Research Paper

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Trends in NPA Management: Comparative Study of Indian PSU Banks & Private Banks

Management

KEYWORDS : Non Performing Asset, NPA management, restructured accounts, Financial distress.

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ABSTRACT

Post reform era has changed the whole structure of banking sector of India. The emerging Competition has resulted in new challenges for the Indian banks. Hence, parameters for evaluating the performance of banks have also changed With the slowdown of the Indian economy a number of Companies/Projects are under stress. As a result the Indian Banking System has seen increase in NPAs and restructured accounts during recent years. The public sector banks as a whole are sitting on time bomb of Nonperforming assets that is ticking away fast. All over the problems faced by the banks either flow from it or are vastly aggravated by it. Not only do financially distressed assets produce less than economically possible, they also deteriorate quickly in value. Therefore there is a need to ensure that the banking system recognizes financial distress early, takes prompt steps to solve it. Dilution of government ownership of banks however is a necessary but not sufficient reform to tide over the crisis. This paper an effort has been made to analyze how efficiently Public and Private sector banks can manage NPA.

Introduction:
Banking system plays a vital role in the economic system of a country by mobilizing the nation's savings and directing them into high investment priorities for better utilization of available resources. Banking in India originated in the last decade of the 18th century. Private and public sector banks occupy a major part of the banking in India. They are the oldest form of banking institution having large volume of operations over a vast area. They are having very good net-work of branches even in rural and semi-urban areas. The Indian banking system has undergone significant transformation following financial sector reforms were set in motion in 1991. It is adopting international best practices with a vision to strengthen the banking sector. The failure of the banking sector may have an adverse impact on other sectors. Non-performing asset (NPA) is 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. The NPA growth involves the necessity of provisions, which reduces the overall profits and shareholders' value. Ballooning NPA of banks across the nation have been a cause of great concern for the bankers. Several prudential and provisioning norms have been introduced, and these are pressurizing banks to improve efficiency and trim down NPAs to improve the financial health in the banking system. Slow pace economy and consequent payment defaults among enterprises is major contributor to the constant surge in NPA levels of banks. Every quarter banks have been projecting more and more grim picture in the financial results. This has not only been sending shivers down the spine of respective banks but it has also been raising serious concern for the regulator and policy makers.

Public sector bank, owned and underwritten by Government of India, valued so poorly by the markets. There are many factors –low profitability, undercapitalization, external interference eroding operational freedom and professionalism. But they all converge on one massive problem: Asset quality or proportion of bad loans that may have to be written off partly or fully-various called non performing asset, troubled loans, restructured loans or stressed assets. All other problems faced by the banks either flow from it or are vastly aggravated by it. However private sector banks both new and old also operate in the same macro economic conditions. Still they are able to contain their bad loans because they are vigilant in credit appraisal, risk management and loan recovery.

Reasons for High Level of NPA:
Slower Economic growth: A sluggish economy has a direct impact on the balance sheets and profitability of many firms who have availed of loans from the banking industry. Over a period of time, some of the hard hit firms will be compelled to default on their loans. Uncertainty in global market had resulted in lower exports of textiles, leather and gems and hence contributed in NPAs.

High Interest Rates: Rising Interest rates is leading to an increase in bad loans among banks in India. High interest rate increases the cost of funds to the credit users and has a debilitating effect especially on the repayment capacity of small and medium enterprises.. A high rate of inflation dilutes the quality of assets of the banking sector. Weak supply demand scenario, high borrowing or leveraging and intense competition contribute to loan defaults.

Delays in Project: Government has encouraged lending in an effort to support development of the country's inadequate infrastructure, but although these intentions are positive, delays to projects due to several reasons and other regulatory issues have weighted on revenues and thus developer's ability to repay debt.
Ban on mining projects and delayed clearances: bad loans grew due to factors such as ban on mining projects and delayed clearances, which affected the power, iron and steel sectors in particular. Volatility in price or raw material and shortage of power has impacted the operations of textile, iron & steel and infrastructure companies.

