

Rising non-performing assets in Banks

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Abstract

Non-performing assets are one of the major concerns for banks in India. NPAs reflect the performance of banks. A high level of NPAs suggests high probability of a large number of credit defaults that affect the profitability and net-worth of banks and also erodes the value of the asset.

NPAs affect the liquidity and profitability, in addition to posing threat on quality of asset and survival of banks. The Indian banking sector has been facing serious problems of rising Non - performing Assets (NPAs). The NPAs growth has a direct impact on profitability of banks. It involves the necessity of provisions, which reduces the overall profits and shareholders' value. The problem of NPAs is not only affecting the banks but also the whole economy. In fact high level of NPAs in Indian banks is nothing but a reflection of the state of health of the industry and trade. It is necessary to trim down NPAs to improve the financial health in the banking system. The Indian banking sector is facing a serious problem of NPAs.

An attempt has been made in this paper that what is NPA? The factors contributing to it, reasons for high NPAs and their impact on Indian banking operations, the trend and magnitude of NPAs in selected Indian banks.

Keywords: Gross NPA, Net NPA, Public banks and Private Sector Banks.

Introduction

Definition of Non-Performing Asset

An account is declared as NPA based on the recovery of instalments and interest on loans and advances and other aspects as per RBI norms. The norms to declare an account as NPA by RBI are as follows:

1. An asset, including a leased asset, becomes non-performing when it ceases to generate income for the bank.
2. A non-performing asset (NPA) is a loan or an advance where;
 - i) Interest and/ or instalment of principal remain overdue for a period of more than 90 days in respect of a term loan,
 - ii) The account remains 'out of order' in respect of an Overdraft/Cash Credit (OD/CC), if the outstanding balance remains continuously in excess of the sanctioned limit/drawing power. In cases where the outstanding balance in the principal operating account is less than the sanctioned limit / drawing power, but there are no credits continuously for 90 days as on the date of Balance Sheet or credits are not enough to cover the interest debited during the same period, these accounts should be treated as 'out of order'.
 - iii) The bill remains overdue for a period of more than 90 days in the case of bills purchased and discounted,
 - iv) The instalment of principal or interest thereon remains overdue for two crop seasons for short duration crops,
 - v) The instalment of principal or interest thereon remains overdue for one
 - vi) Crop season for long duration crops,
 - vii) The amount of liquidity facility remains outstanding for more than 90 days, in respect of a securitisation transaction undertaken in terms of guidelines on securitisation dated February 1, 2006.
 - viii) In respect of derivative transactions, the overdue receivables representing positive mark-to-market value of

a derivative contract, if these remain unpaid for a period of 90 days from the specified due date for payment.

Types of NPA's may be classified into

1. Gross NPA: 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 nonstandard assets like as sub-standard, doubtful, and loss assets.
2. Net NPA: Gross NPA - (Balance in Interest Suspense account + DICGC/ECGC claims received and held pending adjustment + Part payment received and kept in suspense account + Total provisions held).

Asset classification categories of NPA's

Standard assets

Standard assets are the ones in which the bank is receiving interest as well as the principal amount of the loan regularly from the customer. It is also very important to note that in this case the arrears of interest and the principal amount of loan do not exceed 90 days at the end of financial year.

If asset fails to be in category of standard asset that is amount due more than 90 days then it is NPA and NPAs are further need to classify in sub categories.

Banks are required to classify non-performing assets further into the following three categories based on the period for which the asset has remained non-performing and the reliability of the dues:

- **Sub-standard assets with effect from 31 March 2005:** A substandard asset would be one, which has remained NPA for a period less than or equal to 12 month.
- **Doubtful assets:** A loan classified as doubtful if it remained in the substandard category for 12 months.

- **Loss assets:** A loss asset is one which 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.

Factors for rise in NPAs

The banking sector has been facing the serious problems of the rising NPAs. But the problem of NPAs is more in public sector banks when compared to private sector banks and foreign banks.

The NPAs are growing due to external as well as internal factors.

