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A Study of Non-Performing Assets of Commercial Banks in India

Abstract

Public sector Banks, Private sector Banks and Foreign Banks in India play vital role in economic development of country. Management of NPA's has been considered as one of the major criteria of Commercial Banks in India. For this purpose F test one way ANOVA has been used to compare the trends of percentage of Gross NPA's and Net NPA's of Public Sector Banks Private Sector Banks and Foreign Banks in India. Non- performing assets is a central matter in this study because it have not only affected the productivity and the profitability of Banks. The study is limited to the period of five years, i.e. From 2013 to 2017. The study is based on secondary data collected from RBI reports on trends and progress of banking in India. The objective of the study is to find out equal or unequal ratio of Gross NPA's and Net NPA's of Public Sector Banks, Private Sector Banks and Foreign Banks in India.

Chirag P. Surti
Faculty Member
Deptt.of Accounting and Financial Management,
The Maharaja Sayajirao University of Baroda,
Vadodara, Gujarat

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Introduction

Commercial Banks are playing a positive role in an economic development of a country as depositories of community's saving and as purveyors of credit. Commercial Banks provide a short term and medium term financial assistance. The short term credit facilities are granted for working capital requirements. The medium term loans are for the acquisition of land, construction of factory premises and the purchase of machinery and equipments. Commercial Banks include Indian Banks and 44 Foreign Banks in India. Indian Banks include 27 Public Sector Banks and 22 Private Sector Banks. Public Sector Banks by their nature are Government owned Banks and therefore their banking obligations have to be focused on the Government economic programme. Private Sector Commercial Banks incorporated as Joint Stock companies. Private Sector Commercial Banks are required to meet the priority sector lending targets fixed by RBI. The Foreign Banks are branches of Banks incorporated outside India. Foreign Banks in India are concentrated in metropolitan centres', certain state capitals and other important cities and thus they are aloof from the National Development programs. They are also engaged in the financing of export and imports. Normally, these Foreign Banks do not encourage mass Banking and rather cater to the elite of the society since the cost of their services is comparatively high.

Review of Literature

RBI issued descriptive circulars and guideline. Most of daily, weekly, fortnightly and monthly publication carried an article in bold form giving special importance in above issues. Therefore, IBA bulletins, RBI guideline, PSB's handbook and extract from various seminars on the subject to literature review. There are many research performed on the subject of Management of Non-Performing Assets in Public Sector Banks, Private Sector Banks and Foreign Banks in India. Following are the review of few literatures about the NPA management conducted for Banks in India.

Ashly Lynn Joseph & Dr. M. Prakash (2014), In the article tilted "Study on Analyzing the Trend of NPA Level in Private Sector Banks and Public Sector Banks" the author had concluded that NPAs are depleting the capital of the Banks and debilitating their budgetary quality. It is likewise as much a political and a financial issue. The Banks and money related organizations ought to be more proactive to embrace a down to earth and organized non performing assets administration strategy where avoidance of non execution resources gets need. Contrasted with Private Sector Banks, Public Sector Bank is more in the NPA level. This Public Sector

Banks must take more care in diversion any record getting to be NPA by taking legitimate preventive measures in a proficient way.

Hemavathy Ramasubbian and Arunkumar Thangavelu (2015) In the article titled "Forecasting the Trends of NPAs in Indian Banking Sector" the author had concluded that there is noteworthy change in the administration of nonperforming resources of the Foreign Banks and Private Banks in India. The examination at long last watches that the prudential and provisioning standards and different activities taken by the administrative bodies has pressurized banks to enhance their performance and consequently came about into trim down of NPA and in addition change in the financial health of the Indian banking sector. Public, Private Banks and planned business Banks require pressurize more in administration of NPAs.

Vivek Rajbahadur Singh (2016), The Non-Performing Assets have always created a big problem for the banks in India. It is just not only problem for the banks but for the economy too. The money locked up in NPAs has a direct impact on profitability of the bank as Indian banks are highly dependent on income from interest on funds lent. This study shows that extent of NPA is comparatively very high in public sectors banks. Although various steps have been taken by government to reduce the NPAs but still a lot needs to be done to curb this problem. The NPAs level of our banks is still high as compared to the foreign banks. It is not at all possible to have zero NPAs. The bank management should speed up the recovery process. The problem of recovery is not with small borrowers but with large borrowers and a strict policy should be followed for solving this problem. The government should also make more provisions for faster settlement of pending cases and also it should reduce the mandatory lending to priority sector as this is the major problem creating area. So the problem of NPA needs lots of serious efforts otherwise NPAs will keep killing the profitability of banks which is not good for the growing Indian economy at all.

