Inspira-Journal of Commerce, Economics & Computer Science (JCECS)
ISSN : 2395-7069 General Impact Factor : 2.4668, Volume 04, No. 04, October-December, 2018, pp. 223-226

NPAs: A MAJOR DISEASE FOR INDIAN FINANCIAL SECTOR

Dr. Naveen Kumar Ajmera*

ABSTRACT

Banks and financial institutions play a key role in the economy. They are tool to control supply and circulation of funds which is life and blood of the economy. Our banking and financial institutions can proudly claim that they operate under one of the most liberal regimes of Asia. It is unfortunate that our banking system proved to be incapable to take the advantage of their situation. Specifically over the last decade the situation has gone from bad to worse. Ever increasing non-performing assets (NPAs) has led some banks and financial institutions to the stage of precarious health. Disorderliness in financial sector is not new in India. Very first effort for correction as made in 1967 with the nationalization of 14 major banks. Unfortunately, nose was too tight to let the financial sector flourish or was it the case of wrong medicine administered to ailing financial sector at the wrong time, which almost throttled the financial system later on.

KEYWORDS*: Non-Performing Assets (NPAs), Disorderliness in Financial Sector, Financial System.*

Introduction

Non performing assets (NPAs) seem to be number one culprit, which is drawing the banks and financial institutions towards the whirlpool of financial black hole. Non performing assets could be described as the loans given by a bank or financial institutions where the borrowers defaults or delay the payment of principal amount for more than 90 days. Assessment of NPA is not very old concept. It has come into existence only after enormous size of NPAs mushrooming in the last two decades or so. The very principal of defining non performing assets vary from country to country under different norms. In India NPA is calculated as a percentage of advances, whereas is some countries it is calculated as a percentage of total assets. The NPA calculation system in India is near to internationally adopted best practices but the problem lies in the interpretation of some aspects of the norm and the lack of transparency on the part of financial institutions in revealing non performing assets figures.

Objectives of Research

It is an undisputed fact that micro and small scale industries sector has been the backbone of Indian economy and pride of the nation. The contribution of SSI sector to the country's economy in terms of employment generation, industrial production, value of exports has been significant. It is an irrefutable reality that the significant performance of the SSI sector has been made possible due to ceaseless efforts of the SFCs. Setup in 50s and early 60s, SFCs have been the main instruments for financing, medium small and tiny industries and promoting first generation entrepreneurs. This cannot be forgotten that SFCS were providing services at that time when there were no institutions for credit facilities in rural / semi urban and backward regions of the state. Most of the large / medium scale industries had started their bencher initially with the assistance of SFCs.

---

* Ph.D., Department of ABST, Faculty of Commerce, University of Rajasthan, Jaipur, Rajasthan, India.

The SFCs are by and large successfully meeting the challenge of providing service to entrepreneurs, but biggest challenge before them is management of NPAS; hence a matter of great concern for the Indian financial system and is survival of the SFCs as well. In this background, the present research paper strives to make an assessment of NPAs in APSFC, RFC and DFC, general reasons for assets becoming NPAs, methods of management of NPAs and make suggestions to overcome the problems of NPAs in SFCs.

Rationale of Study

Financial institutions play a key role in the economy. They are tool to control supply and circulation of funds which is life and blood of the economy. However, increase in NPAs has led some financial institutions to the stage of precarious health. The NPAs seem to be number one culprit which is drawing the financial institutions towards the whirlpool of financial black hole. There is a worldwide economic recession which has developed a liquidity crunch among the entrepreneurs resulting into adversely affecting their repayment capacity of dues. This in the other way has limited recycling of funds and also shattered the economy. The NPA management therefore, becomes a matter of grave concern.

Scope of Study

The proposed research work derives from the current overriding emphasis on NPA management in financial institutions. The present thesis proposes to study the factors leading to increase in NPAs, methods for management in NPAs and theoretical position based on statistical data associated with it. The research will bring out the methods / strategies that should be adopted for recovery of dues from NPAs, prevention for assets converting into NPAs and elevation of health code category of NPAs to Standard assets. The scope of study will cover the overall performance of selected SFCs i.e. APSFC, RFC, DFC and all attempts will be made to find out the impact of NPAs on the overall economic and industrial scenario and survival of the SFCs as well. The study shall also bring out methods on which attention should be focused so that NPAs may be reduced and the SFCs may also survive well.

