



CCP — Certified Credit Professional

Complete Book | Table of Contents | 29 chapters + 10 sections

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CH-1 Principles of Lending

Topic 1 — Banks as Financial Intermediaries

Banks act as **financial intermediaries**. They accept **deposits** from savers and **lend** these funds to businesses and individuals who need capital for growth and investment.

- **Productive use** — Banks move **idle funds to productive uses** and so support economic development.
- **Core functions** — Deposit taking, lending and investment are the **core functions** of a bank.
- **Income** — Income comes mainly from the **interest spread** between loans and deposits.

Example: A businessman in Delhi keeps ₹5 lakh in a fixed deposit. The bank uses part of this money to finance a start-up in Bengaluru.

Topic 2 — Types of Deposits

Deposit	Key features	Typical users
Savings deposit	Interest-earning, liquid; ATM withdrawals and digital payments	Salaried employees, individuals
Current deposit	Generally no interest ; high liquidity; transactions as per account terms	Businesses, traders
Fixed deposit (FD)	Fixed tenure; higher interest; premature withdrawal allowed with penalty as per terms	Retirees, long-term savers
Recurring deposit (RD)	Monthly instalments for a fixed tenure; earns interest	Students, small investors
Flexi deposit	Combines savings and FD (sweep-in/sweep-out); liquidity with higher interest	High-income individuals, professionals

Savings and current deposits are **demand deposits** (repayable on demand). Fixed, recurring and flexi deposits are **term deposits** repayable on the agreed maturity.

Topic 3 — Why People Deposit Money in Banks

Reason	What the customer gets
Security of funds	Money is safer than cash at home; eligible deposits are covered by deposit insurance up to the statutory limit
Earning interest	Return on savings and term deposits
Easy withdrawals	ATM, cheques, UPI, internet and mobile banking
Convenience	Payments, bill payments and fund transfers from the account

Topic 4 — Lending — the Core Function of Banks

- **Main income** — Banks earn most of their income by charging **interest on loans and advances**.
- **Deployment** — They deploy depositors' money into productive loans and investments.
- **Balance** — They keep enough **liquidity and safety** to repay depositors.
- **Loan types** — Home, vehicle, business, education and personal loans; personal loans are usually unsecured.
- **See** — Ch 2 (p. 5) for the purpose and typical borrowers of each loan type.

Topic 5 — Risk in Lending and Its Mitigation

- **Uncertainty** — Lending is risky because repayment is **uncertain**.
- **Honest default** — Even an honest borrower may fail to repay due to **market conditions, business failure or price volatility**.
- **Response** — Banks therefore use several tools to manage credit risk.

Tool	How it reduces risk
Credit appraisal	Evaluates the borrower's repayment capacity and character
Margin	Bank finances only a part of the requirement; the borrower brings the rest as own stake
Diversification	Spreads loans across sectors, regions and borrowers
Collateral and security	Mortgage, hypothecation or pledge gives a secondary source of recovery
Risk-based pricing	Higher-risk borrowers pay a higher interest rate

Bank finance after margin, where C = cost of the asset or project and m = margin (borrower's contribution as a decimal):

$$\text{Bank Finance} = C \times (1 - m)$$

$$\text{Borrower's Margin} = C \times m$$

Example: A restaurant needs ₹50 lakh for expansion; margin 25%. Bank finance = $50 \times 0.75 = \text{₹}37.5 \text{ lakh}$; owner's contribution = **₹12.5 lakh**. The bank also takes a mortgage of property as collateral.

Topic 6 — Principles of Sound Lending

- **Balance** — Sound lending balances **safety, liquidity and profitability**.
- **Support** — It rests on a lawful **purpose, diversification** and adequate **security**.
- **Art and science** — Lending needs borrower evaluation, credit risk management and cash-flow planning.

Principle	Key focus	Why it matters
Safety	Repayment as agreed from sustainable cash flow	Reduces bad loans (NPAs)
Liquidity	Matching cash inflows and outflows	Bank can meet withdrawals; avoids liquidity crises and bank runs
Profitability	Interest income covers funding, risk and operating costs	Ensures growth of the bank
Purpose	Lawful, productive and permitted use	Purpose drives repayment
Diversification	Spread across borrowers, groups, sectors, geographies	Avoids concentration losses
Security	Collateral as secondary source	Cannot make an unviable project viable

Remember this

- Cardinal trio: **Safety – Liquidity – Profitability**; safety is the primary principle.