Abhani Dhara K (2017), In the article titled "Empirical study of impact of NPA over the profitability of leading private sector banks" the author had concluded that one can state that there is consistently an huge effect of NPA over the profit of the banking sector. NPA demonstrates the general execution of managing an account part. It is one of the major issue of the banks now a days. It is frequently difficult to influence the NPA to proportion to the zero, yet it is defiantly conceivable to diminish the NPA proportion. It just requires legitimate administration, enough pre alerts and convenient follow up of credit reimbursement from customers of the Bank.

Objectives of The Study

1. To understand the concept of Non Performing Assets in Banks.
2. To evaluate the Public Public Sector Banks , Private Sector Banks and Foreign Banks in India with respect to their credit competence.
3. To analyse percentage growth in both Gross NPA's and Net NPA's with Total Advances in Public Sector Banks, Private Sector Banks and Foreign Banks in India.

Research Methodology

The study considered primary data collected through specially arrange visits with the official and directors Centre for Monitoring Indian Economy (CMIE). Secondary data collected from the annual report and website of Central Bank (RBI) and from literature review.

Duration of Study

The paper discusses management of non-performing assets of Public Sector Banks, Private Sector Banks and Foreign Banks in India for the period from 2012-13 to 2016-17.

Concept of Non-Performing Assets

This income recognition norms and assets classification with provisioning norms made balance sheet structure of PSB's so transparent and clear at par with international practices, that global financial organisation got attracted towards Indian Banks in particular and emerging market in general. The Public Sector Banks represent the backbone of the Indian financial system and have admirably managed where key financial indicators compete with the global benchmark standard and hence such status being a fresh with growth in the Indian economy, provide a very interesting challenges to go into the changing scenario of efficient assets management on one hand fulfilment of capital adequacy on the other hand.

Prudential Norms

1 Income recognition
2 Assets Classification
3 Provisioning norms for bad debts

Performing Asset

Performing assets are advances which generates income to the Bank by way of interest and other charges.

Non- performing Asset

Non- performing Asset is that deployment of the Bank's funds which is not earning any income / return for Bank and funds deployed also become illiquid.

Income Recognition

A Bank's advances are to be classified into performing and non performing assets (NPA). The international practice is not to consider the interest income from NPA on accrual basis but to consider such income as and when it is actually received. The RBI issued a detailed guideline to Banks regarding classification of advances between performing and non performing assets which have been revised from time to time. The latest guideline for determining the status of credit facilities are discussed below:

1 Interest and or instalment of principal remains overdue for a period of more than 90 days in respect of the term loan,
2 The account remains out of order for a period of more than 90 days, in respect of an overdraft / cash credits (OD/CC),
3 The bills remain overdue for a period of more than 90 days in the case of bills purchased and discounted,

In case of direct agricultural advances, the following guidelines are applicable for classifying an account as an NPA.

1 A loan granted for the short duration crop will be treated as NPA, if the instalment of principal or interest thereon remains overdue for two crop seasons.
2 A loan granted for long duration crop will be treated as NPA, if the instalment of principal or interest thereon remains overdue for one crop season.
3 Any amount to be received that remains overdue for a period of more than 90 days in respect of any other account will lead to classifying that account as NPA

As a facilitating measure for smooth transition to 90 days norm, Banks have been advised to move over to charging a rate of interest at monthly rates, by April 1, 2002. However, the date of classification of an advance as NPA should not be changed on account of charging of interest at monthly rests. Banks should , therefore continued to classify an account as NPA only if the interest charged during any quarter is not serviced fully within 180 days from the end of the quarter with effect from April 1, 2002 and 90 days from the end of the quarter with effect from March 31, 2004.

Out of Order

An account should be treated as 'Out of Order' if the outstanding balance remain continuously in excess of the sanctioned limit/ drawing limit. In cases where the outstanding balances in the principal operating account are less than the sanctioned limit/ drawing limit , but there are no credits continuously for 90 days as on the date of balance sheet or credits are not enough to cover interest debiting during the same period, these accounts should be treated as 'out of order'.

Overdue

Any amount due to Bank under any credit facility is 'overdue' if it is not paid on the due date fixed by the Bank.

Assets Classification

As per the present guideline of RBI the assets classification and the requisite provisions for doubtful debts is as under.

Banks require classifying the loan assets (advances) into four categories-

1. Standard Assets
2. Sub- standard Assets
3. Doubtful Assets and
4. Loss Assets

Standard Assets

Standard assets are which does not disclose any problem and which does not carry more than normal risk attached to the business. Such assets are considered as performing assets.

Sub-standard Assets

With effect from 31st March 2005, a Sub-standard asset would be one, which has remained NPA for a period less than or equal to 12 months. In such a case, the current net worth of the borrower / guarantor or the current market value of the security charged is not enough to ensure recovery of the dues to the Banks in full. In other words, such an assets will have well defined credit weaknesses that jeopardise the liquidation of the debt and are characterised by the distinct possibility that the Banks will sustain some loss, if deficiencies are not corrected.

