

# Rising Non-Performing Assets in Indian Banking System with Special Reference to Punjab National Bank: A Case Study



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## Abstract

Banking sector is playing important role in the development of Indian economy by creating credit in various forms as loans and advances, cash credits. Non-performing assets (NPA) means credit provided by banks which doesn't come back to the banks. Now days the increasing NPA has become the burning issue in banking sector. This problem is more critical in nationalized banks. Non-performing assets is one of the major challenges facing by banks. This paper analysis the problem of rising non-performing assets in Indian banking system and highlights the impacts of NPA on Indian economy. It also discusses the reasons of increasing NPA and challenges faced by banks regarding non-performing assets and how the banks will manage the NPA.

**Keywords:** Banks, Non Performing Assets, Indian Banking System, Indian Economy, PNB.

## Introduction

Banking system is considered as the life of every country's economy. Banks are playing important role for the development of any economy by creating cash credits. The main function of bank is to mobilize the public deposits and lending to the existing business as well as the new entrepreneurs for the development of the industrial and economic progress. When banks provide credits and it turns into bad debts is known as non-performing assets. It means a loan that is not meeting its stated principal and interest payments. NPA do not generate any income. Interest is not received regularly on NPA.

According to RBI guidelines an Assets has been classified by a bank as sub standard, doubtful or loss assets. When bank loan remained due less than or equal to 12 months it is known as substandard assets. When bank loan remained due 12 months it will be considered as doubtful assets. Loss Asset means a loan asset where the loss has been identified but the amount has not been fully written off. When the interest and principle amount of the bank remains unpaid for more than 90 days, the loan automatically turns as NPA. The account remains 'out of order' for a period of more than 90 days in respect of an overdraft/ cash credit. If bills are purchased or discounted then the bills remains overdue for a period of more than 90 days.

Indian banks are seriously affected by NPA. Non-performing assets affect the liquidity, profitability and quality assets of the banks. Recent days there is increasing tendency of NPAs. Around Rs. 7 Lakh crore worth loans are classified as NPA in India. This worst performance is not a good sign. In 2008 NPA affected the banks of United states of America. In public sector banks, the bad health of banks means a bad return to shareholder which means that government gets less money as a dividend. Therefore it may impact easy deployment of money for social and infrastructure development and results increases of social and political cost.

Several steps have been undertaken by the RBI and the government of India to reduce the trends of NPA in Indian banks, but these steps are not enough to reduce NPA. Most of banks are suffering the problem of NPA. The reports and review of literature reveals that increasing NPA affect the efficiency of the bank. After Liberalisation of the economy the banking sector has faced severer challenges, So NPA must to be controlled and reduced. Restructuring norms are being misused. The main reasons behind NPA is default by borrowers, economic conditions, no proper risk management, speculations, business cycle, miss-management

by the bank officials for the recovery of the loans, inadequate legal provisions, changes in economic policies, non transparent accounting policy and poor auditing practices, lack of coordination between banks and financial institution. Many times the borrowers divert the funds to the other purposes also proper actions were not taken for the recovery of loan. During the time of economic boom, overt optimism shown by corporates was taken on face value by banks and adequate background check was not done in advancing loan increased the trends of NPA. Economic Survey 2015 mentioned over leveraging by corporate as one of the reasons behind rising NPA.

#### **Objectives of the Study**

1. To study the problems of rising Non-Performing Assets in banking system.
2. To know the steps taken for the recovery of NPA.
3. To measure the trend of NPA of PNB in during the last ten years.
4. To analyses the total advances, net profits, gross NPA & net NPA. of PNB
5. To suggest channel to manage NPAs in PNB.

#### **Research Methodology**

The main objective is to study the role of non-performing asset and its impact on Indian banking system with the special reference to Punjab national bank. The research design is descriptive research design. The data has been mainly collected from RBI annual reports and Punjab national bank annual reports and websites. This study covers a period of ten year data from 2008-09 to 2017-18. We use Gross NPA, Net NPA, Net profit and Advances for analyses the data. Hypothesis for this research is  $H_0 = 0$  There is no impact of NPA on Net profit of PNB.  $H_1 \neq 0$  : There is impact of NPA on net profit on PNB. The study is based on the secondary data which are collected from various published sources like annual reports, magazines, journals and websites. This study is quantitative in nature.

