A Study on Non-Performing Assets of Scheduled Commercial Banks in India

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ABSTRACT:

Banking is considered as the life blood of every country's economy. Any issue relating to the banking sector will adversely affect the economy. Indian banking sector has been facing so many serious issues regarding the increasing level of Non- Performing Assets (NPAs). NPAs directly impacts on the liquidity, profitability and the overall quality of the assets and successful survival of the banks. The issue of NPAs is not just influencing the bank but also the entire economy. The NPA size on banking sector is comparatively higher in scheduled commercial banks. To maintain the profitability and efficiency of banks, the NPA must to be controlled and reduced. The level of NPA is best indicator for assessing the health of banking sector of a country. This is evident from the Financial Stability Report released by the RBI on 30th June, 2017 has highlighted that the asset quality also deteriorated due to increase in NPAs. In this context, reducing NPAs has become the primary goal of any bank.

Key words: *NPAs, Gross NPAs and Net NPAs*

INTRODUCTION:

Banks play a pivotal role in the Upliftment of various sectors of an economy. The two main functions of a bank are accepting deposits from public and lending to individuals, corporate and government. The deposits are liability of a bank, as the bank to pay them back along with interest either on maturity or on demand. Similarly, loans are assets as they yield interest to the bank ,which is the primary source of income for a bank. Generally the banks lend money at a higher rate than they pay to depositors or than they borrow it. The difference known as the interest margin i,e profit for the bank. Generally, the more the banks lend the more profitable they become. This motivates a bank to lend vigorously in order to increase profitability.

However, If the customer does not pay either interest or part of principal the loan turns in to bad loans, i,e Non-Performing Assets . According to RBI, terms loans on which interest or instalment of principal remain

overdue for a period of more than 90 days from the end of a particular quarter is called as Non-performing Asset.

However, in terms of Agriculture / Farm Loans; the NPA is defined as under: For short duration crop agriculture loans such as paddy, Jowar, Bajra etc. if the loan (installment / interest) is not paid for 2 crop seasons , it would be termed as a NPA.

For Long Duration Crops, the above would be 1 Crop season from the due date.

The loan assets have been classified under four categories:

1.**Standard assets**: Those assets which generate regular income in the form of interest or instalment without any sign of sickness.

2.Sub-standard assets: Sub Standard assets would be one, which has remain NPAs for a period less than or equal to 12 months.

3.Doubtful assets: An assets would be classified as NPAs, if it has remained in sub standard category for a period of more than 12 months.

4.Loss assets: A loss asset is one, where loss has been identified by the bank or internal or external auditors or the RBI inspection but the amount has not been written off wholly. In other words, such an asset is considered uncollectible and of such little value that its continuance as a bankable asset is not warranted although there may be some salvage or recovery value.

Standard assets are performing assets and remaining three assets i,e sub standard assets ,doubtful assets and loss assets are called as Non-Performing Assets.

NPAs are divided into two categories namely Gross NPAs and Net NPAs.

Gross NPAs : reflects the quality of the loans made by the banks. It is the total of all the loan assets that are classified as NPA on a balance sheet date. It includes sub-standard, doubtful and loss assets.

Net NPAs: It reflects the actual burden of banks. It is calculated as follows

Net NPAs= Gross NPAs-(Balance in interest suspense account + claims received + part payment received + total provisions held) case of newly established banks.

The NPAs are considered to be an important parameter to judge the performance and financial health of banks. This paper attempts to study the status of Non-Performing Assets of Schedules Commercial Banks (SCBs) in India.

REVIEW OF LITERATURES:

Singh (2013) in his paper ―Recovery of NPAs in Indian Commercial Banks‖ emphasised that the reason for the raising NPAs is poor management of credit risk by the banks. Banks should fix pre sanctioning appraisal and an effective post-disbursement supervision.

Asha Singh (2013) in "Performance of Non-Performing Assets in Indian commercial banks" observed that the NPAs of the public sector banks are increasing year by year. On the contrary, the non-performing assets of private sector banks have been decreasing regularly year by year except in some years. Generally reduction in

NPAs shows that banks have strengthened their credit appraisal processes over the years and increased in NPAs shows the necessity of provisions, which brings down the overall profitability of banks.

