Non-Performing Assets in Public Sector Banks in India: An Empirical Study

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ABSTRACT:

Banks play a crucial role in the Indian financial system. Growing non-performing assets is a recurrent problem in the Indian banking sector. In banking, NPA are loans given to doubtful customers who may or may not repay the loan on time. More than two-thirds of household savings are channelled through the banking system, which also provides more than 90% of the commercial credit in the country. Money or Assets provided by banks to companies as loans sometimes remain unpaid by borrowers. This late or non-payment of loans is defined as Non-Performing Assets (NPA). They are also termed as bad assets. The Indian banking system is beleaguered with non-performing assets (NPAs). According to the Reserve Bank of India's Financial Stability Report of December 2017, they currently stand at 10.2 per cent of all assets, while stressed assets, which are believed to be NPAs in effect, stand at 12.8 per cent. Related frauds amount to INR 612.6 billion in the last five financial years and governance failures on account of integrity and competence issues plague the banking system. This paper gives an empirical study on non-performing assets in public sector banks in India.

Keywords: ***Indian Financial System, Non-performing Assets (NPA), Doubtful customers, Bad assets, Commercial credit***

INTRODUCTION:

NPA is a short form of "Non-Performing Assets". In banking, NPA are loans given to doubtful customers who may or may not repay the loan on time. There are two types of assets viz. performing and non-performing. Performing loans are standard loans on which both the principle and interest are secured and their return is guaranteed.

Non Performing assets means the debt which is given by the Bank is unable to recover it is called NPA. Non-Performing Asset [NPA] is a result of asset Liability mismatch, A NPA account in the books of accounts is an asset as it indicates the amount receivable from the Defaulters. It means if any bank gives loan to the customer if the interest for that loan is not paid by the customer till 90 days then that account is called as NPA account.

In a bank-dominated economy, sustained impairment of the banking sector due to balance sheet problems creates a drag on real economic activity and can take the shape of an economic crisis. It is imperative to expeditiously resolve a banking sector crisis so that banks as the primary source of credit can start functioning normally again. In India, banking crisis is a recurrent phenomenon. since the liberalization reforms of 1991, there have been two major banking crisis episodes-the first one took place during the 1997-2002 period and the second one started in the aftermath of the 2008 Global Financial Crisis and is yet to be resolved.

In India, the RBI monitors the entire banking system and, as defined by the country's central bank, if for a period of more than 90 days, the interest or instalment amount is overdue then that loan account can be termed as a Non-Performing Asset. The increase in non-performing assets in Indian banks follows the recognition standards being pursued by the banks after the RBI highlighted it in the Asset Quality Review (AQR). Of course the main reason is inadequate progress in the financial health of the companies.

Assets can be categorized into four categories namely:

- Standard
- Sub -Standard
- Doubtful
- Loss

The last three categories are classified as NPAs based on the period for which the asset has remained non-performing and the reliability of the dues.

Standard assets: The loan accounts which are regular and do not carry more than normal risk. Within standard assets, there could be accounts which though have not become NPA but are irregular. Such accounts are called as special Mention accounts.

Sub-Standard Assets: With effect from 31.3.2005, a sub- standard asset is one, which is classified as NPA for a period not exceeding 12 Months (earlier it was 18 months). In such cases, 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 bank in full. In other words, such an asset will have well defined credit weakness that jeopardize the liquidation of the debt and are characterized 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 asset is to be classified as doubtful, if it has remained NPA or sub standard for a period exceeding 12 months (earlier it was 18 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 weakness makes 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 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 recoverable value.

CAUSES FOR AN ACCOUNT BECOMING NPA:

Those Attributable to Borrower:

- Failure to bring in Required capital
- Too ambitious project
- Longer gestation period
- Unwanted Expenses
- Over trading
- Imbalances of inventories
- Lack of proper planning
- Dependence on single customers
- Lack of expertise
- Improper working Capital Mgmt.

- MIS management
- Diversion of Funds
- Poor Quality Management
- Heavy borrowings
- Poor Credit Collection
- Lack of Quality Control

Causes Attributable to Banks:

- Wrong selection of borrower
- Poor Credit appraisal
- Unhelpful in supervision
- Tough stand on issues
- Too inflexible attitude
- Systems overloaded
- Non inspection of Units
- Lack of motivation
- Delay in sanction
- Lack of trained staff
- Lack of delegation of work
- Sudden credit squeeze by banks
- Lack of commitment to recovery
- Lack of technical, personnel & zeal to work.

