

REMEDIES OF NON-PERFORMING ASSETS ON COMMERCIAL BANKS IN INDIA

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Abstract

The present study reveals Commercial banks in India are facing the problem of Non-Performing Assets (NPAs). The earning capacity and profitability of the banks are highly affected because of the existence of NPAs. Moreover the non-performance or non-receipt of interest and principal blocked banks money in the form of funds and its not available for further use of banking business and thus the profit margin of the banks goes down. As per the prudential norms suggested by the Reserve Bank of India (RBI), a bank cannot book interest on an NPA on accrual basis. In other words, such interests can be booked only when it has been actually received. Therefore, this has become what is called as a 'critical performance area' of the banking sector as the level of NPAs affects the profitability of a bank.

Key Words: Non-performing assets, critical performance area, remedies on NPA

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Introduction

The Reserve Bank has issued directives from 31/03/1993 and presented a new Concept of Income Recognition. This is done on the recommendations of Narsimham Committee.

According to these directives the banks have to classify their credit facilities

Into two parts:

(1) Performing Assets (Standard Assets)

(2) Non – Performing Assets

Performing Assets (Standard Assets)

Standard Asset is one which does not disclose any problems and which does not Carry more than normal risk attached to the business. Such an asset is performing Asset (PA) and should not be an NPA.

Non-Performing Assets

With a view to moving towards international best practices and to ensure greater Transparency of 90 days overdue norms for identification of NPAs have been made applicable from the year ended March 31, 2004. As such, save and except certain relaxations mentioned for Tier I Banks and Tier II Banks as defined below, with effect from March 31, 2004, a non-performing asset shall be a loan or an advance where:

- Interest and/or installment of principal remain overdue for period of More than 90 days in respect of a Term Loan.
- The account remains Out of Order for period of more than 90 days, In respect of an Overdraft/Cash Credit (OD/OS).
- The bill remains overdue for a period of more than 90 days in the case of Bills purchased and discounted.
- In the case of agricultural loans, other than direct finance to farmers for Agricultural purposes, identification of NPAs would be done on the same Basis as non-agricultural advances.
- Any amount to received remains overdue for a period of more than 90 Days in respect of other accounts.

History of NPA in Indian Banking Industry

Reserve Bank of India introduced a critical analysis for a comprehensive and Uniform credit and monitoring by way of the Health Code System, in banks, which Provided information regarding health of individual advances in 1985 – 86. It was Considered that such information would be of immense use to banks’ management for control purpose. Reserve Bank of India advises all commercial banks on 7th November, 1987 to introduce the health classification indicating the quality of Individual advances in the following eight categories with Health Code assigned to Each borrower account.

- **Satisfactory:** The account in which all terms and conditions are Complying with and safety of advances are not in doubt.
- **Irregular:** The account where safety of advances is not suspected, Though there may be occasional irregularities.
- **Sick – viable:** Advances to units which are sick but viable under Nursing or revival programs are under taken.
- **Sick – non – viable / sticky:** Advances where irregularities Continue to persist and there are no immediate prospects of regularization.
- **Advances – recalled:** Advances where the recalled repayment is Highly doubtful and nursing is not considered worthwhile, includes accounts Where decision has been taken to recall the advances.
- **Suit – file – accounts:** Accounts where legal action or recovery Proceedings have been initiated.
- **Decreed debts:** Accounts for which decrees have been obtained.
- **Bad and doubtful accounts:** The accounts in which the Recoverability is in doubtful due to shortfall in the value of the securities an Inability / unwillingness of the borrower to repay the banks dues partly or Wholly.

Objectives

1. To examine the causes for NPAs in commercial banks in India.
2. To identified the procedure for manage non performing assets.
3. To provide proper suggestions to banking sector regarding Non-performing assets.

Causes of NPA

NPA arises due to a number of factors or causes like:-

Speculation: Investing in high risk assets to earn high income.

Default: Willful default by the borrowers.

Fraudulent practices: Fraudulent Practices like advancing loans to ineligible persons, advances without security or references, etc.

Diversion of funds: Most of the funds are diverted for unnecessary expansion and diversion of business.

Internal reasons: Many internal reasons like inefficient management, inappropriate technology, labour problems, marketing failure, etc. resulting in poor performance of the companies.

External reasons: External reasons like a recession in the economy, infrastructural problems, price rise, delay in release of sanctioned limits by banks, delays in settlements of payments by government, natural calamities, etc.

Managing non – performing assets

NPAs have multifold effects on the performance of banks. It shows the Weakness of management of bank. It is necessary to manage non – performing assets for following reasons:

1. To protect the interest of share holders.

Members of the bank are true owners of bank. They contribute or invest their amount in banks to earn dividend. Being amount of NPA with their amount in banks to earn dividend because high amount of NPAs means earning assets are on deterioration

consequently, means lower income of banks that will make unable to satisfy the members by paying high rate of dividend.

2. To protect the interest of depositors.

Depositors are the key person of the banks because of their deposits the banks are able to lend to borrowers. Depositors want consistent interest income on their deposits. When their deposits, advanced to borrowers, which would, later on, if become a NPA, banks would be unable to pay timely interest to depositors will switch of their deposits from one bank to another bank which is not commendable for particular bank. Thus it is very important for banks to manage efficiently their advances, which are likely to turn into NPAs.

3. For profitability:

Non – performing Assets means an asset, which cease to generate any income

Thus more and more NPA will reduce the income of banks as interest which is main component of banks income thus it will jeopardize the profitability or return on assets consequently it will be constraint for banks growth.