Aggressive lending in Past: NPAs have increased due to the sluggishness of the recent past. Delays in collection of receivables for infrastructure projects and aggressive lending by banks in the past have also contributed to the rise in level of bad debts.
Restructured Accounts: Restructured accounts have grown at a compound annual growth rate of 47.86 percent in PSU banks. The corresponding figures for private sector and foreign banks are 8.12 percent and 25.48 percent respectively. These restructured accounts turned as NPAs to the Banks.

Other Factors: Guided lending for banks is one of the reasons for banks; to meet national goals at times, quality of appraisal is relaxed which later creates problems. There are many other causes which are also responsible for accumulation of NPAs, some of them are faulty credit management, lack of professionalism in the work force, unscientific repayment schedule, misutilization of loans by user, lack of timely legal solution to cases filed in different courts, political interference at local levels and waiver of loans by government have also been contributing to mounting NPAs in India.

Literature Review:
Usha Arora, Bhavana Vashist and Monica Bansal (2009)ana-

lyzed and compared the performance in terms of loan disbursement and non-performing assets of credit schemes of selected banks for the last five years. A positive relationship is found between total loan disbursement and total non-performing Assets Outstanding (NPA O/S) of selected banks. They suggested that proper steps like negotiated compromise, legal remedies, acquisition and take over should be taken to solve the NPA problem.

Roopak Kumara Gupta and Ekta Sikarwar (2010)observed that the Commercial banks, especially the dominant public sector banks, have been facing competition from the banks in the private sector. They stated that Asset Quality is one of the components of performance of banks which can be assessed by Net NPA to Net Advances (NNPA/NA). Asset Quality determines the existing and potential credit risk associated with loan and investment portfolios and other off Balance Sheet transactions. Higher the ratio, lower is the asset quality of the bank.

Shalu Rani (2011)examined the existing position of banks in Scheduled Commercial Banks (SCBs) of India in respect of NPAs, the causes and remedial measures thereof and concluded that the level of NPA has increased, eroding whatever reduction was made with the ever increasing level of fresh NPAs and tightening of norms by RBI time to time. Total elimination is not possible in banking business so it is wise to follow the proper policy for appraisal, supervision and follow up of advances to avoid NPAs.

Siraj. K.K and Prof. (Dr). P. Sudarsanan Pillai (2012) states that NPA is a virus affecting banking sector. It affects liquidity and profitability, in addition posing threat on quality of asset and survival of banks. This study explored movement of various NPA indicators; Gross NPA, Net NPA, Additions to NPA, Reductions to NPA and Provisions towards NPA and compare it with Total Advances and Total Deposits of banks. The recessionary pressures faced by the banking sector is an important reason for the growth of NPA indicators, it should be managed to maintain a healthy and viable banking environment. The increased level of additions to NPA remained as an area of concern as it indicates the real efficiency of credit risk management.

Dr. Rohit R. Manjule (2013) analyze in his research paper that Non Performing Assets (NPA) is one of the major concerns for banking system around the globe and Indian Banking system is not an exception to this universal phenomenon. He concludes that it is right time to take suitable and stringent measures to get rid of this problem. An efficient management information system should be developed. The bank staff involved in sanctioning the advances should be trained about the proper documentation and charge of securities and motivated to take measures in preventing advances turning into NPA and constant following up and monitoring of loans after disbursement.
Objectives:

1. To Study the level and Trends of NPAs in banking sector in India.
2. To make a comparative analysis on NPA management by Public sector and Private sector banks in India.

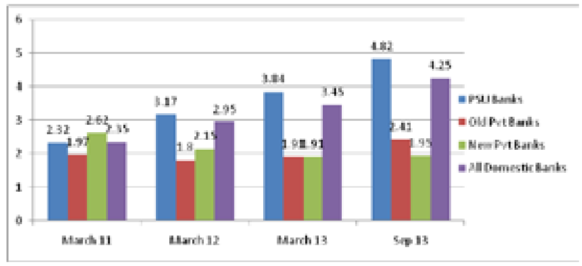
Research Methodology: The research is exploratory in nature and the study uses the latest available published secondary data for the years 2008-2013 compiled from Report on Trends and Progress of Banking in India RBI. For the purpose of analysis of data appropriate trend and percentage analysis is used.