Khanna (2012) in her paper titled ―Managing NPA in Commercial Banks‖ said that mounting NPAs are a major cause of concern as a higher level of NPAs means more probability of credit defaults eroding the profitability and net-worth of the banks.

Prasad &Veena (2011) in their paper on ―NPAs Reduction Strategies for Commercial Banks in India‖ stated that NPAs have a destructive impact on the ROA as NPAs do not generate any net interest income. Consequently, the profits of the banks are reduced and limits the recycling of fund.

Rai (2012) in her study on Study on performance of NPAs of Indian commercial banks find out that corporate borrowers even after defaulting continuously never had the fear of bank taking action to recover their dues. This is because there was no legal framework to safeguard the real interest of banks.

The existing studies generally focused on analyzing NPAs till the end of the year 2015. This paper attempts to examine the trend in NPAs from the year 2008 till 2017 ,which primarily focused on analyzing the Non-Performing Assets in Scheduled Commercial Banks in India.

STATEMENT OF THE PROBLEM

The problem of NPAs in the Indian banking system is one of the foremost and the most formidable problems that had impact the entire banking system. Higher NPA ratio trembles the confidence of investors, depositors, lenders etc. It also causes poor recycling of funds, which in turn will have deleterious effect on the deployment of credit. The non-recovery of loans effects not only further availability of credit but also financial soundness of the banks.

The increased NPAs may pose liquidity issues which is likely to lead run on bank by depositors. Thus, the increased incidence of NPAs not only affects the performance of the banks but also affect the economy as a whole.

Mid-eighties, management of NPAs was left to the banks and the auditors. In 1985, the first ever system of classification of assets for the Indian banking system was introduced on the recommendations of A. Ghosh Committee on final accounts. This system, called the ‘Health Code System’ (HCS), which classified the bank advances into eight categories ranging from 1 (satisfactory) to 8 (bad and doubtful debt).

In 1991, the Narasimhan Committee on the financial system felt that the classification of assets according to the HCS was not in accordance with international standards and recommended that for the purpose of provision, banks should classify their advances into four broad groups, viz. (i) standard assets; (ii) substandard assets; (iii) doubtful assets; (iv) loss assets. According to this prudential norm relating to income recognition, asset classification and provisioning were introduced in the year 1992 in a phased manner. In 1998, the Narasimhan Committee on Banking Sector Reforms recommended a further tightening of prudential standards in order to strengthen the prevailing norms and bring them on par with evolving international best practices. With the introduction of 90-days norms for classification of NPAs in 2001, the NPA guidelines were brought on

par with international standards. This paper attempts to examine the level of Non-Performing Assets in Scheduled Commercial Banks in India.

OBJECTIVES

The objective(s) of the study are as follows: .

1. To study the status of Non-Performing Assets of Scheduled Commercial Banks in India.
2. To study the reason of increasing NPAs in Scheduled Commercial Banks during the study period.
3. To make appropriate suggestions to avoid future NPAs and to manage existing NPAs in Banks.

METHODOLOGY OF THE STUDY

The present study is an empirical one to analyze the NPAs of Scheduled Commercial Banks during the period of study. For this purpose, the data has been collected from the secondary sources, i.e., the RBI reports and bulletins. This research study is aims at to explore the trends of NPAs over a period of study. This is generally analysed by computing through the following ratios.

Gross NPA Ratio = (Gross NPA / Gross Advances) * 100

Net NPA Ratio = (Gross NPAs – Provisions/Gross Advances -Provisions) * 100

SCOPE OF THE STUDY

The study is mainly focused its attention on the NPAs and their trends in the scheduled Commercial Bank in India. It covers the aspects, such as the volume and trends of NPAs, causes of increasing NPAs , impact and suggestion to control the Non-Performing Assets of the banks.

PERIOD OF STUDY

The study covers a period of ten years, i.e., 2007-08 to 2016-17 during these years those loan accounts became Non-Performing Assets are only included in the analysis.

SOURCES OF DATA

The study is mainly based on the secondary data, which is collected from the Reserve Bank of India reports during the period of study. Besides, the data is also collected from the various other published documents and government bulletins .

