A STUDY ON NON PERFORMING ASSET MANAGEMENT OF BANKS WITH SPECIAL REFERENCE TO STATE BANK OF INDIA

Ms. Kavyashree. K *.

**SDM College, Ujire - 574240, INDIA, E-mail : k_kavyashree@yahoo.in*

ABSTRACT

Indian banking industry plays a pivotal in the socio economic development of the country. This role is played by banks by extending credit to various deficit sectors for their growth and development. This credit creation process leads to credit risk which will lead to non performing asset. While the primary function of banks is to lend funds as loans to various sectors such as agriculture, industry, personal loans, housing loans etc., in recent times the banks have become very cautious in extending loans. Non-performing Asset is an important parameter in the analysis of financial performance of a bank as it results in decreasing margin and higher provisioning requirements for doubtful debts. NPA is a virus affecting banking sector. It affects liquidity and profitability, in addition posing threat on quality of asset and survival of banks. The motive of present study is to assess the non – performing assets of State Bank of India and its impact on profitability and to see the relation between total advances, Net Profits, GROSS & NET NPA. The study uses the annual reports of State Bank of India for the period of five years from 2009-10 to 2013-14. The data has been analyzed by using tables and coefficient of correlation. The decline of NPA is essential to improve the profitability of banks. Advances provided by banks need to be done pre-sanctioning evaluation and post-disbursement control to constrain rising non-performing assets in the Indian Banking sector. While analyzing the impact of NPA level on SBI we derived the conclusion that there is a positive relation between Net Profits and NPA of SBI. It simply means that as profits increase NPA also increase. It is because of the mismanagement on the side of bank.

Keywords: Nonperforming assets, Gross non-performing assets, netnon-performing assets, Profitability, Total advances.

Introduction:

The banking system plays a significant and commendable role in the growth and development of the economy and its components. The banking system mobilizes the funds from the surplus units and distributes them to deficit sectors for their productive and efficient utilization. The banking sector in India comprise of public sector bank, private sector banks and foreign sector banks. Public sector banks are those in which majority of equity holding is with government and includes SBI group (State bank and its subsidiaries) and nationalized banks. Modern trade and commerce would almost be impossible without the availability of suitable banking services and it facilitates it in innumerable ways. Banks play an important role in the mobilization, allocation of capital, progress and development of an economy. The modern banking is not only confined to 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.

The main business of banking is to accept deposits for the purpose of lending, so it mobilizes funds by issuing claims against itself and lends this money to others in the form of loans which are assets for banks. The liabilities and assets of banks are in the form of claims unlike other forms of business. The mobilized money is lent in the form of loans which is the major activity of banking and comprises the largest asset in the asset portfolio of the bank. The money lent are called loans or advances which earn income for the bank in the form of interest, in addition to this banks invests a portion of money in securities (both debt and equity) and a minor portion of total funds is invested in real assets like land, building for carrying the operations of banking.

The money is advanced in the form of loans and invested in securities in expectation of income and repayment of principle at periodic intervals as per the contractual obligations between the lender and borrower. The assets which is performing as per the contractual obligations i.e. payment of interest and repayment of principal as and when it fall due, it is called performing asset or standard asset. The asset which fails to meet obligation of payment of interest and repayment of principal within a specified date from due date is called nonperforming asset or non standard asset.

Non-performing asset (NPA) is one of the major concern and problem for banks in India. NPAs reflect the degree of risk and quality of assets of bank and profitability of a bank. 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 reduced income from assets and the necessity of provisions, which reduces the overall profits and shareholders' value. The level of nonperforming assets is at the alarming rate in Indian banking comparatively to other countries. This level is much higher incase of public sector banks due to their directional credit to priority sector projects and social development projects. The public sector banks play an immense role in the development and growth from the very inception. The public sector banks which were operating on social model by mobilising the huge resources and directing them to social and priority sectors for social and economic development of the country. Due to their socio economic role, there was high level of NPAs in their asset portfolio. After the liberalization in 1991, they faced high level competition from private and foreign banks. Due to this fierce competition and challenge on their survival, they were forced to improve the performance and weakness. The biggest weakness and problem they faced was huge NPAs in their portfolio.

Literature Review:

SIRAJ. K. K & PROF. (DR). P. SUDARSANAN PILLAI says 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. The study concluded that NPA still remains a major threat and the incremental component explained through additions to NPA poses a great question mark on efficiency of credit risk management of banks in India.

DEBARSH AND SUKANYA GOYAL (2012) emphasized on management of non-performing assets in the perspective of the public sector banks in India under strict asset classification norms, use of latest technological platform based on Core Banking Solution, recovery procedures and other bank specific indicators in the context of stringent regulatory framework of the RBI. Non-performing Asset is an important parameter in the analysis of financial performance of a bank as it results in decreasing margin and higher provisioning requirements for doubtful debts. The reduction of non-performing asset is necessary to improve profitability of banks.

Vivek srivastava, Deepak bansal (2012) did a "a study of trends of non-performing assets in private banks in India" to find out whether there is positive trend and control of NPA"S by the private sector banks in India. The data were collected for a period of five years from2007-2012 from various secondary sources and analyzed by average and comparative percentage analysis. It was found that that the level of NPAs is alarming with public sector banks in India but there is slight improvement in the asset quality reflected by decline in the NPA percentage. The banks should take timely action against degradation of good performing assets.

Objectives of the study:

- To compare the Total Advances, Net Profit, Gross NPA & Net NPA of SBI
- To study the impact of NPA on bank.
- To study the relationship between Net profit and Net NPA of SBI.

