A STUDY ON NON PEROFORMING ASSETS OF INDIAN COMMERCIAL BANKS

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Abstract: *An asset becomes non-performing when it ceases to generate income for the bank. Earlier an asset was considered as non-performing asset (NPA) based on the concept of **'Past Due'**. A 'non performing asset' (NPA) was defined as credit in respect of which interest and/ or installment of principal has remained 'past due' for a specific period of time. An asset becomes non-performing when it ceases to generate income for a financial institution. A nonperforming asset does not yield any return but it incurs a cost by eating into earnings made by banks. The origin of the problem of increasing non-performing assets lies in the quality of managing credit risk by the banks concerned. The present treatise is an attempt to study the non-performing assets position in Commercial Banks. Non-performing assets are caused as a result of various internal and external factors. The study revealed that the growth rate in advances are decreasing and growth rate in Non Performing Assets is increasing, which is not desirable to the bank. What is needed is having adequate preventive measures in place namely, fixing pre-sanctioning appraisal responsibility and having an effective post-disbursement supervision. Banks concerned should continuously monitor loans to identify accounts that have potential to become non-performing.*

Key words: *Bank advance, Gross NPA, Growth rate, commercial banks*

1. INTRODUCTION:

Modern Banking in India originated in the last decades of the 18th century. The first banks were The General Bank of India, which started in 1786, and Bank of Hindustan, which started in 1770; both are now defunct. The oldest bank still in existence in India is the State Bank of India, which originated in the Bank of Calcutta in June 1806, which almost immediately became the Bank of Bengal. This was one of the three presidency banks, the other two being the Bank of Bombay and the Bank of Madras, all three of which were established under charters from the British East India Company. For many years the presidency banks acted as quasi-central banks, as did their successors. The three banks merged in 1921 to form the Imperial Bank of India, which, upon India's independence, became the State Bank of India in 1955.

In April 1935, the Reserve Bank of India was established. At the time of first phase the progress of banking sector was very sluggish. Between 1913 and1948 there were around 1100 small banks in India. To reform the working and activities of commercial banks, the Government of India came up with the Banking Companies Act, 1949 which was later changed to Banking Regulation Act 1949 as per amending Act of 1965 (Act No.23 of 1965). Reserve Bank of India was vested with extensive powers for the supervision of banking in India as a Central Banking Authority. In 2017, SBI and its associates merged into one. At present 1 SBI, 19 Nationalised Banks, IDBI Bank, 26 Private Banks, 43 Private Foreign Banks, 31 State Co-operative Banks and 56 Regional Rural Banks are in commercial banking business.

In order to reflect a bank's actual financial health in its balance sheet and as per the recommendations made by the Committee on Financial System (Chairman Shri. M. Narasimham), the Reserve Bank has introduced, in a phased manner, prudential norms for income recognition, asset classification and provisioning for the advances portfolio of the banks. Broadly, the policy of income recognition should be objective and based on record of recovery rather than on any subjective considerations. Likewise, the classification of assets of banks has to be done on the basis of objective criteria, which would ensure a uniform and consistent application of the norms. The provisioning should be made on the basis of the classification of assets into different categories.

2. NON-PERFORMING ASSETS (NPA):

An asset becomes non-performing when it ceases to generate income for the bank. Earlier an asset was considered as non-performing asset (NPA) based on the concept of **'Past Due'**. A 'non performing asset' (NPA) was defined as credit in respect of which interest and/ or installment of principal has remained 'past due' for a specific period of time. The specific period was reduced in a phased manner as under:

Year ended March, 31	Specific period
1993	4 quarters
1994	3 quarters
1995	2 quarters

An amount is considered as past due, when it remains outstanding for 30 days beyond the due date. However, with effect from March 31, 2001 the 'past due' concept has been dispensed with and the period is reckoned from the due date of payment.

