



Non-Performing Assets in Public Sector Banks: An Investigation

KEYWORDS

Public Sector Banks, Non Performing Assets, Ratio Analysis, Assets quality.

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ABSTRACT

Indian banking sector has made a significant progress after nationalization especially in three aspects: Branch expansion, deposit mobilization and loan maximization. In the changing scenario of the operations of the Public Sector Banks (PSBs) Non-Performing Assets (NPAs) have been the most vexing problem faced by PSBs. NPAs are treated as an obstacles in the development of the banking sector. This paper analyzed the NPAs level in PSBs in India during 1992-93 to 2010-11. Secondary data has been used for the study. Ratio Analysis technique has been used for the data analysis. This study reveals that Assets quality of Public sector banks in India has been improving over the past five years reflected in the declining NPA to advances.

Banks operating in India can be broadly classified in to two categories viz., commercial banks and co-operative banks. Within the category of commercial banks, there are two types of banks namely scheduled commercial banks, there are two types of banks namely scheduled commercial banks and non-scheduled commercial banks. Depending upon the pattern of ownership, commercial banks can be classified into three groups. They are: (i) Public Sector Banks which include the State Bank of India, its associate Banks and Nationalized Banks and other Public Sector Banks (ii) Private Sector Banks consisting Indian Private Sector Banks and Foreign Banks operating in India and (iii) Other comprising Regional Rural banks and Local Area Banks. Of these, Public Sector Banks (PSBs) have a countrywide network of branches and account for over seventy percent of total banking business. They have strong presence in rural and semi-urban areas.

In tune with the international practices and as per the recommendations made by the Narshimam's Committee on the financial systems, the Reserve Bank of India has introduced norms for asset classification and provisioning for advances of the banks so as to move towards greater consistency and transparency in the published annual report and accounts. As per these guidelines, the classification of assets of banks is done on the basis of objective criteria, which ensures a uniform and consistent application of the norms. Moreover, the provisioning is to be made, according to the classification of assets based on the period for which, the assets has remained non-performing, the availability of security and the realizable value thereof. (Bardia, 2004)

Assets are classified as Non-Performing Assets (NPAs) if due in the form of principal and interest are not paid by the borrower for a period of 90 days. It's a known fact that the banks and financial institutions in India face the problem of swelling NPAs and the issue is becoming more and more unmanageable. In order to bring the situation under control, some steps have been taken by Reserve Bank of India and Government of India. The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 was passed by parliament, which is an important step towards elimination or reduction of NPAs. PSBs have a countrywide network of branches and account for over seventy percent of total banking business in India. Therefore, it is become important to study NPAs level in PSBs in India. This paper is an attempt to study Non-Performing Assets of PSBs in India.

The rest of the paper has been divided into four sections. Section-II provides a brief review of studies related to NPAs. Section-III describes the methodology adopted in this re-

search. Section-IV describes analysis and results of NPAs of Public Sector Banks in India. Section-V describes the conclusion of the paper.

Section II Literature Review

A historical change in the field of Indian financial system is the financial sector reform as a result of economic liberalization policy of the Government of India, which was presented by Union Budget of 1991-92 (July 24, 1991). The Government of India set up a high level committee headed by Narasimham, former governor of Reserve Bank of India as chairman to examine all aspects relating to the structure, organization, functions and procedures of the financial system. The committee submitted its final report in November 1991, which contains a number of suggestions/recommendations for toning up operational efficiency of the banking system. The term "Non-Performing Assets has come into prominence as a result of the recommendations of the Narasimham Committee. (Upadhyaya, 2005)

RBI has constituted various committees- Narasimham Committee (1991, 1998) and Verma Committee (1999) for improving the financial health of banks. In line with the recommendations of both committees, a number of measures have been initiated to resolve the problem of NPAs.

In the India context, several studies have been conducted on aspects of NPAs of PSBs. Notable among them Upadhyaya (2005), Ananda (2005), Karunagaran (2005) Reddy; Babu; Mallikarjuna and Viswanath (2006), Jain (2007). They observed that in terms of absolute NPAs of PSBs increased after 1993 but decreased in terms of Gross NPAs to Gross Advances. They also observed that priority sector advances main contributors in NPAs of PSBs.

