



## A COMPARATIVE ANALYSIS BETWEEN PRIVATE BANKS AND PUBLIC SECTOR BANKS WITH SPECIAL REGARDS TO LOAN FACILITY IN INDIA

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### ABSTRACT :

**B**anks contribute to the growth and success of an economy as they help to mobilize resources that would otherwise be lying idle with the public and direct them to productive use and investments and thus generating flow of money in the economy. To develop a country, the financing sector of the economy also needs to be well developed. The problem of affordable loan has been a persistent challenge for India. A number of institutions have been instrumental in the development of the finance sector in India. Both nationalized and private banks have come forward to contribute to this sector by offering many affordable loan options to the general public. These days the competition in the banking sector has also arisen due to which there is a constant hoard to offer better services and better schemes with a view to lure customers. But there exists major differences in the way loan is sanctioned by private and public banks vis-à-vis interest rates, paperwork, period of loan, amount of installments, pre-payment charges etc. The present study focuses to bring out the comparative differences that exist in the loan processing system of private and nationalized banks. An examination of the banking practices in India is made and trend of loans and its subsequent conversion into NPA is studied.



**KEYWORDS :** loan, banking sector, private banks, public sector banks, NPA, interest rates.

### INTRODUCTION

The financial sector reforms initiated in 1985 and 1991 acted as a catalyst to develop the economy that resulted in higher levels of employment, urbanization, increase in income level etc. Many steps were also taken in the banking sector to bring out the economy from the blues of mismanagement, underdevelopment, poverty etc., the major being nationalization of 19 banks. The government has worked to initiate and strengthen measures to extend the facility of loan to the economically weaker sections of the society. In rural areas, co-operative banks have managed the task of extending loans to the poorer sections of the society that has helped the small scale industries to survive and promoted self-employment activities.

Banks form an integral part of the Indian financial system. The banking sector has undergone a transformation in last few years and has been recognized as an important component of the financial system. The banking system that offers loan products includes both private and public sector banks, NBFCs and other credit societies. All these institutions have a major role to play in nation building and financial inclusion by complementing each other and extending credit to all the segments of the society be it individuals, corporates, MSMEs etc. Generally they offer customized products as per the needs of the needs of their customer. However to survive and constantly grow these institutions have to focus on their core strengths while improving on

weaknesses. In order to survive in this ever increasing competitive market, they need to be very dynamic and constantly endeavor to search for new products and services.

### METHODOLOGY & OBJECTIVES

The paper is based on secondary data. The data has been collected through various websites, newspaper, journals, reports, blogs, press release etc. The main objectives of the study are-

1. To study the loan market in India.
2. To find out the problems faced by Indian customers in availing loan.
3. To study the differences that exist in lending practices of private and public sector banks.
4. To suggest appropriate measures to improve the efficiency in lending by banks.

### LOAN MARKET IN INDIA

Loan market in India is a growing and diverse market as the demand for loans is rising due to growing needs of the society. The purchasing power is increasing which has led to a rise in standard of living which in turn increases the demand for loans. There has been a rapid demand for all kinds of loans be it personal loan, housing loan, vehicle loan, education loan, business loan, loan against PPF, loan against insurance policy etc. Loan products these days are tailor made, easy to apply and obtain for, speedily sanctioned, easily available at cheaper rates of interest which has made them more lucrative to the public. Mortgage loans are also on a rise these days. India has a huge market for gold and thus mortgaging gold and gold jewellery has gained limelight and is an easy option to avail loans. Loans are not restricted to buy houses and big vehicles but also for buying consumer durable goods. Many banks offer loans to women to buy gold and silver. Loans for medical emergency are also easily available which is beyond generic personal loans. To study abroad education loans have especially been in demand. Loans to start up a new business or expand an existing one are also very easily available these days. IDBI and SIDBI offer loans to enterprises to tap emerging technologies. These banks have also helped in the revival of cottage and small scale industries. Working capital loans on collateral security has also seen an upsurge in the recent years. Banks these days also offer choices on how often to make the EMI payment. Loan tenures are flexibly based on the business of the borrower. Different platforms also offer comparison of different loan choices. Due to advancement in technology the loan turn around time has drastically decreased, documents can be submitted online using the E-KYC process, thus helping the banks to provide value added services to its customers.