Trends in Non-performing Assets

Year	Public Sector Banks		Private Sector Banks	
	Gross NPA	Net NPA	Gross NPA	Net NPA
2007-08	2.20	1.00	2.30	0.70
2008-09	2.00	0.94	2.36	0.90
2009-10	2.20	1.09	2.32	0.82
2010-11	2.40	1.20	1.97	0.53
2011-12	3.30	1.70	1.80	0.60
2012-13	4.10	2.00	0.20	0.50

Source: RBI

Data analysis



Gross NPA to Advances by Bank Groups

Source: Department of Banking Supervision, RBI

Figures in the Bar-diagram showed that NPAs in the Banking system have been on the rise in recent times; that an overwhelmingly high share of the increase in absolute NPAs was on account of PSU Banks and that the situation is likely to become worse before it starts improving. Level of Gross NPAs to Advance is drastically changed in Sep 2013 by 4.82 percent then in March 2011 by 2.32 percent in PSU Banks while the same ratio is lesser in Old Private Banks 1.97 to 2.41 percent in same period and in New Private Banks it Gross NPA to Advance is decreased from 2.62 in march 2011 to 1.95 in September 2013.

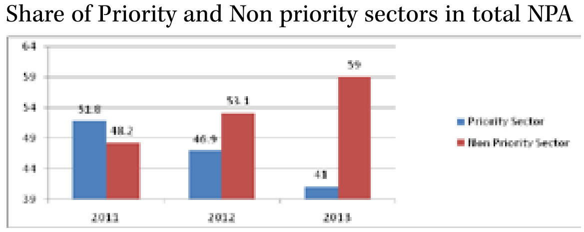
Bank Group-Wise Classification of Loan Assets of Schedule Public and Private Sector Banks from 2008 to 2013 (Rs.Billion) As on March 31

	Year	Standard Advance	Percent Share	Sub Standard Advance	Percent Share	Doubtful Advance	Percent Share	Loss Advance	Percent Share	Gross NPAs	Percent Share	Total Gross Advance
Public Sector Banks	2008	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
	2009	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
	2010	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
	2011	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
	2012	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
	2013	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Private Sector Banks	2008	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
	2009	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
	2010	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
	2011	[illegible]	[illegible]	44	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
	2012	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
	2013	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

Source: Department of Banking Supervision, RBI

The gross NPA ratio at the aggregate level stood at 3.84 per cent at end-March 2013 up from 3.17 per cent at end-March 2012. The deterioration in asset quality was most perceptible for the PSU Banks with its NPA ratio reaching a high of nearly 4 per cent at end-March 2013. Private sector banks succeeded to reduce their Gross NPAs % in the year 2013 at end of march by 1.91% then 2.08% in March 2012.

Share of Priority and Non priority sectors in total NPA



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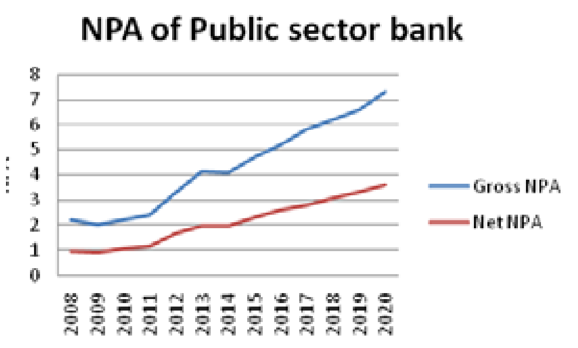
Source: offsite returns for domestic banks

Non-priority sector is the major contributor to rise in NPAs in banking sector in India. Bar Diagram Shows the increasing share of NPA in non priority sector form 2011 to 2013 on the contrary there is a decrease share of NPA in priority sector lending from 51.8% in year 2011 to 41% in 2013.