Section-III Methodology

In with the international practices and as per the recommendations of Narasimham Committee, the Reserve Bank of India for the first time issued certain guidelines for treating a credit policy as a non-performing assets to be allowed from the accounting year 1992-93. Therefore the period of this study confined to 1992-93 to 2010-2011. Secondary data has been used for the study. Ratio Analysis technique has been used for the analysis of Non-Performing Assets.

Section-IV Analysis and Results

The Assets quality of banking sector can be measured on the

basis of Non-Performing Assets. The key NPAs ratios of PSBs were analyzed and it is presented in Table-1.

Gross NPAs

Table 1 show that Gross NPAs of PSBs was Rs. 39253 crores in 1992-93 which increased to Rs. 56493 crores in 2001-02. It

decreased to Rs. 38968 crores in 2006-07 and it increased to Rs. 74614 crores in 2010-11. In terms of absolute quantum, the NPAs for PSBs increased by Rs. 17240 (43.92%) crores during 1993-2002 and it increased by Rs. 18121(32.08%) crores during 2002-2011.

Table-1: Gross and Net NPAs of Public Sector Banks

| Year | Gross NPAs | | | Net NPAs | | |
|---------|-----------------------|----------------------------------|--------------------------------|---------------------|------------------------------|------------------------------|
| | Gross NPAs (Rs in Cr) | Gross NPAs to Gross Advances (%) | Gross NPAs to Total Assets (%) | Net NPAs (Rs in Cr) | Net NPAs to Net Advances (%) | Net NPAs to Total Assets (%) |
| 1992-93 | 39253 | 23.20 | 11.80 | NA | NA | NA |
| 1993-94 | 41041 | 24.80 | 10.80 | 19691 | 14.50 | 5.20 |
| 1994-95 | 38385 | 19.50 | 8.70 | 17567 | 10.70 | 4.00 |
| 1995-96 | 41660 | 18.00 | 8.20 | 18298 | 8.90 | 3.60 |
| 1996-97 | 43577 | 17.80 | 7.80 | 20285 | 9.20 | 3.60 |
| 1997-98 | 45653 | 16.00 | 7.00 | 21232 | 8.20 | 3.30 |
| 1998-99 | 51710 | 15.80 | 6.70 | 24211 | 8.10 | 3.10 |
| 1999-00 | 53033 | 14.30 | 6.00 | 26187 | 7.40 | 2.90 |
| 2000-01 | 54672 | 12.40 | 5.30 | 27977 | 6.70 | 2.70 |
| 2001-02 | 56473 | 11.00 | 4.90 | 27958 | 5.80 | 2.40 |
| 2002-03 | 54090 | 9.40 | 4.20 | 24869 | 4.50 | 1.90 |
| 2003-04 | 51538 | 7.80 | 3.50 | 18860 | 3.00 | 1.28 |
| 2004-05 | 48399 | 5.50 | 2.73 | 16904 | 2.00 | 0.95 |
| 2005-06 | 41358 | 3.60 | 2.05 | 14566 | 1.30 | 0.72 |
| 2006-07 | 38968 | 2.70 | 1.60 | 15145 | 1.10 | 0.62 |
| 2007-08 | 40595 | 1.97 | 1.34 | 17386 | 1.00 | 0.59 |
| 2008-09 | 44957 | 1.97 | 1.30 | 21155 | 0.94 | 0.60 |
| 2009-10 | 59926 | 2.19 | 1.35 | 29375 | 1.09 | 0.66 |
| 2010-11 | 74614 | 2.23 | 1.41 | 36071 | 1.09 | 0.68 |

NA: Not Available

Note: Figures may not tally exactly as they derived from various sources.

Sources: (1) RBI, "Report on Trend and Progress of Banking in India", various issues. (2) Reddy; Babu; Mallikarjuna and Viswanath (2006), "Non-Performing Assets in Public Sector Banks: An Investigation", NPAs in the banking system Trends and Challenges" edited by G Gopala Krishna Murthy, 1st edition, The Icfai University Press, Hyderabad. p.5. (3) Jain, Vibha (2007), "Non-Performing Assets in Commercial Banks", Regal publications, New Delhi, p. 118.