With a view to moving towards international best practices and to ensure greater transparency, '90 days' **overdue*** norms for identification of NPAs have been made applicable from the year ended March 31, 2004. As such, with effect from March 31, 2004, a non-performing asset shall be a loan or an advance where:

- Interest and/or installment of principal remain overdue for a period of more than 90 days in respect of a Term Loan.
- The account remains **'Out of order'**[@] for a period of more than 90 days, in respect of an Overdraft/ Cash Credit (OD/CC).
- The bill remains overdue for a period of more than 90 days in the case of bills purchased and discounted,
- Any amount to be received remains overdue for a period of more than 90 days in respect of other accounts.

3. ASSET CLASSIFICATION:

Banks should classify their assets into the following broad groups, viz.

(i) Standard Assets
(ii) Sub-standard Assets
(iii) Doubtful Assets
(iv) Loss Assets

Standard Assets: Standard Asset is one which does not disclose any problems and which does not carry more than normal risk attached to the business. Such an asset should not be an NPA.

Sub-standard Assets:

- With effect from March 31, 2005 an asset would be classified as sub-standard if it remained NPA for a period less than or equal to 12 months. In such cases, the current net worth of the borrowers/ guarantors 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 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.
- An asset where the terms of the loan agreement regarding interest and principal have been re-negotiated or rescheduled after commencement of production, should be classified as sub-standard and should remain in such category for at least 12 months of satisfactory performance under the re-negotiated or rescheduled terms. In other words, the classification of an asset should not be upgraded merely as a result of rescheduling, unless there is satisfactory compliance of this condition.

Doubtful Assets With effect from March 31, 2005, an asset is required to be classified as doubtful, if it has remained NPA for more than 12 months. For Tier I banks, the 12-month period of classification of a substandard asset in doubtful category is effective from April 1, 2009. As in the case of sub-standard assets, rescheduling does not entitle the bank to upgrade the quality of an advance automatically. A loan classified as doubtful has all the weaknesses inherent as that 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 where loss has been identified by the bank or internal or external auditors or by the Co-operation Department or by the Reserve Bank of India inspection but the amount has not been written off, wholly or partly. In other words, such an asset is considered un-collectible and of such little value that its continuance as a bankable asset is not warranted although there may be some salvage or recovery value.

Provision Norms of NPA

TYPES OF ASSETS	PROVISIONS
Standard asset	0.25% for all type of standard advances
Sub-standard asset	10% for all types of standard advances
Doubtful asset	

-up to 1 year 1 to 3 years More than 3 years	100% of unsecured advances and 20% of secured advances. 100% of secured advances and 30% of secured advances 100% of unsecured advances and 100% of secured advances
Loss asset	100% of unsecured advances and 100% of secured advances

The Reserve Bank of India states that, compared to other Asian countries and the US, the gross non-performing asset figures in India seem more alarming than the net NPA figure. The problem of high gross NPAs is simply one of inheritance. Historically, Indian public sector banks have been poor on credit recovery, mainly because of very little legal provision governing foreclosure and bankruptcy, lengthy legal battles, sticky loans made to government public sector undertakings, loan waivers and priority sector lending. Net NPAs are comparatively better on a global basis because of the stringent provisioning norms prescribed for banks in 1991 by Narasimham Committee.

3. LITERATURE REVIEW:

Kumar (2005) in his article, "Non-Performing Assets in Indian Banks" studied that the Indian banking sector faced a serious problem of NPAs. The extent of NPAs has comparatively higher in public sectors banks.

Harpreet (2006) in her thesis titled "Credit management and problem of NPAs in Public Sector Banks" highlighted the problem of non-performing assets in public sector banks. Author suggested that for effective handling of NPAs, there is an urgent need for creating proper awareness about the adverse impact of NPAs on profitability amongst bank staff, particularly the field functionaries.

