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Mounting of Non-Performing Assets and its Impact on the Performance of Indian Banking Sector

(A Comparative Analysis on the Public & Private Sectors and Foreign Banks)

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ABSTRACT

The financial sector reforms initiated in India as part of the broader canvas of economic reforms since 1991 have led to strengthening of the banking sector in the last two and half decades. The entry of new private sector banks and relaxing the policy towards the foreign banks had led to the creation of a more competitive environment in Indian banking sector. With these developments, the banking sector in India is facing two challenges, i.e., higher Non-Performing Assets (NPAs) culminating into banking crisis on one hand and challenges from younger banks and foreign banks offering diversified banking services tailored according to the needs of customers and compatible with their financial stability. In countries, like Philippines, Korea, Thailand, China, etc., banks were restructured or merged or their NPAs were transferred to the Asset Management Companies or Asset Reconstruction Companies. The Indian banking system luckily has escaped this episode, despite having huge NPAs, because of their ownership with the government. However, the NPAs are still high in respect of public sector banks, whereas the new private banks and foreign banks are performing so well that their net profits are at comfortable level after due coverage of losses due to the NPAs. Against this background, this paper attempts to study the trends of NPAs in Indian banking sector, specifically sector-wise, and identify the causes and consequences of NPAs. Thus, the problem of NPAs needs lots of serious efforts; otherwise, they will erode the profitability of banks, which is not desirable for a growing economy like India.

Introduction

The financial sector reforms initiated in the country as part of the broader canvas of economic reforms since mid-1991 have led to strengthening of the banking sector in the last two and half decades. With this the banking sector in India is facing mainly two challenges, higher NPAs culminating into banking crisis along with low-profit margins on one hand and challenges from private and foreign banks offering diversified banking services tailored according to the needs of the customers compatible with their financial stability.

If the banking system gets into financial crisis, it can engulf the entire economic growth of the economy. If the NPAs touch 10 percent of the banking assets, it leads to the financial crisis of the banking sector wherein the resolution cost of crisis tends to be 2 percent or more of GDP. In other countries, like Philippines, Korea, Thailand, China, etc., banks were restructured or merge or their NPAs were transferred to Asset Management Companies or Asset Reconstruction Companies.

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The Indian banking system luckily has escaped the severe crisis despite having high NPAs and large losses because of their ownership with the government. Besides, restructuring their capital, the banks have improved their capital adequacy ratio, disclosure norms and have been proving provision for NPAs. However, the NPAs are still high, the new banks' performance was good as their net profits more than covered the NPAs.

Thus, the NPAs have been creating lots of buzz in the banking sector throughout their business operation over the years. The NPAs are the loans and advances which discontinue fetching the income to the banks, i.e., when loans and advances cease to generate income for the banks and financial institutions are termed as Non-Performing Assets. These assets not only become a problem for the banks but also bad for the economy. NPAs lead to affect the banks' profitability as well as they increase capital needs for recycling of asset and thus deteriorate the quality of assets. Thus, the major agenda of many Indian banks is trimming down the NPAs, which will improve the profitability of the banks. Till March 2015, the contribution of non-priority sector NPAs was more than 50 percent over the years, obviously, this becomes the case with the priority sector NPAs also. However, the percentage of priority sector NPAs have been declining for the last couple of years but increasing in absolute terms as banks' total advances are increasing. Further, the NPAs level of domestic banks is still high as compared to the foreign banks.

Until 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), 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 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 these prudential norms 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 further tightening of prudential standards 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.

Review of Literature:

In this section, an attempt is made to review the earlier studies made so far on the non-performing assets in Indian banks and highlight the need for the present study.

Baiju S. and Thattil (2000) in their study analyzed the NPAs in commercial banks during the period 1993 to 1998 and found that foreign and new private banks have lower NPAs as compared to the public-sector banks and suggested several ways to recover NPAs. Joshi (2000) in his study identified reasons behind the emergence of NPAs and steps to be taken by the government for their recovery. It is found from the analysis that the interest earned on advances should always be more than interest paid on deposits as a matter of sound banking policy.

Sharma (2001) in a study examined the hypothesis that the problem of NPAs of Indian banks remained unsolved because of the improper sequencing of reforms. She suggested that the proactive approach towards the legislative, infrastructural and regulatory reforms to prevent the build-up of NPAs in future.

Parekh (2002) in his attempt found that the gross NPAs of public, private and foreign banks are rising at a fast rate over the period. Therefore, he suggested that the Indian banking industry embraces the sophisticated risk management practices.

