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Rising NPAs: A Nightmare for Banking Industry

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***Abstract**: Banks's performance is the true reflection of economy of any country. The Indian banking system has been facing serious problem of non- performing assets. NPA's reflects the status of liquidity, Banks's management efficiency, net worth, profitability and eroded value of assets of any banking company. The sound financial position of any company is reflected by level of NPA's in that particular industry. Growth in NPA reflects that there is a need of strengthen the credit appraisal system of that industry because it shows the poor credit management system of the banks and it has negative effect on profitability of banks. The Indian banking system is facing the problem of continuously increment in level of NPA. This paper analyses the status of recovery mechanism through i.e. PROJECT SAKSHAT, SARFAESI Act, One time settlement (OTS) scheme, Lok-adalats and debt –recovery tribunals. This research paper also deals with capital adequacy norms regarding NPAs, major reason for conversion of loans into NPAs and to suggest measure for efficient management of NPA's for improving both profitability and liquidity position of banking industry.*

KEYWORDS: NPA, Capital Adequacy Norms, Project Sakshat, OTS scheme, SARFAESI act.

Introduction: The three letter "**NPA** "strike terror in business and banking industry today. NPA stands for Non – performing assets. The main business of banking company is to receive and lend money. Receiving deposit involves no risk, since it is a banker who owes a duty to repay the deposit, whenever needed. On the other hand lending always involves much risk because there is no any certainty of payment.An asset, including a leased asset, becomes non-performing when it ceases to generate income for the bank and is then termed as Non-Performing Asset (NPA). RBI has defined NPA as a credit facility in respect of which the interest and / or installment of principal has remained 'past due' for a specified period of time as stipulated by RBI. NPA is an important parameter in the analysis of financial performance of a bank as it results in higher provisioning requirements and thus decreasing margin. It affects liquidity and profitability, in addition to posing threat on quality of asset and survival of banks. It points out the credit risk of the banks. On-Performing Asset means an asset or account of borrower, which has been categorized by a bank or financial institution as sub-standard, doubtful or loss asset, in accordance with the directions or guidelines relating to asset classification issued by The Reserve Bank of India.

- **NPA's classification norms according to RBI's new guidelines:**

- 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,
- Interest and/ or installment of principal remains overdue for two harvest seasons but for a period not exceeding two half years in the case of an advance granted for agricultural purpose, and
- Any amount to be received remains overdue for a period of more than 90 days in respect of other accounts.

- **Classification of NPA for banking industry:**

CLASSIFICATION OF NPA

STANDARD ASSETS
That assets which has remained NPA for a period less than or equal to 12 months

SUB-STANDARD ASSETS
That asset which has remained NPA for a period for less than or equal to 18 months

DOUBTFUL ASSETS
That asset which has remained NPA for a period exceeding 18 months

LOSS ASSETS
Those assets which is considered as uncollectible

- **Relation between NPA and Capital Adequacy Ratio (CAR):**

Capital adequacy ratio: CAR is also known as capital to risk-weighted assets ratio, measures a bank's financial strength by using its capital and assets. It is used to protect depositors and promote the stability and efficiency of financial systems around the world. Generally, a bank with a high capital adequacy ratio is considered safe and likely to meet its financial obligations. CAR is calculated by dividing a bank’s capital assets by its risk weighted assets. For calculation of CAR capital is divided into two tiers:

- **TIER 1:** It is comprised of equity capital, ordinary share capital, intangible assets and audited revenue reserves. Tier-one capital is used to absorb losses and does not require a bank to cease operations.

- **TIER 2:**It is summation of unaudited retained earnings, unaudited reserves and general loss reserves. This capital absorbs losses in the event of a company winding up or liquidating.

NPA and CAR both are interdependent. If bank has more NPA then it will have more risk towards CAR weights thus bank will hesitate to give more loans.as per Basel norms, banks are required to maintain adequate capital on risk weighted assets (RWA) on an ongoing basis. Every increase in NPA level adds to risk weighted assets which warrant the banks to shore up their capital base further.

Review of literature: There are a lot of researches have been conducted to study the trend of NPA in banking industry. Many published articles are available in the area of non -performing assets and a large number of researchers have studied the issue of NPA in banking industry.**Mwakajumilo (2014)** assessed the impact of non- performing assets in the growth of banking industry in Tanzania. The research paper found out the different factors which lead the conversion of assets in NPA. For finding out the reason of conversion into NPA, study was conducted on 14 factors. From among the all factors lack of Management, Absence of credit reference Bureau, Poor risk management, Failure to cope with technological changes, Difficult in provision of consumer loans, Lack of information among depositors and among others were main reason of increasing number in NPA's level.**Kavitha & Meethumeenakshi (2016)** studied the trend if NPA's in both private and public sectors for last 5 years and also made comparative analysis between both sectors. The research paper concluded that level of NPA's in banking sectors is more in comparison of private sectors and comparison studied through % of GNPA & % NNPA in both sectors.**Dudhe(2017)** analyzed the trend in NPA in terms of value, gross NPA and profit. The data was collected for time period 2007-2016 of 7 banks. The analysis was done through regression and correlation analysis. This research paper founds out that there is negative relationship between NPA and profitability except PNB and SBI banks because both of these banks are the largest banks in the country and are earning through a variety of different financial services.**Garg(2017)** founded in his study that from 2010 to 2014, level of gross NPA has been increased from 2.4% to 3.84% of gross advances. The study conducted by him also concluded thatthe bank management should speed up the recovery process and a strict policy should be followed to for solving this problem. This research paper focused on to study the impact of NPA on Indian economy if not any steps taken by government to control % of increasing NPA in banking industry.**Jayaramanet al. (2018)** in his study found that there is inverse relationship between RGDP and NPA. This research paper also concluded that gross advances and NPA are directly related to each other and also found out that aggressive credit policy of pushing loans result in increase in higher NPA. Autoregressive Distributed Lag Procedure (ARDL) was adopted to study macroeconomic and specific banking factors which directly affect the NPA growth in the economy.

