board of directors and senior management.

2. Banks must guarantee that the credit-allowing capacity is as a rule appropriately oversaw and that credit exposures are inside levels steady with prudential models and limits. Banks should establish and enforce internal controls and other practices to ensure that exceptions to policies, procedures and accounted for in an opportune way to the fitting level of administration

3. Banks must have a framework set up for overseeing issue credits and different other exercise circumstances.

E. The role of bank management

1. Bank Management should ensure that there is an effective framework in place to recognize measure, monitor and control credit risk as a component of a general way risk management.

2. They should direct an autonomous assessment of a bank's strategies, policies, practices and methods identified with the giving of credit and the continuous

administration of the portfolio. Further, they should also consider setting prudential limits to restrict bank exposures to single borrower or groups of associated counterparties.

3. The Credit risk management is overseen at two levels In the first place is the small scale level and the second being large scale level. The smaller scale level credit risk management concentrates on each credit transaction of the bank, , though the large scale level credit chance considers the total credit exposure of the bank.

Tools of Credit Risk Management

Credit Risk Management encompasses a host of management techniques, which help the banks in mitigating the adverse impacts of credit risk.

Exposure Ceilings

In order to limit the magnitude of credit risk, prudential limits should be laid down on various aspects of credit:

1. Stipulate the current / profitable capital / debt ratio index, the debt service coverage index or other reasons, with flexibility for deviations. Conditions subject to detours are permitted and therefore the authority must also be clearly explained in Credit Policy;

2. Single/group borrower limits, which may be lower than the limits prescribed by Reserve Bank to provide a filtering mechanism;

3. Considerable presentation restrain i.e. whole of exposures expected in regard of those single borrowers getting a charge out of credit offices in abundance of an edge confine, say 10% or 15% of capital assets. The significant introduction cutoff might be settled at 600% or 800% of capital assets; contingent on the level of focus hazard the bank is uncovered;

4. The maximum exposure limits must be established for industry etc. Frameworks should likewise be set up to evaluate exposures at sensible interims and cutoff points should be adequate especially when a particular sector or sector is facing a delay or other sector / sector harms. Limits to exposure to sensitive sectors, such as advances against equities, real estate, etc., The fact that they are subject to a high degree of volatility in the price of assets and specific sectors, subject to frequent economic cycles,

may necessarily be limited. Likewise, high-risk industries, as perceived by the bank, should be located within the lower limit of the portfolio. Any excess of exposure must be fully supported by adequate guarantees or strategic considerations; and

5. Banks may consider the maturity profile of the credit portfolio, taking into account the market risks inherent in the financial statements, the risk assessment capacity, liquidity, etc.

3.11.2 Credit Risk Rating

An important tool for monitoring the quality of individual credits, as well as the total portfolio, is the use of an internal risk classification system. A very much organized inside hazard appraisal framework is a decent method to separate the level of credit risk in various credit exposures of a bank. This will permit a more exact assurance of the general attributes of the credit portfolio, of the fixations, of the issue advances and of the sufficiency of the arrangements for misfortunes on advances.

Need for credit risk rating model

The liberalization of Indian economy has brought up sweeping changes in the economic environment of the country. The banking sector, which has been traditionally used to lend in the closed environment is suddenly open to various kinds of risks arising out of globalization. The consistent reduction in the import duties and withdrawal of subsidies/tax benefits facilitating the industries to compete globally under a free environment has necessitated the banks to assess the risks involved in financing a borrower and update the same on a continuous basis. Typically, an internal risk rating framework arranges credits into different classes intended to consider the degrees in chance. The risk rating framework should to be attracted an organized way, consolidating, between alia, money related investigation, projections and affectability, modern and administration dangers. Banks may utilize the accompanying parameters for building up a risk rating framework suited for the bank:

A. Financial aspects

1. Quantitative parameters: Financial indicators: Financial indicators are mainly net worth, sales turnover, profits, and ratios such as liquidity, profitability, gearing, turnover etc.

- Historical comparison of the indicators
- Inter-firm comparisons
- Operational parameters - conduct of account, turnover in the account, etc. 63
- Collaterals

2. Qualitative aspects:

Qualitative analysis of financial risks that could impact the borrowing company's bottom line such as

- Accounting policies
- Auditor‘s qualifying remarks, etc. B. Management aspects: Evaluation of the management of the borrowing company, such as
- Structure & systems
- Its track record
- Honesty and integrity
- The promoters - their expertise, competence & commitment
- Market perception of the company and its promoters, etc C. Industry aspects such as:
- The trade cycle
- Regulatory aspects such as government policies, controls, etc
- Competition faced from the peers and the market for the products
- Technology levels of the unit vis-à-vis the developments in the country and abroad
- The input profile - raw materials, infrastructure, etc. and their pricing
- Products / user characteristics, the alternatives / substitutes available etc Credit risk rating is summary indicator of a bank's individual credit exposure.