Hypothesis

The SFCs have been set up for Industrialization of respective states. The public money is involved. Almost in all the SFCs, more or less, the NPA management is not good and the NPAs are increasing which have deterious effect in the following ways:

- They erode current profits through higher provisioning requirements;
- They result in reduced interest income;
- They limit recycling of funds;
- They decline the ability to meet out administrative expenditure, payment to outside agencies from where loans and advances were taken including SIDBI;
- There is an erosion of capital resources;
- NPAs reduce the return on assets and return on equity;
- NPAs lead to industrial sickness which aggravates the problem of unemployment.

More effort is required in maintaining advances in performing rather than sanctioning those. In other words, more monitoring and supervision is required after sanctioning facilities.

NPAs : A Major Disease for Indian Financial Sector

Size of NPAs in physical and percentage terms always remain in controversy but there is unanimity about the facts that it exists in sizeable proportion. The controversy in determining the NPAs is more pronounced in respect of sick units under recovery as RBI norms permit leverage to banks to put the loan funds of these units as standard assets in the beginning. Another controversial area is the practice of 'evergreening NPAs' , that is rescheduling the repayment programmes for NPAs and to reclassify them as a standard asset. Such rescheduling is based on better cash flow in future, default in the past due to certain exogenous reasons etc., however, banks are using this clause with blind eyes as a matter of routine they are evergreening bad loans of almost all the defaulters, which matters to them. They are using 'evergreening' as additional lending opportunity to the bad payers. We can name few of the many banks which fall to prey of NPAs - Global Trust Bank, Krushi Bank, Banares State Bank, UCO Bank, Union Bank of India, Allahabad Bank, Madhavpura Bank are few of them. The department of Economic Affairs of the Government of India declared in September, 2001 that 95 co-operative banks were unable to pay even their deposit insurance premium for the last three years, is not the hidden hand of NPAs responsible? If we look at the sorry state some of our important financial institutions and banks individually we find that NPAs of IDBI is at threatening level of 14 per cent of its total assets, one out of every 7 rupee lent out by IDBI to companies may not be repaid unless the NPA problem is sorted out. There is also fear that ICICI loan portfolio is also contaminated. ICICI may also be closed to bankruptcy if we believe certain reports.

The huge losses to financial institutions and banks is making a deep dent in the economy. There must be something really wrong with the system which is causing this disease. If we analyze the pattern of NPAs we find that major culprit responsible for the gravity of this situation are not small defaulters but the large business houses with even larger repute. Sometimes it is an entire sector that has gone sour. The entire financial sector made advances of an estimated Rs. 30,000 crore to the steel industry alone, which can be termed as doubtful. For instance, take the classic case of Rajinder Steel industry, where the entire banking system failed to monitor their advances. The company owes Rs. 362 crores to more than 15 banks and financial institutions including IFCI, ICICI and Canara Bank. The company started in late 1998 and by early 1999 the promoters had enacted vanishing act. It is inexplicable that the bank’s books showed this amount as bad loans only in the year 2000 and classified as doubtful. Other finer metaphors for the ills that is eating away financial sector like Usha Group (Rs. 1200 crore), Parasampura Synthetics (Rs. 563 crore), Flex Industries (Rs. 700 crore), Patheja Stamping and Forgings (Rs. 400 crore) and Malvika Steels (Rs. 1300 crore), they are ’a few’ of them. Some individuals can also take credit for increasing the NPA burden, late Harshad Mehta (Rs. 812 crore), Ketan Pareekh (Rs. 1100 crore).

Document published by All India Bank Employees Association (AIBEA) has provided the names of 1,300 troubed corporate loans account which includes - Lloyds Finance, Onida Savak, Enkay Texofood, Pentafour Products, J.K. Synthetics and Garware Nylon. To quote the secretary of AIBEA, "there is today no Indian corporate house that has not contributed to the NPA problem". He may be exaggerating to some extent but not entirely far away from the truth. It is peculiar that banks and financial institutions claiming to be in very good health suddenly found themselves on the brink of collapse. How does a thing like that happens unless there is the balance sheet in the first place. Does not this point unmistakably towards unreliability of our bankers and banking system?

