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MICRO-FINANCE OPERATION AND ACCOUTABILITY

ASSIGNMENT TOPIC:
WHAT ARE THE LENDING POLICIES IN OPERATING ACCOUNTING WHICH ARE OPERATIONAL IN THE BANKING SYSTEM IN NIGERIA

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INTRODUCTION

The bank policies are normally derived from the objectives of their operations which are products of their mission statements. The bank policies are formulated with the intention of ensuring that the operations of the banks are established on sounding footing which conforms to the best practices of banking operations. This is because bank operations are basically embedded in financial intermediation; sourcing for funds from surplus areas and lending such funds to areas of needs.

Bank policies as observed by Uremadu (2004) affect the organizational structure and by extension also influence the employment of the personnel. Bank policies are also used to mould the bank personality and for shaping the desired course of action in terms of the operational direction of the banks.

Bank policies are normally formulated on operational areas such as follows:

- Organizational structure
- Employment of the personnel
- Modalities of operations
- Lending procedures
- Investment of funds
- Strategies for hedging risks in operations sectoral allocation of loans and advances remuneration of personnel
- Appointment of external auditors, etc.

The formulation of bank policies can be the responsibility of the board of directors. The policies can also be formulated by the chief executive officers and tabled before the board for consideration and approval before their implementation. In some instances, the policies can be formulated by committees constituted by the management for such purpose.

The formulation of bank policies in unit banks with their operations being restricted to specific areas, such as the microfinance banks in the country, can be easily accomplished. This is because of such banks' nearness to their personnel and the understanding of the particular areas where they operate.

For instance, a microfinance bank would have distinct operational policies given the peculiar socio-economic conditions as compared to the operational policies for a microfinance bank which engage in business in an area like Lagos. These are also different from the operational policies of microfinance banks that are doing business in Calabar.

The operational policies of the branch banks do differ from those of the unit banks. This is because of the fact that their operations spread over a large geographical area.

Therefore, the branch managers are expected to make some inputs into the overall corporate policies necessary for successful operations.

Furthermore, the branch manager of each area may like to initiate a different policy on a particular matter which is dictated by the peculiar environment in issues such economic growth, economic activities, socio-economic needs, and people's attitudes towards banks generally. (Uremadu, 2004).

The operational policies of the banks, be they unit banks or branch banks, should be couched on the basis of flexibility due to the changing patterns of environmental conditions. Hence banking policies should be subjected to review on periodical basis because of the changing economic condition and other environmental dictates which shape banks' operations.

Therefore, the need for the formulation and constant review of the bank policies becomes very relevant in the areas of sourcing for deposits from the public, investment of funds on marketable securities, hedging against risks in operations, managing credit risks, and above all lending or granting credits, loans and advances to customers.

PRINCIPLES OF BANK LENDING POLICIES

There are basic principles which normally come into play when the commercial banks consider the establishment of lending policies for their operations. Such principles of bank lending (Jhingan, 2008) are as identified and discussed below.

1. Liquidity

This is the uppermost consideration in bank lending because banks only make use of depositor's money for business, and such depositors are entitled to their funds every time they are in need of the money. Therefore, banks lend money for a short term in most cases. This is because the banks lend public money which can be withdrawn at any time by the depositors.

Basically, the banks advance loans on the understanding that they will be repaid within a short time. More so, they lend money on the basis of security that can be easily marketable and convertible into cash at a short notice.

2. Safety

The safety of the funds lent out by the banks must be safe in this sense that the borrower should be able to repay the loan and interest in time at agreed regular intervals without defaults.

Essentially, the repayment of loans by the beneficiaries depends on their capacity to generate enough funds from business entities and the character of such borrowers. Furthermore, the repayment also depends on other factors such as the financial standing of the borrowers and nature of collateral securities pledged for the loans.

While the nature of the security is important in the consideration of lending to customers, the banks take into consideration the creditworthiness of the borrowers which governs his character, capacity to repay, and his financial standing. Relatedly, the safety of the bank funds depends on the technical feasibility and economic viability of the project for which the loan is granted.

3. Diversity

In the process of granting loans to customers, the banks consider the composition of the loan portfolio so as to strike the desired diversity of the investment. The loans being granted to customers are not normally concentrated in a particular type of sector but in different types of sectors, which will have to conform to the policy of sectoral distribution of loans as demanded by the apex bank.

The distribution of the loan portfolio is also imperative towards minimizing risks that are always inherent in lending of funds. The principle of diversity is also applicable to spreading loans to various industries, firms, businesses and trades. Hence, commercial banks do strive to spread of risks of investment in loan portfolio by giving out credits to various trades and industries.

4. Stability

Commercial banks only advance loans to customers whose businesses generate stable incomes. For instance, a customer who applies for a loan facility should have his project or business evaluated to determine the possibility of such ventures generating constant income with which to serve the loan and make repayment on regular basis.

Therefore, for a new project the technical feasibility and economic viability report will be evaluated to determine the nature of cash inflows in terms of stability of earnings, which will be used for repaying the loan and servicing it. The regularity of the earnings is very important and this will depend on the prudent management of the project.

In the case of existing business, the financial reports for a period of not less than five years on consecutive basis will be evaluated to determine the regularity and quantum of earnings. Such assessment is used to evaluate the stability of such earnings towards definite repayment of loan facility.

5. Profitability

Loans and advances are not just granted customers for the fun of it. They are usually granted with the intention of earning some income for the banks. This income can only be earned by the bank through the interest charges being made from the loans granted to customers.

The interest on loans from the banks to customers are normally established taking into consideration the prevailing market rate and the established bank rate by the apex bank in the economy, which is called the monetary policy rate. The interest rate being charged on loans by the commercial banks is normally higher than the bank rate being charged by the apex bank, and building into it other charges as may be determined by the banks.

MAJOR AREAS OF BANK POLICIES ON LENDING

There are critical areas relating to lending that the banks do not normally take for grant in the formulation of bank policies. Such areas for policy formulation on bank lending are as identified and discussed below.

1. Loan Limit

Policies are normally set for the granting of loans by the various officers of the bank that are directing involved in lending. In setting the magnitude of loan that can be approved by the officers in charge of credits, certain factors are usually taken into consideration.

2. Loan Supervision

It is very important for the bank to set policies on loan supervision. The policies on granting of loans, their supervision, and recovery drive are normally established taking into consideration the relevant strategies used in the past and those ones being utilized by other banks.

3. Credit Risk Management

A policy should usually be established for the management of the credit risk in terms of the problems that can emanate from loan recovery by the bank.

There are other areas of responsibilities for the management of credit risks by various bank officials, which are not covered by above list. Therefore, the list is by no means exhaustive for the purpose of credit management of credit risks by the banks.

4. Managing Difficult Loan Beneficiary

There should be policy on how a difficult loan beneficiary can be managed by relevant bank officials. Such policy should be used to specify the necessary actions to be initiated and taken by the bank officials to recover the amount of loan involved in the transaction.

The necessary directives in managing difficult account involve the following considerations:

5. Controlling Customer Accounts

Policy on controlling the account of the customer who is a loan beneficiary is also necessary for consideration in establishing banking policies. The control of customer account is necessary because of the fact that a customer can be playing pranks on the repayment of loan and payment of interest on such funds.

6. Monitoring and Review of Customer Case

This is done to evaluate the performance of a customer's account. It is necessary in the management of the bank's liquidity particularly in the case of big-time customers of the bank. In addition, there is every likelihood that such customers will use their accounts to demand for overdraft or loans in the course of their operations.