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- PEARLS
  Monitoring System
  1. Protection,
  2. Effective Financial Structure,
  3. Asset quality,
  4. Rates of return and cost
  5. Liquidity and
  6. Signs of growth.

- Setting Parameters

  Before getting into credit business bank should set their working parameters and limits so that the effort of Credit Team will be properly guided to achieve their organizational goal. Those parameters should be guided by country law, social and environmental behaviors, national and international environments. Basically parameters, like targeting lending sectors, processes of risk analysis, working procurers, approving authority, rewards and punishment, can be set through formulating and following under listed policies.

  - Bylaws, Circulars and Directives
  - Credit Policies
  - Risk concentration Management Polices
  - Manuals and procedures Guideline
  - Product Papers
  - Loan Recovery Policy

- Credit Policy
- What to do
  &
  What not to do ?
- Credit Policy
- Internal Control System

- Internal Control System
- **Preventative,**
- **Detective,**
- **Corrective**
- Internal Control System

Internal Check.
At the time of transaction

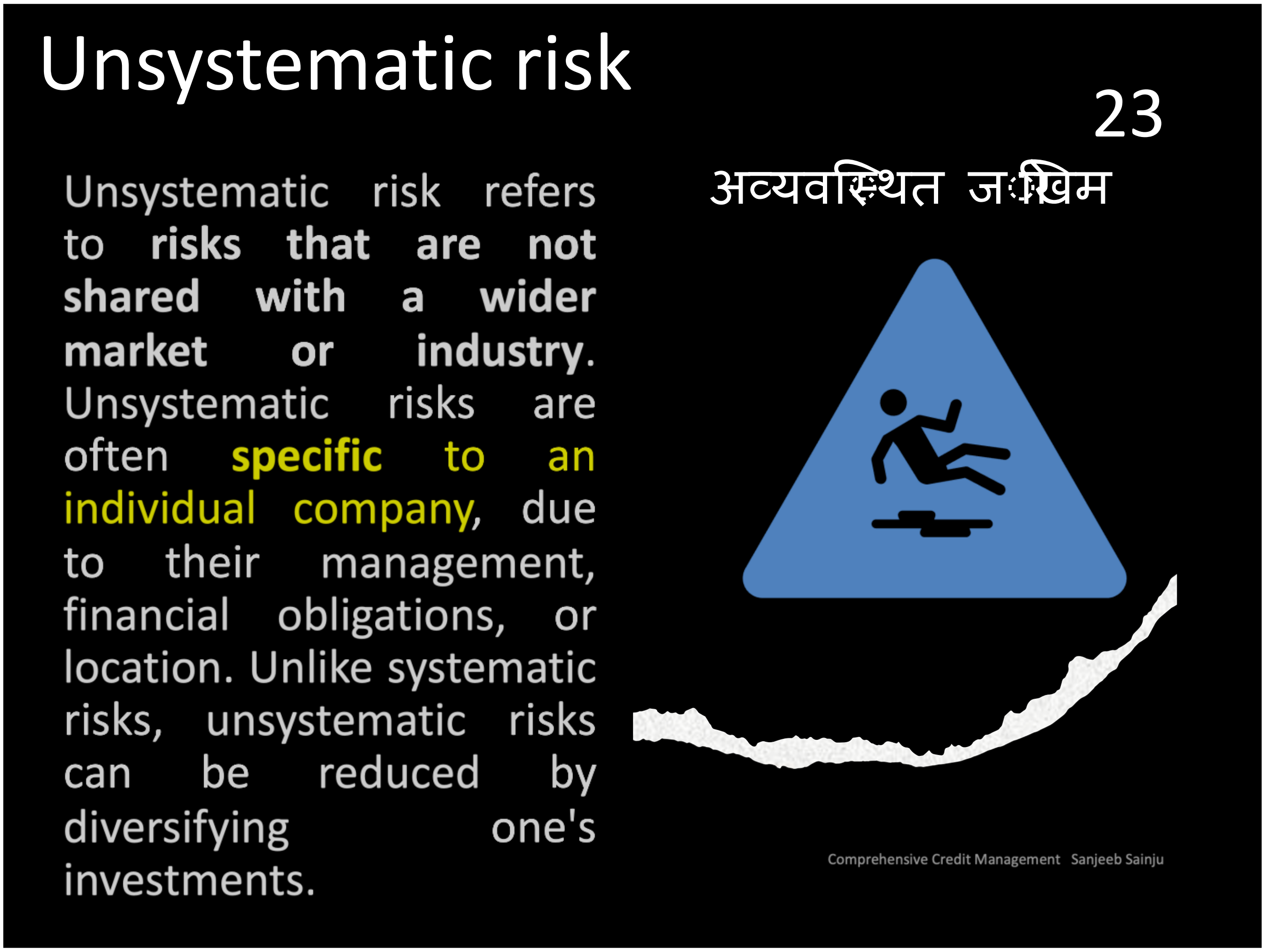
- Customer Targeting and Screening
- What is
  Risk Assets ?
  &
  Why it is called Risk Assets