Goswami (2003) has taken NPAs as one of the factors while deciding to put money in the bank. The declining NPAs of the Indian banks have prompted S&P to revise its outlook on the Indian banking system to 'stable' from 'negative'. Subba Rao (2003) has critically evaluated the existing NPAs realization system. The study found that the problem of NPAs should be handled with strict enforcement of prudential norms and requirements of transparency. Amitabh Joshi (2003) conducted a survey on analysis of NPAs of IFCI Ltd. The study found that profitability and viability of development of financial institutions are directly affected by quality and performance of advances.

Aggarwal (2004) has conducted his study on sectoral analysis, i.e., priority, non-priority and agricultural sector and proved that government to a large extent had met the gap that had arisen in public sector banks in respect of provisioning of capital.

Singh (2006) in his study evaluated the performance of banks against benchmark and ratio analysis was employed as the tools. The study observed that there was a decline in post-liberalization period. The study insisted that the ideal level benchmark is less than one percent; the segments curtail the growth rate of NPAs and followed certain measures to arrest the NPAs.

Jain Vibha (2007) examined the status of NPAs in scheduled commercial banks in India. The study found that there is a more acute problem of gross and net NPAs in Indian public sector banks including foreign banks during the period 1997-2003. The study concluded that the new private sector and foreign banks also failed to prevent this problem.

Singla (2008) studied the financial performance of banks in India in view of increased globalization and competition for a period of six years, i.e., 2001-2006. He concluded that the NPAs have shown a declining trend over a period.

Usha Arora, Bhavna Vashisht and Monica Bansal (2009) in their study analyzed the performance credit schemes of selected banks for a period of five years. They found that there is a positive relationship between loan disbursement and NPAs of the selected banks. Jatna, Ramu (2009) found in their study observed that the main cause of mounting of NPAs in public sector banks is malfunctioning of banks and the Narasimhan Committee also expressed the same opinion.

Meenakshi and Mahesh (2010) in their exploratory study on trends of NPAs at global level, observed that most of the countries that fall under the higher "NPA/Total Loan' ratio category is in the Asian region and the magnitude of NPAs in India is due to the poor recovery mechanism. Goyal, K. (2010) examined the NPAs in Indian public sector banks for the period 2002-09. He opined that there is an increased trend in gross and net NPAs in public sector banks during the period of study. Malyadri & Sirisha (2011) in their study examined the NPAs of the public sector and private sector banks of weaker sections for a period of seven years in India. The study revealed that the public-sector banks have accumulated more NPAs compared to the private sector banks. Kaur and Saddy (2011) conducted a comparative study on non-performing assets of public and private sector banks and they felt that the magnitude of NPAs is more in public sector and measures to control the threat of NPAs are very essential.

Hosmani & Hudagi (2011) conducted a study on "unearthing the epidemic of non-performing assets with reference to public sector banks in India", which shows that the magnitude and trend of public sector banks in India and found that there is a slight improvement in the asset quality reflected by decline in the diverse NPAs during the period of study.

Gurumurthy (2012) in his study, analyzed that in the liberalized economy, banking and financial sector get higher priority. The banks in India are facing the problems of NPAs and with that, the earning capacity and profitability of banks are highly affected. Kaur, A. (2012) in his attempt examined the income and expenditure pattern, profitability performance and the NPAs position of public sector banks in India during 2000-10. The growth rate, the coefficient of correlation, and median test have been used for the analysis. The study concluded that the PSBs have shown downward trends of NPAs with a success in recovery during the period of study. Raja Mohan (2012) described in their study that Indian banking industry plays a pivotal role in the socio-economic development of a country. During the past few years, banks gain sufficient strength to pose good performance through a consistent reduction in NPAs. Olekar & Talawar (2012) studied the NPAs with reference to Karnataka Central Cooperative Bank by calculating few NPAs related ratios and used trend projection method to predict next year advances for the bank. Their finding includes the considerable reduction of NPAs for the bank and offered some suggestions for recovery of the NPAs. Vohra and Dhamu (2012) pointed out in their study that the NPAs have a direct impact on profitability, liquidity, and equity of the banks. It is also found that the NPAs of Indian banks are relatively very high by global standards. Thus, they recommend restricting of lending operations only to secured advances with adequate collateral securities. They also list a few common reasons for an asset turning NPAs, considering economy, industry, borrower and lender sides separately.

Shalini (2013) in her study suggested that the credit management includes planning, organizing, controlling, directing and coordinating the credit sanctioning policies are very crucial to decrease the NPAs. Mohnail & Deshmukh (2013) have suggested in their study that the past reforms era changed the whole structure of banking industry in India. This study provides an empirical approach to the analysis of profitability indicators with a focal point on NPAs. Srinivas (2013) tried in his attempt on the identification of non-performing assets at commercial banks in India. This study highlighted the various general reasons, which convert advances/assets into the NPAs and given suitable suggestions to overcome the mentioned problem. Sikdar & Makkad (2013) in their study provided an insight into the role of NPAs in risk framework of selected Indian commercial banks and try to put forward the means of interpreting credit risk from existing levels of bank NPAs. The study concluded that the problem of NPAs can be tackled only with proper credit assessment and risk management mechanism.

