

Problems of Allocation of Consumer Loans in Commercial Banks

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Abstract

This article examines the complexities and challenges associated with the allocation of consumer loans within commercial banks. By analyzing the literature, it examines the methods used, the results obtained, and discusses the implications. Conclusions from the discussion provide insights and suggestions for addressing these issues.

Keywords: Consumer loans, commercial banks, separation, problems, methods, results, discussions, conclusions, proposals.

Introduction

Consumer loans play an important role in the activity of commercial banks and serve as an important source of income. However, allocating consumer loans in the banking system presents various difficulties. This article examines the nuances of this separation process, aiming to shed light on the challenges faced by commercial banks. Previous studies have highlighted a number of problems with the allocation of consumer loans in commercial banks. These issues range from regulatory compliance to risk management issues. In addition, the literature emphasizes the importance of effective methods in overcoming these barriers.

MAIN PART

In order to better understand the issues, this study uses a qualitative approach, analyzing existing literature and case studies. Methods include a systematic review and content analysis of academic articles, reports, and banking regulations related to consumer credit allocation. Separation of consumer loans within commercial banks from other banking activities can cause a number of problems:

✚ Risk management: Consumer loans generally have a different risk profile than other types of loans, such as commercial or mortgage loans. Unbundling consumer loans is complex and requires a specific risk management strategy tailored to the specifics of consumer loans. Consumer loans, of course, pose unique risks that require a specific risk management strategy. Here are some key points:

✓ Credit Risk Assessment: Consumer loans are often smaller than commercial or mortgage loans, but they are usually unsecured. This means that lenders must focus on rigorously evaluating the creditworthiness of individual borrowers. Using credit scores, income checks, and debt-to-income ratios are common ways to assess consumer credit risk.



✓ Behavioral risk: Consumer behavior is less predictable than that of business or property owners. Factors such as job loss, unexpected expenses or changes in personal circumstances can affect a borrower's ability to repay. A risk management strategy should include scenario analysis to predict and mitigate the risk of these behaviors.

✓ Regulatory Compliance: Consumer credit is subject to consumer protection laws and regulations, such as the Truth in Lending Act (TILA) and the Fair Credit Reporting Act (FCRA). Ensuring compliance with these regulations is essential to avoid legal and reputational risks.

✓ Market Risk: Consumer loan portfolios may be susceptible to economic fluctuations and changes in consumer spending habits. Risk managers should monitor macroeconomic indicators such as the unemployment rate and interest rate movements to accurately assess the impact of market risk.

✓ Collections and Recovery: Collecting funds from consumer loans in the event of default can be difficult and expensive. Effective risk management includes implementing robust portfolio processes and strategies for credit exercise and recovery.

✓ Fraud Risk: Consumer credit is vulnerable to various forms of fraud, including identity theft and loan application fraud. Using advanced fraud detection tools and verification processes is critical to mitigating this risk.

✓ Technology and data risks: With the increasing digitization of lending processes, cyber security and data privacy have become important concerns. Risk managers must ensure the security of customer data and systems to prevent data breaches and cyberattacks.

Given these complexities, it is wise to separate consumer loans for separate risk management. Adapting the risk management strategy to the unique characteristics and challenges of consumer credit helps financial institutions effectively reduce risks while optimizing portfolio performance.

🌈 Operational efficiency: maintaining separate systems and processes for consumer loans in a commercial bank can lead to increased operational complexity and costs. Additional infrastructure, technology and personnel may be required to effectively manage these operations.

Maintaining separate systems and processes for consumer loans in a commercial bank can actually add operational complexity and increased costs. Here's how:

➤ Infrastructure costs: running separate systems means investing in additional infrastructure such as servers, databases, and software licenses to support each system. This includes not only initial setup costs, but ongoing maintenance costs as well.

➤ Technology Integration Challenges: Integrating separate systems can be complex and time-consuming. It often requires custom development or the use of middleware to ensure seamless communication between systems, which increases overall cost and complexity.

➤ Data Management: Managing data across multiple systems can be difficult. This can lead to data duplication, inconsistencies, and errors, requiring additional resources to collate and clean data.