Loan	-	**Assets**
Payback	-	**Future**
Future	-	**Uncertain**
Uncertain	-	**Risk**

- Risk

  Bank risk is usually referred as the potential loss to a bank due to the occurrence of particular events.
- Systematic Risk

  Systematic risk is not specifically associated with the company or the industry one is invested in; instead, it is dependent on the performance of the entire market.



Credit Risk

Credit Risk is the most dominant factor in bank failures. If the Credit Risk can be managed such bank failure can be reduce in significant way. To manage credit first one should identify the risks associate in lending, they should know the cause of borrowing, assessment of requirement and repayment capacity and handling the problematic loans. In a nutshell, we will discuss all these matters within;

Credit Risk also means

- Counter party risk,

- Default risk or
    - Performance Risk
- Silicon Valley Bank Collapsed
- October 17, 1983 established – 39 years
- Failed on 10 March 2023
- 16th Largest Bank of USA
- Collapsed in 36 hours
- Ethical and Reputation Risk
- Absolute Risk v/s Calculative Risk
- How to tackle risk
- Credit Risk Transfer

Collateral
Personal Guarantee
Credit Risk Insurance
Financial Guaranties
Credit Default Swap (CDS)
Assets Reconstruction Company (NPA)

- Credit Risk Transfer

Credit insurance protects the policyholder in the event of a customer becoming insolvent or failing to pay its trade credit debts.

- – Whole turnover credit insurance
- – Major buyer policy (critical customer cover)
- – Single risk cover
- – Export trade credit insurance

- Credit Default Swap (CDS)

A credit default swap (CDS) is a type of credit derivative that provides the buyer (Bank) with protection against default and other risks. The buyer of a CDS makes periodic payments to the seller (CDS company) until the credit maturity date. In the agreement, the seller commits that, if the debt issuer defaults, the seller will pay the buyer all premiums and interest that would've been paid up to the date of maturity.

How are you managing risk factors at your organization ?
You can never identify all the risk,
some risk emerge with time

- **Proactive vs Reactive**
- Proactive

Credit Appraisal

- – Customer Analysis
- – Need Assessment
- – Credit Inquiry
- – Risk Assessment
- – Security Documentation
- – Risk Transfer
- – Monitoring

- Reactive

Recovery & NPA Management

- Follow up
- Public Notice
- Auction
- NBA
- Write off

End of 1st Session

- 2nd Session
- Principals of Good Lending
- Types of Loans
- 5 Cs of good credit
- 6 Cs of bad credit
- Credit Checks
- Borrowing cause
- Financial Analysis
- Credit Appraisal

- Principal of GOOD lending

1. Safety
2. Purpose
3. Liquidity
4. Diversity
5. Profitability
6. Securities
7. *National*

Interest, Suitability

- Safety

The safety of funds lent is one of the prime principle of lending.

Safety means that the borrower should be able to repay the loan and interest in time at regular intervals without default.

Low default risk.

- Purpose

The **purpose** of loan should clear and **explicit**. It should be productive so that the money not only remain safe but also provides a definite source of repayment.

- LIQUIDITY
- It is not enough that the money will come back; it is also necessary that it must come back on demand or in accordance with **agreed terms** of repayment.
- The borrower must be in a position to repay within a reasonable time after a demand for **repayment** is made
- Diversity

Diversification aims at minimizing risks of the investment portfolio of a bank.

A bank should follow the maxim: "Do not keep all eggs in one basket."

- Profitability

Equally important is the principle of '**profitability**' in bank. Banks must make profits in order to sustain.