There are certain maladies which are causing the trouble of NPAs. We can put our finger on the clause of ’secrecy’ in the Banking Regulation Act. This clause of secrecy is used as garb by the bankers, which says that the debtors and the creditors relationship is confidential. This legal cloak bars the banks to reveal the names of defaulters. Same clause exists for financial institutions and banks which are governed by their own act. It helps the debtors immensely as they took loans from the banks without any fear of their names coming in notice of other banks whom they are planning to dupe in future. Banks, also can not verify the credibility of their defaulters. There are several instances where defaulters were given fresh loans on easier and smoother terms and conditions on the excuse of their revival (doubtful), under ’evergreening’ as mentioned above. There is real concern that the banks and financial institutions are throwing good money after bad, steel sector is masterpiece example of it. It necessitates us to think about the number of bad loan accounts that must have been kept well hidden under the veil of secrecy that allows the banks and financial institutions to divulge minimal information to the public.

Conclusion

In the present scenario the role of government and the RBI becomes more important. Though government is trying to focus its attention towards the problem but lots have to be done. RBI mostly restricts its activities to micro management of credit of PSB’s with this background; It comes as no surprise Indian financial institutions are not thinking strategically and certainly not for an international role. The lack of seriousness of the government and the financial institutions regarding NPA can be seen through the working of ’Debt Recovery Tribunals’ (DRTs), which were set up specially to help banks for loan recovery. Here too, secrecy takes the upper hand, as details about the suit filed by the banks against consumers are available only to the parties to the dispute, not any one else, not even to the depositors or shareholders of the bank, whose money the bank has used, rather misused. The legal procedure too, is painfully slow as the number of DRTs is very small. For example, in Jaipur, there is already one and the cases pending are in big numbers. Further, DRTs are supposed to decide a case within 6 months but average time taken is 8-18 months.

Other step which is taken by the government to straighten the working of the banks is amendment to Section 36(1)(vii) of the Income Tax Act in the finance bill is causing tremors down the banking structure. The amendment prevents all companies for claiming provisions for bad debs as deducible from taxable income unless the debt is actually written off. Banks are bound to be adversely affected by this amendment because they have to make provision much above the minimum prudential level prescribed by RBI as desirable practice. Now banks have to be aggressive in their policies and efforts for recovery of loans whether the asset is provided for or written off under the Section 36(1)(vii). The other financial institutions including SFCs also need to make strenuous efforts for recovery of loan. The restructuring of financial sector certainly calls for tough and quick decisions failing which revival may never take place. Apart from DRTs other avenues for loan recovery should be strengthened viz. The Settlement Advisory Committee of financial institutions, Ombudsman's role can be given due respect as an arbitrator. Legal clause of secrecy in debtor relationship should be reconsidered in present situation. The need of the time is complete disclosure and absolute transparency which alone can save the Indian financial system from crumbling to some extent.

References

- Anatomy of NPAs of commercial banks, Applied Finance (2000) - R. Satyanarayan and S. Ganti
- Banking Systems Around the Globe (2000) - Barth J.R., Caprio, G. and Levine
- Enforcement Rights of State Financial Corporations (1992) - S.S.Saxena & Bodhraj Kishore (Aalekh Publishers, Jaipur)
- Hand Book on Project Appraisal and follow up (A practical guide) (1996). - D.P. Sarda (Govind Prakashan, Jaipur)
- Indian Banking in Transition : Issues and Challenges (2000) - T. Ravi Kumar (Vision Books Pvt. Ltd.).
- Indian Financial Sector Reforms and Monetary policies linkaged (1996) - (Ganti Subramanyam)
- Ownership Structure and Financial Performance (1997) - Jinesh N Panchali and Neerav Desai
- Small Banks in India's Deregulated Environment (1996) - Ganti Subramanyam
- The length and cost of banking crises, IMF Working Paper (1999) - Frydl E.J.

◆■◆