Table 1

Gross NPAs and Net NPAs of Scheduled Commercial Banks in India (Rs.in Billions)

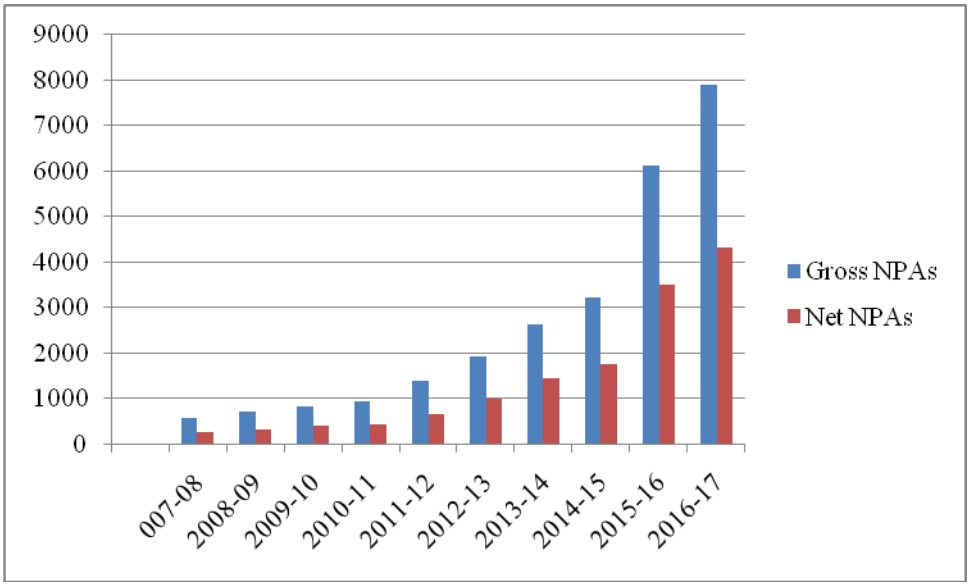
Year	Gross NPAs	Gross NPAs Ratio (%)	Net NPAs	Net NPAs Ratio(%)
2007-08	566.06	2.3	247.30	1.0
2008-09	699.54	2.3	315.64	1.1

2009-10	817.18	2.5	391.27	1.1
2010-11	939.97	2.4	417.99	1.0
2011-12	1369.68	2.9	652.05	1.3
2012-13	1927.69	3.2	986.93	1.7
2013-14	2630.15	3.8	1426.56	2.1
2014-15	3229.16	4.3	1758.41	2.4
2015-16	6116.07	7.5	3498.14	4.4
2016-17	7902.68	9.3	4330.10	5.3

Sources:RBI-Handbook of Statistics on Indian Economy

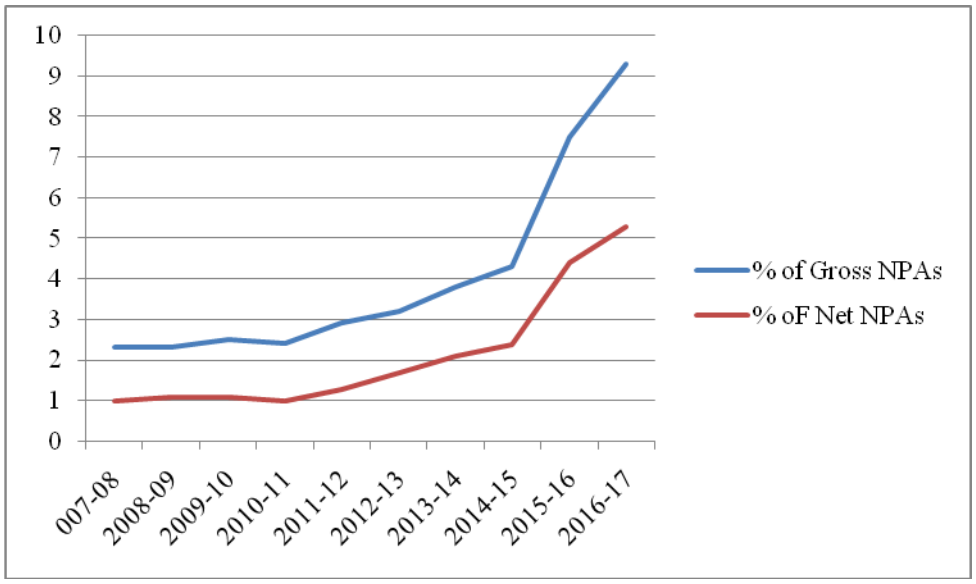
Table 1 shows that the data on the Gross NPAs and Net NPAs as percentage of gross and net advances in SCBs from the year 2007-08 to 2016-17.It can be seen from the data that initially the Gross NPAs as percentage of Gross advances ratio is constant for a period of two years 2007-08 and 2008-09 at 2.3per cent. From the subsequent year the ratio continuously increased and reached at 9.3% in 2016-17 except in the year 2010-11(2.4 per cent).The Net NPAs as percentage of net advances becomes constant in the year 2008-09 and 2009-10.Thereafter increased upto 5.3 % in 2016-17.Both the amount of Gross NPAs and Net NPAs shows increasing trend during the study period.

