Trend Analysis of Non Performing Asset in Scheduled Commercial Banks in India

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Abstract

Banking sector plays a pivotal role in the development of an economy. The development role it undertakes determines the pace of development of the economy. Hence the stability of banking sector is pivotal for the development of an economy. The primary function of banks is to lend funds as loans to various sectors such as agriculture, industry, personal and housing and other to meet the productive use of these funds. In recent times the banks have become very cautious in extending loans, the reason being mounting non-performing assets. Non-performing assets had been the single largest cause of irritation of the banking sector of India.

Non Performing Asset means an asset on which the interest or principal have not been paid by the borrower for the specified period in accordance with the directions issued by RBI.

The paper underlines the in depth study of the conceptual framework of Non Performing Asset commonly known as NPA in banking. It further discusses the NPA trend in the scheduled commercial banks in India for the preceding period of five years i.e. (2008 – 2012). Finally it covers the measures to be undertaken to reduce the menace of NPA in banks.

Key Words: Non Performing Asset, NPA, Scheduled Commercial Banks, Gross NPA, Net NPA, Advances.

1. Introduction

The Introduction of Financial Sector reforms since 1991 have enormously changed the face of Banking in India. The banking industry has moved gradually from a regulated environment to a deregulated market based economy. With the advent of liberalization and globalization, resulting in market development there has been tremendous change in the intermediation role of banks in India. The pace of transformation has been more significant in recent times with technology acting as a catalyst. Consequently, we are noticing the cut throat competition in the banking industry these days. Obviously, the problem of swelling non-performing asset (NPA) is catching attention and accumulation of huge NPA has assumed great importance in terms of risk management. Bankers thus have realized to have effective NPA management on their priority list. Before moving further, let us discuss the conceptual framework of the acronym “NPA”.

2. Conceptual Framework of NPA

2.1. Non Performing Asset (NPA)

Non Performing Asset means an asset of 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 relating to asset classification issued by RBI. Prior to 31st March, 2004 an NPA was defined as a credit facility in respect of which the interest or instalment or...
principal has remained past due for a specified period of time which was 180 days. Due to the improvement in payment and settlement system, recovery climate, up gradation of technology and to match with international banking practices it has been decided with past due concept, with effect from March 31\textsuperscript{st} 2004.

In accordance with the latest asset classification norms, a non-performing asset (NPA) shall be a loan or an advance, where:

- Interest and /or instalment 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 instalment 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.

### 2.2. Asset Classification and Provisioning Norms

- **Standard Assets** – These are those assets which do not create any problem while paying interest/ instalments of the principal. It usually carries more than normal risk attached to the business. Banks are required to keep 0.25% of advances as a provision under this category of asset.
- **Substandard Assets** – Those assets which has remained non performing for a period less than or equal to 12 months. Generally, banks are required to make 10% on total outstanding balance & 10 % on unsecured exposures as provisions.
- **Doubtful Assets** – Assets remained in the sub-standard category for a period of 12 months. 100% to the extent advance not covered by realizable value of security. In case of secured portion, provision may be made in the range of 20% to 100% depending on the period of asset remaining sub-standard
- **Loss Assets** – These assets are those 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. Generally 100% of the outstanding balance is kept as a provision.

### 2.3. Types of NPA

#### 2.3.1. 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.

It is calculated with the help of following ratio:

\[
\text{Gross NPAs Ratio} = \frac{\text{Gross NPAs}}{\text{Gross Advances}}
\]

#### 2.3.2. Net NPA:

These are those NPAs in which the bank has deducted the provision. Net NPA shows the actual burden of banks. Since in India, bank balance sheets contain a huge amount of NPAs and the process of recovery and write off of loans is very time consuming, provisions the banks have to make against NPAs according to the RBI guidelines, are quite significant. As a consequence, difference between gross and net NPA is very high. These are calculated as below:

\[
\text{Net NPAs} = \text{Gross NPAs} - \text{Provisions} / \text{Gross Advances} - \text{Provisions}
\]

### 2.4. Causes of NPA

The banking sector has been facing the serious problems of the rising NPAs. Some of the main causes of NPA are Ineffective recovery, Wilful defaults, Natural calamities Industrial sickness, Sluggish Legal System, Unfavourable Business Cycle, Defective lending process, Inappropriate technology, Poor Quality Management, Managerial deficiencies and Absence of Monitoring and Follow up.

### 2.5. Impact of NPA

NPA is a double edge weapon. On one hand, it does not generate income for the banks, and at the other banks are required to make provisions for such NPAs from their current profits. Because of the money getting blocked the prodigality of bank decreases not only by the amount of NPA but NPA lead to opportunity cost also as that much of profit invested in some return earning project/asset. So NPA doesn’t affect current profit but also future stream of

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profit, which may lead to loss of some long-term beneficial opportunity. Further, the recovery process adds to the woe of time for the employees and management. Apart from internal and external complexities, increases in NPAs directly affects banks’ profitability sometimes even their existence.

3. Objectives and Methodology
Some of the underlying objectives of the study are as follows.
1) To discuss the conceptual framework of Non Performing Asset in banking.
2) To highlight the trend of Gross NPA and Net NPA in Scheduled Commercial Banks in India for the period of five years.
3) To explore the remedies for the management of NPA in banks.

