

## NON PERFORMING ASSETS: THE BURNING ELEMENT OF BANK'S ASSETS

Dr. Pawan Gupta\*

### ABSTRACT

*The Non Performing Assets which is quite a well known term to everybody since last 5 years. In the last years of this decade so many Losses have been occurred to banks due to Non Performing Assets, that Banks are now reluctant to offer the loans to genuine borrowers even. The banking industry has undergone a sky changes after the beginning of economic liberalization since 1991 and thus also impacted Credit management. In these years, as we said banks are very cautious in giving loan to borrowers. The reason is undoubtedly high Non Performing Assets. The banks are taking all precautionary measures to the great extent so that it can prevent itself from falling in a situation of incurring great losses due to non performing assets. Non Performing Assets definitely a profit cutter to the banks portfolio and it is another cause why the depositors do not get benefit. I we analyse the interest benefits passed on by the banks in last 5 years, it is continuously declining and rate of interest on saving has fallen up to 3.5 percent. This is probably the lowest rate of interest on saving bank Accounts ever offered. Hence banks including Reserve Bank of India are taking all corrective actions to pin out the problem and any how fix it or at least put on the minimum count. However sometimes some other external non controllable factors such as COVID-19 occur which impacts the earning of borrower and due to which the repayment capacity of borrower is impacted a lot. If we keep aside such factor, the rest other causes can be measured with proper policy implementation and by making guidelines.*

**Keywords:** Non Performing Assets, Factors Effecting Non Performing Assets, Prudential Norms.

### Introduction

The Banking industry is broadly divided into three categories in India. These categories are Public Sector Banks, Private Sector Banks and Nationalized Banks. Other types of Banks also exist such as cooperative Banks, Regional Rural Banks and Private Banks. Non Performing Asset is an asset which has stopped generating any income to the bank. This could be either in form of Non generation of interest or non generation of interest and Principle both. The Non-performing Asset is further classified as Sub Standard, Doubtful and Loss Asset. The big question is however, how a Loan is classified as Non Performing assets. The below table must help to understand the concept

Type of Loan	Overdue period required to convert the Debt into NPA
Term Loan	Interest and/or principal remain overdue for a period of more than 90 days
Overdraft/Cash Credit	Remains 'out of order' for a period of more than 90 days i.e. either no credit to the Account (in case of overdraft) or interest is not sufficient to cover interest debited or Outstanding balance exceeds the sanctioned limit (in case of Cash Credit) for continuous period of 90 days
Bills purchased and discounted	Bill remains overdue for a period of more than 90 days
Agricultural Advances	<ul style="list-style-type: none"><li>For short duration Crops: Interest and/or principal remains overdue for two harvest seasons or crop season</li><li>For long duration Crops: overdue Period is one harvest or crop season</li></ul> <b>Note:</b> Long Duration Crops means where crop season is longer than 1 year. A crop which is not a long duration Crop is a short duration Crop.

\* Ex Research Scholar, Department of Applied Economics and Commerce, M.U. Bodh Gaya, Bihar, India.

<b>Securitisation Transaction</b>	Amount of Liquidity Facility remains outstanding for more than 90 days
<b>Derivative Transaction</b>	Overdue receivables representing positive mark to market value of a derivative contract remains unpaid for a period of 90 days from the specified date for payment.
<b>Any other</b>	Any amount to be received, remains overdue for a period of more than 90 days

As we said that Non Performing Assets is further classified into Substandard, Doubtful and Loss assets as follows

<b>Standard assets</b>	This does not disclose any problems as well as does not carry more than normal risk.
<b>Sub-standard asset</b>	This includes income which is Classified as Non Performing Asset for a period up to 12 months.
<b>Doubtful assets</b>	Remained NPA for a period exceeding 12 months, but not determined as loss asset by bank or internal auditor.
<b>Loss assets</b>	Where loss has been identified by bank or by the internal or external auditors or by the RBI Inspection, but the amount has not been written off, wholly or partly.