An internal evaluating framework orders all credits into different classes based on fundamental credit quality .A well-structure credit rating framework is a critical device for checking and controlling risk inherent in individual credits as well as in credit arrangement of a bank or a business line. The importance of internal credit rating framework becomes more eminent due to the fact that historically major losses to banks stemmed from default in loan portfolios Once the risk rating frameworks are set up, the appraisals allotted to the borrowers can be utilized as basic contributions for setting evaluating and non-value terms of advances as additionally exhibit significant data for audit and administration of 64 advance portfolio. Inner risk rating frameworks are subsequently vital to credit risk management. These appraisals fill in as imperative apparatuses in checking and controlling credit risk. The rating appointed to borrowers or individual counterparties at the time the credit is conceded must be explored occasionally and the individual credits must get another rating when the conditions An internal rating framework would facilitate banks in a number of ways such as

a) Credit selection

b) Amount of exposure

c) Tenure and price of facility

d) Frequency or intensity of monitoring

e) Analysis of migration of deteriorating credits and more accurate computation of future loan loss provision

f) Deciding the level of Approving authority of loan. Such internal risk rating can be utilized for constantly assessing the credit portfolio and deciding the important changes to the credit technique of the bank.

RBI guideline on credit risk rating

1. Banks should have a complete risk scoring/rating system that serves as a single point sign of diverse risk factors of counterparty and for taking judgment in a reliable manner.

2. The risk rating system should be devised to uncover the general risk of loaning which is the basic contribution for setting cost and non-value terms of credits as additionally show important data for audit and administration of credit portfolio

3. Within the framework of qualifications, banks must also prescribe certain levels of critical standards or parameters beyond which they should not be considered as proposals. Banks may also consider a separate rating structure for large companies / small debtors, etc.

4. Reserve Bank of India in their notification on risk management system in banks have outlined the following guidelines in respect of risk rating of a borrower: 65

5. The overall score for risk is to be placed on numerical scale ranging between1 to 6, 1 to 8, etc.

6. Bank should ensure that un hedged market risk exposures of borrowers (foreign exchange exposure assumed by the corporate who have no natural hedges) should also be considered in the rating framework.

7. The credit risk assessment should be reviewed every two years and should always be removed from the normal renewal exercise

8. In order to ensure consistency and accuracy of internal ratings the responsibility for setting or confirming such ratings should vest with the credit review function and examined by an independent credit review group.

9. Bank should undertake comprehensive study on migration of borrowers in the ratings.

Linkages of credit risk rating

Credit risk rating is the pivot around which various functions of credit department is related. Credit risk rating is linked to the following aspects:-

a. To lend or not: Within the rating framework banks are to decide the rating beyond which they will not take any additional exposure. Credit risk rating facilitates in deciding the rating/grade up to which taking up additional exposure can be considered.

b. Pricing: Borrowers with weak financial position and put under high credit risk classification should to be evaluated high. Banks should develop logical frameworks to value the credit risk which should have a direction on the normal likelihood of default. The evaluating of credits should be connected to chance rating. Be that as it may, the reality, for example value of collateral, market forces, perceived value of accounts, future business potential and strategic reasons may also play an important role in pricing.

c**. Norms for collateral/margins:** The extent of collateral safeguard required and they require stepping up margin requirements are related to credit risk rating of a borrower. The higher the risk category the volume of collateral required will be more and the margins stipulated will be high. Banks may evolve norms on the above aspect related to risk rating criteria.

d. Product mix guidelines: It is necessary to gradually move from the current form of borrowers who resort to the credit line through the limit of the cash credit to term loans in working capital. In the case of a high credit risk category, banks may consider offering sight loans for a shorter duration taking into account the risk involved. Likewise, for borrowers with a low credit risk category, banks may consider setting the pre-financed credit line / limits for short-term disbursement. Similarly, a declining CC rate can be considered based on the amount of credit that can be used by borrowers in low risk categories.

e. Delegation of powers: The delegation of crediting powers may be linked to credit risk rating of a borrower. The authorities at various levels may apply their expertise in evaluating exposure to high credit risk category borrowers rather than high volume borrowers only. Similarly, the delegation of crediting powers should also be linked to the maturity of credit.

f. Vary the frequency of renewal and follow up process: Renewal of facility in case of low credit risk category of borrowers can be considered biannually whereas for high risk rating borrower can be done twice a year or even at quarterly intervals.