Gross NPAs to Gross Advances Ratio

Table 1 show that in the year 1992-93, Gross NPAs to Gross Advances ratio was 23.20% which declined to 11% at the end of March 2002. This shows a significant decrease of 12.2% (23.2% to 11%) for the same period. This ratio declined from 11% as at the end of March 2002 to 2.23% as at the end of March 2011. This shows a significant decrease of 8.77% (11% to 2.23%) for the same period.

Gross NPAs to Total Assets

Table 1 show that in the year 1992-93, Gross NPAs to Total Assets ratio was 11.8% which declined to 4.9% at the end of March 2002. This shows a significant decrease of 6.9% (11.8% to 4.9%) for the same period. This ratio declined from 4.9% as at the end of March 2002 to 1.41% as at the end

of March 2011. This shows a significant decrease of 3.49% (4.9% to 1.41%) for the same period.

Net NPAs

Table 1 show that Net NPAs of PSBs was Rs. 19691 crores in 1993-94 which increased to Rs. 27958 crores in 2001-02. It decreased to Rs. 15145 crores in 2006-07 and it increased to Rs. 36071 crores in 2010-11. In terms of absolute quantum, the NPAs for PSBs increased by Rs. 8267 (41.98%) crores during 1994-2002 and it increased by Rs. 8113 (29.02%) crores during 2002-2011.

Net NPAs to Net Advances Ratio

Table 1 show that in the year 1993-94, Net NPAs to Net Advances ratio was 14.5% which declined to 5.8% at the end of March 2002. This shows a significant decrease of 8.7% (14.5% to 5.8%) for the same period. This ratio declined from 5.8% as at the end of March 2002 to 1.09% as at the end of March 2011. This shows a significant decrease of 4.71% (5.8% to 1.09%) for the same period.

Net NPAs to Total Assets

Table 1 show that in the year 1993-94, Net NPAs to Total Assets ratio was 5.2% which declined to 2.4% at the end of March 2002. This shows a significant decrease of 2.8% (5.2% to 2.4%) for the same period. This ratio declined from 2.4% as at the end of March 2002 to 0.68% as at the end of March 2011. This shows a significant decrease of 1.72% (2.4% to 0.68%) for the same period.

Table-2: Classification of Loan Assets of Public Sector Banks (As at end-March)

(Amount in Rs. crore)

| Year | Standard Assets | | Sub Standard Assets | | Doubtful Assets | | Loss Assets | | Total Advances Amount |
|------|-----------------|----------|---------------------|----------|-----------------|----------|-------------|----------|--------------------------|
| | Amount | Percent* | Amount | Percent* | Amount | Percent* | Amount | Percent* | |
| 1997 | 200637 | 82.2 | 12472 | 5.1 | 26015 | 10.7 | 5090 | 2.1 | 244214 |
| 1998 | 239318 | 84.0 | 14463 | 5.1 | 25819 | 9.1 | 5371 | 1.9 | 284971 |
| 1999 | 273618 | 84.1 | 16033 | 4.9 | 29252 | 9.0 | 6425 | 2.0 | 325328 |
| 2000 | 326783 | 86.0 | 16361 | 4.3 | 30535 | 8.0 | 6398 | 1.7 | 380077 |
| 2001 | 387360 | 87.6 | 14745 | 3.3 | 33485 | 7.6 | 6544 | 1.5 | 442134 |

| | | | | | | | | | |
|------|---------|------|-------|-----|-------|-----|------|-----|---------|
| 2002 | 452862 | 88.9 | 15788 | 3.1 | 33658 | 6.6 | 7061 | 1.4 | 509369 |
| 2003 | 523724 | 90.6 | 14909 | 2.6 | 32340 | 5.6 | 6840 | 1.2 | 577813 |
| 2004 | 610435 | 92.2 | 16909 | 2.5 | 28756 | 4.4 | 5876 | 0.9 | 661975 |
| 2005 | 830029 | 94.6 | 11068 | 1.3 | 30779 | 3.5 | 5929 | 0.7 | 877805 |
| 2006 | 1092607 | 96.2 | 11453 | 1.0 | 25028 | 2.2 | 5636 | 0.5 | 1134724 |
| 2007 | 1425519 | 97.3 | 14275 | 1.0 | 19873 | 1.4 | 4826 | 0.3 | 1464493 |
| 2008 | 1778476 | 97.8 | 17290 | 1.0 | 19291 | 1.1 | 4018 | 0.2 | 1819075 |
| 2009 | 2237556 | 98.0 | 20603 | 0.9 | 21019 | 0.9 | 4296 | 0.2 | 2283474 |
| 2010 | 2673534 | 97.8 | 28791 | 1.1 | 25383 | 0.9 | 5750 | 0.2 | 2733458 |
| 2011 | 3272914 | 97.8 | 34973 | 1.0 | 33180 | 1.0 | 6463 | 0.2 | 3347530 |

* As percent to Gross Advances

Note:(1) Constituent items may not add up to the total due to rounding off (2) Figures may not tally exactly as they derived from various sources.