Dey, (2018) conducted a study to analyze the recovery mechanism of NPA through three mechanismsi.e., recovery through Lok Adalat, DRTs and SARFAESI act and found that recovery through DRTs mechanism was efficient in comparison of other two. This research paper also suggested that Banks should continuously monitor loans to identify accounts that have potential to become non-performing.

Objectives of the Study:

This research paper focused on analysisof different recovery mechanism scheme which has been launched by RBI and government for recovery of NPA's through i.e. PROJECT SAKSHAT, SARFAESI Act, One time settlement (OTS) scheme, Lok-adalats and debt –recovery tribunals.

Research Methodology:

The data has been collected through secondary method of data collection. The sources of data for this article is include the literature published by Indian Banks and the Reserve Bank of India, various magazines, Journals, Books dealing with the current banking scenario and research papers.

- **Different Initiatives Taken by Government towards Conversion NPA into Realizable Assets:**

PROJECT SAKSHAT: Project Sakshat is a 5-point strategy to deal with NPA, which was recommended by a panel which was headed by Sunil Mehta, chairman of Punjab National Bank. The five-pronged strategy includes -- SME resolution approach, bank-led resolution approach, AMC/AIF led resolution approach, NCLT/IBC approach, and asset-trading platform. The goal of the programmed is to connect all institutions of higher learning to the world of knowledge in cyberspace, to maximize the potential of ICT in offering high-quality knowledge modules with appropriate e-contents, and to cater to the individual needs of learners in order to meet their goals.

SARFAESI act: The Act provides three alternative methods for recovery of non-performing assets:

- Securitization
- Asset Reconstruction
- Enforcement of Security without intervention of the court

SARFAESI stand for securitization and Reconstruction of financial assets and enforcement of securities interest act, (2002). Under, this act banks and other financial institutions to auction residential or commercial properties to recover the loans.

One Time Settlement Scheme:OTS is a scheme where the borrower (the one who has defaulted) proposes to settle all the dues at once, and banks agree to accept an amount lesser than what was originally due. The banks settle the loan and waiver/write it off against a one-time installment, thereby compromising on a portion of their profits. OTS scheme is different for different sectors, its guideline is different for agriculture, and MSME and others fields also.

Debt recovery tribunals: The Debt Recovery Tribunals have been established by the Government of India for expeditious adjudication and recovery of debts due to banks and financial institutions. The Debt Recovery Tribunal is also the appellate authority for appeals filed against the proceedings initiated by secured creditors under the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act.

Lok-Adalats: Lok Adalat institutions help banks to settle disputes involving account in “doubtful” and “loss” category, with outstanding balance of Rs. 5 lakhs for compromise settlement under Lok Adalat. Debt recovery tribunals have been empowered to organize Lok Adalat to decide on cases of NPAs of Rs. 10 lakh and above. This mechanism has proved to be quite effective for speedy justice and recovery of small loans. The progress through this channel is expected to pick up in the coming years.

The insolvency and bankruptcy code (IBC): The Insolvency and Bankruptcy Code, 2016 (IBC) is the bankruptcy law of India which seeks to consolidate the existing framework by creating a single law for insolvency and bankruptcy. The code will be able to protect the interests of small investors and make the process of doing business a less cumbersome process.

Status of total recovery from defaulters through different NPA's recovery initiatives:

In the fiscal ended March 2018, banks recovered Rs 40,400 crore worth of bad loans as against Rs 38,500 crore recovered in FY17. The various channels through which lenders recovered their bad loans include the Insolvency and Bankruptcy Code (IBC), SARFAESI Act, debt recovery tribunals (DRTs) and Lok Adalat. While banks recovered Rs 4,900 crore of bad loans through the IBC, the amount recovered through SARFAESI was Rs 26,500 crore in FY18.

Conclusion and Recommendations:

NPAs affect the financial performance of Indian banks as well financial growth of economy. Indian banking system is facing the NPAs problem. Every country's economic growth depends upon their financial system. The financial system mainly comprises banking sectors. This research paper analyzes different initiatives taken by government and RBI for recovery of NPAs and concluded that these initiatives have a positive impact on NPA's recovery but still this problem exist due to misgovernance, financial crisis, diversification of funds to unrelated business, lack of morale and there are many other factors also. On the basis of this research paper it is recommended that besides all those initiatives and schemes, government should focused on credit monitoring and credit appraisal scheme, rotation of staff, penalize for wrongdoing etc. for preventing conversion of good assets into bad loans.

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