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Research Paper

# Measures to Curb Npas in Public Sector Banks

Commerce

KEYWORDS :

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## 1. INTRODUCTION

The public sector banks undertake lending to different sectors of the economy and have geographical spread through their branch network. The viability will depend on the profit generating capacities of their operations. The most critical area in the improvement of the profitability of banks continues to be the reduction of non-performance assets (NPAs). With the introduction of international norms of Income recognition. Asset Classification and Provisioning in the banking sector, managing NPAs has emerged as one of the major challenges facing the banks. The public sector banks (PSBs), with their vast network of branches and mass-retail-business base, cannot escape the applicability of near uniform global standards if they have to become globally competitive.

## 2. SIGNIFICANCE OF THE STUDY

Providing loans for economic activities is the social responsibility of banking. Credit dispensation activity is considered to be major part of funding apart from raising resources through fresh deposits, borrowings and recycling of funds received back from borrowers. Lending is generally encouraged because it has the effect of funds being transferred from the system to productive purposes, which results into economic growth. However lending involves credit risk, which arises from default by the borrowers. The process of credit cycle is affected by non-recovery of loans along with interest. Thus, loan losses and requirement of provisioning for loss affect the banks profitability on a large scale. Though complete elimination of such losses is not possible, but banks can always aim to keep the losses at a low level.

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## 3. OBJECTIVES OF THE STUDY

The specific objectives of the study are as follows

I. to analyze the classification of loan assets in Public Sector Banks;
II. to analyze the composition of NPAs in different sectors; and
III. to examine the causes and remedial measures to arrest NPAs.

## 4. RESEARCH METHODOLOGY

The present study concentrated on PSBs only. For this study secondary data have been collected. The data are collected from annual report of RBI publications including Trend and Progress of Banking in India, Statistical Tables relating to Banks in India, Articles and Papers relating to NPAs published in different journal and magazines were studied and data available on internet and other sources have also been used.

## 5. NON-PERFORMING ASSETS (NPAs)

Assets which generate periodical income are called as performing assets. Assets which do not generate periodical income are called as non-performing assets. NPAs are further classified into sub-standard, doubtful and loss assets based on the criteria stipulated by RBI. An asset, including a leased asset becomes non-performing when it ceases to generate income for the bank for a specified period of time. The RBI guidelines regarding classification of assets and its provisioning with effect from March 31, 2005 are as follows

### 5.1. Classification of Loan Assets

**Standard Assets:** Standard assets generate continuous income and repayments as and when they fall due. So a standard asset is a performing asset. Such assets carry a normal risk and are not NPAs in the real sense. Hence, no special provisions are required for Standard Assets.

**Sub-Standard Assets:** A sub-standard asset was one, which was considered as non-performing for a period of 12 months.

**Doubtful Assets:** All those assets which are considered as non-performing for period of more than 12 months are called as Doubtful assets.

**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

**Table-1 Classification of Loan Assets of Public Sector Banks 2004-2013 (Amount in Rs. crore)**

| Sl. No. | Year | Standard Assets | | Sub-Standard Assets | | Doubtful Assets | | Loss Assets | | Total NPAs | Total Advances |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | Amount | % | Amount | % | Amount | % | Amount | % | | |
| 1. | 2004 | 610435 | 92.2 | 16909 | 2.5 | 28756 | 4.4 | 5876 | 1.0 | 51541(7.8) | 661976 |
| 2. | 2005 | 830029 | 94.6 | 11068 | 1.3 | 30779 | 3.5 | 5929 | 0.7 | 47776(5.5) | 877805 |
| 3. | 2006 | 1092607 | 96.2 | 11453 | 1.0 | 25028 | 2.2 | 5636 | 0.5 | 42117(3.7) | 1134724 |
| 4. | 2007 | 1425519 | 97.3 | 14275 | 1.0 | 19873 | 1.4 | 4826 | 0.3 | 38974(2.7) | 1464493 |
| 5. | 2008 | 1778476 | 97.8 | 17290 | 1.0 | 19291 | 1.1 | 4018 | 0.2 | 40599(2.3) | 1819075 |
| 6. | 2009 | 2237556 | 97.99 | 20603 | 0.90 | 21019 | 0.92 | 4296 | 0.19 | 45918(2.01) | 2283474 |
| 7. | 2010 | 2673534 | 97.81 | 28791 | 1.05 | 25383 | 0.93 | 5750 | 0.21 | 59924(2.19) | 2733458 |
| 8. | 2011 | 3272914 | 97.77 | 34973 | 1.04 | 33180 | 0.99 | 6463 | 0.19 | 74616(2.22) | 3347530 |
| 9. | 2012 | 38255 | 97.0 | 623 | 1.6 | 490 | 1.2 | 60 | 0.1 | 1173(2.9) | 39428 |
| 10. | 2013 | 43957 | 96.4 | 815 | 1.8 | 761 | 1.7 | 68 | 0.1 | 1644(3.6) | 45601 |

