

Tutorial Notes

Class: B.Com (Prog.) Semester VI (DSE3)

Subject: Banking & Insurance.

Topic: Types of Loan and Advance by Banks.

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### **Types of Loans and Advances by Banks**

#### **Lending of Money by Banks**

Lending money is one of the primary functions of the bank. Lending of funds to individuals, traders, businessmen and industrial enterprises, is one of the important activities of commercial banks. Interest earned on these loans and advances are the major source of income of the banks. Interest given on deposits is lower than the interest received on such loans and advances. Amount deposited by the customers forms the main source of loans and advances.

Various types of loans and advances given by banks: Banks lend money in various forms for various purposes which are given below:

**1. Cash Credit:** Cash Credit is a type of advance wherein a banker permits his customer to borrow money upto a particular limit by a bond of credit with one or more securities. The advantage associated with this system is that a customer can withdraw money as and when required. The bank will charge interest only on the actual amount withdrawn by the customer. Many industrial concerns and business houses borrow money in this form.

**2. Overdraft:** An overdraft is an arrangement by which the customer is allowed to overdraw his account. It is granted against some collateral securities. The facility to overdraw is allowed through current account only. Interest is charged on the exact amount of overdrawn subject to the payment of minimum amount by way of interest.

**3. Loan:** Loan is an advance in lump sum amount the whole of which is withdrawn and is supported to be rapid generally wholly at one time. It is made with or without security. It is given for a fixed period at in agreed rate of interest. Repayments may be made in installments or at the expiry of a certain period.

**4. Discounting bill of exchange:** The bank also gives advances to their customers by discounting their bills. The net amount after deducting the amount of discount is credited to the account of customer. The bank may discount the bills with or without any security from the debtor in addition to the personal security of one or more person already liable on the bill.