Narula & Singla (2014) in their study evaluated the non-performing assets of Punjab National Bank and its impact on profitability and to establish the relationship between total advances, net profits, gross and net NPAs. This study concluded that there is a positive relationship between net profits and NPAs of the PNB. The problem of NPAs is because of the mismanagement on the side of the bank. Arora and Ostwal (2014) conducted a study on "unearthing the epidemic of non-performing assets: A study of public and private sector banks" explored the comparison of loan assets of public and private sector banks. The study concluded that private sector banks are improved due to the decline of the NPAs compared to public sector banks and effective recovery management of NPAs.

Need of the Study

After the review of various earlier attempts made so far, it can be said that many of the earlier studies focused their attention on the reasons and amount of NPAs in different banks over the period. Besides, those studies are conducted before 2014 during that period still the banks are with an aim of more of welfare objectives to serve the privileged communities in the society. Apart from it, due to the changed accounting practices in the recent years in the banking sector, NPAs has a direct impact on the profitability of the banks and the size of NPAs is being taken as a parameter to judge the performance and strength of the banks. Hence, the banks are supposed to control their NPAs at the lowest possible size and the studies of this type will be useful to suggest the measures be taken for the effective control of these NPAs.

Against this background, this paper focused its attention on to study the size of NPAs, and examine their trends in the Indian banking sector. Further, it also covers the aspects, such as the causes and consequences of NPAs in Indian banking sector.

More specifically, the following are the objectives of the present study.

Objectives of the Study

(i) To study the volume of NPAs and identify the causes and consequences in Indian banks.

(ii) To make a comparative analysis of the NPAs among public, private and foreign banks.

(iii) To suggest measures, minimize the NPAs in banks to improve their performance.

The Methodology of the Study

The present study is an empirical one to analyze the NPAs of Indian 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 aimed at to explore the trends of NPAs over a period of study. This is generally analyzed by computing through the following ratios.

Gross NPA Ratio = (Gross NPA / Gross Advances) * 100
Gross NPA Ratio = (Gross NPA / Total Assets) * 100
Net NPA Ratio = (Net NPA / Net Advances) * 100
Net NPA Ratio = (Net NPA / Total Assets) * 100

The ideal value of net NPA is zero and for practical purpose, a benchmark is taken as one per cent. Thus, the values of net NPA, which are less than one, may be considered as satisfactory and the values exceeding one per cent indicate a situation calling for improvement by reducing the NPAs. According to the RBI, the reduction of the NPAs should be treated as a national priority item to make the system stronger, resilient and geared to meet the challenges of globalization. Therefore, it is necessary that the Indian banks should start a debate soon on the problem of NPAs and their resolution.

Scope of the Study

The study is mainly focused its attention on the NPAs and their trends in the Indian banking sector. It covers the aspects, such as the volume and trends of NPAs, causes, and consequences of NPAs and their impact on the profitability performance of the selected banks. Hence, it excludes all other aspects like branch expansion, deposit mobilization, advances, etc., from the purview of the present study.

Period of the Study

The study covers a period of fifteen years, i.e., 2000-01 to 2014-15 during these years those loan accounts became non-performing assets are only included in the analysis. The study is based on this data from which conclusions are drawn and measures will be suggested to minimize the problem of NPAs in Indian banking sector.

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 as well as the banks.

Selection of Banks

The analysis on the study of trends in NPAs in the Indian banking sector is organized by grouping the banks into scheduled commercial banks, public sector banks, old private sector banks, new private sector banks and foreign banks. The idea behind this group of classification is that the public-sector banks are more social obligations compelled by the government based on its policies, viz., lending towards developmental schemes, priority sector lending, etc. With these obligations on the part of public sector banks may have more liberal in lending the credit, which leads to failure to realize these loan accounts and they will become NPAs. Whereas the other group of private and foreign banks based on the philosophy of these banks may have less social obligations and so that they may have fewer amounts of the NPAs.