THE INDIAN BANKS SHOULD ALSO CONSIDER "RISING CAPITAL" TO ADDRESS THE PROBLEM OF NPA:

- Using unclaimed deposits
- Monetization of assets held by Banks
- Make Cash Reserve Ratio (CRR) attractive
- Refinancing from the Central Bank
- Structural change to involve private capital

RECENT DEVELOPMENTS AND WAYS TO TACKLE NPA:

- Insolvency and Bankruptcy Code (IBC)
- Credit Risk Management
- Tightening Credit Monitoring
- Amendments to Banking Law to give RBI more power
- More "Hair-cut" for Banks
- Stricter NPA recovery
- Corporate Governance Issues
- Accountability

TO SOLVE ISSUE OF RISING NON-PERFORMING ASSETS IN INDIAN PUBLIC SECTOR BANKS:

Public Sector Banks:

Public Sector Banks (PSBs) constitute over 70 per cent of the banking system and are in a state of crisis. Participants believed that fundamental reforms tended to happen when crisis hit and this was an opportune moment for such reforms and expressed optimism that this was likely under this government.

PSBs have led to a financial deepening in the country. That said, the umbilical cord connecting the PSBs to politicians and bureaucrats, which in turn stems from the ownership structure of PSBs, has led to several inefficiencies including

- Disempowered boards
- Muted incentives for senior management to effect organizational change,
- Cloning of PSBs and the resultant systemic risks due to continual bureaucratic meddling
- External vigilance enforcement causing paralyzed decision-making, on the one hand, and widespread frauds and endemic corruption, on the other hand
- Opacity at various levels
- Distortions in human resource management.

RBI governance and regulation:

The RBI as a regulator has had qualified success in the face of structural impediments, including limited control over PSBs. RBI's internal governance as well as its regulation of NPAs needs improvement.

- Subsidiarisation: The RBI may consider the Bank of England model of subsidiarising its prudential regulatory and supervision functions.
- *Strengthening supervisory capacity:* RBI lacks supervisory capacity to conduct forensic audits and this must be strengthened with human as well as technological resources.
- *Preventing Evergreening:* RBI regulations have permitted banks to "ever-green" and in effect delay the recognition and therefore resolution of NPAs.

Reengineering of banking systems:

- *Secondary Market*: A vibrant secondary market for NPAs is crucial.
- *Concurrent Audit:* There is a real rot in the internal and concurrent audit systems of banks.
- *Diagnostics for willful default:* Banks need better permanent diagnostics to get to the bottom of willful defaults. This can happen though
    - Market intelligence
    - Funds flow analysis
    - Financial analysis
- *Using technology for maker-checker:* Currently, the maker-checker systems require human intervention and are therefore prone to capture and corruption. The use of Artificial Intelligence for the supervision of financial transactions could prevent financial fraud.
- *Combine with low tech – ears on the ground:* Business intelligence must use traditional means- speaking to people in the industry; supplier and customers can be an invaluable source of financial information.

CONCLUSION:

Banks can improve their financial position or can increase their income from credits. The umbilical cord connecting public sector banks to politicians and bureaucrats, which in turn stems from the ownership structure of these banks, has led to several inefficiencies. Diversified market ownership could bring market discipline to Public Sector Banks (PSBs).

Public sector banks suffer from a severe identity crisis and require business, not just financial, restructuring. The Indian banking sector has helped the business and service sector to develop by providing them credit facilities and other finance related facilities. The Indian banking sector is developing with good appreciate as compared to the global benchmark banks. The Indian banking system is classified into scheduled and non scheduled banks. The Banks play very important role in developing the nation in terms of providing good financial services. The NPAs would destroy the current profit, interest income due to large provisions of the NPAs, and would affect the smooth functioning of the recycling of the funds. If we analyze the past years data, we may come to know that the NPAs have increased very drastically. The RBI has also been trying to take number of measures but the ratio of NPAs is not decreasing of the banks. The bank must have to find out the measures to reduce the evolving problem of the NPAs.

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