Topic 7 — Safety

Safety is the **primary lending principle**: the loan must be repaid as agreed. It depends on the borrower's **capacity** and **willingness** to repay.

Factor	What the banker checks
Capacity to repay	Sustainable primary cash flow from business or income



Factor	What the banker checks
Willingness to repay	Character, integrity and credit history (credit information report)
Loan purpose	Productive use, not speculation

Risk assessment tools

Tool	Use
Cash flow analysis	Shows whether future cash flows can service interest and instalments
Net Present Value (NPV)	Tests whether a project adds value at the required rate of return
Break-even analysis	Finds the sales level at which there is no profit and no loss
Credit grading / rating	Scores the borrower into risk grades for decision and pricing
Altman's Z-score	Predicts financial distress from five ratios

NPV, where CF is the cash flow in year t, r is the discount rate and C₀ is the initial investment; break-even quantity, where FC is fixed cost, P is price per unit and V is variable cost per unit:

$$NPV = \sum_{t=1}^n \frac{CF_t}{(1+r)^t} - C_0$$

$$BEP_{units} = \frac{FC}{P-V}$$

Example: Project cost ₹20 lakh; cash inflow ₹6 lakh a year for 5 years; r = 10%. NPV = 22.7447 – 20 = **₹2.74 lakh** (positive, so viable). Fixed cost ₹12 lakh, price ₹500, variable cost ₹300: BEP = 12,00,000 ÷ 200 = **6,000 units**.

Altman's Z-score (X₁ = working capital/total assets, X₂ = retained earnings/total assets, X₃ = PBIT/total assets, X₄ = market value of equity/book value of liabilities, X₅ = sales/total assets):

$$Z = 1.2X_1 + 1.4X_2 + 3.3X_3 + 0.6X_4 + 1.0X_5$$

Z > 2.99: Safe

1.81 ≤ Z ≤ 2.99: Grey zone

Z < 1.81: Distress

Example: X₁ = 0.15, X₂ = 0.20, X₃ = 0.12, X₄ = 1.20, X₅ = 1.20. Z = 0.18 + 0.28 + 0.396 + 0.72 + 1.20 = **2.776** → grey zone; the banker needs closer scrutiny.

Good profits and management quality support the appraisal, but approval still requires the bank's **credit policy and regulatory checks**.

Topic 8 — Liquidity

Banks must keep enough **liquid funds** to meet deposit withdrawals and other obligations. A mismatch between **short-term deposits** and **long-term loans** creates liquidity risk.

Liquidity tool	Meaning
Diversified deposit base	Mix of savings, current and term deposits
Asset Liability Management (ALM)	Monitors cash inflows and outflows across time buckets
Loan repayment planning	Repayment schedule matched to the borrower's cash flow
Easy sale of security	Collateral should be marketable
Short-term government securities	Liquid assets that can be sold or used for repo when needed

Demand deposits must be repaid **on demand**; term deposits on the agreed maturity. ALM helps **identify, measure and control** liquidity risk, but it gives no guarantee.

Example: A bank lends ₹50 crore to a manufacturer for 5 years. If funded wholly by short-term deposits, it may struggle to meet withdrawals; it keeps part of its funds in short-term government

securities.

Topic 9 — Profitability

Loan income must cover the **cost of funds, credit risk (expected loss) and operating costs**. The interest rate depends on the borrower's **credit rating and risk profile**.

Factor	Effect on pricing
Interest rate charged	Higher for riskier borrowers
Credit rating	Better rating → lower rate
Risk-based pricing	Risk premium added over the benchmark rate
Cost of funds	Bank must raise deposits at low cost to earn a spread

Net interest spread, where r_L is the lending rate, r_F is the cost of funds and L is the loan amount:

$$\text{Spread} = r_L - r_F$$

$$\text{Spread Income} = L \times (r_L - r_F)$$

Example: ₹10 crore loan to a software company. At AAA rating the rate is 8%: interest ₹80 lakh. At BB rating the rate is 12%: interest ₹1.20 crore. With a 6% cost of funds, spread income is ₹20 lakh and ₹60 lakh respectively; the extra ₹40 lakh compensates for higher risk.