For our study, we have considered Non Performing Assets in Scheduled Commercial Banks which includes public sector banks, private sector banks and foreign banks which are listed in the Second Schedule of the Reserve Bank of India Act, 1934. The study is based on secondary data. The paper discusses the conceptual framework of NPA and it also highlights the trend of NPA in various banks during the period of 5 years i.e. from 2008 to 2012. Several reputed research journal including research paper and articles have been used by the researchers. Moreover, RBI Report on Trend and Progress of Banking in India for various years, websites and a book on banking has been referred during the study.

4. Discussion and Findings
The Gross and Net NPAs outstanding and as a percentage to Advances of Scheduled Commercial Banks over the preceding five years period is detailed in the below mentioned tables.

Table – 1

<table>
<thead>
<tr>
<th>Year</th>
<th>Gross Advances</th>
<th>Gross NPA (amount)</th>
<th>Gross NPA (percentage)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2008</td>
<td>25,079</td>
<td>564</td>
<td>2.3</td>
</tr>
<tr>
<td>2009</td>
<td>30,383</td>
<td>682</td>
<td>2.3</td>
</tr>
<tr>
<td>2010</td>
<td>35,449</td>
<td>847</td>
<td>2.39</td>
</tr>
<tr>
<td>2011</td>
<td>43,511</td>
<td>979</td>
<td>2.5</td>
</tr>
<tr>
<td>2012</td>
<td>51,589</td>
<td>1,423</td>
<td>3.1</td>
</tr>
</tbody>
</table>

Source: RBI

The above table depicts the amount of Gross Advances, Gross NPA and the percentage of Gross NPA during the period of 2008 to 2012. The amount of advances of has increased from Rs. 25,079 crore in 2008 to 51,589 crore in 2012. Further, the amount of NPA has also increased from Rs. 564 to Rs. 1,423 during the period (2008-2012). Similarly, NPA percentage is also showing the rising trend from 2.3 in 2008 to 3.1 in 2012.

Table – 2

<table>
<thead>
<tr>
<th>Year</th>
<th>Net Advances</th>
<th>Net NPA</th>
<th>Net NPA (percentage)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2008</td>
<td>24,770</td>
<td>247</td>
<td>1</td>
</tr>
<tr>
<td>2009</td>
<td>30,009</td>
<td>314</td>
<td>1.1</td>
</tr>
<tr>
<td>2010</td>
<td>35,013</td>
<td>391</td>
<td>1.12</td>
</tr>
<tr>
<td>2011</td>
<td>43,106</td>
<td>418</td>
<td>0.97</td>
</tr>
<tr>
<td>2012</td>
<td>50,842</td>
<td>649</td>
<td>1.4</td>
</tr>
</tbody>
</table>

Source: RBI

The above table shows the amount of Net Advances, Net NPA and the percentage of Net NPA during the period of 2008 to 2012. The amount of advances has increased from Rs. 24,770 crore in 2008 to 50,842 crore in 2012. Further, the amount of NPA has also increased from Rs.247 crore to Rs. 649 crore during the period (2008-2012).
The percentage of Net NPA has first increased from 1 in 2008 to 1.12 in 2010. Then it has decline to 0.97% in 2011 due to increase in provisions. Later the percentage of NPA have again surmounted to 1.4 in 2012.

Figure 1. Gross and Net NPA (Rs. in crores)

The above figure shows the trend of Gross NPA and Net NPA in crores for the period of five years starting from 2008 till 2012. The x-axis represent the years i.e. First, Second, Third, Fourth and Fifth years as the period of (2008 – 12) whereas y-axis represent the amount of NPA. We can observe here that the Gross and Net amount of NPA has been showing an upward trend beginning from first year till fifth year.

Figure 2. Gross and Net NPA (in Percentage)

The above figure portrays the trend of Gross NPA and Net NPA in percentages for the period of five years i.e from 2008 till 2012. The x-axis represent the years i.e. First, Second, Third, Fourth and Fifth years as the period of (2008 – 12) whereas y-axis represent the percentage of NPA. We can observe here that the Gross and Net percentage of NPA has been showing an upward trend beginning from first year till fifth year except for the fourth year which has shown a decline in the percentage of Net NPA.

5. Management of NPA

Some of the ways to manage the advances turning into NPA have been listed as below.

- There must regular follow-up with the customers and it is the duty of banker to ensure that there is no diversion of funds. This process can be taken up at regular intervals.
- Personal visits should be made after sanction and disbursal of credit and further close monitoring of the operations of the accounts of borrowed units should be done periodically.
- Managers under credit monitoring and recovery department should have dynamism and seal in their work. It has been observed that these personnel are worried due to accountability fixed arbitrarily. Many managers say that “we do not fear to negotiate but we do not negotiate out of fear. Such fear leads to arbitrary negotiation, which fails.
6. Conclusion

Ever since the introduction of financial sector reforms in India the Non Performing Assets of the banking system have been catching attention. NPA cause serious strain on the profitability as, on the one hand banks cannot book income on such accounts and on the other hand they are required to charge the funding cost and provision requirements to their profits. A mounting level of NPA in the banking sector can severely affect the economy in many ways. If NPA’s are not properly managed, it can cause financial and economic degradation which in turns hampers the investment climate which is crucial source looking to the present state of our economy. Bankers do opine that NPA is unavoidable in banking because of the basic nature of the business of banking. However, appropriate remedial measures as discussed above if followed shall restrain the accounts turning NPA signaling the soundness of banking.

References


AUTHOR

Ravindra Nathopanth Sontakke received PhD from RTMNU University, in 2010. Vidyabhusan Pursakar in 2011.He is having 20 years of teaching and 22 years of research experience and also PhD supervisor for RTMNU. He has published more than 25 National & International research
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