



AN OVERVIEW OF THE NON-PERFORMING ASSETS IN INDIA

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KEYWORDS

What is a 'Non-Performing Asset - NPA'

The loans and advances given to customers are the assets of the banks. This loan turns bad loan when the customers are not in a position or for some reason are not willing to pay either interest or part of principal or both. An asset is considered as non performing when it is no longer capable of generating income for the lender. The term NPA is mostly for loans that are in a position of default. The case arises when the borrower fails to make payments i.e. interest and principle for a period of ninety days. Such kind of assets are treated as problematic assets.

Often there is so much pressure from the economic front that increasing numbers of non-performing loans tend to result in heavy write-downs.

Non-performing assets have been classified into three categories which is based on the period for which the asset has remained non-performing and the realisability of the dues. They are:-

1. Sub-standard assets
2. Doubtful Assets
3. Loss assets

A sub standard asset is one which has been classified as NPA for a period not exceeding twelve months and banks have to maintain 15% of its reserves. While a doubtful asset is one which has remained NPA for a period exceeding twelve months and Loss assets are those where either the bank, auditor or central bank inspectors have identified the loss, although the amount has not been written off, completely or partly.

There are various reasons for the occurrence of loans like:-

- Banking operations which are unusual or bad lending practices
- Some kind of a crisis in bank.
- There can be incremental component due to internal bank management.

Not just the banks but the entire economy is affected by NPAs.

There are various bad effects of NPAs, some of which are:-

- The depositors are not able to get their due returns and several times they lose uninsured deposits.
- Bad loans mean redirecting of funds from to bad projects. Thus, the economy enters into losses as it gets deprived of good projects.

The Effects of NPAs

Carrying nonperforming assets, are also called nonperforming loans, on the balance sheet. Loan loss provisions, which are set aside to cover potential losses, reduce the capital available to provide subsequent loans. Once the actual losses from defaulted loans are determined, they are written off against earnings.

Recovering Losses

Lenders generally have four options to recoup some or all of the losses resulting from nonperforming assets. When companies are struggling to service debt, lenders can take proactive steps to

restructure loans to maintain cash flow and avoid classifying loans as nonperforming. When defaulted loans are collateralized by assets of borrowers, lenders can take possession of the collateral and sell it to cover losses to the extent of its market value.

There is an important related term called "provisioning" It is that some extra fund which the banks keep aside in order to cover up the loss. Provisioning Coverage Ratio (PCR) exhibit the funds which have to be kept aside by the banks as fraction to the loans.

Implications of NPA

The most important implication of the NPA is that a bank can neither credit the income nor debit to loss, unless either recovered or identified as loss. In case any borrower has multiple accounts and one of the all accounts would be considered NPA if one account becomes NPA. Gross NPA and Net NPA The NPA may be Gross NPA or Net NPA. In simple words, Gross NPA is the amount which is outstanding in the books, regardless of any interest recorded and debited. However, Net NPA is Gross NPA less interest debited to borrowal account and not recovered or recognized as income. RBI has prescribed a formula for deciding the Gross NPA and Net NPA. NPA and SARFAESI Act The Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act has provisions for the banks to take legal recourse to recover their dues. When a borrower makes any default in repayment and his account is classified as NPA; the secured creditor has to issue notice to the borrower giving him 60 days to pay his dues. If the dues are not paid, the bank can take possession of the assets and can also give it on lease or sell it; as per provisions of the SARFAESI Act.

Reselling of NPAs

In case a bad loan remains NPA for a period of at least two years, the bank can also resell the same to any Asset Reconstruction Companies such as Asset Reconstruction Company (India) (ARCIL). Such sales are simply on the basis of Cash and the purchasing bank or the company would have to keep the accounts for a period of at least fifteen months before it sells to any other bank. They purchase such loans on low amounts and then try to recover from the defaulters as much as possible Their revenue is difference between the purchased amount and recovered amount.

When there was a tightening of regulations in 1993 then Non-Performing Assets were reduced to a great extent but improvement has recently slowed down and the levels of NPA remain high as per the international standards. The Reserve Bank of India norms have defined NPA as a credit facility in respect of which interest has remained past due for a period of four quarters. An amount under any credit facility is past due when it has not been paid within 30 days from the due date. It examines the trends of NPA, trends in Gross advances and Gross NPA, bank-wise NPA, quantum of NPA in public sector banks.

The details from RBI say that out of the total NPAs of Rs 221,400 crore, the rate of recovery of non-performing assets (NPAs) was 10.3 per cent, or Rs 22,800 crore. This was the case during fiscal

that ended on March 2016. This was against Rs 30,800 crore (12.4 per cent) of the total amount of Rs 248,200 crore reported in March 2015.

RBI stated that the rate of recovery was 18.4 % or Rs 32,000 crore out of the total NPAs of Rs 173,800 crore which were reported in the month of March in the year 2014. This rate of recovery was even higher at 22 per cent (Rs 23,300 crore) in the month of March in the year 2013 out of the total reported NPAs of Rs 105,700 crore.

The NPA and Ratios

P/B ratio reflects the price to book ratio – or the market cap of the company compared to (Equity plus reserves). P/E is also called Price to Earnings ratio (market cap divided by net profit). It exhibits the the future earning expectations of the company.

There are various banks like Kotak, J&K, IndusInd, HDFC, Federal who have comparatively high P/E's because of cleaner balance sheets. While SBI has comparative high P/E because of larger book and controlled NPA's.

Not to forget that there are some banks with large books but are not highly valued .

There are some banks like HDFC whose net interest margin is high. But this is not the case with all the banks. Since majority of the banks have marginal increase or de-growth in terms of revenue, With the decrease in credit growth , majority of the public sector banks have witnessed a revenue cut. Banks which are mainly in the retail sector do not have enough exposure towards corporate lending and are not taking a hit on their credit growth.

The profits of the public sector banks have also taken a hit, due to higher provisioning (still most of them have not completed their provisioning quota) and more accounts going into NPA. This applies to ICICI and Axis Bank as well.

- The total revenue of above said 37 banks together is at Rs. 2.59 Trillion and it grew by 4.16% YoY.
- The total net profit of above said 37 banks together is at Rs 8862 cr. A contraction of 53.20% YoY.
- SBI and its subsidiaries accounted for 21.73% of all the revenue generated (last year same quarter 20.88%). And in terms of profit, SBI and its subsidiaries accounted for 12.23% of the profits (last year same quarter 21.85%)

Conclusion

Since there is a rising trend with bad loans , so there is an urgent need to have a look at the rate of recovery of bad assets by the banks. Moreover on the default of the loans, they should be collateralized by assets of borrowers. The lenders may cover losses to the extent of its market value by taking possession of the collateral and by selling it. Banks should give importance to provisioning meaning that the banks should keep some extra fund aside so as to cover up the loss.

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