A PROJECT REPORT ON CREDIT APPRAISAL

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ABSTRACT
The world economy has been majorly affected from the crisis. The securities in stock exchange have fallen down drastically which has become the root cause of bankruptcy of many financial institutions and individuals. The root cause of the economic and financial crisis is credit default of big and company's and individuals which has badly impacted the world economy. So in the present scena rio analysing one's credit worthiness has become very important for any financial institution before providing any form of credit facility so that such situation doesn't arise in near future again. Analysis of the credit worthiness of the borrowers is known as Credit Appraisal. In order to understand the credit appraisal system followed by the banks this project has been conducted

The project has analysed the credit appraisal procedure with special reference to Corporation Bank which includes knowing about the different credit facilities provided by the banks to its customers, how a loan proposal is being made, what are the formalities that is to be satisfied and most importantly knowing about the various credit appraisal techniques which are different for each type of credit facility. Before going further it is necessary to understand the need and basic framework of the project. Therefore this chapter provides an introduction to the topic, objective of the project, reasons for selecting the project and the basic structure and framework how the project proceeds.

Whenever an individual or a company uses a credit that means they are borrowing money that they promise to repay with in a pre-decided period. In order to assess the repaying capability i.e. to evaluate their credit worthiness banks use various techniques that differ with the different types of credit facilities provided by the bank. In the current scenario where it is seen that big companies and financial institutions have been bankrupted just because of credit default so Credit Appraisal has become an important aspect in the banking sector and is gaining prime importance

KEYWORDS: Credit Appraisal, financial institutions, Stock exchange .

I. INTRODUCTION

Credit Appraisal is an innovative and timely financing technique that has been used on many high-profile corporate projects, including Euro Disneyland and the Eurotunnel. Employing a carefully engineered financing mix, it has long been used to fund large-scale natural resource projects, from pipelines and refineries to electric-generating facilities and hydro-electric projects. Increasingly, Credit Appraisal is emerging as the preferred alternative to conventional methods of financing infrastructure and other large-scale projects worldwide.

Credit Appraisal discipline includes understanding the rationale for project financing, how to prepare the financial plan, assess the risks, design the financing mix, and raise the funds. In addition, one must understand the cogent analyses of why some Credit Appraisal plans have succeeded while others have failed. A knowledge-base is required regarding the design of contractual arrangements to support project financing; issues for the host government legislative provisions, public/private infrastructure partnerships, public/private financing structures; credit requirements of lenders, and how to determine the project's borrowing capacity; how to analyze cash flow projections and use them to measure expected rates of return; tax and accounting considerations; and analytical techniques to validate the project's feasibility Project finance is different from traditional forms of finance because the credit risk associated with the borrower is not as important as in an ordinary loan transaction; what is most important is the identification, analysis, allocation

and management of every risk associated with the project.

The purpose of this project is to explain, in a brief and general way, the manner in which risks are approached by financiers in a project finance transaction. Such risk minimization lies at the heart of project finance. In a no recourse or limited recourse project financing, the risks for a financier are great. Since the loan can only be repaid when the project is operational, if a major part of the project fails, the financiers are likely to lose a substantial amount of money. The assets that remain are usually highly specialized and possibly in a remote location. If saleable, they may have little value outside the project. Therefore, it is not surprising that financiers, and their advisers, go to substantial efforts to ensure that the risks associated with the project are reduced or eliminated as far as possible. It is also not surprising that because of the risks involved, the cost of such finance is generally higher and it is more time consuming for such finance to be provided.

Project finance is the financing of long-term infrastructure and industrial projects based upon a complex financial structure where project debt and equity are used to finance the project. Usually, a Credit Appraisal scheme involves a number of equity investors, known as sponsors, as well as a syndicate of banks which provide loans to the operation. The loans are most commonly non-recourse loans, which are secured by the project itself and paid entirely from its cash flow, rather than from the general assets or creditworthiness of the project sponsors. The financing is typically secured by all of the project assets, including the revenue-producing contracts. Project lenders are given a lien on all of these assets, and are able to assume control of a project if the project company has difficulties complying with the loan terms.

Generally, a special purpose entity is created for each project, thereby shielding other assets owned by a project sponsor from the detrimental effects of a project failure. As a special purpose entity, the project company has no assets other than the project. Capital contribution commitments by the owners of the project company are sometimes necessary to ensure that the project is financially sound. Project finance is often more complicated than alternative financing methods. It is most commonly used in the mining, transportation, telecommunication and public utility industries.

Risk identification and allocation is a key component of project finance. A project may be subject to a number of technical, environmental, economic and political risks, particularly in developing countries and emerging markets. Financial institutions and project sponsors may conclude that the risks inherent in project development and operation are unacceptable (unfinanceable). To cope with these risks, project sponsors in these industries (such as power plants or railway lines) are generally completed by a number of specialist companies operating in a contractual network with each other that allocates risk in a way that allows financing to take place. The various patterns of implementation are sometimes referred to as "project delivery methods." The financing of these projects must also be distributed among multiple parties, so as to distribute the risk associated with the project while simultaneously ensuring profits for each party involved.

Credit appraisal means an investigation/assessment done by the bank prior before providing any loans & advances/project finance & checks the commercial, financial & technical viability of the project proposed its funding pattern & further checks the primary & collateral security cover available for recovery of such funds.

