REASONS FOR GROWING NPAs IN THE CURRENT PERSPECTIVE

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Abstracts:

Since 1991, the banking reforms in India have mostly been discussed in terms of the substantial steps that have been adopted to establish a more lively, healthy, stable, and efficient banking industry in India. The impact of a highly regulated banking environment on asset quality, productivity, and bank performance necessitated the reform process, which resulted in the adoption of prudential norms for income recognition, asset classification, and provisioning, and capital adequacy, all of which are in line with international best practices. The major goal of the reform initiatives was to enhance asset quality and reduce non-performing assets. Against this backdrop, the current study objectively analyses the trend in the movement of nonperforming assets of public sector banks in India from 1993 to 2013, allowing for a more accurate assessment of NPA management in the post-millennium period. Non-performing assets are impacted by various bank performance indicators as well as macroeconomic conditions and are not only a function of loan/advance. This study not only described the trend in the NPA movement but also the moderating and mediating function of different bank performance and macroeconomic factors on the incidence of NPA.

Keyword: Non-Performing Assets, Gross Non-Performing Assets, Net Non-Performing Assets, Profitability, and Mismanagement.

1. Introduction

Banking is primarily concerned with intermediation, or accepting deposits and directing them into lending operations. Banks' 'Liabilities' are deposits received from depositors that must be reimbursed by the bank, while banks' 'Assets' are loans issued to borrowers that must be repaid by them, therefore assets are bank loans and advances.

Commercial Banks incur the risk of the borrower defaulting on either principal or interest payments in the traditional banking operation of lending backed by client deposits. Accounts, where payment of interest and/or repayment of principle is not forthcoming, are considered as Non-Performing Assets, according to the Reserve Bank of India. An asset, including a leased asset, ceases to produce income for the bank when it ceases to provide money for the bank. Non-performing assets are an unavoidable aspect of the banking industry, and every bank has some in its advanced portfolio. Any financial institution, however, should be concerned about the high amount of nonperforming assets (NPA).

2. Public Sector Banks In India

Commercial banks and cooperative banks make up India's banking system, with Commercial Banks accounting for more than 90% of the banking sector's assets. Commercial banks can be classified into three types based on their ownership patterns: I State-owned or Public Sector Banks (PSBs), which include the State Bank of India and its subsidiaries, as well as nationalized banks (27 PSBs are operating in India as of 31.3.2014), (ii) Private Banks under Indian ownership, and (iii) Foreign Banks operating in India.

The PSBs controlled the country's banking industry. They accounted for as much as 91 percent of total assets in 1990-91, with private Indian banks accounting for 3% and foreign banks accounting for 6%. The PSBs continued to dominate the Indian Banking Industry with the introduction of several new Private Indian Banks in the mid-1990s. PSBs accounted for little under 80% of total assets at the end of 2000-2001, with the Indian private sector accounting for over 12% and foreign banks accounting for 8%. PSBs accounted for around 72.7 percent of total assets in the Indian banking industry at the end of March 2013, compared to 20.8 percent for private banks and 6.5 percent for international banks9. For the first time, reliable evaluations of the extent level of NPAs in the Indian banking system were possible thanks to the categorization of advances according to the newly imposed 'prudential criteria.' Asset quality in the banking sector has deteriorated in the post-crisis years, with PSBs having the greatest level of stress in terms of non-performing assets and restructured advances among bank groups.

3. Implications of NPAs

The most significant commercial effect of NPAs is that credit risk management takes precedence over other parts of a bank's operations. Instead of focusing on developing business, the bank's whole machinery would be preoccupied with recovery operations. A bank with a high level of non-performing assets (NPAs) would be compelled to suffer carrying costs on these assets. Other consequences include a decrease in interest income, a high level of provisioning (banks are required to set aside a portion of their operating profit as provisions; as NPAs rise, banks must increase the amount set aside as provisions, reducing net profits), stress on profitability and capital adequacy, a gradual decline in the ability to meet steady increases in costs, increased pressure on Net Interest Margin (NIM), reducing competitiveness, and a gradual decline in the ability to meet steady increases in costs.

