AN EMPIRICAL EXAMINATION OF MEASURES TAKEN BY BANKS FOR THE MANAGEMENT OF NON–PERFORMING ASSETS (NPAs)

Dr. Vijay Kumar*

Surinder Kumar**

ABSTRACT

Non-Performing Assets (NPA's) management is a matter of concern to entire banking industry. Before drawing up a proper plan for the recovery of NPAs what one has to see is the background of an NPA and the reasons for its origin. A lot of NPAs result from lack of proper monitoring and control. There are NPAs which occur due to the factors beyond the control of the borrowers. Sometimes, NPAs occur due to diversion of funds by the borrower. But, effective monitoring and control will definitely restrict NPAs. The eagerness shown by the banks to reduce NPAs is definitely a welcome step in a right direction. But, it should be ensured that NPAs are being reduced by taking stringent measures at the time of loans sanctioning, regular monitoring, systematic evaluation and legalised recovery and not through excessive provisioning to mislead the competitors, stakeholders and public at large.

*Department of Commerce and Management, Shri Guru Nanak Khalsa College, Yamuna Nagar .

**Department of Commerce, D.A.V. College, Sadhaura, Yamuna Nagar.

INTRODUCTION OF NPAs:

The principal objectives of commercial banking operations are to generate profits and contribute to growth process of the country. The technique that commercial banks adopt to fulfill these objectives has a direct bearing on their assets and liabilities. Banks always strive to adopt an appropriate operational approach with a view to maintain liquidity and profitability of their assets. But there are many assets in the banking system, where there is an imbalance between the liquidity and profitability. Such assets are known as non performing assets, for instance, term loan, overdraft, cash credit account, government securities, etc. The amount to be received from these assets remains unpaid or remains overdue. The government securities, bonds and debentures of corporations can also be included in non performing assets, if interest is not received regularly from them and if still there are some recoverable arrears. In other words, an asset will become non-performing asset, if it does not generate income to the bank.

An asset is classified as non-performing asset if dues in the form of principal and interest are not paid by the borrower for a period of 180 days. However, with effect from March 2004, default status would be given to a borrower if dues are not paid for 90 days. If any advance or credit facilities granted by banks to a borrower becomes non-performing, then the banks will have to treat all the credit facilities granted to that borrower as non performing without having any regard to the fact that there may still exist certain credit advances having performing status.

The most calamitous problem being faced by commercial banks all over the world in recent times is spiraling non-performing assets (NPAs). They are affecting their viability and solvency. NPAs adversely influence lending activity of banks as non recovery of loan installments and interest on the loan portfolio negates the effectiveness of credit dispensation process. Non recovery of loans also hurt the profitability of banks. Besides, banks with high level of NPAs have to carry more own funds by way of capital and create reserves and provisions and to provide cushion for the loan losses. NPAs, thus, make two pronged attack on the bottom lines of commercial banks: one, interest applied on such assets is not taken into account because such interest is to be taken into account only on its realisation, two, banks have to make provisions for NPAs from the income earned by them on performing assets. Persistently high level of NPAs make banks and financial institutions fragile leading ultimately to their failure. This shakes confidence both of domestic and global investors in the banking system.

Thus, managing bad loans and keeping them at the lowest possible level is critical and need of the hour for banks. An NPA level of over five percent is indicator of poor quality of loan portfolio. With growing competition and shrinking spreads, banks should strive to keep NPAs much below the level of ten percent to make net earnings necessary for their survival and growth. Under the new RBI monitoring system a bank's performance has become crucially dependent on the recognition of income and non performing assets. Before discussing how to manage loans in commercial banks, it would be pertinent to comprehend the concept of NPAs and examine factors contributing to the emergence of NPAs in the loan portfolio of banks.

