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Recovery Management in Indian Commercial Banks

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ABSTRACT *Banks have traditionally played the key role in the financial system by acting as financial intermediaries between ultimate servers and borrowers. With liberalization competition among commercial banks have increased to lure the customers. They are competing among themselves to attract more and more prospective applicants for loans; in their quest for attracting more and more customers for loans most of the banks have sanctioned loans without taking applicants capacity to repay loan its consideration. The result is forming of NPAs. It is the most worrying aspect as banks are expected to follow prudential norms quoted in Basel I, II and III norms. Present study has made an attempt to analyse the level of NPAs in Indian commercial Banks with available data using simple statistical tools. The study has found all sectors' banks on an average have maintained above 96 percent standard assets. Private sector banks have maintained standardness above 97 percent. However, in foreign Banks, Doubtful assets have increased from Rs. 698 crores (0.7%) in 2006 to Rs. 2113 crores (1.1%).*

KEYWORDS : Recovery Management, NPAs, Standard Assets, Doubtful Assets.

1. Introduction:-

Banks have traditionally played the key role in the financial system by acting as financial intermediaries between ultimate servers and borrowers. As asset transformers then have accepted deposits with one of the characteristics and credited asset with a different set in particular, they have engaged in maturity transformation with debt contracts on both sides of the balance sheet. Deposits create assets for a bank on one hand and credit on other hand. Similarly, loans create asset in the long run if loans are recovered fully without default. Otherwise a loss in its total assets to the tune of loan advanced. Despite banks primary assessment of primary and collateral security there are loan losses. These financial institutions are competing among themselves to attract more and more prospective applicants for loans; in their quest for attracting more and more customers for loans most of the banks have sanctioned loans without taking applicants capacity to repay loan its consideration. The result is forming of NPAs and banks have to initiate legal process under securitization act. It is found that the loans advanced become NPAs because of willful default and non Payments, accidents of Vehicles (Rai 2012, Prasad & Veena, 2011).

Commercial Banks refer to both scheduled and non-scheduled commercial banks which are regulated under Banking Regulation Act, 1949. Important of commercial banks are public sector banks, private sector banks and foreign Banks. Recovery Management is the process of planning, testing, and implementing the recovery procedures and standards required to restore service in the event of a component failure; either by returning the component to normal operation, or taking alternative actions to restore service. Recovery Management is the acknowledgement that failures will occur regardless of how well the system is designed. Recovery is a key to the stability of the banking sector there should be no hesitation in stating that Indian banks have done a remarkable job in containment of Non-Performing Assets (NPA) considering the overall difficult environment. Recovery management holds the key to future health and competitiveness of the Indian banks (Singh, 2012).

Objectives of Recovery management are Reduction in NPAs, Growth of Deposits and Credits. These three objectives although have cause and effect on each other, Reducing NPAs (Non- Performing Assets) is a difficult one banks to achieve as there will be somewhere defaulters of credit. Deposits and Advances are two major important functions of a bank. Deposits have grown over the years considering from the period of establishment of banks. However, credits have grown following Nationalisation of Commercial banks twice.14 Banks were nationalized in 1969 and 6 banks were nationalized in 1980. With liberalization New Private sector banks and Foreign Banks have also started operating. Notwithstanding, limiting banks' NPAs is a daunting task.

Non- Performing Assets or a problem loan can be defined as *"A loan where the lender has some doubts or is experiencing difficulties in obtaining repayments &, irrespective of the time frame, the outcome could be a loss of capital"*. In other words, loans those are in jeopardy or default. An account is declared as NPA based on the recovery of installments and interest on loans and advances and other aspects as per RBI norms. The updated norms to declare the account as NPA are as follows as per RBI guidelines: An asset, including a leased asset, becomes nonperforming when it ceases to generate income for the bank.

In order to reflect a bank's actual financial health in its balance sheet and as per the recommendations made by the Committee on Financial System (Chairman Shri M. Narasimham), the Reserve Bank has introduced, in a phased manner, prudential norms for income recognition, asset classification and provisioning for the advances portfolio of the banks. Broadly, the policy of income recognition should be objective and based on record of recovery rather than on any subjective considerations. To strengthen further, the recovery of dues by banks and financial institutions Government of India promulgated The Recovery of Debts Due to Banks and Financial Institutions Act, 1993 and The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002. In this study, an attempt is made to analyse the level of NPAs bank group wise. Present study is purely based on Secondary data collected form Reserve Bank of India (RBI). The data is collected on loans and advances made, Standard Assets, Sub-standard Assets, Doubtful Assets, and Gross NPAs by bank ownership wise. The statistical analysis is carried out with the help of tables and graphs.

2. Impact of NPAs:-

- NPAs do not generate income
- They require provisions.
- Borrowing cost of resources locked in NPAs
- Enhances administrative, legal & recovery costs.
- Reduces profitability substantially.
- Affect the morale of the employees & decision making for fresh loan suffers.