Table-1: Gross and Net Non-Performing Assets of Scheduled Commercial Banks (Rs. in crores)

Years	Gross NPAs Amount	GNPAs as % of Gross Advances	GNPAs as % of Total Assets	Net NPAs Amount	NNPAs as % of Net Advances	NNPAs as % of Total Assets
2000- 01	63471	11.4	4.9	32461	6.2	2.5
2001- 02	70861	10.4	4.6	35554	5.5	2.3
2002- 03	68717	8.8	4.1	29692	4.0	1.8
2003- 04	64812	7.2	3.3	24396	2.8	1.2
2004- 05	59373	5.2	2.5	21754	2.0	0.9
2005- 06	51097	3.3	1.8	18543	1.2	0.7
2006- 07	50486	2.5	1.5	20101	1.0	0.6
2007- 08	56309	2.3	1.3	24730	1.0	0.6
2008- 09	68328	2.3	1.3	31564	1.1	0.6
2009- 10	84698	2.4	1.4	38723	1.1	0.6
2010- 11	97900	2.5	1.4	41700	1.1	0.6
2011- 12	142903	3.1	1.7	65205	1.3	0.8
2012- 13	194053	3.2	2.0	98694	1.7	1.0
2013- 14	263372	3.8	2.4	142656	2.1	1.3
2014- 15	323345	4.3	2.7	176093	2.4	1.5

Source: RBI. Handbook of Statistics on the Indian Economy, 2013-14

Table-1 shows the data on the GNPAs and NNPAs as % of Gross and Net Advances in Scheduled Commercial Banks from 2000-01 to 2014-15. It can be seen from the data that initially the GNPAs as % of Gross Advances ratio is 11.4% in 2000-01, it started to decline gently till 2006-07, it became constant for a period of 2 years i.e., 2007-08 & 2008-09 at 2.3%. From the subsequent year, the ratio increased and reached 4.3% in the year 2014-15. The NNPAs as % of Net Advances started to decline and reached 1.2% in 2005-06. In the next year, it started to decline even further to 1% and remained constant for 2 years i.e., 2006-07 and 2007-08. Again from 2008-09 it increased by 0.1% and remained constant at 1.1% for 3 years. However, from 2011-12 it started to increase and reached 2.4% by 2014-15. Further, it can also be viewed from the data in Table-1 that the GNPA ratio started to decline gradually to 1.5% in 2006-07. It further declined to 1.3% for the next 2 consecutive years. Similarly, the trend continued for the next 2 years also in which the ratio stood constantly at 1.4%. From 2011-12 it started to increase to 1.7% and further increased to 2.7% by the year 2014-15. The NNPAs as % of total assets declined from 2.5% in 2000-01 to 0.7% in 2005-06. From the next year, it further declined to 0.6% and remained constant for 5 consecutive years i.e., from 2006-07 to 2010-11. The ratio continued to increase subsequently and reached 1.5% in 204-15.

Table-2: Gross and Net NPAs of Public Sector Banks during 1992-93 to 2012-13 (Rs. in crores)

Years	Gross NPAs Amount	GNPAs as % of Gross Advances	GNPAs as % of Total Assets	Net NPAs Amount	NNPAs as % of Net Advances	NNPAs as % of Total Assets
2000-01	546.72	12.4	5.3	279.77	6.7	2.7
2001-02	564.73	11.1	4.9	279.58	5.8	2.4
2002-03	540.90	9.4	4.2	248.77	4.5	1.9
2003-04	515.37	7.8	3.5	193.35	3.1	1.3
2004-05	483.99	5.5	2.7	169.04	2.1	1.0
2005-06	413.58	3.6	2.1	145.66	1.3	0.7
2006-07	389.68	2.7	1.6	151.45	1.1	0.6
2007-08	404.52	2.2	1.3	178.36	1.0	0.6
2008-09	449.57	2.0	1.2	211.55	0.9	0.6
2009-10	599.26	2.2	1.3	293.75	1.1	0.7
2010-11	746.00	2.4	1.4	360.00	1.2	0.7
2011-12	1124.89	3.2	1.9	593.00	1.5	1.0
2012-13	1644.62	3.6	2.4	900.00	2.0	1.3

Source: RBI. Handbook of Statistics on the Indian Economy, 2005-06, 2013-14

Table-2 presents the data about the GNPAs and NNPAs of PSBs from 2000-01 to 2012-13. There is a gradual decrease in the GNPAs in 2001-02 to 2006-07 afterwards there is an increasing trend during the period of study. The same trend can be observed in the case of NNPAs. The GNPA ratio to GA has declined from 12.4% in 2000-01 to 20% in 2008-09 and afterwards it registered an increasing trend and the same was observed in the case of NNPAs also during the period of study. Initially, the NNPA ratio to NA was 6.7% in the subsequent years and it started to decline and reached its minimum of 0.9% in 2008-09, then it started to increase merely and finally reached 2.0% in 2012-2013

It can also be seen from the data in table-2 that the GNPAs and NNPAs as % of TA during the period of study from 2000-01 to 2012-13. The ratio of GNPA to TA is highest in 1992-93 at 5.3% and is started to collapse gradually till 2.7% in 2008-09, from the subsequent year it started to increase and reached 2.4% in 2012-2013. Similarly, NNPAs to TA % was highest in 1994-1995 at 4%. It further 1started to decrease till 0.6% in 2006-07 and it became constantly for a period of three consecutive years, i.e., from 2006-07 to 2008-09. In the next two years, it stood constant at 0.7% and by the end of 2012-13 it further increased and reached 1.3%.