- **Securities/ Collateral**
- ***National Interest, Suitability***
- Even when an advance satisfies all the aforesaid principles, it may still not be suitable. The advance may run counter to national interest.

What IS LOAN?

- What is Loan ?

Loan is a sum of money borrowed by a customer from a bank or Financial Institution, often for a specific purpose and time, which needs to be pay back in prescribe repayment schedule with interest.

Loan Structure

- P E A R L S Monitoring System

Effective Financial Structure

- 95% productive assets composed of loans (70-80%), and liquid investments (10- 20%)

- 5% unproductive assets composed of primarily fixed assets (land, buildings, equipment etc.)
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- **<u>Component of Loan Structure</u>**

Cause of Borrowings
Types of Loan

- Type of Loan based on other factors
- Character
- Capacity
- Capital
- Condition
- Collateral
- Highly liquid and easy Marketability

The security should be easily convertible to cash. This is possible only when it is freely traded in the market place

- Ascertain ability

The value of the security should be easily ascertainable. Availability and transparency of pricing is a must to verify the value at periodic intervals.

- Stability of value

The market value of the security should not fluctuate very widely to ensure that available margin is not eroded

- Transferability

The security should be easily transferable to the lender's name and such ownership should be legally transferable.

- CAMPARI

THE CAMPARI METHOD STANDS FOR

1. character,
2. ability,
3. means,
4. purpose,
5. amount,
6. repayment, and

insurance

Character	–	Willingness to pay versus ability to pay
Ability to repay	–	Adequacy of cash to meet repayment
Margin of finance	–	The client must contribute a certain margin as commitment. The banker seldom grants 100% financing.
Purpose	–	The purpose of the loan must be defined. Speculative purposes are considered risky and will not be entertained.
Amount	–	The amount the financier is willing to contribute to the client. This prompts a question. How much is too much for a client? Any amount beyond the repayment capacity of a client is too much.
Repayment terms	–	The structure and terms of repayment
Insurance	–	In the event the borrower dies, the loan can be settled from insurance proceeds

- Types of Collaterals

Primary collateral

Primary collateral are such collaterals which are directly related with the business of the borrower. Such collateral play main role in operation and earning of the business.

- Currents assets (Stocks and Receivables)
- Plant and Machinery
- Project property
- Marketable security (margin lending)

- Type of collateral

Secondary collateral

The unrelated assets / collateral with business of the borrower. Secondary collateral might some personal belongings of the borrower or their business units.

– Real-estate collateral

- Jeweler
- Fixed Deposit
- Marketable security
- Collateral Check

- Land identification in field with help of Land Map / Trace.
- Verify land with nearby emblems or land marks.
- Check accessibility to the land map and site.
- Crosscheck ownership with neighbors.
- Check owner’s name in Lalpuja and verify building construction approval.
- Reconfirm the fake reference.

Why Loans turns BAD ?

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- Six C’s of Bad Credit

6 C’s of Bad Credit

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Avoiding 6 C’s of Credit help insuring a higher probability of repayment

Complacency

Situation that prevents you from trying harder. Complacency can come from an overreliance on past performance of the company. “I don’t need to watch this borrower; they have always paid on time.”

Carelessness

Proper Documentation, Lack of Monitoring , Site visits, Record Keeping and filing, Analysis of collaterals.

- Six C’s of Bad Credit

Communication

Communication breakdown between lenders (RM/BM) and borrower. Borrower getting out of contact.

Contingencies

Sensitivity analysis, Stress Test. Low margin for error.

- Six C’s of Bad Credit

Competition

Compromise in quality of lending. Borrower requirement, repayment sources, past performance, security analysis

Cluelessness

Lacking understanding or knowledge. Inexperienced staff.

- End of 2nd session
- 3rd Session
- Credit Appraisal
- Credit Facility Offer Letter
- Documentations
- Monitoring Customer Performance
- Debt Service
- Delinquent Vs Default
- Credit Check
- **Credit Checks**

Credit Check is a process where a lender seek credit background of the borrower from credit rating companies.

- **Credit Scoring**

Credit scoring is statistical analysis used by credit bureaus to evaluate individual worthiness to receive credit.

- **Credit Bureaus**
- **Credit Rating vs. Credit Score**

What’s the Difference?

