Shabd Braham ISSN 2320 – 0871

International Research Journal of Indian languages 17 April 2014

Study of Non Performing Assets in Indian Private Sector Banks

*Prof. Neha Garg , **Dr.Rajendra Sharma
*Asst. Prof. Annie Besant College, Indore
**Professor of Commerce, PMB Gujrati College, Indore

Abstract

In India, the financial sector comprises of banking and non-banking financial institutions. Banking institutions simply accept the long term deposits from the public and then lend to the borrowing community. Banking institutions are creators and purveyors of credit. While the liabilities of banks are part of the money supply, this may not be true of non-banking financial institutions. There is no hard and fast rule to distinguish between banking and non-banking institutions.

The banking system is the heart of the financial system. The Indian financial system comprises of a large number of commercial and cooperative banks and specialized developmental banks for industry, agriculture, external trade and housing, social security institutions, collective investment institutions, etc..

Introduction

A developing country faces many problems like poverty, scarcity of capital, lack of entrepreneurship, etc. There is a high dependence on agriculture and at the same time agriculture is not modernized and the means of transport is underdeveloped1. There are inter-regional and inter-sector disparities. There is also unequal distribution of wealth.

Banks play a very useful and dynamic role in the economic life of every modern state. They are important constituents of the money market and their demand deposits serve as money in the modern community. Banks can work as catalytic agents of growth by following the right kind of policies in their working, depending upon the socio-economic conditions prevailing in a country. It is realized that since banks have the required investment potentiality, they can make a significant contribution in eradicating poverty, unemployment and they can bring about progressive reduction in inter-regional, inter-state and inter sector disparities through rapid expansion of banking services.

Banking system is also referred to as a system provided by the bank which offers cash management services for customers, reporting the transactions of their accounts and portfolios throughout the day. The banking system in India should not only be hassle free but also be able to meet the new challenges posed by the technology and any other external and internal factors. For the past three decades, India's banking system has had several outstanding achievements to its credit. The Banks are the main participants of the financial system in India. Although deregulation and liberalization in the banking sector have resulted in enhanced efficiency and systematic resilience, they have also raised legitimate concerns with regard to the quality of customer services provided by banks 2. The Banking sector offers several facilities and opportunities to their customers. All the banks safeguard the money and valuables and provide loans, credit and payment services, such as checking accounts, money orders and cashier's cheques. The banks also offer investment and insurance products. As a variety of models for cooperation and integration among finance industries have emerged, some of the traditional distinctions between banks, insurance companies and securities firms have diminished. In spite of these changes, banks continue to maintain and perform their primary role - accepting deposits and lending funds from these deposits.

Commercial banks have come to play a significant role in the development of

countries. The two basic functions of commercial banks are: mobilization of the savings of the people and disbursement of credit according to direction. The world over, banking system is the focal point in the financial setup of any developing country. In India too economic development has evolved around the banking system 3.

Functions of the Bank

The following functions of the bank explain the need of the bank and its importance:

1 To provide the security to the savings of customers.

2 To control the supply of money and credit.

3 To encourage public confidence in the working of the financial system, increase savings speedily and efficiently.

4 To avoid focus of financial powers in the hands of a few individuals and institutions.

5 To set equal norms and conditions (i.e. rate of interest, period of lending etc) to all types of customers.

Banking System In India

Indian banking industry has been divided into two parts, organized and unorganized sectors. The organized sector consists of Reserve Bank of India, Commercial Banks and Co-operative Banks and Specialized Financial Institutions (IDBI, ICICI, IFC etc). The unorganized sector, which is not homogeneous, is largely made up of money lenders and indigenous bankers. An outline of the Indian Banking structure may be presented as below:

1. Reserve banks of India.
2. Indian Scheduled Commercial Banks.

a) State Bank of India and its associate banks.

b) Twenty nationalized banks.

c) Regional rural banks.

d) Other scheduled commercial banks.

3. Foreign Banks.
4. Non-scheduled banks.
5. Co-operative banks.

Role of Banks in Indian Economy

Banking is an important segment of the tertiary sector and acts as a backbone of economic progress. Banks play a very useful and dynamic role in the economic life of every modern state. They are important constituents of the money market and their demand deposits serve as money in the modern community4. The banks render vital services to the masses belonging to the various sectors of the economy like Agriculture, industry whether small scale large scale5.

The Indian financial sector has considerably widened and depends there by on lending strong support to capital accumulation and overall economic growth. And the commercial banks in India constitute the single most important component of the Indian Financial System in bringing about the financial intermediation process in India. Within the banking institutions, the role of commercial banks has occupied a new meaning and significance, in view of the changing structure and requirements of a developing economy. The increasing horizon of commercial banks identifies itself with the problems and responsibilities for making banking an instrument for bringing about social and economic transformation of a developing country, Social responsibilities have undergone far-reaching changes. Banks have become the prime movers and pace setters for the achievement of socio-economic objectives of the country. The operations of commercial banks record the economic pulse of economy of almost all countries big or small, rich or poor, socialist or capitalist and they are faced with the problem of regional disparities in economic development.