#### **Review of Literature**

Ganesan and Santhanakrishnan (2013) analysed that the sound financial position of a bank depends on the recovery of credits and the level of Non-performing Assets (NPAs). The NPAs level of our banks is high when contrasted with the outside bank. K.T.Srinivas (2013) analysed that at present NPA is burning issue in commercial banks as well as nationalized banks. The main objective of this study is to find out the general reasons of Non-performing assets. He also focused that by proper monitoring, a bank can controlled the problem of increasing NPA of banks.

Samir, Karma Deepa (2013) analysed that the profitability, liquidity and solvency of the banks are adversely affected by the status of Non-performing assets. In this paper an analysis of the position of NPAs in selected banks namely State Bank of India (SBI), the Punjab National Bank (PNB) and Central Bank of India (CBI). Narula Sonia, Singla Monika (2014) analysed that Non-performing assets is an important parameter in the analysis of financial performance of a bank. The objective of this study is to compare the total advances, net profit, Net NPA of PNB and the impact of NPA on banks. In this study

correlation between Net profit and Net NPA was calculated.

Dr. Rajesh Rathore (2016) focused the impact of NPA on Indian banking industry. He also presented classification and reasons of NPA also presented the increasing trends and high volume of NPA.

Goyal and Piyush (2017) analysed the non-performing assets, net NPAs, net NPAs of 8 banks in India and to see the connection between net benefit, net NPAs also and gross NPAs.

Suvitha K. Vikram, and Gayathri G. (2018) focused the effects of NPA on Indian banking system.

#### **Problem of rising NPA in Indian Banking System**

Non-Performing Assets affects Indian banking system. The NPAs do not generate any interest income for banks and on the other side banks are bound to provide provisions for NPAs from current profits, that's why the efficiency is also affected. Banks are providing around 25% to 30% additional provision on incremental NPAs which has direct affects on the profitability of the banks. In developing countries like India NPAs are one of the biggest problem for socio-economic growth. The high level of NPAs affects the profitability and liquidity of banks. So, banks are required to make effort to strong their risk management system and internal control. The high level of NPAs affects the banking operations by decreasing the return on investment, decline in interest income, increasing the cost of capital, declines the capital adequacy ratio and reduces the recycling of funds.

The huge amount of NPA will increase the high risk also it affects adversely the profits of the banks. Due to NPA, money stock and liquidity of banks will reduce and also banks will not provide credits to good projects. Many times banks may begin charging higher interest rates. Due to mismatch of assets and liabilities the economic value addition of banks gets disturbed. The former RBI governor Dr. Raghuram Rajan said that banks have to improve the efficiency of the recovery system. Recovery should be focused on efficiency and fairness. Some banks lend to higher risk customers than others and therefore tend to have a higher proportion of NPA but will make up for this by charging borrowers higher interest rates, increasing spreads.

Many times promoters were very optimistic in setting up large projects. Mostly projects were expecting that loans would be arranged from the capital markets which were booming at the time of the project appraisal. When the capital markets crashed, the requisite funds could never be raised, promoter often lost interest and lenders were left stranded with incomplete projects. Some borrowers were undercapitalized and over burdened with debt to absorb the changing economic situation in the country. Higher NPA ratio affects the confidence of investors, depositors, lenders etc. because as per guidelines of RBI, banks whose Net NPA is 5% and above are required to take permission to declare the dividend.

The non-recovery of loans affects not only availability of credit but also financial soundness of the banks. It affects the credibility and performance of banking system. NPA impact some financial ratio like return on assets, profitability ratio, dividend payout ratio, provision coverage ratio.

#### **Impact of NPA on Indian Economy**

The development of the economy depends upon the effectiveness and firmness of the banking sector. Banking sector is one of the most important base for strong economy because it channels the savings into the investment. NPA affects not only banking system but also Indian economy and economic growth because banks provide the credit facility to various sectors like infrastructure, textile, metals, telecom, and engineering. These sectors are contributing for the development of Indian growth and increasing Indian economy. The recent trend of NPA percentage in infrastructure is 32.80%, textile 6.90%, metals 13.6%, food processing 5.3%, telecom 1.33%, engineering 5.30%.

Increasing trend in various sectors slow down the economy. After post demonetization it was stated that profitability of the manufacturing sector was reduced. The shortage of funds affects the growth of the industrial sector. Industrial sector is one of the most important sector in economy which affect the growth of other sectors. Food processing is most employment intensive industry and its growth also

pushes the growth of agriculture. Other sectors will also affect the economic scenario due to huge amount of NPA.