**Source: Reports on Trend and Progress of Banking in India.**

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Table 1 presents the data pertaining to classification of loan assets of PSBs during the year 2004 to 2013. The amount of standard assets showed an increasing trend during the stated period. In the initial year 2004 the ratio of standard assets to total advances stood at 92.2 percent. It increased to 96.4 percent in 2013. The ratio of sub-standard to total advances

showed a decreasing trend, it was 2.5 percent in 2004 and reduced to 1.8 percent in 2013. The ratio of doubtful assets to total advances showed a decreasing trend recording the percentage 4.4 in 2004 and 1.7 percent in 2013. The ratio of loss assets to total advances showed a decreasing trend from 0.9 per cent in 2004 to 0.1 percent in 2013. The total NPAs to total advances ratio reduced from 7.8 percent in 2004 to 3.6 percent in 2013. Though the amount of NPAs is increased from Rs.51,541 crore in 2004 to Rs.74,616 crore in 2011, later the total NPAs decreasing trend from Rs. 74,616 crore in 2011 to Rs. 1,644 crore in 2013, its percentage to total assets has been reduced from 7.8 % to 3.6%. It shows the effectiveness of follow-up actions of PSBs in monitoring NPAs. Total advances of Public Sector Banks is increased from Rs.6,61,976 crore in 2004 to Rs.39,428 crore in 2012.

### 5.2 Gross and Net NPAs of Public Sector Banks

Gross NPA is an advance which is considered irrecoverable, requires provisioning and which is still held in banks' books of account.

**Table-2 Gross and Net NPAs of Public Sector Banks (Amount in Rs. crore)**

| Sl.No. | Year | Gross NPAs (Rs.) | % of Gross NPAs to Gross Advances | Net NPAs (Rs.) to Net Advances | % of Net NPAs |
|---|---|---|---|---|---|
| 1. | 2004 | 51537 | 3.5 | 19335 | 1.3 |
| 2. | 2005 | 48399 | 2.7 | 16904 | 1.0 |
| 3. | 2006 | 41358 | 2.1 | 14566 | 0.7 |
| 4. | 2007 | 38968 | 1.6 | 15145 | 0.6 |
| 5. | 2008 | 40598 | 2.2 | 17836 | 1.0 |
| 6. | 2009 | 44957 | 1.97 | 21155 | 0.94 |
| 7. | 2010 | 59926 | 2.19 | 29375 | 1.09 |
| 8. | 2011 | 74614 | 2.23 | 36071 | 1.09 |
| 9. | 2012 | 1178 | 3.3 | 593 | 1.5 |
| 10. | 2013 | 1650 | 4.1 | 900 | 2.0 |

**Source: Reports on Trend and Progress of Banking in India.**

Data presented in the Table 2 reveals the decreasing trend in Gross NPAs and Net NPAs during the study period. This shows that there is a significant improvement in NPAs recovery by PSBs. But at the end of the study period Gross NPAs to increased from 2.19 per cent in 2010 to 4.1 per cent in 2013. The Net NPAs to per cent of Net Asset ratios it was 1.3 per cent in 2004 and increased to 2.0 per cent in 2013.