3.14 Testing risk rating model

Creating a risk-rating model requires a period of intense testing for a relatively short period of time. Three of the most important aspects of testing any credit rating system are the following:

1. Sensitivity of ratings to real changes in credit quality
2. Lead time with respect to recognized changes in quality,
3. Stability of ratings when no change has occurred.

One of the biggest problems for the banks in general is that they are too slow to recognize real changes. Lowering of rating based on false alarms can also have negative consequences for a relationship with a borrower. There is a tendency to give the customer the benefit of doubt and to wait and see. Unfortunately, the reluctance to recognize the truth about a borrower can lead to problems if real deterioration takes place

Credit Metrics Model Credit Metrics is a factual model created by J.P Morgan, the speculation bank, in 1995 for inward utilizes, yet is presently utilized worldwide by several banks. This model takes a shot at factual ideas, for example, likelihood, means and standard deviation, connection and focuses. This model was produced with

destinations in the frontal area Develop a Value at Risk (VAR) framework applicable to all institutions around the world that involve credit risks in the course of their business.

• Develop a portfolio vision that shows the correlation of credit events that can identify merger costs and the benefits of diversification in a market environment Apply it when making the following decisions: investment decisions, risk mitigation actions, determination of risk-based credit limits across the portfolio and capital allocations based on rational risk. Credit Metrics is a tool for assessing portfolio risk due to changes in the value of debt caused by changes in the credit quality of the debtor. This model includes changes in value caused not only by possible predetermined events, but also by credit quality updates and decreases, as the value of a particular credit varies with the quality of the corresponding credit. Credit Metrics also evaluates value at risk (VAR), volatility of value, not just expected losses. The model assesses the risk in the complete context of a portfolio that addresses the correlation of credit quality movements between debtors. This allows you to directly calculate the benefits of diversification or the potential of mergers across the portfolio. The transition table is determined for the various categories of bonds and therefore the combined probability for both combinations. Then the NPV of the portfolio is determined for all combinations and a probability distribution is constructed. These probabilities are actually an analysis of past migrations and the same is the case of the probability of default. In the event of default, a recovery rate is considered as the value of the portfolio. This distribution provides us with two measures of credit risk: standard deviation and percentile. Credit Metrics has the following applications:

• **Reduce the risk of the portfolio:** there are three options available: review the debtors that have the largest absolute dimensions, arguing that a single default among these would have the greatest impact, revaluing the debtors who have the highest level of risk percentage claiming that these are most likely to contribute to portfolio losses, re-evaluate debtors who contribute to the greatest absolute risk, arguing that these are the largest contributors to portfolio risk. The last classifications are the "fallen holy messengers", whose extensive shows were made when their appraisals were better, yet now they have a substantially higher rate hazard because of late deals.

• **Definition of limits: of course**, what types of risk measures to use for limits, and what kind of policy to adopt in relation to limits are management decisions? A user

can use credit metrics for two different purposes, namely what type of limit set, which risk measure to use for limits, and which policy to use against limits. These limits could be established in terms of percentage risk, exposure size and absolute risk. Identify correlations across the portfolio so that the potential concentration can be reduced and the portfolio is adequately diversified into unrelated components. The concentration can lead to an undue accumulation of risks at some point. This model has some limitations on the availability of data, but does not require any change as such for its application in the Indian scenario.

3. KMV Model

This model was developed by KMV Corporation based on Merton's (1973) analytical model of firm's value. This model uses stock prices and the capital structure of the firm to estimate its probability. The beginning stage of this model is the recommendation that a firm would default just if its advantage esteem falls beneath certain level (default point), which is a component of its obligation. Gauge the estimation of the organization's benefits and its unpredictability of advantages in view of the market estimation of capital and obligation structure in the opinion theory. Using these two values, a metric is constructed (distance from the default value or DFD) that represents the standard deviation number that the asset value of the company is far from the predetermined point. Finally, an assignment is made between the predetermined values and the predetermined actual frequency, based on the predetermined historical experience. The resulting probability is called the predicted default frequency (EDF).

Therefore, the EDF is calculated in three steps:

I. Estimate of the value of assets and volatility of assets in the value of equity and of the volatility of the performance of the shares,

II. Calculation of DFD, DFD = (Asset value – Default point) / (Asset value * Asset volatility)

III. Calculation of expected default frequency.

CAMELS Model of rating

1. Capital Adequacy: The capital adequacy measures the bank's capacity to handle the losses and meet all its obligations towards the customers without ceasing its operations. This can be met only on the basis of an amount and the quality of capital, a bank can access. A ratio of Capital to Risk Weighted Assets determines the bank's capital adequacy.

