

Credit in the Financial System

Improve your learning

Q. 1. Most of the credit needs of the poor households are met from informal sources. The dependence of richer households on informal credit is less. Do you agree? Use the data from Table 1 to support your answer.

Answer : Yes. Most of the credit need of the poor households are met from the informal sources. They are forced to take from the informal sources because of a lack of knowledge about the credit system. Around 48% of the rural households are dependent on the informal sources of credit. The rural households are unaware of the credit system because of lack of education.

In rural areas, the educational sector is very poor compared to the urban sector. Moreover poor are not guided with education because of the poverty. The richer people will depend less on the informal source of credit because they are aware of the banking system. Another main reason for the dependence of informal source of credit as collateral. Banks and other institutions need collateral for advancing the loan. Poor people will not have any collateral for raising fund from the formal sources of credit whereas richer people will have.

Q. 2. How are high-interest rates on loans harmful?

Answer : Interest rates are the main component of the loan which makes the loan costlier. Cost of borrowing will be high if the interest rates are very high. When the rate of interest is very high, then the loan instalment will be high which is to be paid in a fixed tenure. This will make the fixed income group people face a very critical situation because of the increase in the amount to be paid.

Q. 3. What is the basic idea behind the SHGs for the poor? Explain in your own words.

Answer : Self Help Groups is a voluntary organization formed by the women to enhance the microcredit for the members in it and the women members get to indulge in the entrepreneurial activities such as run a canteen, small shops...etc. The main motive of the bank is to accept the deposit and lend that deposit as a loan to investors.

In a country like India, an ordinary person will not do not have any excess money to save as a deposit in the bank especially in rural areas. The members of the organization save their money by fixing an amount to be deposited weekly, the amount will be such everyone can afford that. That deposited money can be advanced as a loan to any of the member in the group who is actually in need of it, but the loan will be advanced by the consent the group members. There is transparency in the working of the organization because all the group members will be from the same village and all of them will be neighbours.

Q. 4. Talk to a banker and find out what are the purposes for which people in urban areas generally take loans?

Answer : There are varieties of reasons for which people take a loan and also there are different types of loans. There are housing loan, car loan, gold loan, education loan and small business loans. In urban areas, people are mostly with a high standard of living, therefore, they concentrate more on their welfare activities and further betterment of life. For increasing the way of living, there is a need for the fund to be raised. There are different types of loans which are raised by urban people.

EDUCATIONAL LOAN:

Educational loans are being advanced to the students who are pursuing their higher education. These are provided to only those students who are really not in a condition to raise the fund for pursuing higher education.

• Documents required

It requires admission in any University and income proof of parents. Immoveable property documents in some cases

HOME LOANS

These loans are taken by the people to build a house for them. These loans help the people to raise a huge amount of fund.

• Documents required

Salaried employees will be required to present their salary certificate, other documents and other property required documents. Self-employed people will be required to submit the other documents and property documents of specific value.

CAR LOAN

The finance procured for buying either a new or a used car is known as a car loan. A car loan is one of the complex loan products in India as car dealers tend to include various discounts offered by car manufacturers or lenders (banks and other financial institutions) in the interest rate offered to the buyer.

• Documents required

Income proof and proof of original address is the mainly required documents for the advancement of the car loan.

GOLD LOAN

A gold loan helps in achieving the requirement of finance through the precious asset that otherwise just lies under lock and key.

- **Documents required**

The borrower needs to furnish only the KYC (Know Your Customer) documents. This comprises of Identity proof and address proof.

These are the most sources used by the people in urban areas. But there are further different types of loans which are used the urban people.

Q. 5. What is the difference between the bank loan and through SHG?

Answer : Bank loan advances the loan by mortgaging any property as collateral, but SHG advances their loan without any collateral. Both are the formal sources of credit, but the advancement procedure and working of the system is different. Bank accept the deposit from the depositors and advance that amount keeping a fraction of ratio as a reserve they advance that amount as loan.

The members of the organization save their money by fixing an amount to be deposited weekly, the amount will be such everyone can afford that. That deposited money can be advanced as a loan to any of the member in the group who is actually in need of it, but the loan will be advanced by the consent the group members.

Banks works as a formal organization which is registered, but the SHG can be with registered or unregistered. The rules in the banks make the loan procedure rigid whereas the SHGs give loans to the members itself and without any rigid procedures.

Q. 6. Read paragraph 3rd under the heading of 'Self Help Group for the Poor' and answer the question. How are SHGs working in your area?

Answer : An SHG is a small group of persons who come together with the meaning of finding a key to a common problem such as medical issues, livelihood generation or watershed management, with a degree of self-sufficiency. However, in Andhra Pradesh, the groups largely are the medium through which micro credit is routed to the poor in the belief that it will serve as a catalyst in helping them to pull out of poverty.

The state-sponsored Velugu program working in over 860 sub-district geographical unit in 22 districts, aims to reach 2.9 million of the poorest of rural poor. Both the number and structure of self-help groups in Andhra Pradesh has been scaled up. The major motive of the bank is to accept the deposit and lend that deposit as a loan to investors. A number of social issues including gender and family, child labor, disability and health related to poverty alleviation need to be addressed in the context of SHGs. SHG formations largely take place around women since women are seen as more credit-worthy than men.

Velugu addresses child labor and high dropout rates through regular campaigns to sensitize parents. Especially mothers, youth, other community members and school teachers about the significance of education and its long-term implications for child welfare and poverty decrease. Velugu also aims to directly address the problems of the disabled by organizing them into mutual support groups.

Under Velugu, as the social recruitment process matures in a village, communities are encouraged to analyze their livelihood situations, which in turn disclose options for the community to act. Self-help groups political potential is powerful. Federations form the training ground to make leaders and potential political aspirants. This critical mass has tremendous potential to work for the betterment of the regions they represent.