In modern economy, bankers are to be considered not merely as “dealers in money” but move realistically as the “lenders in development”. Similarly, banks are not just the storehouses of the country’s wealth but are the reservoirs of resources necessary for economic development. Banks are the purveyors of money and credit to the factors of production in every country and thus help in the acceleration of growth6. Banks are the

pivot of modern commerce; industrial innovations and business expansions become possible through finance provided by banks. Economic Development needs an appropriate monetary policy. But a well-defined banking is a necessary pre-condition for the effective implementation of the monetary policy7.

Banking is a basic industry, which not only caters to the development of a trade, commerce and industry, but also helps in removing many obstacles in the way of economic development.

Non Performing Assets (NPAs)

Authentic history of banking tells that it deals with lending and collection of money. However, it followed the basic law of demand and supply where persons having excess money lent to persons who needed it for more productive purposes and were willing to pay a price for this. The operations were limited to the money lender knowing every person he lent money to.

Proper regulation and organization of these activities was necessitated, over a period of time, as the operations began to grow because of increase in the number of clients. Gradually, simple banking transformed itself into commercial banking and the commercial banking itself has undergone numerous changes all over the world, during the last five decades. In the regard, India is not an exception and in fact, the changes that have taken place in India have been far more significant and much more radical in some regards, than elsewhere in the world.

The concept of Non-Performing Assets (NPAs) was introduced for the first time in the Narasimham Committee on “Financial System Reforms” that was tabled in Parliament on December 17th, 1991. The Committee studied the prevailing financial system, identified its short comings and weaknesses and made with ranging suggestions and recommendations in line with internationally accepted norms. Based on the recommendations of the Committee on “Financial System Reforms”, the RBI evolved prudential norms on Income recognition, Asset classification and Provisioning and issued revised instructions to banks in April 1992. While conveying non-performing category and their anxiety to present rosy picture of their affairs the above instructions to banks also advised them that as per practice followed internationally, income on NPAs is not to be recognized on accrual basis but is to be looked only when it is actually realized because an asset becomes non-performing when it ceases to generate income. The above instructions of RBI have since been implemented by banks from the financial year ended March 1998.

The problem of NPAs is linked to the function of lending money. The lending of money collected from the public, for interest, instead of one’s own money, was the beginning of banking. Though the present day banking does not restrict itself to traditional deposit collection and money lending, encompassing a wide sphere of financial activity, lending still remains the prime activity connected with banking. Most credit needs of the society, for carrying, commercial activities are fulfilled by the banks. The conventional credit from the banking system to the Commercial sector comprises bank loans and advances in the form of term loans, demand loans, cash credit, overdrafts, inland and foreign bills purchased and discounted as well as investments in instruments issued by non-government sector.

Non-performing assets (NPAs) constitute integral part of banks' operations. A bank gives out money upfront and earns income over a time on the promise of a borrower to repay. When loans are not repaid, the bank loses both its income stream, as well as its capital. Lending is always accompanied by the credit risk arising out of the borrower’s default in repaying the money8. The level of nonperforming loans is recognized as a critical indicator for assessing banks' credit risk, asset quality and efficiency in allocation of resources to productive sectors.

The most calamitous problem facing commercial banks all over the world in recent times is spiraling NPA's which are affecting their viability and solvency and thus posing challenge to their ultimate survival. So the problem of NPAs should be nipped in the bud. It is possible only if the check is placed on NPAs from the very beginning.

The major cause for the NPA can be attributed to:

1 Improper selection of borrower's activities
2 Weak credit appraisal system
3 Industrial problem
4 Inefficiency in management of borrower
5 Slackness in credit management & monitoring
6 Lack of proper follow up by bank
7 Recession in the market
8 Due to natural calamities and other uncertainties

Banks are ultimately made to finance the losses incurred by constituent industries and businesses. The lack of preparedness and structural weakness of our banking system led to the emerging scenario and trying to switch over to globalization were only aggravating the crisis. The major reason for this situation was that the threat of NPAs was being surveyed and summarized by Reserve Bank of India (RBI) and Government of India with a bird's eye-view of the banking industry, independent from the rest of the economy.

Objective of the Study

The present study has been taken with the following objectives:

1 To understand the performance of Private Sector banks in terms of Percentage of NPA to Gross Advances and Net Advances.
2 To compare magnitude and dimension of NPA's of new private sector banks and old private sector banks.
3 To examine the measures and strategies followed for reduction of the burden of NPA's
4 To suggest for the Private banks to effectively handle the challenge posed by NPA's

Methodology

The study is primarily based on secondary data which is collected from RBI bulletins and statistical tables. IBA bulletins were also referred for collection of secondary data. The data so collected was tabulated and compared with the help of generally acceptable statistical tools which are used for analysis of large data.