As per Reserve Bank of India Directions Banks has to follow two distinct guidelines once an Account turns Non Performing. The first one is the income on such Advances shall be recorded on receipt basis and recognition on accrual basis shall be discontinued immediately. Hence this becomes a critical performance area of the banks because this reduces the profitability of banks. The second one is, the Banks has to create proviso on all Non performing assets. This also reduces the profitability of banks as provisions shall be charged from Profit & Loss account only. The provisioning requirements is as follows

- **Loss Assets:** Should be written off or 100% provision should be made for the amount outstanding.
- **Doubtful Assets:**
  - Hundred Percent provisions for unsecured portion should be made. The realizable value of the security available should be determined on realistic basis.
  - In regard to the secured portion, no provision needs to be made towards the guaranteed portion by DICGC (Deposit Insurance And Credit Guarantee Corporation) or ECGC (Export Credit Guarantee Corporation). Over & above guaranteed portion should be provided for as per the period for which asset has remained doubtful:

<b>Period for which Advance has been considered as doubtful</b>	<b>% of Provision</b>
Up to 1 years	25*
More than 1 year and up to 3 years	40*
More than 3 years	100

- **Sub-standard Assets:** A provision of 15% on total outstanding and an additional provision of 10% is required to be made on 'unsecured exposure'.
- **Standard Assets:**
  - Provision for Advances given directly to agricultural and small and Micro Enterprises (SMEs) sectors shall be at 0.25%.
  - Provisions for Advances to Commercial Real Estate (CRE) Sector shall be at 1%.
  - Provision for Housing loans extended at teaser rates.
  - Provision for all other loans and advances not included in (a) (b) and (c) above shall be at 0.40%.

Therefore, a Non Performing Asset do not only decreases profitability of banks by having provisions in the profit and loss account, but their cost of management and carry also increases which results in excess & avoidable management attention. The other aspect which also need to taken care is banks also need to maintain capital Adequacy which is not possible without adequate profit, hence banks uses their internal financial Strength to fulfill the norms which causes a slow decrease or curtailment in their net worth.

If we talk in today's context, the level of Net Non Performing Assets of Public Sector Bank's (Public Sector Banks carries around three Fourth of total financial Assets of Indian Banking System) 0.72 and Level of Gross Non Performing Assets are at 2.5 percent. However there is no doubt that whenever there will be slowdown in private expenditure and corporate earnings, corporate borrowers will not be in position to pay their debts and no doubt the level of Non Performing Assets will increase. If interest rates in the government Bond Market unfortunately takes high, treasury income of Bank's will decline and banks will not have much profits to even make provisions.

Hence considering these circumstances management of Non Performing Assets is a difficult as well as required task; hence the study in this research paper focuses on the problem of Non Performing Assets being faced by Banks. In our research we will also find out reasons and solutions to the growing level of Non Performance Assets.

### **Review of Literature**

Though many published articles are available in the area of credit management and non-performing assets, which are bank specific or banking sector specific.

**Reddy, 2004** A review of the literature by the researcher has shown various insights into the determinants of Non Performing Assets of entire country. The bank's Lending Policy could have an influence on Non Performing Assets. The researcher has critically examined various issues relating to the credit practice of Banks in India. After examination he came to conclusion that having power is not at all having any impact on Illegal activity. In the same way a defaulter doing default is not taking an irrational decision. Rather he is acting smartly and doing default after considering the cost and benefits of his decision of defaulting in making the payment.

**Mohan (2003)**, while lighting on the policies of lending of Banks and investment portfolio of Banks has an international prospective regarding credit culture and lazy Banking Attitude, premier highlights that Bank's Lending Policy is a major driver of Non Performing Assets. This aspect has also been highlighted by many other authors and researcher in their study.

**Bhattacharya (2001)** He has encouraged a very intelligent point in his study by mentioning that in case rates of borrowing increases, a smart borrower will definitely switch over to other avenues or options for their funding requirements, such as capital markets or Internal accruals or savings or reserves. If it happens, the banks would not have any option other than to diversify or dilute the quality of borrowers which will definitely increase the possibility of Non Performing Assets.

**Muniappan (2002)**, In another study, researcher observed rates of interest on Deposits and Government have come down but simultaneously rate of lending has not decreased. Banks have reduces Prime Lending rates of but still the effective rates of lending has remain to be very high. The problem of Non Performing Assets is related to several factors including Internal and External, which confront the Borrowers.