### 5.3. Causes of Non-Performing Assets

The causes of NPAs are varied in nature. These include:

- Lack of a uniform approach among Fls and Banks, poor credit decisions taken by bank management, priority sector lending, poor industry analysis, infrequent customer contact, the absence of loan supervision, poor controls on loan documentation, excessive centralization and decentralisation on loan, authorities and excessive overdraft lending.
- Many reputed companies closed down their shutters due to their inability to cope with the technological advances during transition period. The advances given by banks to these companies became NPAs.
- Where interest rates go up marginally companies are further squeezed, causing NPAs.
- In an RBI study, it was found that diversion of funds for expansion, diversion and modernization of new projects and for promoting associated concerns is the single most prominent reason for NPAs. The study says that it explains that combined with recessionary trend, which also failed to raise capital, diverted bank funds ended up being sticky. Diversion by business houses to promote industries is hardly new, but after liberalisation, economy has become prey to cyclical swings. Both business and banks, it would seem, were not ready for the exposure to business cycles (and important competition) after planning took a back seat. NPAs reflect the structural change in the economy, not-sub-standard banking per se.
- External factors like raw material shortage, price escalation, power shortage, excess capacities and natural calamities like floods and accidents have also contributed to the mounting NPAs in the books of banks. Internal factors like business failure, inefficient management, strained labour relations, inappropriate technologies and product obsolescence have also contributed to fall in NPAs.
- The high proportion of NPAs in priority sector advances was attributed to the directed and pre-approved nature of loans sanctioned under sponsored programmes, absence of any security, lack of effective follow-up due to the large number of accounts and legal recovery measures being considered not cost-effective.
- Credit appraisal of banks even today lacks professionalism. The amount of banks credit (estimated at around 20000 crore), locked up in sick units, bears, testimony to this fact.
- Delay in finalisation of rehabilitation packages by BIFR.
- The corporate India and larger borrowers take better advantage of the antiquated legal system and frangible law enforcement machinery plagued by chronic delays. This also contributes to NPAs.

### 5.4 Measures to arrest NPAs

- The present system of consortium lending should be dispensed with and its place a system of syndication or participation in lending by institutions and banks should be encouraged. The same was recommended by Narasimham Committee-1.
- The legal system should be revamped by according priority to recovery of banks' dues. Exemplary and deterrent penalties should be imposed without delay on borrowers who submit falsified financial statements and divert funds for unintended purpose. Urgent measures are required to improve functioning of BIFR so that unscrupulous borrowers fo not gain time for transferring or disposing of their assets.
- Better co-ordination between financial institutions and banks, a new credit insurance scheme for priority sector lending, gradual shift from bank based to market based system and technology banked and sound credit risk management skills will enable banks to meet the challenges in environment and keep their NPAs low.
- Cases of delinquent and dishonest officials perpetrating frauds, both individually and in collusion with the borrowers, should be investigated and severe punishment should be meted out to them.
- Banks could be pro-active in recognising sickness an them going to the courts for obtaining relief, before the borrower could take the shelter of BIFR proceedings. The lending banks should initiate action against the borrower as soon as the accumulated losses crossed half of the net worth. They should not wait till they wipe out the entire net worth, thus making a rehabilitation under BIFR more difficult.
- Revamping of recovery process and delegation of more powers to the branch managers and concentrate on recovery of blocked funds.
- Constant touch with borrowers, continued follow up through official correspondence and by personal visits have proved effective in a majority cases.
- Banks need to be given wider powers like those given to SFCs to take over or realise/enforce securities charged to them without going to courts. These provisions will reduce court cases, improve environment and discourage wilful defaulters.
- The revival effort should be done within the stipulated time frame.

**5.5 CONCLUSION**

Total elimination of non-performing assets is not possible in banking business owing to external factors but their incidence can be minimised. It is always wise to follow the proper policy for appraisal, supervision and follow-up of advances to avoid non-performing assets. Special Recovery Cells may be set up at regional/zonal levels. Similarly, Recovery officers may be appointed at branches having sizeable NPAs and their recovery progress may a be monitored on a monthly basis. Banks should encourage mergers acquisition of sick units wherever they feel it may reduce the NPAs. A large number of compromise proposals are being approved by banks with a view to reducing the NPAs and recycling the funds instead of resorting to expensive recovery proceedings spread over a long period.

Banks should take full advantage of the Tribunals by taking necessary steps. It is hoped that established of DRTs may not only facilitate quick decisions but also induce borrowers to enter into settlements with banks Establishment of Asset Recovery Branches at critical centres for undertaking recovery, fix targets of recovery and draw time bound action programme will help reduce the NPAs to a certain. Branch Management have to put in sincere efforts to improve recoveries by personally contacting the borrowers instead of issuing notice to them. A number of follow-up visits and regular stock inspection significantly improve recovery.

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