Bhatia (2007) in his research paper entitled, "Non-Performing Assets of Indian Public, Private and Foreign Sector Banks: An Empirical Assessment", aims to find the fundamental factors which impact NPAs of banks. A model consisting of two types of factors, viz., macroeconomic factors and bank-specific parameters, is developed and the behavior of NPAs of the three categories of banks is observed

Meenakshi Rajeev and H P Mahesh (2010), in their working paper "Banking Sector Reforms and NPA: A study of Indian Commercial Banks" identified that the NPA is the root cause of the recent global financial crisis. It remains true that NPA in the priority sector is still higher than that of the non-priority sector. Within the priority sector, the SSI's performance is the worst. However, even this sector has shown reduction in bad loans over time

Dr. Harpreet Kaur and Neeraj Kumar Saddy (2011), in their article titled a comparative study of non-performing assets of public and private sector banks observed that the NPAs have always been a big worry for the banks in India.

Poongavanam.S (2012), in his working paper Non Performing Assets: Issues, Causes and Remedial Solution" detailed that the banking industry has undergone a major change after the first phase of economic liberalization; hence the importance credit management has emerged. In recent time banks are very cautious in extending loan, because of mounting NPA.

Pallab Sikdar & Dr. Munish Makkad (2013), in their research paper **"**Role Of Non Performing Assets In The Risk Framework Of Commercial Banks – A Study Of Select Indian Commercial Banks", have described the problem of NPAs can be tackled only with proper credit assessment and risk management mechanism.

Ankit Garg (2016), in his paper titled "A Study on Management of Non-Performing Assets in Context of Indian Banking System" noticed that the Non-performing Asset is one of the prevalent problems of Indian Banking sector. The problem of NPA impacts profitability, Liquidity and credit loss. Unless and otherwise proper remedial measures are taken the quantum of non-performing assets cannot be reduced and the bank will incur losses to a great extent.

4. OBJECTIVES OF THE STUDY:

- To study the progress of Gross & Net advances of Commercial Banks
- To study the changes in Non Performing Assets of Commercial Banks

4.1 Analysis of the data:

Gross Advances: Gross advances are the sum of total standard assets and Gross NPA. Net advance is the difference between the Gross advances and Provisions/deducations.
Gross advance = Standard Advances + Gross NPA
Net Advance = Gross Advance - Deductions

Deductions

- Provisions held in the case of NPA Accounts as per asset classification (including additional Provisions for NPAs at higher than prescribed rates).
- DICGC / ECGC claims received and held pending adjustment
- Part payment received and kept in Suspense Account or any other similar account

- Balance in Sundries Account (Interest Capitalization - Restructured Accounts), in respect of NPA Accounts
- Floating Provisions
- Provisions in lieu of diminution in the fair value of restructured accounts classified as NPAs
- Provisions in lieu of diminution in the fair value of restructured accounts classified as standard assets

Table 1: statement of Gross & Net advances given by Commercial Banks

(In Billions)

year	Gross Advances	Growth Rate	Net Advances	Growth Rate
2005-06	15513.79	--	15168.12	--
2006-07	20125.1	29.72	19812.37	30.62
2007-08	25078.85	24.61	24769.37	25.02
2008-09	30382.54	21.15	29999.25	21.11
2009-10	35449.65	16.68	34970.54	16.57
2010-11	40114.35	13.16	42987.04	22.92
2011-12	46576.12	16.11	50735.59	18.03
2012-13	59797.17	28.39	58797.73	15.89
2013-14	68757.48	14.98	67352.14	14.55
2014-15	75606.66	9.96	73881.79	9.69
2015-16	82637.45	9.3	80760.73	9.2

Source: Statistical reports of RBI

The volumes of gross advances are 5 times increased in a span of one decade. The above statistics reveals that the growth rate in the advances is more in the beginning of the study period and it is less in the later period. In 2006-07, gross and net advances are at a growth rate of 30% and are decreased to 10% in the year 2014-15. This phenomenon is common in both in the gross and net advances. The same growth is experienced in all forms of commercial banks viz.., public sector banks, private sector banks and foreign banks.

TYPES OF NPAs

NPAs are broadly divided into: a) Gross NPAs, and b) Net NPAs

Gross NPAs: Gross NPAs are the sum total of all loan assets that are classified as NPAs as per RBI guidelines as on Balance Sheet date. Gross NPA reflects the quality of the loans made by banks. It consists of all the non standard assets like as sub-standard, doubtful and loss assets.