Doubtful Assets

With effect from 31st March 2005 an assets would be classified as doubtful if it has remained in the substandard category for a period of 12 months. A loan classified as doubtful has all the weaknesses inherent in assets that were classified as sub-standard, with the added characteristic that the weaknesses make collection or liquidation in full on the basis of currently known facts, conditions and values- highly questionable and improbable.

Loss Assets

A loss asset is one which 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.

Provisions for Doubtful Debts

Strict provisioning norms have been specified in the case of various categories of NPA, via sub- standard assets, doubtful assets and loss assets. In addition to nominal value 0.25% for direct advances to agricultural and SME sector and all other loans and advances at 0.40%. Further, a conservative policy was put in place in respect of loans, which have been either rescheduled or renegotiated. The provision has been extended from credit risk to market risk as well.

The primary responsibility for making adequate provisions for any diminution in the value of loan assets, investment or other assets is that of the Bank management and statutory auditors. The assessment made by the inspecting officer of the RBI is furnished to the Bank to assist the Bank management and statutory auditors in taking a decision in regard to making adequate and necessary provisions in terms of prudential guidelines.

In conformity with the prudential norms, provisions should be made on the Non performing assets on the basis of classifications of assets into prescribed categories mentioned above. Taking into account the time lag between an accounts becoming doubtful of recovery, its recognition as such, the realisation of the security and the erosion over time in the value of security charged to the Bank, the Banks should make provision against different categories of the assets as under.

Loss Assets

The entire amount should be written off or full provision should be made for the amount outstanding

Doubtful Assets

1. Full provision to the extent of the unsecured portion should be made. In doing so, the realisable value of the security available to the Bank should be determined on a realistic basis.

Deposit Insurance and Credit Guarantee Corporation/ Export Credit Guarantee Corporation of India (DICGC/ECGC) cover is also taken into account. In case of the advance covered by Credit Guarantee Fund Trust for Small Industries (CGTSI) guarantee becomes non- performing, no provision need be made towards the guaranteed portion. The amount outstanding in excess of the guaranteed portion should be provided for as per the extent guidelines on provisioning for NPA.

2. Additionally, 20% - 100% of the secured portion should be provided for depending upon the period for which the advances have been considered as doubtful assets, as follow
-Up to one year 20% provision but one year to three years 30% provision and more than three years 100% provision should be made.

Sub- Standard Assets

A general provision of 10% on total outstanding should be made without making any allowances for DICGC/ECGC cover and securities available. An additional provision of 10% (i.e. total 20% of the total outstanding) is required to be made on 'unsecured exposure' of loan. Generally, such a situation may arise in case of personal and education loans etc. Unsecured exposure is defined as an exposure where the realisable value of the security is not more than 10% of the outstanding exposure. Security should not include guarantees, comfort letters etc.

Standard Assets

With effect from 15- November -2008, the provisioning norms for standard assets amended. It has been clarified that the provision should be made on the global portfolio basis and not on domestic advances alone.So direct advances to agricultural and SME sector at 0.25% and all other loans and advances at 0.40%.

Reasons for Mounting NPA's

The various causes that make an asset NPA can be classified into two categories like internal causes and external causes.

External Causes

1. Natural calamity leading to destruction of assets
2. Recession in the industry
3. Closure of factory due to strikes, court orders
4. Adverse Government policy guideline affecting the production, marketing sales of the product (Ex Import duties)
5. Adverse change in the projected demand due to factors like environmental regulation, change of fashion, change in consumer needs etc.

Internal Causes

Management

1. Fraudulence of partners, directors, proprietor etc.
2. Will full default, Dispute among partners and directors.
3. Lack of proper organizational set up and control

Marketing

1. Scarce product base
2. Lack of distribution channels
3. Irregular delivery
4. Unsuitable pricing

Financing

1. Lack of resources, Costly outside borrowing
2. Diversion of funds for unproductive expenditure
3. Faulty costing and pricing, Increased cost of production

Production

1. Inappropriate technology
2. Poor labour productivity
3. Poor quality control
4. Lack of production planning and control
5. Inferior quality of finished goods
6. Frequent machine breakdowns

Other Causes

1. Liberalisation of the economy
2. Poor monitoring of credit and stoppage to identify before time caution indication by standard assets.
3. Unexpected rolling of capital markets and stoppage to increase sufficient finance.
4. Granting of credit for various segments on the basis of Government orders

Research Hypothesis

To achieve the above objectives, following hypothesis are formulated and tested on the basis of "F" Test

H0

Null Hypothesis

Public Sector Banks, Private Sector Banks and Foreign Banks in India have equal (No different) in % of GNPA to Total Advances.

H1

Alternative Hypothesis

Public Sector Banks, Private Sector Banks and Foreign Banks in India have unequal (different) in % of GNPA to Total Advances.