From the foregoing analysis, it can be concluded that though the volume of GNPAs and NNPAs has been increasing in size during the period of study, the GNPAs as % of Gross Advances, Total assets and NNPAs as % of Net advances and Total assets has been steadily declined up to 2008-09 and afterwards it showed a marginally increased trend. It can be inferred that the PSBs are able to control the NPAs during the period between 2000-01 and 2008-09 because of financial reforms and after that, they are a slow start for increasing trend.

Table-3 Gross, Net NPAs and Total Advances of Old Private Sector Banks (Rs. crores)

Years	Gross NPAs	GNPAs as % of Gross Advances	GNPAs as % of Total Assets	Net NPAs	NNPAs as % of Net Advances	NNPAs as % of Total Assets	Advances	
							Gross	Net
2001-02	48.51	11.0	5.2	30.13	7.1	3.2	440.57	422.86
2002-03	45.50	8.9	4.3	25.98	5.2	2.5	513.29	494.36
2003-04	43.98	7.6	3.6	21.42	3.8	1.8	579.08	556.48

2004-05	42.00	6.0	3.1	18.59	2.7	1.4	704.12	677.42
2005-06	37.59	4.4	2.5	13.75	1.7	0.9	851.54	829.57
2006-07	29.69	3.1	1.8	8.91	1.0	0.6	948.72	928.87
2007-08	25.57	2.3	1.3	7.40	0.7	0.4	1134.04	1116.7
2008-09	30.72	2.4	1.3	11.59	0.9	0.5	1303.52	1285.04
2009-10	36.22	2.3	1.3	12.71	0.8	0.5	1563.57	1541.36
2010-11	36.00	1.9	1.2	9.00	0.5	0.3	1872.96	1846.47
2011-12	42.00	1.8	1.1	13.35	0.6	0.4	2329.18	2300.79
2012-13	52.10	1.9	1.2	20.06	0.7	0.5	2731.2	2699.37

Source: RBI. Handbook of Statistics on the Indian Economy, 2013-14

Table-3 presents the data about the GNPAs and NNPAs of old private sector banks from 2001-02 to 2012-13. There is a gradual decrease in the GNPAs in 2001-02 to 2007-08 afterwards there is an increasing trend during the period of study. The same trend can be observed in the case of NNPAs. The GNPA ratio to GA has declined from 11.0 percent in 2001-02 to 1.8 percent in 2011-12 and afterwards it registered an increasing trend and the same was observed in the case of NNPAs also during the period of study. Initially, the NNPAs ratio to Net Advances was 7.1 percent in the subsequent years and it started to decline and reached its minimum of 0.5 percent in 2010-11, then it started to increase merely and finally reached 0.7 percent in 2014-15. It can also be seen from the data in table-3 that the GNPAs and NNPAs as % of TA during the period of study from 2001-02 to 2014-15. The ratio of GNPA to TA is highest in 2001-02 at 5.2% and is started to collapse gradually till 1.1 percent in 2011-12, from the subsequent year it started to increase and reached 1.2 percent in 2012-2013. Similarly, NNPAs to TA % was highest in 2001-02 at 3.2 percent. It further started to decrease to 0.4 percent in 2007-08 and it registered fluctuating trend afterward.

From the foregoing analysis, it can be concluded that though the volume of GNPAs and NNPAs has been increasing in size during the period of study, the GNPAs as % of Gross Advances, Total assets and NNPAs as % of Net advances and Total assets has been steadily declined up to 2011-12 and afterwards it showed a marginally increased trend. It can be inferred that the old private sector banks are able to control the NPAs during the period between 2001-02 and 2011-12 because of financial reforms and after that, they are a slow start for increasing trend.

Table-4: Gross, Net NPAs and Total Advances of New Private Sector Banks (Rs. Billion)