Objectives:

- To study the Credit Appraisal Methods.
- To understand the commercial, financial & technical viability of the project proposed & it's funding pattern.
- To understand the pattern for primary & collateral security cover available for recovery of such funds.
- To study the credit policy of the bank and the credit appraisal process as a whole.
- To study the credit rating methods followed by the bank for different credit ranges.
- To study a credit appraisal report of a firm

II. LITERATURE REVIEW

CREDIT APPRAISAL SYSTEM IN BANKING SECTOR

Credit appraisal is the process of accepting or rejecting the proposal for finance from the public carried out by department of credit of the banks. Finance is required at every stage of business either for meeting day to operations or for starting up a new project. One of the important sources of raising finance is loans from banks. Commercial lending is one of the prime functions of any bank. The fund of depositors i.e, general public are mobilized by means of such advances/investments. Thus it is extremely important for lender bank to assess the risk associated with credit, thereby ensure the fund deposited by depositors. This paper describes and gives the idea about How does the bank appraises the creditworthiness of a borrower? What are the criterions to be fulfilled for granting loans? These questions are being answered in this paper.

AN OVERVIEW OF CREDIT APPRAISAL SYSTEM WITH SPECIAL REFERENCE TO MICRO SMALL AND MEDIUM ENTERPRISES (MSME)

The Credit Appraisal is a complete exercise which starts from the time a potential borrower walks into the branch and concludes in credit delivery and monitoring with the objective of certifying and maintaining the quality of lending and managing credit risk. Credit appraisal is the assessment of the viability of proposed long term investments in terms of shareholder wealth and the formal analysis of all project costs and benefits which is used to justify the project proposal. The bank has over the years designed and adopted the Best Practices Code. This in effect represents the bank's philosophy towards effective Corporate Governance. The liberalization of the financial sector demands a new technology to cope with the rising pressures on the profitability of banks and financial sector institutions. Analyzing lending strategies, credit appraisal, risk analysis and lending decisions, while keeping in mind the broad framework of corporate banking strategy, this book emphasizes that lending is no longer an activity restricted to the assets side of the balance sheet. An invaluable tool for practicing managers and students of business and financial management, this book demands no prior specialized knowledge of the subject, taking readers from the rudiments of credit appraisal to advanced levels of decision making. Numerous examples from the world of business have been provided to facilitate a better understanding of the vast and significant changes in the financial market. The objective of credit analysis is to look at both the borrower and the lending facility being proposed and to assign a risk rating.

CREDIT APPRAISAL DETERMINES YOUR LOAN ELIGIBILITY

Acredit appraisal is an important part of determining the eligibility for a home loan, and the quantum of the loan. A prospective borrower has to go thorough the various stages of the credit appraisal process of the bank. Each bank has its own criteria to satisfy itself on the credit worthiness of the borrower. The eligibility for the loan that a person can get depends on his credit worthiness, determined in terms of the norms and standards of the bank. Being a crucial step in the loan process, a borrower needs to be careful in planning his financing modes. The credit worthiness, basically, assures the repayment capacity of the borrower - whether the borrower is capable of repaying the loan and dues on time.

BANKING STRATEGY, CREDIT APPRAISAL AND LENDING DECISIONS: A RISK-RETURN FRAMEWORK

The liberalization of the financial sector demands a new technology to cope with the rising pressures on the profitability of banks and financial sector institutions. Analyzing lending strategies, credit appraisal, risk analysis and lending decisions, while keeping in mind the broad framework of corporate banking strategy, this book emphasizes that lending is no longer an activity restricted to the assets side of the balance sheet. It must emanate from and fit snugly into the overall corporate objective of a lending organization and, in the process, it must integrate the expanding range of activities into the mainstream lending business. An invaluable tool for practicing managers and students of business and financial management, this book demands no prior

specialized knowledge of the subject, taking readers from the rudiments of credit appraisal to advanced levels of decision-making. Numerous examples from the world of business have been provided to facilitate a better understanding of the vast and significant changes in the financial market.

III. RESEARCH METHODOLOGY:

Primary Data:
Informal interviews with Branch Manager and other staff members
Secondary Data:
Books and magazines
Internal reports of the banks
Library research
Websites

IV. CONCLUSION

Finance management is the backbone of any organizations and hence yields a number of job options ranging from strategic financial planning to sales.

Bank load policy contains various norms for sanction of different types of loans. There all norms does not apply to each & every case. Bank norms for providing loans are flexible & it may differ from case to case.

The CRA models adopted by the bank take into account all possible factors, which go into appraising the risk associated with a loan, these have been categorized broadly into financial, business, industrial, and management risks & are rated separately.

Usually, it is seen that credit appraisal is basically done on the basis of fundamental soundness. But, after different types of case studies, our conclusion was such that, in Bank, credit appraisal system is not only looking for financial wealth. Other strong parameters also play an important role in analyzing creditworthiness of the firm.

Moreover, The study at Bank gave a vast learning experience to us and has helped to enhance our knowledge. During the study We learnt how the theoretical financial analysis aspects are used in practice during the working capital finance assessment. We have realized during my project that a credit analyst must own multi-disciplinary talents like financial, technical as well as legal know-how.

The credit appraisal for working capital finance system has been devised in a systematic way. There are clear guidelines on how the credit analyst or lending officer has to analyze a loan proposal. It includes phase-wise analysis which consists of 5 phases:

- Financial statement analysis
- Working capital and its assessment techniques
- Credit risk assessment
- Documentation
- Loan administration

To ensure asset quality, proper risk assessment right at the beginning, is extremely important. That is why Credit Risk Assessment system is an essential ingredient of the Credit Appraisal exercise. The Bank was the first to formulate a Credit Risk Assessment model. It considers important parameters like profitability, repayment capacity, efficiency of the unit, historical / industry comparisons etc… which were not factored in other models. It is equally efficient as the SIDBI's CART (Credit Assessment and Rating Tool) model.

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