Forecasting NPAs of PSU Banks and Private Banks:

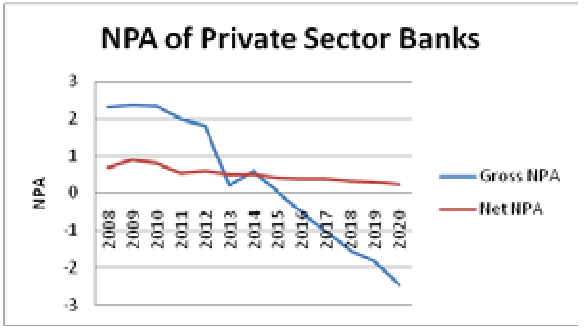
Forecasting of NPAs in near Future for PSU Banks

Year	Public Sector Banks	
	Gross NPA	Net NPA
2008	2.2	1
2009	2	0.94
2010	2.2	1.09
2011	2.4	1.2
2012	3.3	1.7
2013	4.1	2
2014	4.06	2
2015	4.7	2.3
2016	5.2	2.6
2017	5.8	2.8
2018	6.2	3.1
2019	6.6	3.3
2020	7.3	3.6



Forecasting of NPAs in near Future for Private Banks

Year	Private Sector Banks	
	Gross NPA	Net NPA
2008	2.3	0.7
2009	2.36	0.9
2010	2.32	0.82
2011	1.97	0.53
2012	1.8	0.6
2013	0.2	0.5
2014	0.6	0.5
2015	0.026	0.42
2016	-0.54	0.37
2017	-1.047	0.37
2018	-1.53	0.31
2019	-1.83	0.28
2020	-2.45	0.23



Findings:

Gross nonperforming assets of Public sector banks rose to 5.17% of their advances at the end of December 2013, against 4.18% a year before. The highest NPAs, at 7.21% of advances, are in loans to small and medium enterprises, followed by agriculture at 5.99%. The exposure of PSBs towards infrastructure is around 15%, while for private banks is less than 2%. NPA to the corporate sector were 5.28% at the end of December-2013 and 2.74% and 1.83%, respectively to the retail and real estate segments. Most of bad loans are in infrastructure sector because of economic slowdown and policy paralysis. In the last two decades, private sector banks-ICICI Bank, HDFC Bank, Yes Bank, Axis Bank and so on-have been gaining market share at the expense of state-owned banks. For example, they have increased their current account savings account (CASA) market share to 17% in 2013 from14% in 2009. The focus on retail segment has helped new private sector banks in the last five years when the economy passed through a slowdown. However public sector banks continued to focus on the corporate loan segment in this period, which proved to be bad strategy. With consumption pattern changing further in favor of discretionary spending, good growth is likely in consumer loans namely home loans, auto loans and credit cards. With private sector banks eyeing growth in semi-urban and rural areas, they are likely to further eat into the existing market share of state-owned banks.

Public sector banks seem to be fair game for businessmen with strong political connections. They manage to get large loans for dubious projects, happily default and carry on with business-as-usual. They have strong industry associations and lobbies to plead their case. By eroding profitability and depressing market valuation of the public sector banks, NPAs have made under-capitalization of banks an intractable problem. The stock market perception of public sector banks is worse. India has 24 listed government owned banks- State bank of India and three associates, 14 banks nationalized in 1969, and six banks nationalized in 1980. The combined market value of these banks as on March 2013, with the exception of State Bank of India, was about Rs 1.59 lakh crore. That was fractionally less than the value of a single private sector bank: HDFC Bank which started from scratch in 1993 and had a market cap of Rs 1.6 lakh crore. Even the State Bank of India, the best and the brightest among the public sector banks, had a value on market (Rs 1.21 lakh crore) that was less than that of ICICI Bank (Rs 1.21 lakh crore). In other words, two private sector banks which were set up relatively are valued more highly by the stock market than the entire public sector banking system. Even if the NPA problem had not acquired the alarming proportion that it has, banks in general and public sector banks in particularly would still need massive doses of fresh capital just to maintain their growth by meeting new norms for capital adequacy. In a recent report, Moody's estimates recapitalization requirement at Rs 22,500-36000 crore by March 2015, against the allocated Rs 11,500 crore in the interim Budget.