NEED FOR MANAGEMENT OF NPAs:

Since the adoption of liberalisation, privatization, globalisation and financial sector reforms, banks and financial institutions are under tremendous pressure to reduce and bring down their NPAs at par with international standards. The reduced NPAs will improve the profitability of such institutions. The concept of NPAs introduced during the year 1992-93 in Indian banking industry forced the financial institutions to keep their lending rates high because NPAs results in higher operational cost and erode the capital. The NPAs also have a double effect on the profit and loss account, firstly the income arising on accrual basis is not recognised and secondly the sufficient provision is to be made in the balance sheet. This is definitely going to strain the profit and loss account which, in turn, jeopardises the solvency of the financial institutions. The guidelines issued by the Reserve Bank of India on income recognition, assets classification and provisioning norms have compelled banks in India not only to show the true financial picture in the balance sheet but also to take corrective steps for improving their loan portfolio.

NPA management is a matter of concern to entire banking industry. Before drawing up a proper plan for the recovery of NPAs what one has to see is the background of an NPA and the reasons for its origin. A lot of NPAs result from lack of proper monitoring and control. There are NPAs which occur due to the factors beyond the control of the borrowers. Sometimes, NPAs occur due to diversion of funds by the borrower. But, effective monitoring and control will definitely restrict NPAs.

The eagerness shown by the banks to reduce NPAs is definitely a welcome step in a right direction. But, it should be ensured that NPAs are being reduced by taking stringent measures at the time of loans sanctioning, regular monitoring, systematic evaluation and legalised recovery and not through excessive provisioning to mislead the competitors, stakeholders and public at large.

MEASURES TAKEN BY BANKS TO MANAGE NPAs:

NPA is not just a problem for banks, they are bad for the economy. The money locked up in NPAs is not available for productive use purpose and to that extent the banks seek to make provisions for NPAs or write them off. It adversely affects their profitability over a long period of time and results in higher rate of interest to their diligent credit customers. Steps taken at the appropriate time may help in avoiding NPAs. Qualitative appraisal, supervision and follow up should be taken up for the present advances to avoid further NPAs. Things have reached a stage where a hard look at some of the basic issues will have to be taken to improve bank general capabilities and to meet the prudential requirements. Reduction of NPAs should be treated as a national priority item to make the Indian banking system stronger, resilient and geared to meet the challenges of globalization. The following are the some measures for reduction of NPAs:-

Preventive Measures

(a) Proper Borrower Selection

(b) Financing Viable Schemes

(c) Holding of Recovery Camps

(d) Proper Sanction

(e) Avoiding Overdrawing

(f)Ensuring Proper End-use

Corrective Measures

(a) Recovery

(b) Rephasement

(c) Rehabilitation

Drastic Measures

(a) Filing of Suit

(b) Enforcement of Primary Securities

RESEARCH DESIGN:

The present study was taken for knowing the measures taken by Banks for the management of the NPAs. to attain this target following banking institutions operating at their local, regional and zonal levels have been approached to provide the requisite data and information. Banks operating at all the three levels include State Bank of India, Oriental bank of Commerce, Union bank of India, Allahabad Bank, Bank of Baroda, Canara Bank and Punjab National Bank. Banks operating at two levels include Bank of India, Central Bank of India, Dena Bank, Punjab & Sindh Bank, Sate bank of Patiala, Syndicate Bank and Vijaya bank. Banks operating at only one level include Andhra Bank, Bank of Maharastra, Corporation bank, Indian Bank, Indian Overseas Bank, United bvank of Infdia and UCO Bank.

In all 54 Bank branches of 21 public sector banks have been included in the study. These branches have been located in Haryana, Punjab, Delhi, U.P. and Chandigarh. The secondary data was collected from number of books, journals and websites. The collected primary information have been put to statistical tests like weighted average score, average standard deviation and chi-square.