Graph 1 Amount of Gross NPAs and Net NPAs (Rs.in Bilions)



The above figure shows the trend of Gross NPA and Net NPA in billions for the period of 2007-08 to 2016-17. The x-axis represent the years i.e. as the period of (2007-08 – 2016-17) whereas y-axis represent the amount of NPAs. We can observe here that the Gross and Net amount of NPAs has been showing an upward trend beginning from 2007-08 to 2016-17.

Graph 2 Ratio of Gross NPAs and Net NPAs



The above figure portrays the trend of Gross NPAs and Net NPAs in percentage of Gross advances and Net advances for the period of 10 years i.e. from 2007-08 till 2016-17. The x-axis represents the years whereas y-axis represents the percentage of NPAs. We can observe here that the Percentage of Gross and Net NPAs has been showing upward trend from 2007-08 to 2016-17.

REASONS FOR THE RISE IN NPA LEVELS

- From 2000-2008, the Indian economy was in a boom phase and banks, especially public sector banks, started lending extensively to companies.
- However, with the financial crisis in 2008-09, corporate profits decreased and the Government banned mining projects. The situation became serious with the substantial delay in environmental permits, affecting the infrastructure sector – power, iron, and steel – and resulting in volatility in prices of raw materials and a shortage of supply.
- Another reason is the relaxed lending norms adopted by banks, especially to the big corporate houses, foregoing analysis of their financials and their credit ratings.

PREVENTIVE MEASURES OF NON-PERFORMING ASSETS

- **Insolvency and Bankruptcy Code (IBC)** – With the RBI's push for the IBC, the resolution process is expected to quicken while continuing to exercise control over the quality of the assets. There will be changes in the provision requirement, with the requirement for the higher proportion for provisions going to make the books better.

- Credit Risk Management involves credit appraisal and monitoring accountability and credit by performing various analysis on profit and loss accounts. While conducting these analyses, banks should also do a sensitivity analysis and should build safeguards against external factors.
- A proper and effective Management Information System (MIS) needs to be implemented to monitor warnings. The MIS should ideally detect issues and set off timely alerts to management so that necessary actions can be taken.
- The present scenario allows the RBI just to conduct an inspection of a lender but doesn't give them the power to set up an oversight committee. With the amendment to the law, the RBI will be able to monitor large big accounts and create oversight committees.
- For quite some time, PSU lenders have started putting aside a large portion of their profits for provisions and losses because of NPA. The situation is so serious that the RBI may ask them to create a bigger reserve and thus, report lower profits.
- The Government needs to amend the laws and give more power to banks to recover NPA rather than play the game of "wait-and-watch."
- Banks, especially the public sector ones, need to come up with proper guidance and framework for appointments to senior level positions.
- Lower level executives are often made accountable today; however, major decisions are made by senior level executives. Hence, it becomes very important to make senior executives accountable if Indian banks are to tackle the problem of NPAs.

With the potential solutions above, the problem of NPAs in Scheduled Commercial Banks can be effectively monitored and controlled, thus allowing the banks to achieve a clean balance sheet.

CONCLUSION:

The Non-Performing Assets have always created a big problem for the banks in India. The money locked up in NPAs has a direct impact on profitability of the bank as Indian banks are highly dependent on income from interest on funds lent. To improve the efficiency and profitability,various steps have been taken by government to reduce the NPAs. It is highly impossible to have zero percentage NPAs. But at least Scheduled Commercial Banks should take care to ensure that they give loans to creditworthy customers.

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