Years	Gross NPAs	GNPAs as % of G. Advances	GNPAs as % of Total Assets	Net NPAs	NNPAs as % of Net Advances	NNPAs as % of Total Assets	Advances	
							Gross	Net
2001-02	68.11	8.9	3.9	36.63	4.9	2.1	769.01	741.87
2002-03	72.32	7.6	3.8	13.65	1.5	0.7	947.18	895.15
2003-04	59.83	5.0	2.4	19.86	1.7	0.8	1195.11	1151.06
2004-05	45.82	3.6	1.6	23.53	1.9	0.8	1274.2	1236.55
2005-06	40.52	1.7	1.0	17.96	0.8	0.4	2325.36	2300.05
2006-07	62.87	1.9	1.1	31.37	1.0	0.5	3252.73	3218.65
2007-08	104.4	2.5	1.4	49.07	1.2	0.7	4124.41	4067.33
2008-09	138.54	3.1	1.7	62.52	1.4	0.8	4547.13	4468.24
2009-10	140.17	2.9	1.6	52.34	1.1	0.6	4877.13	4783.58
2010-11	145	2.7	1.3	34	0.6	0.3	5450.14	6128.86
2011-12	145.68	2.2	1.1	30.65	0.4	0.2	6475.28	7363.23
2012-13	158.61	1.8	1.0	39	0.4	0.3	8860.23	8733.11
2013-14	245.42	1.8	1.1	88.62	0.7	0.4	13602.53	13429.35
2014-15	341.06	2.1	1.3	141.28	0.9	0.5	16073.39	15843.14

Source: RBI. Handbook of Statistics on the Indian Economy, 2014-15.

Table-4 presents the data about the GNPAs and NNPAs of New Private sector banks from 2001-02 to 2014-15. There is a gradual decrease in the GNPAs in 2001-02 to 2012-13 afterward there is a fluctuating trend was during the period of study. The same trend can be observed in the case of NNPAs. The GNPA ratio to GA has declined from 8.9% in 2001-02 to 1.8% in 2014-15. Initially, the NNPA ratio to NA was 4.9% in the subsequent years and it started to decline and reached its minimum of 0.4% in 2010-11, then it started to increase merely and finally reached 0.7% in 2014-15. It can also be seen from the data in table-4 that the GNPAs and NNPAs as % of TA during the period of study from 2001-02 to 2014-15. The ratio of GNPA to TA is highest in 2001-02 at 3.9% and is started to collapse gradually till 1.0% in 2012-13, from the subsequent year it started to increase and reached 1.0% in 2012-13. Similarly, NNPAs to TA % was highest in 2001-02 at 2.1 and it further started to decrease till 0.2% in 2011-12 and it registered and increasing trend.

From the foregoing analysis, it can be concluded that though the volume of GNPAs and NNPAs has been increasing in size during the period of study, the GNPAs as % of Gross Advances, Total assets and NNPAs as % of Net advances and Total assets has been steadily declined up to 2011-12 and afterwards it showed a marginally increased trend. It can be inferred that the new private sector banks are able to control the NPAs during the period between 2001-02 and 2011-12 because of financial reforms and after that, they are a slow start for increasing trend.

Table-5: Gross, Net NPAs and Total Advances of Foreign Banks (Rs. Billion)

Years	Gross NPAs	GNPAs as % of G. Advances	GNPAs as % of Total Assets	Net NPAs	NNPAs as % of Net Advances	NNPAs as % of Total Assets	Advances	
							Gross	Net
2001-02	27.26	5.4	2.4	9.20	1.9	0.8	506.31	487.05
2002-03	28.45	5.3	2.4	9.03	1.7	0.8	541.84	521.71
2003-04	28.94	4.6	2.1	9.33	1.5	0.7	626.32	605.06
2004-05	21.92	2.8	1.4	6.39	0.8	0.4	770.26	753.54
2005-06	19.28	1.9	1.0	8.08	0.8	0.4	989.65	975.62
2006-07	22.63	1.8	0.8	9.27	0.7	0.3	1278.72	1263.39
2007-08	28.59	1.8	0.8	12.47	0.8	0.3	1629.66	1611.33
2008-09	64.44	3.8	1.5	29.96	1.8	0.7	1697.16	1653.85
2009-10	71.33	4.3	1.6	29.77	1.8	0.7	1674.37	1632.6
2010-11	50.00	2.5	1.0	12.00	0.6	0.3	1993.21	1955.39
2011-12	62.97	2.8	1.1	14.12	0.6	0.2	2267.77	2298.49
2012-13	79.77	3.1	1.3	26.63	1.0	0.4	2604.05	2636.8
2013-14	115.65	3.9	1.5	31.61	1.1	0.4	2995.75	2911.42
2014-15	107.71	3.2	1.4	17.57	0.5	0.2	3366.09	3276.15

Source: RBI. Handbook of Statistics on the Indian Economy, 2014-15

Table-5 presents the data about the GNPAs and NNPAs of foreign banks from 2001-02 to 2014-15. There is a gradual decrease in the GNPAs in 2001-02 to 2007-08 afterwards there is a fluctuating trend. The same trend can be observed in the case of NNPAs. The GNPA ratio to GA has declined from 1.9 percent in 2001-02 to 0.7 percent in 2006-07. Initially the NNPA ratio to NA was 0.8% in the subsequent years and it started to decline up to 2007-08 and afterwards it registered a fluctuating trend. It can also be seen from the data in table-2 that the GNPAs and NNPAs as % of TA during the period of study from 2001-02 to 2014-15. The ratio of GNPA to TA is highest in 2001-02 at 2.4% and has started to decline gradually to 0.8% in 2007-08, from the subsequent year it started to increase and reached 1.5% in 2013-14 and fell to 1.4% in the year 2014-15. Similarly, NNPAs to TA % was highest in 2001-02 at 0.8% and it further started to decrease till 0.3% in 2007-08 and it registered a fluctuating trend afterward.