4. High provision:

Higher NPA leads banks to compel higher provision for Bad Debts Reserve as Per the norms of RBI. Provision will be done by realized profit and NPA will block the actual profit of banks for current year thus NPA has a dual effect i.e. not Realization of interest income and separate provision for NPA from Profit & Loss Account.

5. Creditworthiness of the Banks:

NPA works as a tool for worthiness of particular bank. If banks are having high NPA level then it will be very difficult to raise additional funds from market. It will make bad impression of banks on people.

6. Expansion plan:

For instance banks want to start as its expansion plan and its NPA level is higher. Then prescribed by RBI that is 15% of advances, banks will not be able to get permission from the RBI for starting a new branch. Thus it is necessary to control NPA level within prescribed limit for future growth of banks.

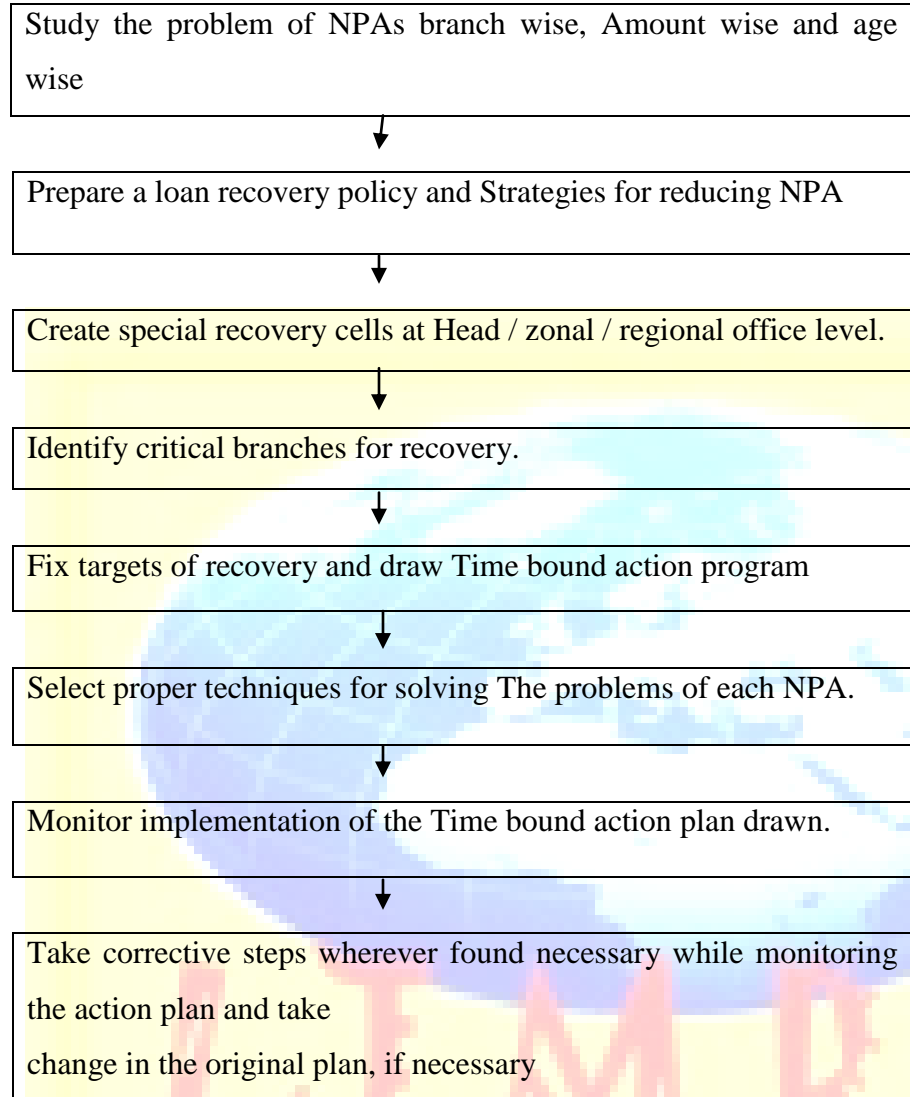
7. Welfare of employees:

If banks are having high NPA it will ruin the whole capital and past reserves, which raises question for existence of banks. Thus, many personnel will loss employment, but also banks cannot make any provision for welfare activities of the employees future benefits due to lack of availability of free reserves.

8. In the interest of sustained economic growth:

For the interest of sustained economic growth it is necessary to control and Minimize NPAs of nations banking sectors. High NPA leads to inflation in economy. Further, NPAs will reduce the opportunities for productive investment, ruin the efforts of directed allocation of funds, preferred investment areas, subsequently economy of country will not be able to achieve expected growth, which is decided on formation of budget.

Various steps for reducing NPAs



Suggestions

1. Replacement of loans
2. Rehabilitation of potentially viable units
3. Acquisition of sick units by health units
4. Compromised with borrowers
5. Calling up of advances and filling of civil suits
6. Approaching debt recovery tribunal
7. Recovery of advances given under Government sponsored programs
8. Settlement of claims with DICGC / ECGC
9. Establishment of assets recovery branches
10. Write off the outstanding.

Conclusion

This Study concluded that level of NPA has been increased year by year due to mismanagement of banking sector. The banker should follow different criteria when the banker going to sanction a loan for a customer. The banker should get both the formal and informal information about the customer from various sources i.e. knows the goodwill of the customer. If this customer had been proved that a failure to pay any loan there is no question to sanction any loan for this customer. The banker can reduced the non-performing assets in bank by using of various technologies like core banking solution in apex bank should make more reachable to all borrowers.

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