**Bloem and Gorter (2001)** More or less the amount of Non-Performing Assets, whether it is predictable or not or if it is predictable whether accurately or not, and whether it differs from year to year, it always causes due to wrong economic decision of Individuals or because of their Bad luck such as inclement weather or change in price levels of certain products). In such circumstances, the borrower of the Loan can make a portion of his loan as Bad Debts and or may go for other option. Because of this The Bank's Non Performing Assets increases, Profits declines and a substantial loss to capital as well as economy will arise. Economy may reach at very though level.

### **Objective of Study**

The proposed study has been undertaken with following objectives:

- To examine the policies of banks in Credit Sector in Banks in India.
- To finds out the reasons and areas of NPA's in Banks on higher segments.
- To find out the methods of solving problems of NPA's management with the help of prudential norms on NPA as issued by RBI.
- To find out the role and effect of NPA's on Financial Reforms and functioning of Banks.
- To find out the measures that shall be adopted in area of NPA management by Banks and RBI.

### **Rational of Study**

Nationalization of major commercial Banks in 1969 changed the complexion and dimensions of commercial Banks in India. Further, the announcement of economic liberalization by the government and consequent trends towards market economy changed the complexion and dynamics of banks business

in India. Thus the banks in India are expected to change their role with the change in the government's economic and social policies. Now the trends of the market economy create NPA's, sever competition to public banks with the result they have changed their functions organizational structure, relationship, culture, goals and their mission etc.

The above study intends to explore the ways and means of management if NPA's in improving overall effectiveness and to find out the prevailing defects of banking policy of the government/RBI. Although a number of literature is available on above topic but still as such no systematic and well structured literature available in this field, hence the proposed research work would be of immense relevance. The researcher would attempt to scan the literature available and would systematically organize it.

### **Hypothesis for Study**

In order to present the role of government, RBI, Bank Officers and Society in accumulating and interpretation of the data to resolve problems of NPA and to evaluate overall effectiveness, following hypothesis are being undertaken:

- Had the Banks of India reviewed the quantum of recovery from NPA's on continuous basis so that the government/RBI may decide about the uniform policy for such cases.
- There is an element of overstaffing in Public Sector banks of India, Hence proper identification and quantification of this problem can improve the existing NPA's Management practice.
- Prudential Norms of RBI for classification of NPA is observed by banks in the manner as issued by RBI.
- Proper installation, application and utilization of modern Technologies and policy can resolve the conflicts and disputes and an effective NPA's Policy guidelines has direct impact on the performance of people in the organization.
- There is no significant difference of NPA on overall performance between selected banks.
- There is no significant difference on efficiency in managing NPA between selected banks
- There is no significant change in the Ratio of Net NPA to total Advances of all Commercial Banks over the study period.
- Published figures of RBI and various Banks are correct.

### **Scope of the Study**

For the present study, 5 banks have been considered. The banks taken in the study are SBI, BOB, PNB, Axis Bank, and ICICI Bank.

The period covered under the present study is 5 years, beginning from 2013 to 2018. Various research Techniques and statistical Techniques have been considered such as ratio, percentages, average analysis.

### **Research Methodology**

Research methodology is a process through which a researcher tries to resolve an issue or find out the solution of a problem. It is, in other words a science of studying how research is done scientifically and trends and ratios are analyzed with some Statistical Techniques and Methods.

- **Research Objective**

The research was conducted to make a comparative analysis of Non Performing Assets management in the public and private banking sectors. The Research paper also focuses on the weak points that are to be amended so as to reduce the proportion of Non Performing Assets in the Advances portfolios of Public and Private Sector Indian banks.

This study is intended to analyze the Non Performing Asset's of Indian Banks. For the purpose of the Research data has been collected from secondary sources. The main source of information has been through RBI reports and bulletins.

- **Sample Design**

For the data collection and analysis, Random Sampling and Stratified Random Sampling Techniques have been used.

- **Sample Size**

A Sample of fifty to Hundred Material Management Professionals from all the selected Tractor Manufacturing companies has been taken for the purpose of data analysis.

**Data Collection**

Secondary data was collected from published sources like RBI database, annual reports of Banks and financial Journals for period from 2013-18.