From the foregoing analysis, it can be concluded that though the volume of GNPAs and NNPAs has been increasing in size during the period of study, the GNPAs as % of Gross Advances, Total assets and NNPAs as % of Net advances and Total assets has been steadily declined up to 2010-11 and afterwards it showed a marginally increased trend. It can be inferred that the foreign banks are able to control the NPAs during the period between 2001-02 and 2011-12 because of financial reforms and after that, they are at slow start for increasing trend.

Trends in NPAs

It can be said from the foregoing analysis that the NPAs in Indian banking sector are of huge size despite having registered a declining trend during the period of study. It is a fact that the erosion of profits, provisioning and write-off, the requirement of additional capital are some major problems created by raising the non-performing assets in Indian banks. A huge amount of banks' resources is blocked due to the rising of such bad loans and thus it becomes unavailable for further lending. Now, in this section an attempt is made to examine the gross and net NPAs of the Indian banks for the last one and half decade period.

Discussion

A close look at the gross and net NPAs reported revealed the following points:

1. The amount of NPAs (both gross and net) of scheduled commercial and also public sector banks shows a mixed trend during the last 15-year period from 2001-15. It can be said that it is a clear indication of undesirable and disturbing aspect. In contrast to it, the percentage with respect to the advances shows a declining trend over the period of study, indicating a concerted effort by these banks to reduce the NPAs.

2. Likewise, the similar trend was observed in the case of public sector banks also. The volume of GNPAs and NNPAs has been increasing in size during the period of study, the

GNPAs as % of Gross Advances, Total assets and NNPAs as % of Net advances and Total assets has been steadily declined up to 2008-09 and afterward, it showed a marginally increased trend. It can be inferred that the PSBs are able to control the NPAs during the period between 2000-01 and 2008-09, because of financial reforms and after that, they are a slow start for increasing trend.

3. Though the same trend was observed in the case of private sector banks, there is no much seriousness of NPAs. It can be inferred that the old private sector banks are able to control the NPAs during the period between 2001-02 and 2011-12 because of financial reforms and after that, they are a slow start for increasing trend. The private sector banks particularly those, which are new have the NPAs often less than one percent, it shows their efficiency of NPAs management is more.

4. From the analysis on trends in NPAs in case of foreign banks, it can be concluded that though the volume of GNPAs and NNPAs has been increasing in size during the period of study, the GNPAs as % of Gross Advances, Total assets and NNPAs as % of Net advances and Total assets has been steadily declined up to 2010-11 and afterwards it showed a marginally increased trend. It can be said from this that the foreign banks are able to control the NPAs effectively when compared to private sector and public sector banks during the period of study

Causes and Consequences of NPAs

Now, an attempt is made to identify the causes and the consequences of NPAs. The opinions of the default borrowers and the views of the bank officials for non-recovery of the loans explained the facts of the cases. The following are the major causes expressed by the respondents both from the loaners as well as the bankers, which contribute to becoming NPAs. They are classified as (a) Internal, and (b) External factors.

(a) Internal Factors:

(i) Diversion of funds for expansion / modernization/setting-up of the new projects.

(ii) Business failure, inappropriate technology, product obsolescence, etc.

(iii) Time/cost overrun during the project introduction and also implementation stage.

(iv) Deficiencies on the part government, like delay in release and payments/subsidies.

(v) Willful defaults, siphoning of funds, misappropriation, fraud, disputes, etc.

(vi) Other causes, viz., poor credit appraisal, monitoring, delaying in settlements, etc.

(b) External Factors:

(i) Sluggish legal system, viz., long legal tangles, changes in laws, other legal matters.

(ii) Recession, input shortages, power shortages, price escalation, natural calamities, etc.

(iii) Delay in payment of overseas bills, adverse exchange rates, remittances restrictions, etc.

(iv) Government policies, like changes in customs and excise duties, pollution control, etc.

Effects of NPAs on Performance of the Banking Sector

- Continuous draining of profit.
- Negative impact on goodwill.
- Adverse growth of equity value.
- Restricted cash flow by the bank.
- Result in reduced interest income.
- Erode current profits through provisioning requirements.
- Erosion of capital base and reduction in their competitiveness.
- Decline in profit has its bearing on statutory variables.