External factors

- Ineffective functioning of Govt. Departments - The Govt. has set up numbers of recovery tribunals, which works for recovery of loans and advances. Due to their negligence and ineffectiveness in their work the bank suffers from the consequences of non-recovery, thereby reducing their profitability and liquidity.
- Wilful defaulters - There are borrowers who are able to pay back loans but are intentionally withdrawing it. These groups of people should be identified and proper measures should be taken in order to get back the money extended to them as advances and loans.
- Natural calamities - This is the major factor, which is creating alarming rise in NPAs of the PSBs. Every now and then India is hit by major natural calamities thus making the borrowers unable to pay back their loans. Thus the bank has to make large amount of provisions in order to compensate those loans, hence end up the fiscal with a reduced profit.
- Industrial sickness - Improper project handling, ineffective management, lack of adequate resources, lack of advance technology, day to day changing govt. Policies give birth to industrial sickness. Hence the banks that finance those industries ultimately end up with a low recovery of their loans reducing their profit and liquidity.
- Lack of demand - Entrepreneurs in India could not foresee their product demand and start production which ultimately piles up their product thus making them unable to pay back the money they borrow to operate these activities. The banks recover the amount by selling of their assets, which covers a minimum label. Thus the banks record the non-recovered part as NPAs and have to make provision for it.
- Directed loans system - Under this commercial banks are

required to supply 40% percentage of their credit to priority sectors. Most significant sources of NPAs are directed loans supplied to the —micro sector are problematic of recoveries especially when some of its units become sick or weak.

- Corruption and Political Pressure: It has been observed especially in Public Sector Bank's that many big ticket loans are given to lenders due to political pressure and corruption.

Internal factors

- Defective lending process – It refers to faulty and weak system of determining the credit worthiness of the borrower, which often results in wrong or over financing.
- Lack of proper credit monitoring: After disbursement of loans, comes the stage of credit monitoring wherein it should be ensured that the funds are properly deployed and the assets are created. However many times it has been seen that monitoring is not proper leading to rise in NPA's.
- Unsecured Advances: Advances covered under CGTMSE or Education Loans are usually unsecured and therefore there is no major pressure on the borrower to repay the loan. As a result the chances of NPA increase in the unsecured advances.

Impact of NPA

NPA directly impacts the performance and profitability of banks. The most notable impact of NPA is change in banker's sentiments which may hinder credit expansion to productive purposes

Banks may incline towards more risk free investments to avoid and reduce riskiness, which is not conducive for the growth of economy. If the level of NPAs is not controlled timely they will:

- Reduce the earning capacity of assets and badly affect the ROI.
- The cost of capital will go up.
- The assets and liability mismatch will widen.
- Higher provisioning requirement on mounting NPAs adversely affect capital adequacy ratio and banks profitability.
- The economic value additions (EVA) by banks gets upset because EVA is equal to the net operating profit minus cost of capital.
- NPAs causes to decrease the value of share sometimes even below their book value in the capital market.
- NPAs affect the risk facing ability of banks

NPA POSITION OF SCHEDULED COMMERCIAL BANKS AS ON 31.03.2015

S. No.	Bank	(Amt. in million)			
		Gross NPAs		Net NPAs	
		As on March 31.03.2014	As on March 31.03.2015	As on March 31.03.2014	As on March 31.03.2015
		1	2	3	4
1	STATE BANK OF BIKANER & JAIPUR	27328	29451	17709	17692
2	STATE BANK OF HYDERABAD	58242	49848	29849	23485
3	STATE BANK OF INDIA	616054	567253	310961	275906
4	STATE BANK OF MYSORE	28189	21364	16303	11216
5	STATE BANK OF PATIALA	37584	43597	24045	30492
6	STATE BANK OF TRAVANCORE	30769	23571	19285	13987
	STATE BANK OF INDIA & ITS ASSOCIATES	798165	735085	418151	372777
7	AXIS BANK	31464	41102	10246	13167
8	CATHOLIC SYRIAN BANK LTD	3336	4748	1932	3646
9	CITY UNION BANK LIMITED	2931	3358	1973	2328