Measures	**Frequency of use**				**WAS Rank**	**Summary**			
	Never	**Occasionally**	**Always**	**Total**		**WAS**	**Avg.**	**SD**	**CV**
Preventive Measures									
(a) Proper Borrower Selection	–	4 (7.41)	50 (92.59)	54 (100)	1	0.93	2.93	0.26	8.87
(b) Financing Viable Schemes	–	9 (16.67)	45 (83.33)	54 (100)	3	0.83	2.83	0.37	13.07
(c) Holding of Recovery Camps	1 (1.85)	20 (37.04)	33 (61.11)	54 (100)	7	0.59	2.59	0.53	20.46
(d) Proper Sanction	–	6 (11.11)	48 (88.89)	54 (100)	2	0.89	2.89	0.31	10.73
(e) Avoiding Overdrawing	2 (3.70)	15 (27.78)	37 (68.52)	54 (100)	6	0.65	2.65	0.55	20.75
(f)Ensuring Proper End-use	3 (5.56)	10 (18.51)	41 (75.93)	54 (100)	5	0.70	2.70	0.57	21.11
Corrective Measures									
(a) Recovery	–	13 (24.07)	41 (75.93)	54 (100)	4	0.76	2.76	0.43	15.58
(b) Rephasement	1 (1.85)	42 (77.78)	11 (20.37)	54 (100)	10	0.19	2.19	0.43	19.63
(c) Rehabilitation	3 (5.56)	39 (72.22)	12 (22.22)	54 (100)	11	0.17	2.17	0.50	23.04
Drastic Measures									
(a) Filing of Suit	2 (3.70)	39 (72.22)	13 (24.08)	54 (100)	9	0.20	2.20	0.49	22.27
(b) Enforcement of Primary Securities	5 (9.25)	30 (55.56)	19 (35.19)	54 (100)	8	0.26	2.26	0.61	26.99

Table shows that the analysis of the preventive measures explains highest respondent banks (92.59 percent) have used 'proper borrower selection' measure to check the NPAs followed by 'proper sanction', 'financing viable scheme', 'ensuring proper end-use', 'avoiding overdrawing' and 'holding recovery camps'. As far as the corrective measures are concerned 'recovery' measure seems to be more popular with the banks as ¾ of the respondents have ‘always' made the use of it. ‘Rephasement’ and 'Rehabilitation' have been 'occasionally' used. The drastic measures consisting of 'filing a suit' and 'primary security enforcement' have not 'always' been used in a great fashion. The majority of the banks have ‘occasionally’ used the drastic measures.

The coefficient of variation is minimum for preventive measure of 'proper borrower selection' and highest for drastic measure of ‘primary security enforcement’. It signifies respondents are more consistent for preventive measures as compared to drastic measures.

To sum up, it can be described that banks have made the use of all types of preventive, corrective and drastic measures in various degrees taking the ‘always’ and ‘occasionally’ together.

To sum up, the segment devoted to management of NPAs provided certain insights about following up of guidelines of RBI by banks at various levels, opinion about fairness of 90 days norm, use of various preventive, corrective and drastic measures, methods for reducing NPAs, use of OTS, DRT and Securitisation Act and machinery to deal with NPAs and different measures undertaken by banks for checking the menace of NPAs.

REFERENCES

1. Ahmed, J.U., “Assets Quality and Non-Performing Assets of Commercial Banks” (New Delhi : M.D.Publications, 2008).
2. Bedi, H.L., “Theory and Practice of Banking” (Mumbai, Jeevan Deep Parkashan. 1984).
3. Bidani, S.N., “Managing Non-Performing Assets in Banks” (Vision Books, 2002).
4. Jain, Vibha, “Non Performing Assets in Commercial Banks” (New Delhi: Regal Publications, 2007).
5. Reddy, B. Ramachandra, “Management of Non Performing Assets in Banks and Financial Institutions”, (New Delhi: Serials Publications, 2004).
6. Umarji, M.R., “Law and Preactical Relating to Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest” (Mumbai, Taxmann Pub. Pvt. Ltd., 2006).