

ADVANCES

Learning Objectives :

To explain the different kinds of advances.

Structure:

- 1.1 Introduction.
- 1.2 Secured Loans.
- 1.3 Unsecured Loans.
- 1.4 Partly Secured.
- 1.5 Status of Banker.

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1.1 Introduction

- Banking

“the acceptance for the purpose of lending or investment, of deposits from the public, repayable on demand or otherwise, and withdrawal by cheque, draft, order or otherwise.’

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1.1 Introduction

The rate of income from lending or investment, is greater than

the rate allowed for the acceptance of deposits from the public.

- This provides a source of income to banks.

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1.1 Introduction

The rate of income from lending, is greater than

the rate of income from investment .

- Thus lending, loans or advances provide a major portion of income to banks.

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1.1 Introduction

**A bank's strength is,
therefore,
dependant on the quality
of its lending operations
or advances.**

Loans or advances can be

- **Secured.**
- **Unsecured or**
- **Partly secured.**

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1.2 Secured Advances

" A loan or advance made on the security of assets, the market value of which is not at anytime less than the amount of such loan or advance. "

- Secured loan or advance.
- Section 5(n)
- Banking Regulation Act, 1949.

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1.2 Secured Advances

Banks try to make secured advances as it reduces their risk. The stronger the security lesser the risk.

examples –

Loan on

- mortgage of house [or any immovable property].
- hypothecation of a vehicle.
- pledge of shares or fixed deposit [or any other title deed].

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1.2 Secured Advances

Types of security -

• 'primary' one offered by the borrower herself.

• 'collateral' one deposited by a third party to secure loan made to bank's customer.

• 'tangible' one that is visible, transferable etc.

• 'personal' promise from a borrower or guarantor.

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1.2 Secured Advances

Distinguishing features -

- A charge on any such assets offered as security must be created in favour of the banker.
- The market value of such security must not be less than the amount of the loan at anytime, until it is fully repaid. In case it becomes less, the advance is partly secured.

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1.2 Secured Advances

Distinguishing features -

• The market value of security in the form of wasting assets such as vehicles or machinery, decreases with passage of time due to wear tear.

Banker must ensure that sufficient amount of principal of the loan is repaid periodically in a manner that amount outstanding is lower than the new realizable value of the security.

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1.3 Unsecured Advances

- Are loans without any security from the borrower.
- Such advances are arranged based on borrower's assurance to repay.
- Bankers rely on borrower's reputation & credit standing.

examples

Overdrafts or personal loans to meet medical, holiday, education expenses.

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1.4 Partly Secured Advances

• Are loans with security from the borrower that does not fully cover the amount of the advance.

• Such advances are arranged based on borrower's reputation & credit standing and not necessarily because borrower has insufficient assets to offer as a security.

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1.5 Status of a Banker

☪ For secured advances:

As a secured creditor, in case of default, banker has right to sell assets over which a charge is created in his favour and recover advance from sale proceeds.

☪ For unsecured advances:

The legal status is that of an unsecured creditor. In case of default he is at par with other unsecured creditors.

The End