NPAs create a vicious circle of consequences on the financial system's viability and development, and if not managed appropriately, can lead to bank failure.

4. Factors Responsible For NPAs

The following variables facing borrowers are responsible for the occurrence of nonperforming assets (NPAs) in banks:-

a. Using finances for growth, modernization, or the start-up of new initiatives, as well as assisting in the promotion of sister concerns.

b. Project implementation time/cost overruns.

c. External causes such as a scarcity of raw materials, an increase in raw material/input prices, a power deficit, an industrial slowdown, surplus capacity, and natural disasters such as floods and accidents.

d. Business failures such as product failure to grab market share, ineffective management, strike/strained labor relations, incorrect technology, technical issues, product obsolescence, and so on.

e. Failure, non-payment/overdue in other countries, recession in other nations, externalization issues, unfavorable currency rate, and so forth.

f. Government measures such as excise, changes in import duties, deregulation, and pollution control decrees, and so on.

g. Willful default, money laundering, fraud, misappropriation, promoters/management feuds, and so on.

5. Indian Banking and NPA regulations:

NPA management was left to the banks and auditors until the mid-1980s. On the recommendations of the A. Ghosh Committee on Final Accounts, the first-ever system of asset categorization for the Indian banking sector was implemented in 1985. The 'Health Code System' (HCS) entailed categorizing bank advances into eight categories, ranging from 1 (acceptable) to 8 (bad and questionable debt)4. In 1991, the Narasimhan Committee on the Financial System concluded that the HCS categorization of assets was not in conformity with international norms, and recommended that banks divide their advances into four broad divisions for provisioning purposes. viz.

(i) Standard assets; (ii) substandard assets; (iii) doubtful assets; (iv) loss assets.

Following that, prudential standards for revenue recognition, asset categorization, and provisioning were brought in starting in 1992. The Narasimhan Committee on Banking Sector Reforms suggested tightening prudential requirements even more in 1998 to reinforce existing regulations and bring them up to date with growing worldwide best practices. In 2001, the NPA rules were brought up to international standards with the introduction of 90-day requirements for the categorization of NPAs.

NPAs are divided into two categories: gross NPAs and net NPAs. Gross nonperforming assets (NPAs) are the total of all loan assets categorized as nonperforming assets (NPAs) as of the balance sheet date, according to RBI criteria. It is a reflection of the quality of bank loans. (The Gross NPAs Ratio is calculated as Gross NPAs divided by Gross Advances.) Net NPAs are NPAs for which the banks have deducted the provisions for NPAs. Net NPAs = Gross NPAs-Provision/Gross Advances-Provisions) depicts the banks' true burden.

6. Objectives of the study

Following are the objectives of the study:

- Analyses the trend in the movement of nonperforming assets of public sector banks in India

7. Methodology and Research Design

S.No	Particulars	Research Design
1	Research Design	Descriptive research Design
2	Population of the study	All Banks in India
3	Sample frame	Public Sector Banks
3	Data Collection	From secondary data
4	Source of Data Collection	Journals, Articles, Websites, Newspaper.

8. Share Of Public Sector Banks In Gross NPAs Among All Banks Group

In the case of nonperforming assets (NPAs), PSBs bear a disproportionate and growing burden across bank groups (i.e. share in gross NPAs as compared to share in advances). Over the previous decade, and especially since 2009, the proportion of PSBs in gross NPAs has risen. In 2013, PSB NPAs accounted for 85 percent of the banking system's NPAs, up from 75 percent in 2003. The PSB's proportion of overall bank credit rose just a little throughout this time, from 74 percent to 76 percent. This is in stark contrast to the success of other areas of the banking system, particularly new private sector banks, whose percentage of nonperforming assets (NPAs) has decreased from over 14% in 2003 to 8% in 2013.