Methodology:

This paper is descriptive and analytical in nature. Here an attempt has been made to examine the relationship between Net profit and Net NPA of SBI. The paper is completely based on secondary source of information. The information is collected from various official websites and annual reports of SBI. The data has been analyzed by using tables and coefficient of correlation. Table is used to compare total advances, gross NPA, net NPA & profits of SBI.

Study Analysis:

A mounting level of NPA's 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 turn signals the adverse investment climate. Nonperforming Asset is an important constraint in the study of financial performance of a bank as it results in declining margin and higher provisioning requirement for doubtful debts. Various banks from different categories together provide advances to different sectors like SSI, agricultural, priority sector, public sector & others. These advances need to be done pre-sanctioning evaluation and post-disbursement control to constrain rising non-performing assets in the Indian Banking sector. The decline of NPA is essential to improve profitability of banks and fulfill the capital adequacy norms.

Table 1: SBI TOTAL ADVANCES COMPARED WITH NET PROFIT, GROSS NPA & NET NPA.

Date	Total Advances	Net Profit	Gross NPA	Net NPA
31-03-2014	363402	2777	18211	10719
31-03-2013	340321	3678	11589	6143
31-03-2012	289148	3626	8538	4418
31-03-2011	240423	3598	5066	2444
31-03-2010	204573	2959	3505	1693

Source: Annual Reports of SBI

Interpretation of Result: The table is comparing Total advances with NET Profit, Gross NPA & Net NPA of SBI. The table reveals that the total advances and the net profit is increasing continuously since 2010. This shows that bank is performing very well. But Gross NPA & Net NPA is also increasing which proves the mismanagement of funds by the bank.

Impact of NPA:

1)Liquidity:

Money is getting blocked leading to lack of liquid cash which leads to borrowing money for short period of time from outside which further leads to additional cost to the bank. Difficulty in operating the functions of bank is another cause of NPA. Due to lack of money routine payments and dues are not paid on time.

2) Credit loss:

In case of banks facing problem of NPA then it adversely affect the value of bank in terms of market credit. It will lose its goodwill and brand image as the bank is not able to pay its dues on time and its negative impact is that people start withdrawing their money from bank which then cause liquidity problem and also decrease in credibility.

3) Involvement of management:

Time and efforts of management is another indirect cost which bank has to bear due to NPA otherwise time and efforts of management in handling and managing NPA would have been diverted to some fruitful activities, which would give good returns. Now a day's banks have special employees to deal and handle NPAs, which is additional cost to the bank.

4) Profitability:

NPA means booking of money in terms of bad asset, which occurred due to wrong choice of client. Because of the money getting blocked the profitability of bank decreases not only by the amount of NPA but the NPAs leading to opportunity cost as that profit could be invested in some return earning project/asset. So NPA not only affect current profits but also future stream of profits, which may lead to loss of some long-term beneficial opportunity. Another impact of reduction in profitability is low ROI (return on investment), which adversely affect current earnings of bank.

Relationship between Net NPA& Net Profits of SBI:

Correlation: Correlation is a numerical measure used to determine the degree of relationship between Variables. By using the correlation an attempt is made to determine the relationship between Net Profits and Net NPA of SBI.

Formula:

$$r = \frac{N\sum dxdy - \sum dx\sum dy}{\sqrt{[n(\sum dx2) - (\sum dx)2]} * \sqrt{[n(\sum dy2) - (\sum dy)2]}}$$

CALCULATION OF CORRELATION BETWEEN NET PROFIT & NET NPA OF SBI:

Year	Net Profit (X)	dx = X-A A=2777	dx^2	Net NPA (Y)	dy = Y–A A= 10719	dy^2	dxdy
2014	2777	0	0	10719	0	0	0
2013	3678	901	811801	6143	-4576	20939776	-4122976
2012	3626	849	720801	4418	-6301	39702601	-5349549
2011	3598	821	674041	2444	-8275	68475625	-6793775
2010	2959	182	33124	1693	-9026	81468676	-1642732
	∑X=16638	∑dx=2735	$\sum dx^2$=2239767	∑Y=25417	∑dy=-28178	$\sum dy^2$=210586678	∑dxdy= -17909032

Interpretation of Result: r that is correlation coefficient is 0.046. It means that there is a positive relation between Net Profits and NPA of SBI. It simply means that as profits increase NPA also increase. It is because of the mismanagement by the bank. NPA is directly related to Total Advances given by bank and bank's main source of income is interest earned on advances. As stated earlier the total advances are increasing and hence the income earned in the form of interest is also increasing and thereby increasing the profits. But as we know there are two types of Customers (good and bad). Good customers' leads to increase in profits by paying interest and installments on total advances regularly and Bad customers leads to increase in NPA by not paying interest and installment on total advances. This is because of mismanagement and wrong choice of client by the banks. This is the main cause for positive relation between NPA and Profits. On the other hand if there is good management by bank, there would be reduction in the amount of NPA and increase in the Profits. This would lead to the negative relation between profits and NPA.

Findings of the study

- There is a continuous increase in Gross NPA and Net NPA of SBI.
- Total advances granted by SBI and Net Profits are increasing continuously since 2010.
- Due to the mismanagement of funds by bank there is a positive relation between Total Advances, Net Profits and NPA of the bank which is not a good indication.
- There is no consistency in the performance of the bank.

Suggestions:

- Advances provided by banks need to be done pre-sanctioning evaluation and post-disbursement control so that NPA can decrease.
- Good management needed on the side of banks to decrease the level of NPA.
- Proper selection of borrowers & follow ups is required to get timely repayment.

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