2. Asset Quality: An asset represents all the assets of the bank, Viz. Current and fixed, loans, investments, real estates and all the off-balance sheet transactions. Through this indicator, the performance of an asset can be evaluated. The ratio of Gross Non-Performing Loans to Gross Advances is one of the criteria to evaluate the effectiveness of credit decisions made by the bankers.

3. Management Quality: The board of directors and top-level managers are the key persons who are responsible for the successful functioning of the banking operations. Through this parameter, the effectiveness of the management is checked out such as, how well they respond to the changing market conditions, how well the duties and responsibilities are delegated, how well the compensation policies and job descriptions are designed, etc.

4. Earnings: Income from all the operations, non-traditional and extraordinary sources constitute the earnings of a bank. Through this parameter, the bank's efficiency is checked with respect to its capital adequacy to cover all the potential losses and the ability to pay off the dividends. Return on Assets Ratio measures the earnings of the banks.

5. Liquidity: The bank's ability to convert assets into cash is called as liquidity. The ratio of Cash maintained by Banks and Balance with the Central Bank to Total Assets determines the liquidity of the bank. 6. Sensitivity: Sensitivity covers how particular risk exposures can affect institutions. Examiners assess an institution's sensitivity to market risk by monitoring the management of credit concentrations. In this way, examiners are able to see how lending to specific industries affects an institution. These loans include agricultural lending, medical lending, credit card lending and energy sector lending. Rating Framework CAMEL model of rating was first developed in the 1970s by the three federal banking supervisors of the U.S (the Federal Reserve, the FDIC and the OCC) as part of the Uniform assessment system of financial institutions" of the regulatory authorities, to provide a convenient summary of the banking conditions at 71 the time of its examination on the site.

The banks were valued in five different components with the acronym C-A-M-E-L: capital adequacy, asset quality, administration, profits and liquidity. The banks received a score of "1" to "5" for each CAMEL component and a final evaluation of CAMEL which represents the total composite score of the CAMEL components as a measure of the bank's general conditions. The CAMEL system was revised in 1996, when the agencies added an additional "S" parameter to assess the "sensitivity to market risk", so it is "CAMEL" that is fashionable nowadays. Presently, each of the components of CAMELS is rated on a scale of 1-100 in ascending order of performance. The score of each CAMELS element is arrived by aggregating (by assigning proportionate weights) the scores of various sub-parameters that constitute the individual CAMELS parameter. Each parameter is awarded a rating A-D (A-Good, B – Satisfactory, C -unsatisfactory, and D-poor). Further, to bring granularity in rating, there are modifiers by way of (+) and (-) under each of A, B and C making a total of ten scales A+ through to D. The "composite CAMELS evaluation" is obtained by adding each of the component weights. In addition, the overall composite score is adjusted downwards to achieve reduced performance in one or more components. Banks can evaluate the usefulness of these models with appropriate changes to the Indian environment to adjust credit risk management. The achievement of credit chance models impacts time arrangement information on historical credit loss rates and other model factors, which cover different credit cycles. Banks may, therefore, endeavor building adequate database for switching over to credit risk modeling after a specified period of time.

Risk Based Scientific Pricing

Risk-return pricing is a fundamental rule of risk management. In a risk-return situation, borrowers with a weak financial position and therefore placed in a highcredit category should have a high price. Therefore, banks should evolve the scientific systems to assess credit risk, which should affect the probability of default expected. The pricing of credits normally should be linked to risk rating or credit quality. The probability of default could be derived from the past behavior of the credit portfolio, 72 which is the function of credit loss provision/charge offs for the last five years or so. Banks should build historical database on the portfolio quality and provisioning / charge off to equip themselves to price

the risk. But the value of collateral, the strength of the market, the perceived value of the accounts, the future potential of companies, the exposure of the portfolio / industry and the strategic reasons can also play an important role in pricing. Price review (risk premia) should also be made more flexible due to changes in the rating / value of collateral over time. Large banks all over the world have already implemented a risk-adjusted RAROC system for credit prices, which requires data on the behavior of the portfolio and the allocation of capital based on the credit risk inherent in credit proposals. Within the scope of RAROC, the lender begins by charging a margin of interest to cover the expected loss, the expected default rate of the borrower's rating category. Thus, the lender assigns sufficient capital to the possible credit to cover a certain amount of unexpected losses: the variability of default rates. In general, international banks allocate sufficient capital for the reserve or a provision for expected credit losses plus the capital allocated to cover 99% of the credit loss results. The systems for determining the price of credit risk must be scientific and take into account the expected probability of default. The price of credits is usually related to the risk assessment or credit quality. Hence, risk rating, especially in the case of commercial credits, will be the anchor for pricing credits. However, this may be duly supplemented and supported by other factors, such as:

- Market forces and competition
- Portfolio / industry exposure
- Value of collateral
- Value of account, both short term and long term
- Strategic reasons such as additional business potential or threat of loss of business, etc.