- Credit scores are numbers used for individuals and some small businesses.
- Credit ratings are expressed as letter grades and used for businesses and governments.
- **Rating Agencies of Nepal**

- Financial Documents
- Financial Analysis

Financial analysis is comparative study of financial statements to find out financial position, activity, profitability, liquidity of the company.

Comparative study of financial statements could be of analysis of Balance Sheet and Profit & Loss account of same company or similar companies within same industry.

- **Ratio Analysis**
- Ratio Analysis is most widely used financial analysis tools and technique.
- A ratio can be computed from any pair of financial figure available in Balance sheet and / or Profit and loss account.
- Comparing ratios of more than one two year with historical data of same company or similar industry is ratio analysis.
- Current Ratio

The current ratio is a financial ratio that use to examine the liquidity of a company and its ability to pay short-term liabilities (debt and payables) with its short-term assets (cash, inventory, receivables).

- Credit Analysis

It is an evaluation process of borrower financial requirement and their repayment capacity satisfying lenders protection and purpose of borrowing based on Past History, Assumption and Predication .

Credit Appraisal also called Credit Proposal / Credit Report / Loan Proposal / Credit Assessment / Credit Evaluation is important credit documentation which consist of borrowers background, purpose, business analysis, financial analysis, collateral details observation etc. Based on this report bank approve or decline loan proposal.

Prudent Credit Appraisal

- Sanction Letter

A sanction letter is a document that is provided by lending institution to a borrower, stating that the loan has been approved.

It contains the terms and conditions based on which the loan will be provided.

- Credit Facility Offer Letter

Sanction Letter / Credit Facility Offer Letter / Loan agreement letter, whatever we named , bring the borrower and lenders in one common ground. Signing of this document makes the lender and borrower agree to give and take credit facilities obeying the terms and condition mentioned thereon.

- Credit Facility Offer Letter

After Approval Bank issues "**Credit *Facility* Offer Letter**" which contain

Approved facility details

Loan Amount / Rate of Interest/ Tenure

Collateral / Security to be provided to the bank

Details of land and building / vehicles / Fixed assets / Current Assets

Other Security documentation

Loan Deed / Promissory Note/ Letter of continuity / Guarantee

- Credit Facility Offer Letter

Covenant (Terms and condition)

Do and Don't

Event of Default

Occurrence of which certify the borrower become defaulter

Signature of customer

Space to sign by the customer certifying the facility with all above terms and condition has been accepted

- security and legal documents
    - Loan Deed
    - Promissory Note
    - Letter of Continuity

    - Mortgage deed
    - Hypothecation over stocks
    - Assignment of receivables
    - Letter of setoff
    - Personal Guarantee
- Corporate Guarantee
- **Credit Monitoring**

Credit Monitoring is a supervision of a loan account on an ongoing basis to avoid slippage of accounts into Non Performing Assets.

Effective Credit Monitoring ensure

Proper utilization of funds,

Operation of the business,

Compliance of terms of sanction,

Maintain asset quality of the Bank

A good sanction can become bad if not properly monitored & supervised

- Four Stages Of Monitoring
- **Monitoring Customer Performance**
- Once the borrower withdraw the loan amount it is very important for lender to monitor the performance of the customer.
- A good sanction can become bad if not properly monitored & supervised
- **Monitoring**
  Customer Performance

Post disbursement monitoring Activities

- Monitoring Customer Performance
- End of 3rd session
- 4th Session
- Debt Service
- Identifying Trouble Signs
- Early Warning Signal
- Black Listing
- A Strategy for Problem Loans
- NPA Management & Recovery
- Debt Service

Debt service is the cash required to pay back the principal and interest of outstanding debt for a particular period of time.

Debt Service basically is repayment of the loan including interest and principal.

- Means of Debt Service – Channeling

Debt Service Management provide service to borrower to pay the installment in convenient way.

  - Pick up service provide bank.
  - Payment through Mobile app.
  - Payment through ATMs.
  - RTGS.