Table: 1Share of GNPA among Bank Groups (in percent)

Bank Group	Mar-03	Mar-07	Mar-08	Mar-09	Mar-13	Sep-13
PSBs	75.4	76.6	71.1	64.5	84.8	86.1
Share in total bank credit	-74	-72.8	-72.5	-75.2	-76.2	-75.3
Old Pvt Banks	6.2	5.9	4.6	4.5	2.8	2.8
Share in total bank credit	-6.2	-4.7	-4.5	-4.3	-4.6	-5
New Pvt Banks	14.2	12.5	18.7	20.3	8	6.8
Share in total bank credit	-12.8	-16.2	-16.4	-15	-14.8	-14.7
Foreign Banks	4.2	4.9	5.6	10.7	4.3	4.3
Share in total bank credit	-6.9	-6.4	-6.5	-5.6	-4.5	-5

Source: *op. cit. Two Decades of Credit Management*

9.1TRENDS IN NPAs IN PUBLIC SECTOR BANKS

The first number for NPAs was rather high: as of March 31, 1992, the PSBs' combined bad loans accounted for Rs.17,400 crores or 14.5 percent of outstanding advances or 6.7 percent of total assets.

Table: 2
Gross and Net NPAs of Public Sector Banks since 1992-93 to 2012-13

(Amount in Rs. billion)

Year	Gross NPAs Amount	Gross NPAsas a percentage of Gross Advances	Gross NPAs as a percentage of Total Assets	Net NPAs Amount	Net NPAs as a percentage of Net Advances	(Percent) Net NPAs asa percentage of Total Assets
1993	392.5	23.2	11.8	–	–	–
1994	410.4	24.8	10.8	–	–	–
1995	383.8	19.5	8.7	–	10.7	4.0
1996	416.6	18.0	8.2	–	8.9	3.6
1997	435.77	17.8	7.8	202.85	9.2	3.6
1998	456.53	16.0	7.0	212.32	8.2	3.3
1999	517.10	15.9	6.7	242.11	8.1	3.1
2000	530.33	14.0	6.0	261.87	7.4	2.9
2001	546.72	12.4	5.3	279.77	6.7	2.7
2002	564.73	11.1	4.9	279.58	5.8	2.4
2003	540.90	9.4	4.2	248.77	4.5	1.9
2004	515.37	7.8	3.5	193.35	3.1	1.3
2005	483.99	5.5	2.7	169.04	2.1	1.0
2006	413.58	3.6	2.1	145.66	1.3	0.7
2007	389.68	2.7	1.6	151.45	1.1	0.6
2008	404.52	2.2	1.3	178.36	1.0	0.6
2009	449.57	2.0	1.2	211.55	-0.9	0.6
2010	599.26	2.2	1.3	293.75	1.1	0.7
2011	746.00	2.4	1.4	360.00	1.2	0.7
2012	1124.89	3.2	1.9	593.00	1.5	1.0
2013	1644.62	3.6	2.4	900.00	2.0	1.3

Source: (i) RBI. Handbook of Statistics on the Indian Economy, 2005-06, 2013-14
http://dbie.rbi.org.in

(ii) Rajiv Ranjan and Dhal, Sarat Chandra, Non-Performing Loans and Terms of Credit,RBI Occasional Paper, Volume 24, No.3 Winter 2003

9. Discussion of Impact and Reducing the loss

Except for the year 1995, as shown in Table-2, nonperforming assets continued to rise in absolute terms throughout the 1990s decade. On March 31, 2002, gross nonperforming assets in PSBs totaled Rs.564.73 billion, accounting for 11.1 percent of gross loans and 4.9 percent of total assets. Following that, gross nonperforming assets (NPAs) decreased in value, reaching Rs.389.68 billion at the end of March 2007. However, in 2008, when NPAs skyrocketed, the tendency reversed. Between 2009 and 2012, the gross NPAs climbed the greatest, rising from Rs.449.57 billion in 2009 to Rs.1124.89 billion in 2011-2012 and then to Rs.1644.62 billion in 2012-13. From March 2010 (Rs.599.26 billion) to March 2014, the gross nonperforming assets of public sector banks surged by about fourfold (Rs.2272.64 billion).