Sources: (1) RBI, "Report on Trend and Progress of Banking in India", various issues. (2) Reddy; Babu; Mallikarjuna and Viswanath (2006), "Non-Performing Assets in Public Sector Banks: An Investigation", NPAs in the banking system Trends and Challenges" edited by G Gopala Krishna Murthy, 1st edition, The Icfai University Press, Hyderabad. p.5. (3) Jain, Vibha (2007), "Non-Performing Assets in Commercial Banks", Regal publications, New Delhi, p. 118.

Analysis of Assets Quality

Breakup of the loan assets of PSBs during 1997-2011 based on the four-tier category prescribed by the RBI is given in Table 2. The four-tier categorization of loan assets based on the asset to generate income reveals the health of the banks, as loan assets are the only source of income for the banks. The quality of loan portfolio of the PSBs has improved quite impressively over the period 1997-2011. The share of standard assets in total advances of PSBs increased from 82.2% in 1996-97 to 97.8% in 2010-11. The NPAs of 17.8% in 1996-97 consist of sub standard assets (5.1%) doubtful (10.7%) and loss assets (2.1%) while in 2010-11 the share of sub standard, doubtful and loss assets decreased to 1%, 1% and 0.2% respectively. It can be seen that the share of standard assets was increasing every year, both in percentage and absolute terms. As a consequence the percentage of sub standard, doubtful and loss assets to total advances were reducing during the study period. However, though sub standard, doubtful and loss assets were increasing in absolute terms since last four years.

Recovery of Gross NPAs is another important component of asset quality management in the banking sector. SARFAESI Act (The Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002); Debt Recovery Tribunals and Lok Adalats are different channels available for the banking sector to recover their NPAs. The RBI in its latest report "Trend and Progress of Banking in India 2010-11" observe that during the year 2010-11, PSBs recovered 62% of the outstanding Gross NPAs (as at end March 2010) through various channels.

Sectoral Analysis of NPAs in PSBs

Bank credit has been classified into two categories, viz; priority sector and non-priority sector. Priority sector represents the advances to those areas which are identified as the thrust area by the government. Lending to this category of borrowers is warranted. The directed credit is aimed at ensuring funds to the most crucial segments which may not find favor with the banks otherwise. NPAs are classified on the basis of loan category, e.g., priority sector NPAs, non-priority sector NPAs and public sector NPAs.

Table-3: Non-Performing Assets of Public Sector Banks-

Sector-wise (As at end March) (Amount in Rs. crore)

| Year | Priority Sector NPAs | | Non-priority Sector NPAs | | Public Sector NPAs | | Total Gross NPAs |
|------|----------------------|----------|--------------------------|----------|--------------------|----------|------------------|
| | Amount | Percent* | Amount | Percent* | Amount | Percent* | Amount |
| 1995 | 19208 | 50.0 | 17861 | 46.5 | 1316 | 3.4 | 38385 |
| 1996 | 19106 | 48.3 | 19067 | 48.2 | 1411 | 3.6 | 39584 |
| 1997 | 20774 | 47.7 | 21341 | 49.0 | 1461 | 3.4 | 43577 |
| 1998 | 21184 | 46.4 | 23107 | 50.6 | 1362 | 3.0 | 45653 |
| 1999 | 22606 | 43.7 | 27608 | 53.4 | 1496 | 2.9 | 51710 |
| 2000 | 23715 | 44.5 | 28524 | 53.5 | 1055 | 2.0 | 53294 |
| 2001 | 24159 | 45.4 | 27307 | 51.4 | 1711 | 3.2 | 53174 |
| 2002 | 25150 | 46.2 | 28405 | 52.2 | 903 | 1.7 | 54458 |
| 2003 | 24939 | 47.2 | 26781 | 50.7 | 1087 | 2.1 | 52807 |
| 2004 | 23840 | 47.5 | 25698 | 51.2 | 610 | 1.2 | 50148 |
| 2005 | 23397 | 49.1 | 23849 | 50.0 | 450 | 0.9 | 47696 |
| 2006 | 22374 | 54.1 | 18664 | 45.1 | 340 | 0.8 | 41378 |
| 2007 | 22954 | 59.5 | 15158 | 39.3 | 490 | 1.3 | 38602 |
| 2008 | 25287 | 63.6 | 14163 | 35.6 | 299 | 0.8 | 39749 |
| 2009 | 24318 | 55.2 | 19251 | 43.7 | 474 | 1.1 | 44042 |
| 2010 | 30848 | 53.8 | 25929 | 45.3 | 524 | 0.9 | 57301 |
| 2011 | 41245 | 58.1 | 29525 | 41.6 | 278 | 0.4 | 71048 |