### PROBLEMS FACED BY CUSTOMERS

A few problems faced by the Indian customers while proceeding for Loan from banks are listed as follows-

- + Rejection at first step due to strict rules
- + Processing fee not refunded
- + Desired loan not sanctioned
- + The interest rate dilemma
- + Difference in property valuation
- + The down payment
- + Title deeds and NOC Documentation problems

These problems are common and can be avoided if borrower follows all the procedures and banks form flexible rules keeping customers benefits in mind .

### DIFFERENCES IN LENDING PRACTICES

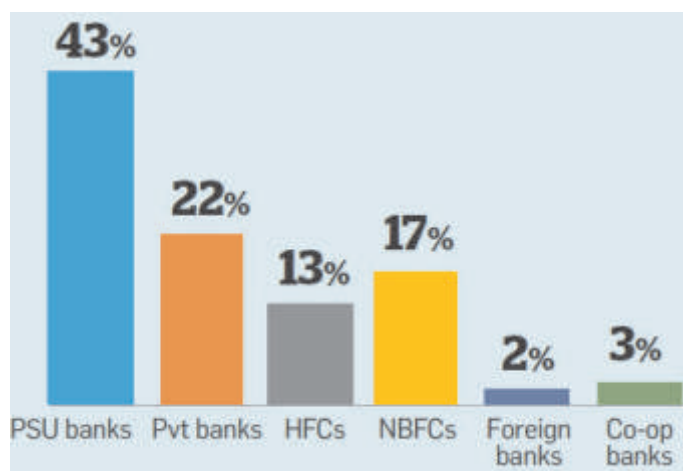
Public Sector Banks consist of all the nationalized banks eg., State Bank of India & its associates, Punjab National Bank, Canara Bank, Bank of India, United Bank of India, Bank of Baroda etc. whereas Private sector banks are privately owned such CitiBank, Axis Bank, HDFC, ICICI etc. Although all the Banks are regulated by RBI, there exists few differences in the day to day management between the two types of banks such as differences in

lending money, different rates for interest for borrowing and accepting deposits, bank charges etc.

#### A FEW MAJOR POINTS OF DISTINCTION ARE DISCUSSED BELOW-

**1. Paper work-** Private bank employees work on target based incentives. So they have a fixed amount of products that need to be sold within a fixed time period. Thus they work efficiently and speedily to process all paper work in time. This is basically done to meet the sales target. The processing time is less so loan is disbursed more quickly. Thus they offer hassle free loan.

Public sector banks do not have any strict target based work so they are not as efficient in carrying out the paper work. They take more time in processing as more compliance procedures need to be followed by them.



Source- economictimes

Even though the complexities involved and time taken in processing of loans by public sector banks, they emerged as the largest lenders in the year 2016. This is because of the faith public vests in these banks.

**2. Processing charges-** It is the fee charged to process an application for loan. Such a fee is charged to cover some of the basic costs involved in processing the application which includes basic administration costs, cost of paperwork, documentation charges, legal fees, credit appraisal etc. These costs are not borne by the banks themselves but ultimately by the customer. There are two methods for charging such fees- either a lump sum amount is charged based on the amount of loan or a fixed percentage on the total value of loan is charged.

Private Banks generally charge 1% - 3% of the amount of loan as processing charges as they rely on direct selling agents (DSAs) for creating customers, thus the commission is paid to such DSAs from this amount. On the other hand, public sector banks charge only about 0.5% - 2% as processing charges as they do not engage intermediaries and thus no commission is required to be paid to them.

**3. Interest rates-** The REPO rate maintained by the RBI has a direct bearing on the rate of interest, both on loan and savings. Generally private banks are seen to increase the interest rate on loans as soon as the RBI raises the Repo rate but do not decrease it with immediate effect when the Repo rate decreases. On the contrary, public sector banks charge same rate of interest from all customers and follow the RBI guidelines on maintaining the rate of interest. PSU banks have a traditional customer base and rural customer base which needs to be taken care of.

<b>1 Year MCLR of few selected Banks</b>	
<b>BANK</b>	<b>AS ON JAN 2017</b>
State Bank of India	8.00%
HDFC Bank	8.15%
ICICI Bank	8.20%
Axis Bank	8.25%
Bank of Baroda	8.35%
Punjab National Bank	8.45%
Canara Bank	8.45%
Central Bank of India	8.50%
Allahabad Bank	8.60%
IDFC Bank	8.95%
Kotak Mahindra Bank	9.00%
IDBI Bank	9.15%

Source- Capitalmind.in

MCLR refers to minimum interest rate below which a Bank cannot lend except in some cases allowed by RBI. MCLR actually describes the method by which the minimum interest rate for loans is determined by the Bank.