It can be calculated with the help of following ratio:

Gross NPAs Ratio = Gross NPAs / Gross Advances

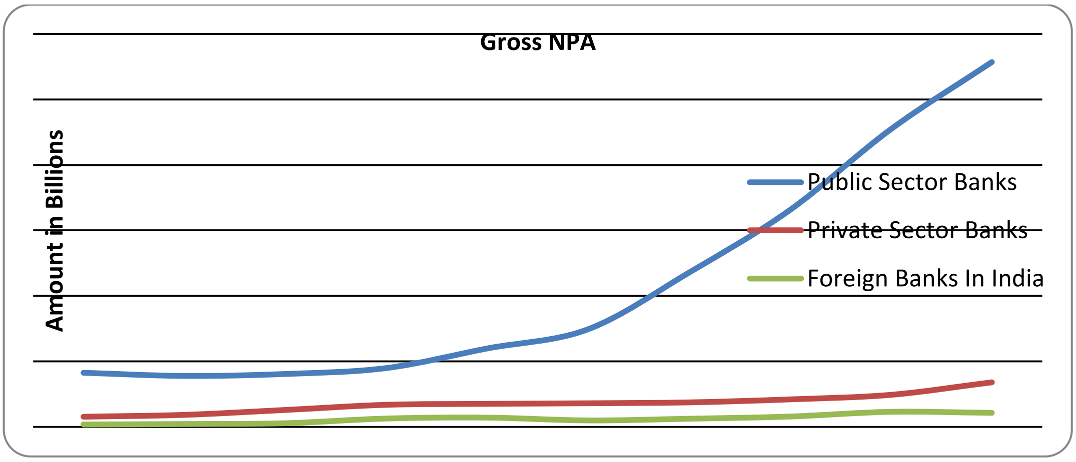
Table 2: Statement showing Gross NPA of commercial banks

(In Billions)

Year	Gross NPA			Total	In %		
	Public Sector Banks (PSB)	Private Sector Banks (Pvt.SB)	Foreign Banks In India (F.B)		Share of PSB	Share of Pvt.SB	Share of F.B
2005-06	413.58	78.11	19.28	510.97	0.81	0.15	0.04
2006-07	389.68	92.56	22.63	504.87	0.77	0.18	0.04
2007-08	404.52	129.97	28.59	563.08	0.72	0.23	0.05
2008-09	449.57	169.26	64.44	683.27	0.66	0.25	0.09
2009-10	599.26	176.39	71.33	846.98	0.71	0.21	0.08
2010-11	746	181	50	977	0.76	0.19	0.05
2011-12	1178.39	187.68	62.97	1429.04	0.82	0.13	0.04
2012-13	1656.06	210.71	79.77	1946.54	0.85	0.11	0.04
2013-14	2272.64	245.42	115.65	2633.71	0.86	0.09	0.04
2014-15	2784.68	341.06	107.71	3233.45	0.86	0.11	0.03
2015-16	4179.88	561.87	158.05	4899.8	0.85	0.11	0.03

Source: Statistical reports of RBI

Chart 1: Gross NPA of different commercial banks



The above figures clearly explain the failure of Public Sector Banks, as it reflects major proportion of total value of gross NPA. It is 80.94% in the year 2005 – 06 and increased to 86.12 in the year 2014-15. Initially (2005 – 2010) public sector banks are able to decrease the portion in total gross NPA, later it was increased. Private sector banks are able to manage the Gross NPA as it decreases from 15.29% (2005-06) to 10.55 (2014-15). Foreign banks are also effective at controlling the growth of Gross NPAs in the study period as it increased in the first 5 years and later it starts decreasing. The share of Gross NPA is 3.77 in the year 2005-06 and it is 3.23 in the year 2015 -16. It explains that foreign banks are most effective at managing the Non Performing Assets.