Increase of NPA will increase inflation and decline GDP. NPA is the indicator to assess the soundness of economic growth. It reduces the lending capacity of bank and it adversely affect the economic productivity. Even the domestic business cannot survive without credit facility. This result in negative balance of trade and large unemployment. So there is a need to reduce the NPA trends. The reduction of NPA will increase the Indian economy and economic growth.

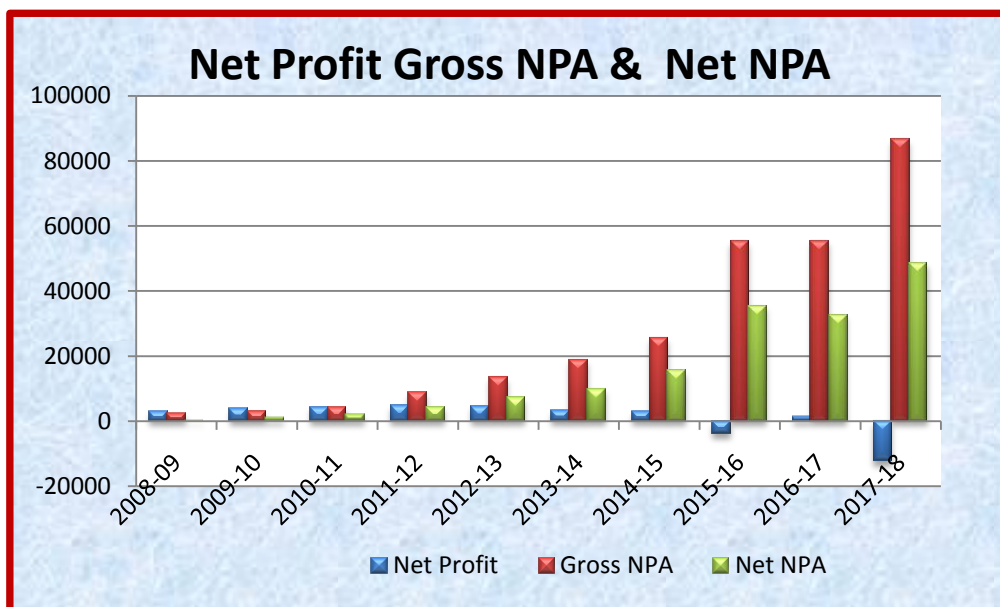
#### **Analysis of NPA in Punjab National Bank**

Punjab national bank is playing important role for the development of the country and economic growth. The Bank has the second largest branch network amongst public sector banks with 6983 domestic branches. But the large percentage of NPA has a harmful impact on the performance of a bank. There are two NPA. Gross NPA is advance which is considered irrecoverable, for which bank has made provisions, and which is still held in bank's books of accounts. Net NPA is obtained by deducting items like interest due but not recovered, part payment received and kept in suspense account from gross NPA. The following table is showing total advances, net profit, gross NPA and Net NPA.

**Table 1 Total Advances, Net profit, Gross NPA, Net NPA**

Years	Total Advances	Net Profit	Gross NPA	Gross NPA %	Net NPA	Net NPA %
2008-09	154703	3091	2506	1.62%	264	0.17%
2009-10	186601	3905	3214	1.71%	982	0.53%
2010-11	242107	4433	4379	1.79%	2039	0.85%
2011-12	293775	4884	8720	2.93%	4454	1.52%
2012-13	308796	4748	13466	4.27%	7237	2.35%
2013-14	349269	3343	18880	5.25%	9917	2.85%
2014-15	380534	3062	25695	6.55%	15397	4.06%
2015-16	412326	-3974	55318	12.90%	35423	8.61%
2016-17	419493	1325	55370	12.53%	32702	7.81%
2017-18	433735	-12283	86620	18.38%	48684	11.24%

**Source:** Annual Reports of PNB



It was analysed by taking ten years data that the trends of NPA in PNB is in the increasing manner the gross NPA in 2008-09 was only 1.62%. It continuous increase and in the year of 2017-18 the gross NPA stands at 18.38%. The Net NPA in 2008-19 was .17% and in the year 2017-18 it stands 11.24%. In the year of 2017-18 the PNB suffered the loss of 12283 crore. Recently one scam was found in PNB, Nirav Modi, a luxury diamond jewellery designer, who had done the scam of Rs. 14357 crore in June 2017 with PNB bank. Letter of credit was granted by bank and a huge scam took place which affects the profitability of PNB.