Very high rates can push borrowers into **default**; very low rates leave the bank without profit. The bank must balance both.

Topic 10 — Purpose of Loan

- **No automatic loans** — Banks do not lend merely because someone asks.
- **Purpose test** — The purpose must be **lawful, permitted and affordable**.
- **Consumption loans** — They need not generate business income but must be repayable from the borrower's income.

Productive use	Example
Working capital	Short-term funds for operations, e.g. an exporter financing a bulk order
Term loan	Capital expenditure: machinery, factory expansion
Retail loans	Personal finance for individuals
Corporate loans	Funding large enterprises

Topic 11 — Restricted and Regulated Lending Purposes

- **Prohibited** — Lending for **illegal activities** is prohibited.
- **Other restrictions** — These depend on the **instrument and purpose** of the loan.
- **Sensitive activities** — Lawful but sensitive activities need specific checks, limits and the lender's own policy approval.

Area	Current position
Loans on security of the bank's own shares	Prohibited under Section 20 of the Banking Regulation Act, 1949; loans to directors and their interested concerns are restricted
Loans for purchase of gold	Not permitted for primary gold, bullion, jewellery, coins, gold ETF or gold mutual fund units; loans against eligible gold collateral follow RBI's gold and silver collateral directions
Loans against listed shares (individual)	Up to ₹1 crore per individual, with LTV cap of 60%
IPO / FPO / ESOP financing (individual)	Up to ₹25 lakh per individual
Acquisition finance	Bank funding up to 75% of deal value; acquirer brings at least 25% from own funds

Area	Current position
Lawful but sensitive activities (e.g. casinos)	No universal RBI ban; depends on law, bank policy and risk appetite

The capital market exposure limits above apply under RBI's revised capital market exposure directions, effective from 1 July 2026.

Topic 12 — Priority Sector Lending

- **Mandate** — RBI requires banks to lend a minimum share of credit to **priority sectors**.
- **Base** — Targets are a percentage of **Adjusted Net Bank Credit (ANBC)** or **Credit Equivalent of Off-Balance Sheet Exposures (CEOBE)**, whichever is **higher**.
- **Education** — Loans for education, including vocational courses, qualify up to ₹25 lakh.
- **See** — Ch 16 (p. 70) for foreign-bank targets, export credit and housing limits, and the PSL target formula.

Category	Domestic SCBs and foreign banks with ≥20 branches	RRBs	SFBs	UCBs
Total PSL	40%	75%	60%	60%
Agriculture	18% (non-corporate farmers 14%, incl. SMF 10%)	18%	18%	—
Micro enterprises	7.5%	7.5%	7.5%	7.5%
Weaker sections	12%	15%	12%	12%

Example: ANBC ₹1,20,000 crore; CEOBE ₹90,000 crore → base ₹1,20,000 crore. Total PSL 40% = ₹48,000 crore; agriculture 18% = ₹21,600 crore; SMF 10% = ₹12,000 crore; micro 7.5% = ₹9,000 crore; weaker sections 12% = ₹14,400 crore.

Remember this

- PSL: **40 – 18 – 10 – 7.5 – 12**; RRB 75, SFB 60, UCB 60.

Topic 13 — Diversification of Risk and Exposure Limits

Banks must not lend too much to a single **borrower, group, sector or location**. Economic downturns, political events, natural disasters or market crashes can hit a concentrated portfolio hard.

Method	Meaning
Sector-wise caps	Internal limits on industries such as steel, textiles, pharma, real estate
Geographical diversification	Lending across states and cities to avoid regional shocks
Exposure limits	No excessive lending to a single borrower or connected group

- **RBI limits** — RBI sets counterparty and group limits under the **Large Exposures Framework**.
- **Base** — Limits are a percentage of the bank's **eligible capital base (Tier 1 capital)**.
- **Sector limits** — Sector concentration is controlled by the bank's Board-approved policy.
- **See** — Ch 2 (p. 5) for the Large Exposures Framework limits and an illustrative sector-wise portfolio mix (e.g. real estate 15% of a ₹2,000 crore book).