➤ Personnel requirements: the operation of separate systems may require the hiring and training of personnel with specialized skills to operate each system. This increases payroll costs and can create inefficiencies if employees are not rotated between systems.



➤ **Operational inefficiencies:** Having separate processes for consumer loans can lead to repetitive efforts and manual workarounds to transfer information between systems. This not only slows down processes, but also increases the likelihood of errors and delays.

➤ **Regulatory Compliance:** Compliance with regulatory requirements becomes more complicated when working with multiple systems. Ensuring consistency and accuracy in reporting across systems requires additional oversight and resources.

Consolidating consumer credit systems and processes can alleviate these challenges and lead to long-term operational efficiencies and cost savings. By centralizing operations, banks can streamline workflows, reduce duplication of effort, and leverage economies of scale in technology infrastructure and staffing.

✚ **Capital allocation:** banks need to allocate capital properly to support their lending activities. Allocation of consumer loans may require a separate capital allocation methodology, which may affect the bank's overall capital structure and profitability.

Capital allocation is essential for banks to have sufficient funds to support their lending activities while maintaining a healthy balance sheet. When it comes to consumer loans, banks often use separate capital allocation methodologies due to the distinct risk profiles associated with different loans. For example, consumer loans typically have shorter terms and lower risk than commercial loans. Therefore, banks can allocate less capital to consumer loan portfolios. This allows them to optimize their capital structure by allocating more capital to risky assets that meet regulatory requirements while maintaining profitability. By using separate capital allocation methodologies, banks can better manage their risks and ensure that they have sufficient capital to withstand potential losses in different segments of their loan portfolio. This approach helps banks to maintain stability and stability in the face of economic uncertainties.

❖ **Regulatory Compliance:** Consumer credit is subject to various regulations designed to protect consumers and ensure fair lending practices. Unbundling consumer loans may require compliance with additional regulatory requirements specific to consumer credit, adding another layer of complexity to regulatory compliance efforts.

❖ **Cross-selling opportunities:** commercial banks often benefit from cross-selling products and services to their customers. Unbundling consumer loans could potentially limit cross-selling opportunities and synergies with other banking products, impacting profitability.

❖ **Economies of scale:** Commercial banks typically benefit from economies of scale by offering a wide variety of financial products and services. Diversification of consumer loans can reduce economies of scale and affect the bank's overall profitability.

❖ **Customer Experience:** Customers often value convenience and seamless integration of financial services. If customers have to interact with different departments or systems for different types of banking services, the separation of consumer loans can lead to customer separation.

❖ **Brand image and trust:** A bank's reputation can be affected by its ability to effectively manage its various lending activities. Unbundling consumer loans can affect a bank's brand image and trust if customers perceive it as service fragmentation or a lack of expertise in consumer loans.

Overall, while there may be potential benefits to unbundling consumer loans within commercial banks, such as increased focus and specialization, it also raises several issues that



need to be carefully considered and managed. The discussion explores the implications of these challenges and explores potential strategies to address them. This highlights the need for simplified regulatory frameworks, improved risk management practices and investment in technology infrastructure. In addition, cooperation between banks and regulators is essential to effectively manage complexities.

CONCLUSION

In conclusion, the separation of consumer loans in commercial banks creates multifaceted problems, which need to be solved together. While regulatory compliance remains an important concern, operational and technological constraints also pose significant obstacles. However, by adopting proactive measures and developing partnerships, banks can mitigate these issues and improve the efficiency of their loan allocation processes. Based on the findings, it is recommended that commercial banks prioritize investments in technology to automate loan origination processes and improve data management capabilities. In addition, developing close cooperation with regulatory authorities can facilitate compliance efforts and make the regulatory environment more conducive.

In addition, continuous monitoring and evaluation of separation procedures is essential to adapt to evolving market dynamics and regulatory requirements. In conclusion, the problems related to the distribution of consumer loans in commercial banks are important, but they cannot be solved. By proactively addressing regulatory, operational and technological challenges, banks can improve efficiency and stability in managing their consumer loan portfolios.

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