  - Electronic Clearing Service
  - Wallet based Payment
- Debt Service Policy

General Guidelines

- When and Where to follow up
- Authorization and Authority to staffs
- Maintain privacy
- Follow fair debt collection practices / act

Appointing of recovery agency
Giving notice to borrowers
Repossession of Security
Valuations and Sale of Property
Opportunity for the borrower to take back the security

- Delinquent

A loan is considered "delinquent" when a borrower doesn't make a loan payment on time. As such, loans are considered delinquent immediately after the first payment is missed

Once a loan is delinquent for a certain period of time, it becomes at **risk of going into default.**

- <u>Risk Assets Classification</u>

P = Protection

- <u>Loan Loss Provision</u>
- <u>Willful defaulter</u>

Unified Directives – 12 (Credit Information/ Black Listing)

1. Defaulter having past due over 1 year but not is banks' contact, neither approached for restructure / reschedule, not committed to for settlement.
2. Not willing to sale property/collateral to settle the loan or creating hindrance for sale of property/collateral by bank.
3. Not willing to *pay the loan by income* from other business or from others assets

- <u>Willful defaulter</u>

4. Loan used for different purpose (Diversion of fund), Income generated from concern business not use to pay loan (Siphoning off)
5. Loan taken by "de facto" borrower
6. Not willing to give additional security/collateral / PG of defaulted loan
7. Providing false statement / information regarding collateral / business

- <u>Willful defaulter</u>

8. Mutilate / damage / violate collateral
9. Loan taken under bribery / undue pressure / illegal bargaining
10. Loan provided by overvaluation of project, false evaluation

- **Indication of <u>UNHEALTHINESS</u> of business**
- Old Stocks
- High ageing of debtor turnover.
- Excessive stocks.
- Delay in submission of financial statement
- Borrowing continue after seasonal needs

- Change in key person
  Early Warning Signals
- **<u>Early Warning Signals</u>**

<u>Symptoms</u>

  - Evidence of legal action against the borrower by other creditors.
  - Deteriorating relationships with trade supplier
  - Concurrent outside borrowing
  - No account movement or Low Transaction
  - Frequent request for time extension of loans
  - Not able to meet the financial obligations
  - Non compliance of terms of loan agreement
  - Change of contract numbers / mobile
  - Communications Problem / Mobile switched off.
- Non Legal Measures
  - Restructure
  - Reschedule
  - Strategic Management
  - Amicable Settlement
- Legal Measures
- Black Listing

is an recovery action taken by member banks of CICL restricting the defaulter and other FIs for the followings;

- Availing / providing new loan,
- Releasing undisbursed portion of loan
- Renewing the facilities
- Other restrictions
- <u>Before go into Legal Measures</u>
- Check where loan documents has been properly signed, stamped , witness or not.
- Check the security / collateral status and conduct field visit.
- Check the mortgage status at malpot office is intact or not.
- Check valuation / revaluation of the property.
- Try to complete / obtain pending documents, signature, stamp, witness prior to initiating legal action.
- <u>Precautions</u>

1. Field report / Fact Sheet (Muchulka) to be prepared.
2. Take signature of the persons / representative engaged in the seizure.
3. Take signature of borrower or his family member / representative as far as possible.
4. Issue a letter to the borrower regarding capture of goods.
5. Make sure the property has been

insured and well covered.

- Auction
  An **auction** is a **<u>public sale</u>** where goods are sold to the person who <u>offers</u> the highest price.
- NBA

The **assets** which are acquired by the bank to settle the bad debts of borrowers are called “Non Banking Assets” (NBA). Primarily NBA are real estate collateral. But it can be other assets as well.

It is also called REO (Real Estate Owned) properties, when real estate collaterals take over by the banks.

- As per the decision of the Council of Ministers, Debt Recovery Tribunal (DRT) came into operation on 17 July, 2003 for speedy settlement and recovery of debts due to banks and financial institutions
- All commercial banks and other financial institutions as specified by Nepal Rastra Bank are eligible lending agencies can file cases into DRT.
- These agencies can file a appeal if the principal recoverable amount is NRs 500,000 or more.
- Write off

In banking and finance, the term “write-off” is really just an accounting term. It means the bank or lender doesn’t count the money borrower owes to it. This is needed to cleanse the balance sheet of the bank.

There is no meaning that the borrower is pardoned or got exempted from payment.

His debt will remain and recovery measures against him will continue.

Write-off does not mean that recovery comes to a stop

WRITE-OFF DOES NOT MEAN THAT RECOVERY COMES TO A STOP

Thank You all
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