

A Study of Non-Performing Assets on Selected Public and Private Sector Banks

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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. This paper provides an empirical Approach to the analysis of profitability indicators with a focal point on non-performing assets (NPAs) of public and private sector banks. Non-performing assets are one of the major concerns for banks in India. NPAs reflect the performance of banks. The earning capacity and profitability of the banks are highly affected because of the existence of NPAs. A high level of NPAs suggests that large number of credit defaults that affect the profitability and net-worth of banks. Private and public Sector banks are highly affected by this three letter virus NPA, This paper an effort has been made to evaluate the operational performance of the selected PSBs & Private bank in India and also analyze how efficiently Public and Private sector banks can managing NPA. The magnitude of NPA was comparatively higher in public sectors banks compared to private banks under study but now, they have managed the number at lower end. ICICI bank still do have higher NPA figure compared to PSB under study*

Keywords: non- performing assets, public sector banks, private sector banks

1. Introduction

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. Now they are not only engaged in their traditional business of the accepting and lending money but have diversified their activities into new fields of operations like merchant banking, leasing, housing finance, mutual funds and venture capital. They have introduced a number of innovative schemes for mobilizing deposits. In addition to the above they are providing valuable services to their customers, issuing drafts, traveller cheques, gift cheques, accepting valuables for safe custody and modern banking facilities. Since the process of liberalization and reform of the financial sector were set in motion in 1991, banking has undergone significant changes. The underlying objective has been to make the system more competitive, efficient and profitable. A strong banking sector is important for flourishing economy. 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.

2. Non-Performing Assets (NPAS) – Meaning

Assets which generate periodical income are called as performing assets. Assets which do not generate periodical income are called as non-performing assets. NPAs are further classified into sub-standard, doubtful and loss assets based on the criteria stipulated by RBI. An asset, including a leased asset becomes non-performing when it ceases to generate income for the bank for a specified period of time.

3. Gross NPA and Net NPA

Gross NPA is advance which is considered irrecoverable, for bank has made provisions, and which is still held in banks' books of account. Net NPA is obtained by deducting items like interest due but not recovered, part payment received and kept in suspense account from Gross NPA.

4. Literature Review

Many studies have been conducted by researchers on NPAs in banking industry. The researcher has made attempts to present a brief review of the literature available, which are published in the form of research articles and technical papers published in the journals, magazines and websites in the related area. Kaveri (2001) studied the non-performing assets of various banks and suggested various strategies to reduce the extent of NPAs.

Prashanth k Reddy (2002) in his study focuses on comparative study on Non-Performing Assets in India in the Global context. Similarities and dissimilarities,

remedial measures and conclude the importance of a sound understanding of the macroeconomic variables and systemic issues pertaining to banks and the economy for solving the NPAs. Dong He (2002) reviews the nature of Non-Performing Assets in the Indian banking system and discusses the key design features that would be important for the Assets Reconstruction Companies to play an effective role in resolving such NPAs

Muniappan (2002) expressed that the problem of NPAs is related to several internal and external factors confronting the borrowers. The internal factors are diversion of funds for expansion, diversification and modernisation, taking up new projects, helping/promoting associate concerns, time/cost overruns during the project implementation stage, business (product, marketing, etc.) failure, inefficient management, strained labour relations, inappropriate technology/technical problems, product obsolescence, etc., while external factors are recession, non-payment in other countries, inputs/power shortage, price escalation, accidents and natural calamities. Das and Ghosh (2003) empirically examined non-performing loans of India's public sector banks in terms of various indicators such as asset size, credit growth and macroeconomic condition, and operating efficiency indicator

5. Objectives of the study

The Non-Performing Assets (NPAs) problem is one of the foremost and the most formidable problems that have shaken the entire banking industry in India like an earthquake. Like a canker worm, it has been eating the banking system from within, since long. It has grown like a cancer and has infected every limb of the banking system. At macro level, NPAs have choked off the supply line of credit to the potential borrowers, thereby having a deleterious effect on capital formation and arresting the economic activity in the country. At the micro level, the unsustainable level of NPAs has eroded the profitability of banks through reduced interest income and provisioning requirements, besides restricting the recycling of funds leading to serious asset liability mismatches. Unfortunately the high level of NPAs of banks is adversely affecting the profitability, liquidity and solvency position of the banking sector. Therefore NPA should be brought down to internationally accepted level (i. e. 2-3% of loan assets). The objectives of the present study are:

- Find out trends in NPA Level.
- Highlight the NPAs position of selected PSB's and Private Banks
- Assess the comparative position of NPA in selected PSBs & Private banks.
- Assess the variation of NPA ratio in selected PSBs & Private banks

6. Categories of NPAs

- Standard Assets: Standard assets generate continuous income and repayments as and when they fall due. So

a standard asset is a performing asset. Such assets carry a normal risk and are not NPAs in the real sense. Hence, no special provisions are required for Standard Assets.

- Sub-Standard Assets: A sub-standard asset was one, which was considered as non-performing for a period of 12 months.
- Doubtful Assets: All those assets which are considered as non-performing for period of more than 12 months are called as Doubtful assets.
- 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 recovery value.