Portfolio Management

The existing framework for monitoring unpaid credits at the balance sheet date does not indicate the quality of the entire credit. Banks must develop adequate systems to 73 identify credit weaknesses well in advance. The CRMD, established in the central office,

must be assigned the responsibility for the periodic monitoring of the portfolio. The quality of the portfolio could be assessed by monitoring the migration (up or down) of borrowers from one rating scale to another. This process would be meaningful only if the qualifications of the borrowers are updated at quarterly / halfyearly intervals. Data on movements within the classification categories provide a useful understanding of the nature and composition of the credit portfolio. Banks could also consider the following measures to maintain the quality of the portfolio:

1.Stipulate quantitative upper limit on aggregate exposure in specified rating categories, i.e. certain percentage of total advances should be in the rating category of 1 to 2 or 1 to 3, 2 to 4 or 4 to 5, etc.;

2. Evaluate the rating-wise distribution of borrowers.

3. Exposure to one industry/sector should be evaluated on the basis of overall rating distribution of borrowers in the sector/group. In this context, banks should weigh the pros and cons of specialization and concentration by industry group. In cases where portfolio exposure to a single sector is not functioning properly, banks can increase the quality environment and experience rapid changes. Stress tests would reveal unidentified areas of possible credit risk exposure and links between different risk categories In unfavorable conditions, there might be a considerable connection between's different dangers, specifically credit risks. Stress tests can range from relatively simple changes to assumptions about one or more financial, structural or economic variables to the use of highly sophisticated models. The Board should review the outcome of these stress tests for the entire portfolio and make appropriate changes to the prudential risk limits to protect quality. Stress tests could also include contingency plans, detailing management responses to stressful situations.

4. Introducing discriminatory plans for the renewal of borrower limits. Low-level borrowers whose finances show signs of problems should be subject to renewal review twice / three times a year. Banks must develop an appropriate framework to monitor credit risks, in particular the exposure to currency risk of companies that do not have natural cover on a regular 74 basis. Banks must also designate portfolio managers to

observe the degree of concentration of the credit portfolio and exposure to counterparties. For the overall assessment of client exposure, banks may consider the appointment of relationship managers to ensure that the overall exposure to a single borrower is monitored, acquired and restricted. The Relationship Managers may service mainly high value credits so that a substantial share of the credit portfolio, which can alter the risk profile, would be under constant surveillance. Banks should likewise build up formalized frameworks for the identification of records that show credit weaknesses pronounced well in advance and also prepare internal guidelines for such an exercise and establish a time frame for deciding the courses of action. Many banks have adopted credit risk models for the valuation of the credit portfolio. Credit risk models provide banks with a framework to examine exposures to credit risk, in geographical locations and product lines in a timely manner, centralizing data and analyzing contributions from marginal and absolute .

Chapter Summary:

In this chapter researcher analysed the opinion of borrowers and branch managers on credit risk management in District Central Co-operative Banks, Meerut Division. Out of the 400 respondents of the study, 89.50% respondents told that the bank takes more time for sanctioning the loan, 83% respondents told that after sanctioning of the loan the bank officers are not prompt in disbursement of the loan so delay procedure and delay disbursement were the problem of respondents. 95% respondents told that crop failure, 87.5% respondents told that business failure and 67.5% respondents told that natural calamities were the important factors affect loan repayment to banks. Above problems were the reasons of repayment of loan to bank by respondents.

Out of the 40 branch managers of this study, 50% branch managers have experience working with in the branches more than 15 years, 35 % branch managers who have working experience in the branches ranging between 11 - 15 years. As per the branch managers only 15% of branches have credit risk management department. Branch managers told that 95% willful defaulter, 75% interference of political, 75% poor documentation of customer, 65% branch lack of proper post supervision/follow up were the causes of credit risk. After review of literature and data analysis proposed step given by

the researcher will helpful for reduction credit risk. In the first step bank manger easily identified the credit risk if bank have credit history of borrower, in the second and third step bank manager assesses and calculate the credit risk with the help of different methods. In the forth step bank can reduce the credit risk with the help of mitigate techniques of credit risk