10	DCB BANK LIMITED	1385	1861	740	1057
11	DHANLAXMI BANK	4858	5583	3019	2526
12	FEDERAL BANK	10874	10577	3216	3733
13	HDFC BANK	29893	34384	8200	8963
14	ICICI BANK	105058	150947	32980	62555
15	INDUSIND BANK	6208	5629	1841	2105
16	ING VYSYA BANK	2630	7452	1020	4490
17	JAMMU & KASHMIR BANK LTD	7834	27641	1020	12363
18	KARNATAKA BANK LTD	8359	9442	5380	6236
19	KARUR VYSYA BANK	2792	6778	1399	2810
20	KOTAK MAHINDRA BANK LTD	10594	12372	5736	6091
21	LAKSHMI VILAS BANK	5465	4546	4434	3025
22	NAINITAL BANK	611	774	-	-
23	SOUTH INDIAN BANK	4326	6435	2817	3571
24	TAMILNAD MERCANTILE BANK LTD	4280	3187	2098	1355
25	THE RATNAKAR BANK LIMITED	778	1112	305	386
26	YES BANK LTD.	1749	3134	261	877
	PRIVATE SECTOR BANKS	245424	341062	88615	141283
27	ALLAHABAD BANK	80680	83580	57218	59789
28	ANDHRA BANK	58576	68765	33425	36886
29	BANK OF BARODA	118759	162614	60348	80695
30	BANK OF INDIA	118686	221932	76795	137747
31	BANK OF MAHARASHTRA	28599	64021	18073	41266
32	BHARATIYA MAHILA BANK LTD.	0	-	-	-
33	CANARA BANK	75702	130400	59655	87401
34	CENTRAL BANK OF INDIA	115000	118730	66490	68070
35	CORPORATION BANK	47368	71067	31806	44650
36	DENA BANK	26160	43930	18189	30143
37	IDBI BANK LIMITED	99602	126850	49023	59925
38	INDIAN BANK	45622	56704	27637	31470
39	INDIAN OVERSEAS BANK	90205	149225	56581	98133
40	ORIENTAL BANK OF COMMERCE	56179	76662	39044	48162
41	PUNJAB AND SIND BANK	25535	30822	19186	22660
42	PUNJAB NATIONAL BANK	188801	256949	99170	153965
43	SYNDICATE BANK	46111	64424	27206	38437
44	UCO BANK	66214	102651	35564	63306
45	UNION BANK OF INDIA	95637	130309	53403	69190
46	UNITED BANK OF INDIA	71180	65529	46641	40814
47	VIJAYA BANK	19859	24432	12624	16597
	NATIONALISED BANKS	1474474	2049595	888076	1229305
48	AB BANK LIMITED	70	85	53	53
49	ABU DHABI COMMERCIAL BANK	231	231	69	14
50	AMERICAN EXPRESS BANKING CORP.	195	202	110	152
51	ANTWERP DIAMOND BANK NV	503	56	-	-
52	AUSTRALIA AND NEW ZEALAND BANKING GROUP LIMITED	185	-	-	-
53	BANK INTERNASIONAL INDONESIA	0	-	-	-
54	BANK OF AMERICA N.A.	0	145	-	98
55	BANK OF BAHRAIN & KUWAIT B.S.C.	803	399	576	253
56	BANK OF CEYLON	14	14	-	-
57	BANK OF NOVA SCOTIA	1935	1932	1164	320
58	BANK OF TOKYO-MITSUBISHI UFJ LTD	95	1075	8	457
59	BARCLAYS BANK PLC	4639	3111	887	32
60	BNP PARIBAS	163	122	-	-
61	CITIBANK N.A.	14842	7806	7013	2449
62	COMMONWEALTH BANK OF AUSTRALIA	0	-	-	-
63	CREDIT AGRICOLE	174	6	84	-
64	CREDIT SUISSE AG	0	-	-	-
65	CTBC BANK	78	77	19	18
66	DBS BANK LTD.	21156	12839	15440	6575
67	DEUTSCHE BANK AG	1673	1193	254	466
68	DOHA BANK QSC	0	-	-	-
69	FIRSTRAND BANK LTD	342	221	-	151
70	HONGKONG AND SHANGHAI BANKING CORPN.LTD.	6601	7915	976	2381
71	HSBC BANK OMAN S.A.O.G.	0	-	-	-

72	INDUSTRIAL AND COMMERCIAL BANK OF CHINA	0	-	-	-
73	JP MORGAN CHASE BANK N.A.	234	-	-	-
74	JSC VTB BANK	0	216	-	183
75	KRUNG THAI BANK PUBLIC COMPANY LIMITED	0	-	-	-
76	MASHREQ BANK PSC	0	-	-	-
77	MIZUHO BANK LTD	1503	1366	1080	694
78	NATIONAL AUSTRALIA BANK	0	-	-	-
79	RABO BANK INTERNATIONAL	0	-	-	-
80	ROYAL BANK OF SCOTLAND N.V.	1136	821	-57	59
81	SBERBANK	200	487	170	414
82	SHINHAN BANK	0	-	-	-
83	SOCIETE GENERALE	4	-	-	-
84	SONALI BANK	29	28	8	6
85	STANDARD CHARTERED BANK	57826	66564	3063	2306
86	STATE BANK OF MAURITIUS LTD	1019	799	688	487
87	SUMITOMO MITSUI BANKING CORPORATION	0	-	-	-
88	UBS AG	0	-	-	-
89	UNITED OVERSEAS BANK LTD	0	-	-	-
90	WESTPAC BANKING CORPORATION	0	-	-	-
91	WOORI BANK	0	-	-	-
	FOREIGN BANKS	115650	107708	31607	17567

(Source: dbie.rbi.org.in)

Conclusion

The NPAs 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 as compared to private 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.

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