NPAs and Role of the Government:

Some recent initiatives taken by the government to address the rising NPAs include:

(i) Appointment of Nodal officers in banks for recovery at their head offices/Zonal offices/for each Debts Recovery Tribunal (DRT). Thrust on the recovery of lost assets by banks and designating asset reconstruction companies (ARC) resolution agents of banks.

(ii) Directing the state-level bankers' committees to be proactive in resolving the issues.

(iii) Sanction of fresh loans based on information sharing amongst banks. Conducting sector/activity-wise analysis of NPAs.

(iv) Close watch on NPAs by picking up early warning signals and ensuring timely corrective steps by banks including early detection of the sign of distress, amendments in recovery laws, and strengthening of credit appraisal and post credit monitoring.

A strong banking sector is important for a flourishing economy, like India. The failure of the banking system may have an adverse effect on other sectors. Thus, there is a need to ensure that the banking system recognizes financial distress early, takes prompt steps to resolve it, and ensure fair recovery for lenders and investors so that banking sector start functioning without stress.

Procedural Initiatives for Realization of NPAs

The Government of India with the guidelines of the Reserve Bank of India has taken several steps for the realization of the NPAs. Therefore, the operating measures of the banks should make efforts to manage and reduce NPAs. In the developing nations, like us, though not eliminate and to have a zero NPAs, the bank managements should speed-up the recovery process. Table-6 presented the recovery process and channels used to collect the due amount from the loaners.

Table-6: NPAs of Schedule Commercial Banks recovered through various channels

Year	Recovery Channel	Lok Adalats	DRTs	SARFAESI Act	Total
2012-13	No. of cases referred (in lakhs)	8.41	0.13	1.91	10.45
	Amount involved	66	310	681	1057
	Amount recovered*	4	44	185	233
	#	6.1	14.1	27.1	21.9
2013-14	No. of cases referred	16.37	0.28	1.95	18.60
	Amount involved	232	553	953	1738
	Amount recovered*	14	53	253	320
	#	6.2	9.5	26.6	18.4
2014-15	No. of cases referred	91.31	1.71	12.41	105.43
	Amount involved	887	3789	4705	9381
	Amount recovered*	43	531	1152	1726
	#	4.8	14	24.5	18.4

* Refers to the amount recovered during the given year, which could be with reference to cases referred during the given year as well as during the earlier years.

(i) DRTs- Debt Recovery Tribunals.
(ii) SARFAESI Act -The Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002.
(iii) # indicates amount involved as percentage of recovered

From the data in table-6, the number of cases referred to the Lok Adalats year by year is shown an increasing trend during the period of study. Similarly, the number of cases referred by DRT also shows the same trend and further, the high trend is observed in the case of the settlements through the SARFAESI, because of its efficiency in recovering the NPAs of commercial banks.

Conclusions

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 the profitability of the banks as Indian banks are highly dependent on income from interest on funds lent. Till the March 2015, the contribution of non- priority sector NPAs were more than 50 percent over the years, obviously, this becomes the case with the priority sectors NPAs. Still, these both sectors have a significant amount of NPAs, which arrest the banks' overall performance. Similarly, non-priority sector NPAs are increasing both in percentage contribution to total NPAs as well as in absolute terms. Significantly, based on the insights of the study, it can be concluded that both the scheduled commercial banks and public sector have a significant effect due to the NPAs rather than the other private and foreign banks. The NPAs level of our banks is still high as compared to the foreign banks. Despite the contribution of these sectors in rising bad loans, it is also evident that it contributes to socio-economic development as well.

Therefore, the operating measures of banks and government should make efforts to manage and reduce NPAs. It is not at all possible to have zero NPAs. The bank management should speed-up the recovery process. The problem of recovery is not with small borrowers but with large borrowers and a strict policy should be followed for solving this problem. The government should also make more provisions for the faster settlement of pending cases and it should reduce the mandatory lending to priority sector as this is the major problem creating areas. So, the problem of NPAs needs lots of serious efforts, otherwise, NPAs will keep killing the profitability of banks, which is not good for the growing Indian economy at all.

Suggestions

The banks should take steps for better management of NPAs, it is useful to first assess the causative factors for NPAs so that the corrective actions can be taken accordingly. The following steps may help for a better NPAs management.

i. Developing a reliable and up to date information system on the banking operations.
ii. Employing a tested credit risk evaluation system, which can incorporate dynamic market conditions.

iii. Establishing a sound control and feedback mechanism system on banking operations.

iv. Creating an environment of trust and confidence in the management of banking system.

v. Monitoring the assets continuously and making serious efforts for the recovery of NPAs.

vi. Putting in place a rigorous screening process before granting credit to the customers.

vii. Public sector banks may emulate some of the effective steps taken by their private sector and foreign counterparts in this regard.

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