Trends in the ratio of GNPAs to NNPAs are also seen in Table 2. A higher percentage indicates that asset quality is deteriorating. PSBs' gross nonperforming assets (NPAs) ratio, which was 17.8% at the end of March 1997, steadily decreased to 2.0% at the end of March 2009. The ratio of gross nonperforming assets to gross loans increased to 2.2 percent in 2009-10, then to 2.4 percent in 2010-11, 3.2 percent in 2011-12, and 3.6 percent in 2012-13.

The ratio of net NPAs to net advances increased from 1.1 percent in 2009-10 to 2% in 2012-13, following a similar pattern. In 2013-14, the Total Gross NPA Ratio increased to 4.36 percent.

10.REASONS FOR GROWING NPAs IN THE CURRENT PERSPECTIVE

The consequences of the global crisis, along with internal variables such as the downturn in the local economy, have had a detrimental influence on the performance of corporate as well as small and medium firms, resulting in a negative impact on credit quality in recent years. In comparison to private sector banks, PSBs' asset quality deteriorated as high ticket corporate loans made up a bigger portion of their credit portfolio. According to data from the Finance Ministry, thirty firms owe Public Sector Banks a total of Rs.16,877 crore as of September 30, 2013.

Another cause for the significant increase in gross NPAs at PSBs has been attributed to a switch from manual to system-based NPA identification. Before this, most banks' calculations were done manually at the branch level and were thus vulnerable to management discretion.

Infrastructure, Iron and Steel, Textiles, Aviation, and Mining were identified as stressed industries by the RBI in its Financial Stability Report released in December 2013. PSBs have a lot of exposure to the 'industrial' sector in general, and too-stressed industries in particular. Switchover to system-based identification of NPAs by PSBs, slowing economic development, and aggressive lending by banks in the past, especially during good times, are all factors contributing to the rise in bank NPAs. PSBs dominate the Indian banking sector, and the rise in their nonperforming assets (NPAs) is causing worry. As a result, initiatives are being made to ameliorate the situation.

11.Initiatives are taken by the government

The government has recently taken the following steps to combat the growing number of nonperforming assets (NPAs):

- Nodal officers for recovery are appointed by banks at their head offices/zonal offices/for each Debts Recovery Tribunal (DRT).

- Banks are being pushed to recover lost assets and designate asset reconstruction corporations (ARC) as resolution agents.

- directing state bankers' committees to take the initiative in settling difficulties with state governments

- New loans are approved based on information exchange across institutions.
- Conducting NPA analysis by sector or activity.

- Keep a close eye on NPAs through detecting early warning signs and requiring banks to take prompt remedial action, such as early identification of signs of distress, changes to recovery regulations, and improved credit evaluation and post-credit monitoring.

A thriving economy requires a healthy banking sector. Because the failure of the banking system could hurt other sectors, it is critical to ensure that the banking system acknowledges financial distress early, takes swift action to resolve it, and ensures a fair recovery for lenders and investors so that the banking sector can resume normal operations.

12. Conclusions

Banking is primarily concerned with intermediation, or the acceptance of deposits and the subsequent channeling of those deposits into lending operations. Banks' Liabilities are deposits received from depositors that must be reimbursed to them by the bank, while banks' Assets are loans issued to borrowers that must be repaid by them, therefore assets are bank loans and advances. Commercial Banks are confronted with the danger of the borrower defaulting on either principal or interest payments in the traditional banking operation of lending backed by client deposits. In banking jargon, this is referred to as 'Credit Risk,' and accounts that do not receive interest or return of principle are referred to as Non-Performing Assets. According to the Reserve Bank of India, a non-performing asset, including a leased asset, is one that no longer generates money for the bank. Non-performing assets are an unavoidable aspect of the banking industry, and every bank has some in its advance portfolio. Any financial institution, however, should be concerned about the high amount of nonperforming assets (NPA).

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