3. Classification of Assets as Non-Performing

Banks should classify their assets into the following broad groups, viz.

(i) Standard Assets: Standard Asset is one which does not disclose any problems and which does not carry more than normal risk attached to the business.

(ii) Sub-standard Assets: With effect from March 31, 2005 an asset would be classified as sub-standard if it remained NPA for a period less than or equal to 12 months.

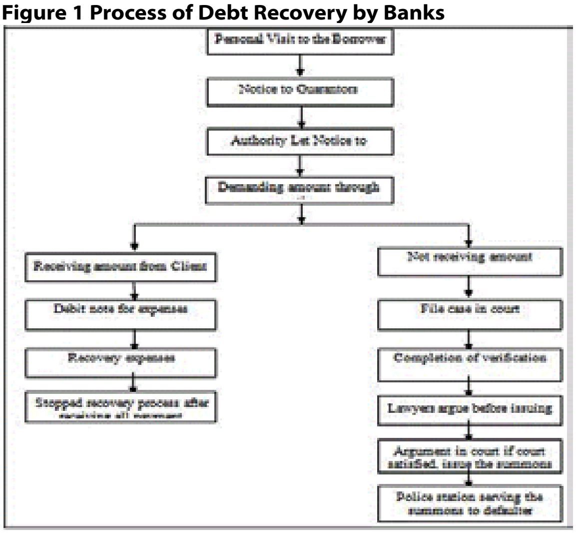
(iii) Doubtful Assets: With effect from March 31, 2005, an asset is required to be classified as doubtful, if it has remained NPA for more than 12 months. A loan classified as doubtful has all the weaknesses inherent as that classified as sub-standard, with the added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently known facts, conditions and values, highly questionable and improbable.

(iv) Loss Assets: A loss asset is one where loss has been identified by the bank or internal or external auditors or by the Co-operation Department or by the Reserve Bank of India inspection but the amount has not been written off, wholly or partly. In other words, such an asset is considered un-collectible and of such little value that its continuance as a bankable asset is not warranted although there may be some salvage or recovery value.

RBI's mechanism for recovery of NPAs:-
- Debt Recovery Tribunals
- Recovery through Private Agencies
- Lok Adalats
- Recovery Camps
- SERFAESI ACT- 2002
- Regional Level Review Committee (RLRC) and
- Compromise Settlement

Process of Debt Recovery by Banks:
Every bank in order to recover the dues has a recovery process set for them. The usual legal process of recovery which is adopted by the bank is as shown in figure 1.

Figure 1 Process of Debt Recovery by Banks



4. Results and Discussion
Table 1 shows Banks' Sector Wise composition of NPAs in priority sector, non-priority sector and public sector. NPAs accrued by advancing loans to priority sector are very significant in Public Sector Banks or Nationalized Banks and State Bank of India and its Associates. Over the years from 2002 to 2011, they have increased significantly from Rs. 16173 crores to Rs. 25678 crores in 2011 for nationalized Banks. Similarly there is increasing NPAs in SBI group from Rs. 8977 crores in 2002 to Rs. 15567 crores in 2011.

Table 1 NPAs in Indian Commercial Banks

TABLE 7.2 : COMPOSITION OF NPAs OF PUBLIC SECTOR BANKS - 2002 TO 2011

(Amount in Rs. crore)

Bank Groups / Years	As on March 31						
	Priority Sector		Non-Priority Sector		Public Sector		Total
		Per cent share		Per cent share		Per cent share	Amount
	(1)	(2)	(3)	(4)	(5)	(6)	(7)
A. Nationalised Banks							
2002	16173	45.78	18742	53.05	413	1.17	35328
2003	16886	47.10	18402	51.33	561	1.57	35849
2004	16705	47.74	17895	51.14	390	1.12	34990
2005	16381	49.81	16225	49.33	283	0.86	32888
2006	15124	53.66	12845	45.58	216	0.76	28185
2007	15779	60.58	9965	38.26	302	1.16	26046
2008	16385	66.80	7941	32.38	202	0.82	24528
2009	15871	60.65	10001	38.22	297	1.13	26169
2010	19908	56.13	15283	43.09	280	0.79	35470
2011	25678	59.84	16957	39.52	273	0.64	42907
B. State Bank of India & its Associates							
2002	8977	47.01	9628	50.42	490	2.56	19095
2003	8053	47.49	8379	49.41	526	3.10	16958
2004	7136	47.07	7803	51.48	220	1.45	15159
2005	7017	47.39	7624	51.48	168	1.13	14808
2006	7250	54.95	5819	44.10	125	0.95	13193
2007	7175	57.15	5193	41.36	188	1.50	12556
2008	8902	58.49	6222	40.88	97	0.63	15220
2009	8447	47.26	9250	51.75	177	0.99	17874
2010	10940	50.11	10646	48.77	244	1.12	21831
2011	15567	55.32	12567	44.66	6	0.02	28140
Public Sector Banks (A+B)							
2002	25150	46.21	28371	52.13	902	1.66	54423
2003	24938	47.23	26781	50.72	1087	2.06	52807
2004	23840	47.54	25698	51.24	610	1.22	50148
2005	23397	49.05	23849	50.00	450	0.94	47696
2006	22374	54.07	18664	45.11	341	0.82	41378
2007	22954	59.46	15158	39.27	490	1.27	38602
2008	25287	63.62	14163	35.63	299	0.75	39749
2009	24318	55.21	19251	43.71	474	1.08	44042
2010	30848	53.83	25929	45.25	524	0.91	57301
2011	41245	58.05	29524	41.56	278	0.39	71047