Example: Tier 1 capital ₹5,000 crore: single counterparty ₹1,000 crore (₹1,250 crore with Board approval); group ₹1,250 crore; reporting as large exposure from ₹500 crore.

A bank that lends **50%** of its book to real estate can suffer heavy losses if property prices crash; a spread portfolio limits the damage.

Remember this

- LEF: **20 + 5** single, **25** group, **10** = large exposure.

CCP | Module A | CH-1 | MCQs

Q1. A borrower needs ₹80 lakh to buy machinery and the bank stipulates a 20% margin. What is the maximum bank finance? [Ref: Topic 5, p. 2]

- (a) ₹16 lakh (b) ₹60 lakh (c) ₹64 lakh (d) ₹80 lakh

Q2. A bank's ANBC is ₹2,00,000 crore and CEOBE is ₹2,20,000 crore. What is its agriculture target? [Ref: Topic 12, p. 4]

- (a) ₹39,600 crore (b) ₹36,000 crore
(c) ₹44,000 crore (d) ₹16,500 crore

Q3. A bank has Tier 1 capital of ₹8,000 crore. What is its normal exposure limit to a group of connected counterparties? [Ref: Topic 13, p. 4]

- (a) ₹1,600 crore (b) ₹2,000 crore (c) ₹800 crore (d) ₹2,400 crore

Q4. A bank lends ₹5 crore at 11% when its cost of funds is 7%. What is the annual spread income? [Ref: Topic 9, p. 3]

- (a) ₹35 lakh (b) ₹55 lakh (c) ₹15 lakh (d) ₹20 lakh

Q5. A unit has fixed costs of ₹18 lakh, selling price ₹900 per unit and variable cost ₹600 per unit. What is its break-even quantity? [Ref: Topic 7, p. 2]

- (a) 2,000 units (b) 6,000 units (c) 3,000 units (d) 20,000 units

Q6. A borrower's Altman ratios are $X_1 = 0.10$, $X_2 = 0.15$, $X_3 = 0.05$, $X_4 = 0.50$ and $X_5 = 0.80$. How is the borrower classified? [Ref: Topic 7, p. 2]

- (a) Distress zone (Z about 1.60) (b) Grey zone (Z about 2.10)
(c) Safe zone (Z about 3.10) (d) Grey zone (Z about 2.50)

Q7. A bank's ANBC is ₹1,00,000 crore and CEOBE is ₹80,000 crore. What is the minimum lending to micro enterprises? [Ref: Topic 12, p. 4]

- (a) ₹6,000 crore (b) ₹12,000 crore
(c) ₹7,500 crore (d) ₹10,000 crore

Q8. A bank approves a loan mainly because a valuable property is offered, though the project's cash flows are weak. Which principle is ignored? [Ref: Topic 7, p. 2]

- (a) Liquidity
(b) Diversification
(c) Profitability
(d) Safety, which rests on primary cash flow

Q9. A bank funds 10-year infrastructure loans entirely with 1-year deposits. Which principle is most at risk? [Ref: Topic 8, p. 3]

- (a) Liquidity (b) Safety
(c) Purpose (d) Diversification

Q10. What is the priority sector limit for an education loan to an individual, including vocational courses? [Ref: Topic 12, p. 4]

- (a) ₹10 lakh (b) ₹20 lakh (c) ₹50 lakh (d) ₹25 lakh

Q11. A customer offers shares of the lending bank itself as security for a loan. The bank should: [Ref: Topic 11, p. 3]

- (a) Accept at 50% margin
(b) Accept with Board approval
(c) Decline, as Section 20 of the BR Act prohibits it
(d) Accept only for a term loan

Q12. An individual wants a bank loan to subscribe to an IPO. What is the maximum bank finance per individual? [Ref: Topic 11, p. 3]

- (a) ₹25 lakh (b) ₹10 lakh (c) ₹1 crore (d) ₹50 lakh

Q13. A bank has 50% of its loan book in real estate and plans to bring it down to 15%. Which principle is it applying? [Ref: Topic 13, p. 4]

- (a) Profitability (b) Liquidity
(c) Diversification of risk (d) Purpose of loan



Q14. A bank's single counterparty exposure in exceptional cases with Board approval can go up to what share of Tier 1 capital? [Ref: Topic 13, p. 4]