**Parameters** which are used for “Reasons of NPAs” are as follows:

- Market Failure
- Willful Defaults
- Poor follow-up and Supervision
- Non-cooperation from Banks
- Poor Legal framework
- Lack of Entrepreneurial Skills
- Diversion of funds

**Results and Analysis**

The Data collected from the sources, for Banks selected for the purpose of the research. The same has been presented in the tables below

**Table 1: Position of Advances in various Banks**

(Rs. in crores)

Year	Advances				
	SBI	BOB	PNB	AXIS	ICICI
2020	2326053.81	689361.02	470916.96	600000.00	717295.04
2019	2189202.66	468738.74	457896.34	547378.64	658127.67
2018	1934642.23	427741.35	433131.67	488000.00	584617.82
2017	1570808.63	383050.85	418719.59	408862.56	520470.96
2016	1464750.66	383517.79	411416.96	360285.71	498005.62

**Table 2: Position of NPA's in various Banks**

(Rs. in crores)

Year	NPA				
	SBI	BOB	PNB	AXIS	ICICI
2020	51871	21577	27219	9360	10114
2019	65895	15609	30038	11276	13557
2018	110855	23483	48684	16592	27886
2017	58277	18080	32702	8627	25451
2016	55807	19406	35423	2522	13297

**Table 3: Percentage of NPA's on Advances in various Banks**

Year	% of NPA on Advances				
	SBI	BOB	PNB	AXIS	ICICI
2020	2.23	3.13	5.78	1.56	1.41
2019	3.01	3.33	6.56	2.06	2.06
2018	5.73	5.49	11.24	3.4	4.77
2017	3.71	4.72	7.81	2.11	4.89
2016	3.81	5.06	8.61	0.7	2.67

\*\*all Data is taken from moneycontrol.com

**Table 1** depicts that total advances of commercial Banks (Both Pvt. And public) has increase from 2016 to 2020. In case of public sector banks it has increased almost up to 70%. In case of private sector banks it is up to 60%.

However at the same time NPA has also increased gradually with the increase of advances but increase in NPA is higher than corresponding increase in Advances.

One of the reasons for the accumulation of higher ratio of NPAs is that the lending is not linked to productive investment and the recovery of credit is not linked to product scale. In public sector banks the borrowers are mainly farmers and small scale industries owner whose financial condition are generally weak. Sometimes the pressure of BIFR and government to grant Loan to sick industries is also there with Public Sector Banks.

Another reason for high NPAs is the improper lending policy and making compulsory to lend to priority sector by banks. There are many other causes such as faulty credit management like defective credit recovery mechanism, lack of professionalism in the work force, time lag between sanctions and disbursement of loan, unrealistic repayment schedule, not utilization of loans for mentioned purpose by user, untimely communication to the borrowers regarding their due date, lack of sponge legal mechanism, politics at local levels and waive-off policy of loan by government

**Table 3** depicts that percentage of NPA to Advance is also increased in 2020 compare to 2016, but not very significantly. Even some Banks has shown (like ICICI Bank) a Decrease in NPA. Except ICICI bank, all other Banks has a zigzag flow i.e. they are not showing a consistent trend. It is increasing then showing a trend of decrease. The performance of ICICI Bank seems to be satisfactory as NPA has increased in 2017 and 2018 but then it has shown a decreasing Trend. Inconsistency in NPA trend indicates that efforts on the part of Banks to recover dues as well as to slow down the amount of NPA are not sufficient.

### Conclusion and Recommendations

Since the Non Performing Assets is still a trouble for the Banks. Although the trend indicates that that banks has put their efforts to recover the amount of Non Performing Assets, and they also implemented the policy on their part for sanctioning the Advances and making a practice to Advance only to genuine borrower with all proper caution and care. However, still the Non Performing Assets will generate.

In this Respect Reserve Bank of India and Ministry of Finance has to come out with a detailed set of policies and measures to provide a road map to the Banks how they should sanction the Loan and the measures to be adopted. The problem will never discontinue or eliminate because every defaulter is not a willful defaulter. Some time the unavoidable circumstances permit the borrower to make a default. Still all precautionary measures along with a detailed road map has to be find out.

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