Table: 1. Percentage of Gross Non Performing Assets to Total Advances

Year	Public Sector Banks (% of GNPA)	Private Sector Banks (% of GNPA)	Foreign Banks (% of GNPA)
2013	3.72	1.84	3.02
2014	4.45	1.82	3.97
2015	5.08	2.10	3.30
2016	9.65	2.92	4.34
2017	12.32	4.21	4.61
Total	35.22	12.89	19.24
Average	7.04	2.58	3.85

(Source : www.iba.org.in)

F Test One way ANOVA

Source	Bracket	Sum of Square	Degree of Freedom	Mean Square	F.c	F.t
Between Group	A= 355.354	52.9525	02	26.4763	5.10	3.89
Within Group	Y= 417.5697	62.2157	12	5.184		
Total	T= 302.4015	115.1682	14	31.6609		

Findings

F Test shows that the calculated value of F= 5.10 and table value of F= 3.89 (2,14) at 5% level of significance. Here calculated value of F is more or greater than the table value of F. So H0 null hypothesis has been rejected and alternative hypothesis has been accepted. It means that Public Sector Banks, Private Sector Banks, Foreign Banks in India have unequal (Different) GNPA to Total advance ratio.

H0

Null Hypothesis

Public Sector Banks, Private Sector Banks and Foreign Banks in India have equal (No different) in % of NNPA to Total Advances.

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Alternative Hypothesis

Public Sector Banks, Private Sector Banks and Foreign Banks in India have unequal (different) in % of NNPA to Total Advances.

Table: 2 Percentages of Net Non Performing Assets to Total Advances

Year	Public Sector Banks (% of NNPA)	Private Sector Banks (% of NNPA)	Foreign Banks (% of NNPA)
2013	2.01	0.52	1.00
2014	2.56	0.66	1.08
2015	2.92	0.86	0.54
2016	5.73	1.39	0.76
2017	6.89	2.21	0.71
Total	20.11	5.64	4.09
Average	4.02	1.13	0.82
(**Source :** www.iba.org.in)			

F Test One way ANOVA

Source	Bracket	Sum of Square	Degree of Freedom	Mean Square	F.c	F.t
Between Group	A= 90.59	31.2283	02	15.6142	9.07	3.89
Within Group	Y= 111.2266	20.6366	12	1.7197		
Total	T= 59.3617	51.8649	14	17.2339		

Findings

F Test shows that the calculated value of F= 9.07 and table value of F= 3.89 (2,14) at 5% level of significance. Here calculated value of F is more or greater than the table value of F. So H0 null hypothesis has been rejected and alternative hypothesis has been accepted. It means that Public Sector Banks, Private Sector Banks, Foreign Banks in India have unequal (Different) NNPA to Total advance ratio.

Conclusion

From the above analysis it is observed that average percentage of Gross NPA to Total Advances of Public Sector Banks is very high (7.04%) but moderate in case of Foreign Banks (3.85%) and very less in case of Private Sector Banks (2.58%) which shows that percentage of GNPA to Total Advance ratio of Public Sector Banks, Private Sector Banks, Foreign Banks in India have unequal (Different)

Similarly from the above analysis it is observed that average percentage of Net NPA to Total Advances of Public Sector Banks is very high (4.02%) but moderate in case of Private Sector Banks (1.12%) and very less in case of Foreign Banks (0.82%) which shows that percentage of NNPA to Total Advance ratio of Public Sector Banks, Private Sector Banks, Foreign Banks in India have unequal (Different)

Suggestions

1. All borrowed funds should be so deployed remuneratively so that the cost of funds and service cost for such deployments of funds is fully recovered from the utilisation of such borrowed funds and not only that but even a reasonable margin should remain available to Bank. In simple words if deployments of borrowed fund do not service its entire cost then shortfall together with repayment instalment must be provided and such provision should be critically carried out in statutory audit every year.
2. After compliance of all statutory requirements the surplus funds must find. Such investments whose rate of return should outperform similar investment make by other financial organisation. This should be however a comparable exercise to monitor profits of the Banks and no provision would be necessary unless principal amount of investment get eroded on market to market basis.
3. Banks intangible assets such as overdue outstanding balances in suspense account and claims made against the Banks or Banks claim on other remaining in dispute should be provided 100%
4. Banks investment in fixed assets must be critically assessed in terms of utilisation of such assets and its corresponding value to determine fair cost absorb by the Bank for investment made in such fixed assets. Illustratively if Bank has acquired a premises of 5000 sq ft involving total cost of Rs.50 lacs and if that premises after being ready for use, is either not utilise or underutilise then the difference between the cost of funds invested in the premises and income that would have been generated from utilisation of such premises, the difference there to should be provided. Such an exercise will compel Bank management to take a prudent care either in liquidating the non remunerative fixed assets or profitability utilised fixed assets for more income generation

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