Suggestions:

The first set of measures relates to the RBI controlling bank activity:

1. First RBI should mandate that banks should not lend to the companies not repaying loans. Time and money should be spent on following up the borrower and to take up legal, non-legal measures like persuasion, one time settlement (OTS). Besides, lending decisions are with the bank management and can at best be placed before the Board.
2. Second, RBI should actually set sectoral limits for lending. Currently the RBI has limits on company and group lending. It is possible that the RBI can identify the top five sectors periodically-either quarterly or annually- and mandate that banks con not go beyond a limit of say 10% of incremental credit to these sectors.
3. Third RBI should ask the board to closely monitor lending to these vulnerable sectors and insist that banks should have an internal policy on how much lending is done to such sectors. Hence, it will be in a position to know in advance how banks are lending.

The Second set of issues examines ways to deepen the role of RBI as a regulator:

1. Extra capital should be provided for that portion of NPA amount which is not covered by the value of the security held against the loan. The idea is to ensure that banks should have adequate buffers for such eventualities. Here are two ways worth exploring. The first is in the area of provisioning. With Basel III being implemented in the context of capital and RBI's own policy on dynamic provisioning for NPAs the same should be extended to the case of vulnerable industries.
2. Necessary steps should be taken for dynamic provisioning for standardized assets in potentially weak sectors that are being supported by banks. Currently, the provisioning norms on sub-standard, doubtful and loss assets are quite firm. In case of standard assets there is a general provisioning norm of 0.4% with higher rate for specific sectors. Here, the RBI should mandate that a current standard asset in a vulnerable sector will necessitate higher provisioning which scales up as one move along the rank. Therefore, if infrastructure has the highest NPAs and mining the lowest, then the provisioning norm for mining should be 0.5% and can go up to say 2.5% for infrastructure.
3. Stoppage of recycling of funds which otherwise could have been lent to other needy ones and thus stoppage of resolving income. However, what is needed most is greater care before giving loan and greater monitoring after giving it. A notable initiative in this direction is RBI's recent guideline Early Recognition of Stressed assets should be follow in such a manner that bank can identify stressed asset well before it results in NPAs.

Conclusion

The increase in NPAs also shows that neither was assets created nor was the promoter's margin found adequate during recovery. During FY 13, both Indian and global economies faced exorbitant challenges putting additional stress on asset quality eventually resulting in increase in GNPAs, net non performing assets and restructured assets. PSBs faced larger asset quality implications owing to the fact that they were the prime lender to crucial and slowing sectors like power and agriculture which took substantial hit during the economic slowdown. However Private sector banks both new and old also operate in the same macro economic conditions. Still they are able to contain their bad loans because they are vigilant in credit appraisal, risk management and loan recovery. They lend less to wily businessmen who knows all the tricks in the book to dodge a loan and more to middle class people who are far more honest and regular in repaying their debt. Even when they lend to corporate houses, it is more to meet short term working capital need than long term projects that may take years to complete and are dogged by uncertainties of several kinds. The problem of NPAs and restructured assets has become quite exasperating with their combined level crossing the double-digit mark. The problem reside in sectors such as infrastructure, steel, textiles, aviation and mining. The RBI has been voicing concern and has warned banks to keep them under check and has said promoters cannot get away with bad loans. If the NPAs are caused by willful defaulters, then there is a case to chastise banks for supporting them. But if it is due to conditions beyond control several effective redressal measures should be taken.

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