- (a) 20% (b) 15% (c) 30% (d) 25%

Q15. Which of the following loans does a bank decline under current RBI rules? [Ref: Topic 11, p. 3]

- (a) Gold loan against jewellery as collateral
(b) Loan to buy gold coins
(c) Home loan of ₹30 lakh
(d) Working capital to an MSME

Answer key

Q	Ans	Q	Ans	Q	Ans	Q	Ans	Q	Ans
1	c	4	d	7	c	10	d	13	c
2	a	5	b	8	d	11	c	14	d
3	b	6	a	9	a	12	a	15	b

CH-2 Credit Policy

Topic 1 — Credit Policy

The **Credit Policy (Loan Policy)** of a bank is a structured, **Board-approved** guideline that directs how the bank **grants, manages and monitors** loans and advances.

Purpose	What it achieves
Efficient lending	Lending grows while credit risk is kept under control
Balance	Balances credit volume, earnings and asset quality
Alignment	Aligns lending with regulatory requirements and corporate goals
Customer and profit	Maintains customer satisfaction and profitability

Example: A bank's credit policy allows loans only to customers with **verified income** and a **good credit history**.

Topic 2 — Key Components of a Credit Policy

Component	Purpose	Application
Customer Acceptance Policy	Defines who can apply and the eligibility criteria	Lending only to customers with stable income and a good credit record
Know Your Customer (KYC) Policy	Identity verification to prevent fraud and money laundering	An accepted Officially Valid Document (OVD) plus PAN or Form 97 (formerly Form 60); Aadhaar is one OVD option and is not always mandatory
Retail and Corporate Lending Guidelines	Rules for home, business and corporate loans	Credit-score cut-off is set by lender policy ; RBI prescribes no universal minimum score
Customer Due Diligence	Evaluates repayment ability and creditworthiness	Financial documents analysed before a ₹10 lakh loan

Example: A ₹50 lakh business loan cannot be sanctioned without checking **financial documents, business stability and repayment capacity**.

Topic 3 — Need for a Credit Policy

Reason	Benefit
Regulatory compliance	Bank follows RBI directions and risk-management rules
Risk management	Fewer loan defaults and bad debts
Loan portfolio quality	Balanced distribution of loans across sectors
Consistent decision-making	No biased or inconsistent sanctions
Customer and shareholder trust	Confidence in the bank's financial stability

Excessive concentration (for example in **real estate**) is avoided through **Board-approved sector limits** and **RBI exposure norms**. RBI does not prescribe a universal sector percentage.

Topic 4 — Credit Function — Loans and Advances

Facility	Purpose	Typical users
Home loan	Buying or constructing a house	Salaried and business persons, professionals
Personal loan	Unsecured loan for personal needs	Individuals — medical, travel, weddings
Business loan	Funding operations or expansion	Small and large businesses
Working capital loan	Short-term business finance	Retailers, traders, MSMEs
Term loan	Long-term capital investment	Factories, industries
Overdraft	Flexible borrowing for cash-flow management	Businesses with fluctuating income
Letter of Credit (LC)	Facilitates trade payments, including international trade	Importers and exporters
Bank Guarantee	Secures financial or performance obligations in business deals	Contractors, businesses

LCs and guarantees are **non-fund based** facilities; the rest are **fund based**.

Example: A Surat textile unit seeks a **₹1 crore working capital** loan; the bank checks its financials and sanctions it under business-lending guidelines.

Topic 5 — Objectives of Credit Policy

Objective	How it is achieved
Loan portfolio quality	Lend only to creditworthy borrowers; monitor repayments regularly
Profitability vs risk	Earn interest while minimising defaults; diversify across sectors
Liquidity	Avoid excessive long-term lending from short-term deposits; keep liquid reserves for withdrawals
Regulatory compliance	Follow RBI norms and laws; implement AML and KYC policies

Example: Strict due diligence before a **₹5 crore** corporate loan prevents bad debts and fraud.

Topic 6 — Credit Policy Framework

- Meaning** — The **Credit Policy Framework** is a formal document approved by the bank's **Board**.
- Role** — It guides all lending while ensuring regulatory compliance and risk management.
- RBI expectation** — Every bank must have a **comprehensive Board-approved credit-risk policy**.