Data, Interpretation and, Findings

Advances (Rs. In Billions)

Year (End-March)	Old Private Sector banks	New Private Sector banks
2000-01	379.73	300.86
2001-02	422.86	741.87
2002-03	494.36	895.15
2003-04	556.48	1151.06
2004-05	677.42	1236.55
2005-06	829.57	2300.05
2006-07	928.87	3218.65
2007-08	1116.70	4067.33
2008-09	1285.04	4468.24
2009-10	1541.36	4783.58
2010-11	1846.47	6128.86
2011-12	2301.00	7363.00

Source: www.rbi.org.in

It can be observed that the new private sector banks grown at more than double the growth rate of old private sector banks. Where in the last 12 years, old private sector banks could grow 6 times, the new private sector banks grown 24 times. We can say that old private sector banks lagging behind in acceptance of deposits. However, one can argue that the old private sector banks

utilize their deposits in a more conservative way.

NPA (Rs. In Billions)

Year (End-March)	Old Private Sector banks	New Private Sector banks
2000-01	43.46	16.17
2001-02	48.51	68.11
2002-03	45.50	72.32
2003-04	43.98	59.83
2004-05	42.00	45.82
2005-06	37.59	40.52
2006-07	29.69	62.87
2007-08	25.57	104.40
2008-09	30.72	138.54
2009-10	36.22	140.17
2010-11	36.00	145.00
2011-12	42.00	145.00
Source: www.rbi.org.in		

Net NPA as percentage of Net Advances

Year (End-March)	Old Private Sector banks	New Private Sector banks
2000-01	7.3	3.1
2001-02	7.1	4.9
2002-03	5.2	1.5
2003-04	3.8	1.7
2004-05	2.7	1.9
2005-06	1.7	0.8
2006-07	1.0	1.0
2007-08	0.7	1.2
2008-09	0.9	1.4
2009-10	0.8	1.1
2010-11	0.5	0.6
2011-12	0.6	0.5
Source: www.rbi.org.in		

It is evident from the above table that old private sector banks have somehow been able to maintain their Non Performing assets. On the other hand when we see the NPA of new private sector banks we observe that they have grown substantially. NPA of new private sector banks have grown 9 times while the old private banks remained as it is. It can once again be connected to the details of advances and can be interpreted that old private sector banks selected their advances with caution. This is the reason of their low advances vis-à-vis NPA's. NPA of private sector banks have reduced till 2007-08 and then there was a trend of increment till 2012.

Gross NPA as percentage of Gross Advances

Year (End-March)	Old Private Sector banks	New Private Sector banks
2000-01	10.9	5.1
2001-02	11.0	8.9
2002-03	8.9	7.6
2003-04	7.6	5.0
2004-05	6.0	3.6
2005-06	4.4	1.7
2006-07	3.1	1.9
2007-08	2.3	2.5
2008-09	2.4	3.1
2009-10	2.3	2.9
2010-11	1.9	2.7
2011-12	1.8	2.2
Source: www.rbi.org.in		

The Gross NPA as percentage of Gross Advances has revealed that in old private sector banks initially NPA was almost 10-11 percent of advances while the same was only 5 percent in new private sector banks. The latest information about gross NPA as percentage to Gross Advances is that the old private sector banks have been able to control gross NPA as in a better way compared to new private sector banks. In the year 2012 the Gross NPA as percentage to Gross Advances was 20 percent less than the percentage of new private sector banks.

If we observe the Net NPA as percentage of Net Advances we will find that at the end of March 2012 both Old Private Banks and New Private Banks are almost on the same position. The Net NPA to Net Advances for

Old Private Sector Banks is 0.6 percent while same is 0.5 percent for New Private Sector Banks.

Conclusion

With respect to the study of non Performing Assets of Indian Private Sector Banks we can conclude that both New Private sector and Old Private sector Banks are doing extremely well in not only the recovery of Non Performing assets but in selection of advances as well. Although we can observe that the magnitude of NPA's is large it is headed towards a downturn. In both New and Old Private Sector Banks, NPA are now reducing. Banka are further suggested that an integrated information system for advances should be constructed so that it becomes easy for the bankers to exchange the detailed information of defaulters. This will definitely be reducing the credit risk and hence occurrence of more NPAs.

References :

1 Probodh Kumar, "Banking and Economic growth", Subrahmanyam N.K., "Modern Banking in India", Deep and Deep Publication, New Delhi, 1985, p.54.

2 Mithani D.M., "Money, Banking, International Trade and Public Finance", Himalaya Publishing House, Mumbai, 2008, p.224.

3 Dr. Bihari S.C., "Indian Banking – A Case of Resilience in turbulence", International Journal of Research in Commerce and Management, Vol.No.1, Issue No.5, 2010.

4 Mithani D.M., "Theory of Income", Himalaya Publication House, Mumbai, 1991.

5 Vashist, Avtar, Krishnan, "Public Sector Banks in India", H.K. Publications, New Delhi, 1991, p.3.

6 Share B.P., "The Role of Commercial Banks in India's Developing Economy", S.Chand and Company Private Limited, New Delhi, 1974, p.289.

7 Somashekar N.T., "Banking", New Age International, karnataka,2009, p.25

8 Harpreet Kaur and Pasricha J.S., "Management of NPAs in Public Sector Banks", The Indian Journal of Commerce, Vol.57, No.2, 2004, p.14.