After NiravModi scam the PNB has now focus to recover loans and NPA account to prevent further incidents. Above mentioned such cases and performance of NPAs that are rising day by day defines the scenario of banks and growing incidence of NPA in different banking sector. Banks try to recover the amount of credit from their borrowers as much as they are capable of and rest is declared as NPA which causes downfall in the share in market value and goodwill of the banks. So, it is necessary to reduce NPA, in order to maintain a better position and working of the banks. NPA also affect the image of a bank because the customer do not prefer to do transaction with a bank which has huge amount of NPA.

**Suggestions**

After analysing the PNB status on NPA it was found that banks should take some steps for reducing the NPA. The loan sanctioning process of banks should be strong. Banks should check the financial statement and history of promoters. Banks are required to maintain proper capital on risk assets. The bank should prepare a loan recovery policy for reducing NPA. The advances provided by bank should be given after pre-sanctioning evaluation and post-disbursement control for reducing NPA. The bank should create special recovery cells. NPA

should be reduced by proper selection of borrowers & clients.

There is a need to give proper and skilful manpower to the branches for NPA management. The employees looking after NPA management should be experienced, well qualified and trained so that they can understand the problems of recovery and deal with them effectively. To reduce the NPA, Government of India and RBI are announcing one time settlement schemes. In this system when the borrowers are farmers, small entrepreneurs etc and they are finding difficulty to pay their dues for various reasons however, they have the inclination to repay their debts to the banks, this type of action or scheme is very much helpful to the borrowers and the lending institutions.

Bank should give some incentive to the loyal customers also banks should coordinates with borrowers, NGO and social organizations for identifying the proper borrowers. Some steps taken by RBI when Nirav Modi scam was identified like Restructured standard account provisioning has been increased to 5% making it easier for banks to go for restructuring. On the other side, this has the potential to enhance tendency of ever greening of loans. RBI has directed banks to give loans by looking at CIBIL score. RBI has directed banks to report to Central Repository of Information on Large Credit (CRILC) when principle/interest payment not paid between 61-90 days.

The transformation exercise “Mission Parivartan” launched in June 2017, highlights ten key focus areas for enhanced efficiency, profitability and productivity that preserve the main strength and encourage progress. “Mission Parivartan” serves as a guidepost for the bank to remain focused on the critical aspects that would fuel growth and help drive more profitable business through wider reach and sharper execution. RBI permitted the bank to make provision against this fraud @ 25% without debiting

other reserves and provide remaining amount during the first three quarters of the ensuing financial year.

As soon as the fraud was detected the bank took immediate corrective action as required. Bank organized MeghaRinMuktiShivirs to the recovery of loans in small advances. Concept of recovery champions has been introduced to felicitate the outstanding in the field of recoveries in NPA accounts during each month or quarter or year. As per RBI guidelines notices were issued to various borrowers identified as wilful defaulters. This exercise resulted in declaration of 1089 wilful defaulters as on 31<sup>st</sup> march 2018. For resolution of high NPA post sanction monitoring tool will be integrated for effective utilization at all levels so that weaknesses of borrowed accounts are captured timely.

#### Conclusion

In this paper we analyse the impact of NPA on Indian banking system and Indian economy. In this paper Hypothesis is  $H_0 = 0$  There is no impact of NPA on Net profit of PNB.  $H_1 \neq 0$  :There is impact of NPA on net profit on PNB. So by the analysis of Net profit, Gross NPA and Net NPA we can say the hypothesis  $H_0$  was rejected and  $H_1$  is accepted. There is need to bring more transparency in the system and list of all the defaulters whose loans have been written off by the bank should be made public.

A committee has to be constituted to finalize recovery process in case of loan given to big corporate houses by various banks need to recognise stress in their portfolio early and classify them into special mention account depending on the period of repayment delay. The government has given rights to the banks to take commercial decision without any interference from the government SARFAESI Act. There is a need for decisive changes in the banking structure to enable it to grow in size, resources efficiency and inclusivity. If the banks follow efficient monetary mechanism and controlling measures then banks can reduce the NPA level. It should be considered as a primary task by banks.

Competition among banks and with the rest of the financial sector will increase. New banks are proposed to be licensed shortly. Banks should follow guidelines the RBI and the Government have formulated to mitigate NPA problem. Proper monitoring system and risk management system should be developed. Credit data must be shared and large exposures across banks monitored closely.

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