Source : Off-site returns (domestic) - Latest updated database, Division of banking Supervision, RBI.

On the other hand Non- Priority Sector NPAs have reduced in all bank sectors. In Nationalized Banks reduced from 53.05 percent (2002) to 39.52 percent (2011). There is marginal decline in non priority sector NPAs in SBI and its Associates from 50.42 per cent (2002) to 44.66 (2011). Notwithstanding, NPAs accrued due to advances to Public sector activities is very marginal and not significant and has declined over the years.

Figures 2, 3 and 4, reveals the level of standard assets, sub standard assets and doubtful assets of by ownership sector wise- public sector banks, private sector banks and foreign banks. Standard assets are those which have no risks of defaults. Sub standard assets are those which remain as NPAs for equal or less than 12 months. Doubtful assets are NPAs which remain as so for more than 12 months.

Figure 2.2 Loan Assets of Public Sector Banks

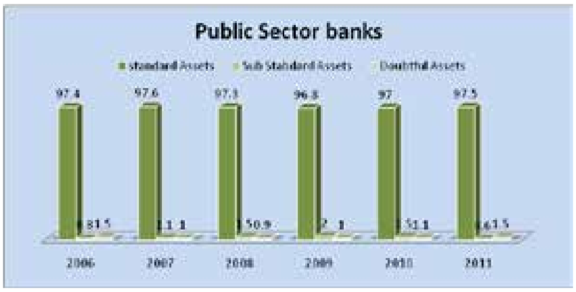


Figure 2.3 Loan Assets of Private Sector Banks

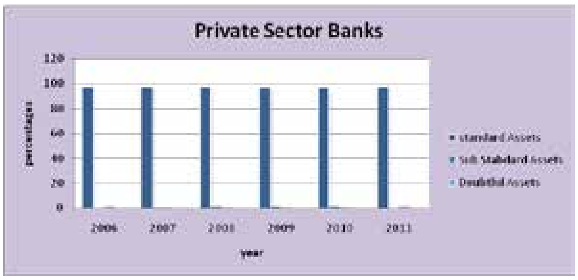


Figure 2.4 Loan Assets of Foreign Banks

All sectors' banks on an average have maintained above 96 percent standard assets. Private sector banks have maintained standardness above 97 percent. Sub standard assets are around 1 percent in public and private sector banks. But in foreign sector banks, they have increased to 3.5 per cent in 2009 and 2.9 per cent in 2010. In terms of doubtful assets, public sector banks have Rs. 24804 crore (2006) which has increased to Rs. 31919 crores (2011). Private sector Banks have high doubtful assets in 2011 (Rs. 10735 crores). In foreign Banks, doubtful Assets are increasing both in relative and absolute terms. Doubtful assets have increased from Rs. 698 crores (0.7%) in 2006 to Rs. 2113 crores (1.1%).

5. Conclusion and Summary:

This study has made an attempt to understand the theoretical background and the course of policy developments made over the years to reduce increasing NPAs in public sector banks, Private Banks and Foreign banks. Basel II and Basel III norms have already placed prudential norms for all banks to cope up. Therefore, all the banks needless to say have to reduce mounting NPAs and strictly abide to level of NPAs.

A strong banking sector is important for flourishing economy. Lending by banks has positive effect on economic growth and development as it creates physical asset and employment. The multiplier impact is evident as it generates assets, income and employment. However, defaulting increases banks' losses and decreases standard assets. It has impact on banks profitability and making sometimes banks to fail if there are large defaulters as it happened in US economy during 2008-09 Recession. Banks failure will does affect the whole economy and economic activities. Considering Indian Banks, although they are at safer zones of NPAs, still in absolute terms NPAs are huge. Therefore it is the responsibility of Banks, RBI and Individual bank customers to utilize the loans in better and protect the sanctity of bank with no defaults or minimizing chances of occurrence of defaults by making proper use of advances taken and timely repayment of loans so as to make economy more efficient and productive.

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