* As percent to Gross NPAs

Note:(1) Constituent items may not add up to the total due to rounding off (2) Figures may not tally exactly as they derived from various sources.

Sources: (1) RBI, "Report on Trend and Progress of Banking in India", various issues. (2) Reddy; Babu; Mallikarjuna and Viswanath (2006), "Non-Performing Assets in Public Sector Banks: An Investigation", NPAs in the banking system Trends and Challenges" edited by G Gopala Krishna Murthy, 1st edition, The Icfai University Press, Hyderabad. p.5.(3) Jain, Vibha (2007), "Non-Performing Assets in Commercial Banks", Regal publications, New Delhi, p. 118.

Table-3 gives the break up of NPAs in priority and non-priority sector lending. For every 100 rupees of NPAs of PSBs as on March 2011, the distribution is: priority sector (58.1%), non-priority sector (41.6%) and public sector (0.4%).

The share of priority sector advances in gross NPAs of PSBs decreased from 50% (Rs. 19208 crore) in March 1995 to 44.5% (Rs. 23715 crore) in March 2000 but again increased to 58.1% (Rs.41245 crore) in 2011.

The share of non-priority sector advances in gross NPAs of

PSBs increased from 46.5% (Rs. 17861 crore) in March 1995 to 53.5% (Rs. 28524 crore) in March 2000 but again decreased to 41.6% (Rs.29525 crore) in 2011.

The share of public sector advances in gross NPAs of PSBs decreased from 3.4% (Rs. 1316 crore) in March 1995 to 2.0% (Rs. 1055 crore) in March 2000 and it again decreased to 0.4% (Rs.278 crore) in 2011. Table -3 shows that Gross NPAs in terms of absolute amount in priority sector and non-priority sector significantly increased during last two years

Section-IV Conclusion

The Non performing assets have become a most critical factor governing the performance of banks. The study has shown that in terms of absolute quantum, the NPAs for PSBs increased by Rs. 17240 (43.92%) crores during 1993-2002 and it increased by Rs. 18121(32.08%) crores during 2002-2011. Gross NPAs increased by 24.51% in 2010-11 compared to 2009-10. The Gross NPAs to Gross Advances Ratio significantly decreased from 23.20% in 1992-93 to 2.23% in 2010-11 and Net NPAs to Net Advances ratio also decreased from 14.50% to 1.09% during 1993-94 to 2010-11. The share of standard assets in total advances of PSBs increased from

82.2% in 1996-97 to 97.8% in 2010-11. Total advances increased by Rs. 3103316 (1270.74%) crore during 1997-2011. In terms of absolute quantum, the Gross NPAs of PSBs increased due to gross advances increased during the study period. The shares of priority sector and non-priority sector advances were 58.1% and 41.6% respectively in 2010-11. Though the proportion of the priority sector NPAs to Gross NPAs is increasing, it still remains significantly high to merit special attentions. The banks have not been able to devote adequate attention to the priority sector portfolio due to its large volume. The study also shows that overall assets quality of PSBs improved during the study period.

The problems of NPAs can only be solved when the PSBs put in place proper credit assessment and risk management will have to be supported extremely by proper legal framework where under quick action against a defaulting borrower can be taken. Therefore RBI and government should modify present legal framework for quick action against defaulting borrower to reduced Gross NPAs level of PSBs.

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