**4. Pre- payment charges-** Pre payment is the early repayment of loan by a borrower which can be either paid partially or fully. This option is usually adopted by the borrower to take advantage of lower rates of interest. RBI in 2014 directed the banks not to levy any penalty on individual borrowers for pre-paying floating loans. Floating loan product includes housing, corporate, vehicle and personal loans.

Private banks generally include a penalty cause for pre-payment of loan as they are going to lose the amount of interest if a loan is prepaid. Generally they charge 2% on outstanding amount of loan as pre-payment charges. Public sector banks have an upper hand in this case as most of the banks do not charge any amount when the whole or part of loan is paid at an early date. A restriction on the period of pre-payment is also placed by private banks as a borrower cannot pre-pay any amount of loan before completing at least 180 days i.e. 6 months of the loan. No such clause is practiced by public banks in general.

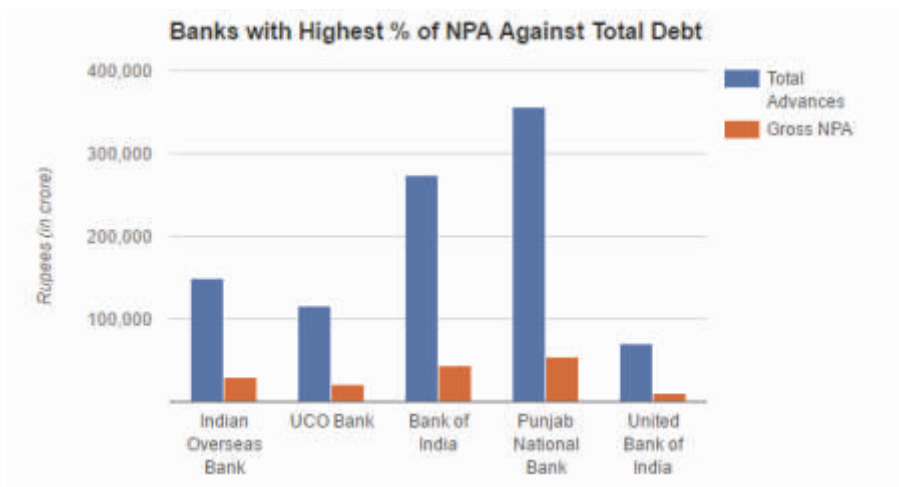
**5. Customer Service-** Customer service is the key factor in banking when it comes in dealing with customers. Customer service is the service which a bank offers to customers. There is a big difference between Private bank and Public banks. Public banks have standardized service delivery system where as Private banks have customized service delivery system.

## **BANKS & NPA**

The advances of a Bank may be classified into Performing Assets(PA) and Non-Performing Assets(NPA). As long as the asset generates income to the Bank and no potential risk is attached to it, it is considered as performing asset (PA). An asset becomes NPA when it ceases to generate any income for Bank. Any advance outstanding for a period less than 90days is Potential NPA and after 90 days it becomes NPA.

The NPA in the banking sector whether public banks or private banks has shown a rising trend and it continues to rise as such. The various reasons attributed to the rise in NPA could be poor governance and mismanagement in handling of funds, inappropriate lending decisions, poor recovery management, debt borrowed and used for a purpose other than it is entitled for, intentional defaults and frauds in payment, growing number of willful defaulters such as big corporate houses, deficiency in settlement procedures and repayment, increasing interest rates, lack of knowledge and awareness etc.

As of June 2016, the Gross NPAs for public and private sector banks is around Rs. 6 lakh crores. The amount of top 20 Non Performing Assets accounts of Public Secor Banks stands at Rs. 1.54 lakh crores.



Source- RBI

Indian Overseas Bank fares worst having the highest ratio of NPA to total advances- 20.26%. Most banks in the country are heavily debt ridden and a substantial portion of which is unlikely to be recovered. The loans if improperly managed would ultimately convert into NPA which is difficult to recover. Thus the lending practices followed by banks needs to undergo changes to prevent any losses due to bad debts.

#### SUGGESTIONS-

1. Private banks can reconsider charging pre-payment charges and lowering of processing charges so as to make loans more lucrative to general public.
2. Public banks may improve the customer service to gain an upper hand in gaining customer satisfaction.
3. Pre-closure of existing loans, strict procedures at the time of processing of loans, document verification, refusal of granting loans to people with record of willful defaults will help achieve the target of reducing NPAs.
4. Red-tapism and delay in decision making to process loans should also be avoided.

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