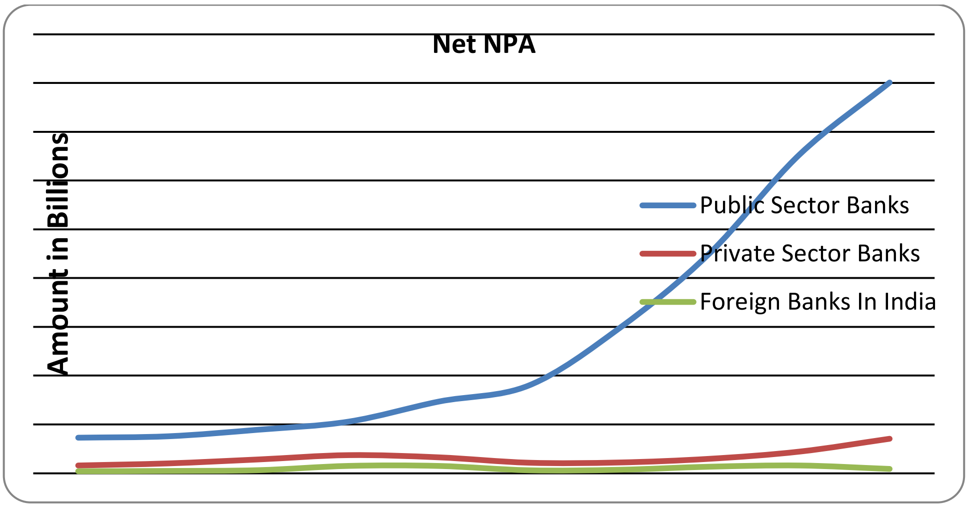
Table 3: Statement showing Net NPA of commercial banks

(In Billions)

year	Net NPA			Total	In %		
	Public Sector Banks (PSB)	Private Sector Banks (Pvt.SB)	Foreign Banks In India (F.B)		Share of PSB	Share of Pvt.SB	Share of F.B
2005-06	145.66	31.71	8.08	185.45	78.54	17.1	4.36
2006-07	151.45	40.28	9.27	201	75.35	20.04	4.61
2007-08	178.36	56.47	12.47	247.3	72.12	22.83	5.04
2008-09	211.55	74.11	29.96	315.62	67.03	23.48	9.49
2009-10	293.75	65.05	29.77	388.57	75.6	16.74	7.66
2010-11	360	43	12	415	86.75	10.36	2.89
2011-12	593.91	44	14.12	652.03	91.09	6.75	2.17
2012-13	900.37	59.06	26.63	986.06	91.31	5.99	2.7
2013-14	1306.35	88.62	31.61	1426.58	91.57	6.21	2.22
2014-15	1602.08	141.28	17.57	1760.93	90.98	8.02	1
2015-16	2514.81	266.77	27.67	2809.25	89.52	9.5	0.98

Source: Statistical reports of RBI

Chart 2: Net NPA of different commercial banks



Management of Net Non Performing Assets by the foreign banks is exceptionally good, as they are able to manage and decrease the share from 4.36% to 0.98% in the last decade. The public sector banks are under the pressure of government involvement, directed lending, poor appreciation at the time of granting loans etc., and are the reasons for growth in Non Performing Assets. The private sector banks are successful at controlling the growth of Net NPA from 17.1% (2005-06) to 9.5 (2015-16). The public sector banks are not able to manage the Net NPA, as it increased from 78.54% (2005-06) to 89.52% (2015-16).

5. CONCLUSION:

The primary functions of a bank is collecting deposits and lending money. Lending money is related to offering loans and advances to different categories of customers. To strengthen the banking system RBI introduced the system of assessing the quality of loan or advance and categorizing an asset in different types of assets. This quality measurement leads to creation of NPA and managing it becomes the primary responsibility of the banker. The growth rate in lending money is decreasing and the Gross NPA and Net NPA ratios are increasing year by year. The foreign banks are able to manage the NPAs, the public sectors banks are need to observe the same from foreign banks and banks should get free from the intervening of government. The government should consider priority lending along with the safety of depositors.

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