The major cause for the NPA can be attributed to:

- Improper selection of borrower's activities
- Weak credit appraisal system
- Industrial problem
- Inefficiency in management of borrower
- Slackness in credit management & monitoring
- Lack of proper follow up by bank
- Recession in the market
- Due to natural calamities and other uncertainties

7. Impact of NPAs on Banking Operations

The efficiency of a bank is not reflected only by the size of its balance sheet but also by the level of return on its assets. The NPAs do not generate interest income for banks. At the same time, banks are required to provide provisions for NPAs from their current profits. The NPAs have deleterious impact on the return on assets in the following ways:

- The interest income of banks will fall and it is to be accounted only on receipt basis.
- Banks profitability is affected adversely because of the providing of doubtful debts and consequent to writing it off as bad debts.
- Return on investments (ROI) is reduced.
- The capital adequacy ratio is disturbed as NPAs enter into its calculation.
- The cost of capital will go up.
- Asset and liability mismatch will widen.
- It limits recycling of the funds

8. Reporting of NPAs

Every year on 31st March, Banks must report on NPAs after completion of audit. The NPAs would relate to banks' global portfolio, including advances at the foreign branches.

Whenever NPAs are reported to RBI, the amount held in interest suspense account, should be shown as a deduction

from gross NPAs as well as gross advances while arriving at the net NPAs. Banks which do not maintain Interest Suspense account for parking interest due on non-performing advance accounts, may furnish the amount of interest receivable on NPAs as a foot note to the report.

The amount of technical write off, if any, should be reduced from the outstanding gross advances and gross NPAs to eliminate any distortion in the quantum of NPAs being reported

9. Research Methodology

The foregoing review indicates that existing studies concentrated on PSBs & comparison of PSBs with private & foreign banks. But the present study has focused on the comparison of NPAs between public and private sector banks. The banks selected for the study are prominent banks among all banks in their respective sector and includes:

- Public Sector: State bank of India (SBI) & Punjab National Bank (PNB)
- Private Sector: HDFC Bank & ICICI Banks

For the study, secondary data has been collected using annual report of „Reserve Bank of India“ publication including „Trend & Progress of banking in India“, statistical tables related to banks in India and report on currency and finance. Articles and papers relating to NPA published in different business journals, magazines, newspaper, periodicals were studied and data available on internet and other sources has also been used. Major guidelines issued by RBI from time to time were studied in depth. Along with this assets quality of banks and recommendations also studied.

In the present study, Measure of central tendency, frequency distribution, Standard Deviations, coefficient of variation and test have been used to analyze and interpret the data. In the light of objective mentioned above, the present study is confirmed to examine the various aspects of NPAs in PSBs & Private banks of India (selected banks). The study covers the period from 2002-03 to 2011-2012. To study NPA ratio variation data over the year 2011-2012 have been analyzed.

10. Analysis

NPA position is different and present in PSBs & Private Banks of India. Basically, there are many banks but in this study some prominent banks are selected among all in their respective sector. And the data related to NPA of all these banks i. e. SBI, PNB, HDFC, ICICI is collected and their comparison is done on this basis.

11. NPA ratio (in %)

It is clear from **table** that there has been marginal decrease in NPAs level over the period in all selected banks. NPAs ratio of SBI decreased from 11.95 percent at the end of

March 2003 to 3.28 percent at the end of March 2012. In Case of PNB this ratio decreased from 11.38 percent at the end of March 2003 to 1.79 percent at the end of March 2012. And in HDFC NPAs ratio decreased from 3.18 percent at the end of March 2003 to 1.06 percent at the end of March 2012. In improvement term PNB has shown the significant result while in ICICI trend has started reversing from 2007 and its NPA is 5.80 in 2012.

12. Tables and Figures

YEAR	SBI	PNB	HDFC	ICICI
2002-03	11.95	11.38	3.18	10.23
2003-04	9.34	11.58	2.22	8.72
2004-05	7.75	9.35	1.86	4.70
2005-06	5.96	5.96	1.69	4.27
2006-07	3.61	4.10	1.44	1.51
2007-08	2.92	3.45	1.39	2.08
2008-09	3.04	2.74	1.42	3.30
2009-10	2.86	1.60	1.98	4.32
2010-11	3.05	1.71	1.44	6.52
2011-12	3.28	1.79	1.06	5.80

Source: Reports on Trend & Progress of Banking in India

Banks	Mean	Standard Deviation	Co-Efficient Of Variable
SBI	5.37	3.09	57.53
PNB	5.36	3.78	70.59
HDFC	1.76	0.57	32.24
ICICI	5.14	2.60	50.53

Analysis of Mean, Standard Deviation & Coefficient of Variation

13. Conclusion

To be concluding, Gross NPAs ratio of PNB is less and it has been reduced over the period in comparison to SBI. On the other side as far as Private Banks are concerned HDFC has better performance in comparison to ICICI. So, it is very necessary for bank to keep the level of NPA as low as possible. Because NPA is one kind of obstacle in the success of bank and affects the performance of banks negatively so, for that the management of NPA in bank is necessary. And this management can be done by following way

1. Framing reasonably well documented loan policy and rule
2. Recovery effort should starts from the month of default with prompt legal action.
3. Position of overdue accounts is reviewed on a weekly basis to arrest slippage of fresh account to NPA.
4. Credit appraisal and monitoring.
5. Inspection and credit audit.
6. Half yearly balance confirmation certificates should be obtained from the borrowers.
7. A committee is constituted at Head Office, to review irregular accounts.

8. Due to lower credit risk and consequent higher profitability, greater encouragement should be given to small borrowers.
9. Recovery competition system should be extended among the staff members. The recovering highest amount should be felicitated.
10. Adopting market intelligence for deciding the credibility of the borrowers
11. Creation of a separate "Recovery Department" with Special Recovery Officer.

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