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Unmasking The Ordeal Of Growing Npas In IndianBanking Sector-

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ABSTRACT: *The role of Indian banking sector has evolved over the years from being just a factory of credit to that of instrument of economic growth. Banks lay the foundation for strong and independent economy .In highly global competitive world banks act as a prominent stimulus for accelerating the pace of development. However playing the role of an agent of economic development and growth has also burdened banks with enormous responsibilities and obligations. The enormous pressure from the economy side, has led to excessive lending by the banks therby compromising their profitability .This is especially true for the public sector banks of India. Banks today are facing the challenges of rationalizing their resources for meeting the short-term and the long term objectives of the economy. Non-performing Assets are the results of such pressures on the Indian banking sector.*

KEY WORDS: *Credit, Economic growth, Non –performing Assets, Public sector banks*

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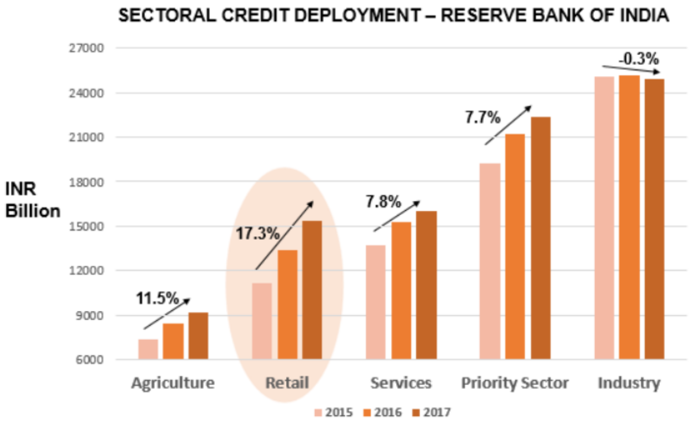
I. INTRODUCTION

Transformation of Indian banking sector:Indian banking sector has evolved remarkably from the role of an intermediary to that of an important instrument of development. Indian banks whether public sector banks or the private banks has established close links with the industrial houses , agricultural sector .Thus the objectives is to meet the competition in the credit market ,to meet the need of small and medium sectors and to bring impetus to agricultural sector in the form of easy credit supply. There has been plethora of inherent structural changes like progressive reduction in CRR.SLR, Bank rate, rationalizing and de-regulation of interest rates, greater accessibility to the capital markets and liberalized new bank licensing regime. These reforms were inevitable since the economy needed much acceleration keeping in tune with the global advancements. There has also been demand for diversified financial services from the rising middle class.

India's move towards inclusive society has necessitated financial inclusion to bring about the desired growth and development. Infrastructural projects, speedy implementation of capital –intensive projects, spurt in start-ups, and paves way for short –terms as well as long term credit needs. Rising disposable incomes, increasing consumerism, changing lifestyles and penetration of e-commerce are the major factors impacting this growth.

RBI in its monthly Sect oral Credit Deployment Report which is based on the inputs from 41 scheduled commercial banks., classified the credit market in five major segments, namely- agriculture, industry, services, priority sector and retail credit. As per the data from Reserve Bank of India bank loans to individuals and businesses rose from whooping 9.64% to Rs 79.6 lakh crore as on 24 ,2017 .This can be illustrated in the figure below depictingsect oral credit deployment.

Figure 1



Source: http://creditvidya.com

II. METHODOLOGY:

2.1 Statement of the problem: Banks are the lifeblood of an economy. They play a decisive role in the development of agriculture, industry, trade .A well-developed banking system helps in directing resources to the most productive channels and thereby bring economic, social development and growth. However the banking sector especially in a developing country like India has been facing surmountable pressure of meeting the growing needs of the economy. The growing needs of the priority as well as non-priority sectors to meet the challenges of the competitive world has led to the problem of credit crunch in the financial market. There has been excessive loan obligations .resulting in decline in asset quality rate (ARC) and consequently slippages into stresses assets category also known as Non-performing Asset. The main focus of this paper is to assess the reasons behind the burgeoning NPAs.

2.2 Scope of the paper:

The paper focusses on the importance of banking sector and its contribution to the development of an economy like India. It highlights the reasons for growing stressed assets both in the priority as well as non-priority sector. It also focuses on the measures as proposed by policy makers for re-energising the banking system.

2.3 Sources of Data

The data collected is mainly secondary in nature. The sources of data include the literature published by Indian Bank and the Reserve Bank of India, various magazines, Journals, Books dealing with the current banking scenario and research papers.

2.4 Objectives of the paper:

1. To understand the concept of non-performing assets.
2. To assess the factors behind NPAs in India.
3. To state the impact of NPAs on the economy.

III. LITERATURE REVIEW

Many studies have been conducted by researchers on non-performingassets in the banking sector. Few relevant studies related to this paper has been described below:

Neha Rani (2014) in her research paper "Analysis of Non-Performing assets of Public Sector banks" differentiated the NPAs in priority sector and non-priority sectors and revealed that the NPA S in nationalized banks in priority sector after 2008 December showed declining trend .It was the Non-priority sector which gained prominence in the loan disbursements and thus consequent rise in NPAs .

Singh (2013) in his paper entitled 'Recovery of NPA in Indian Commercial Banks traced the origin of the NPA's in the credit risk management of the Banks. He stressed on taking adequate preventive measures to be taken by the banks while sanctioning the loans.

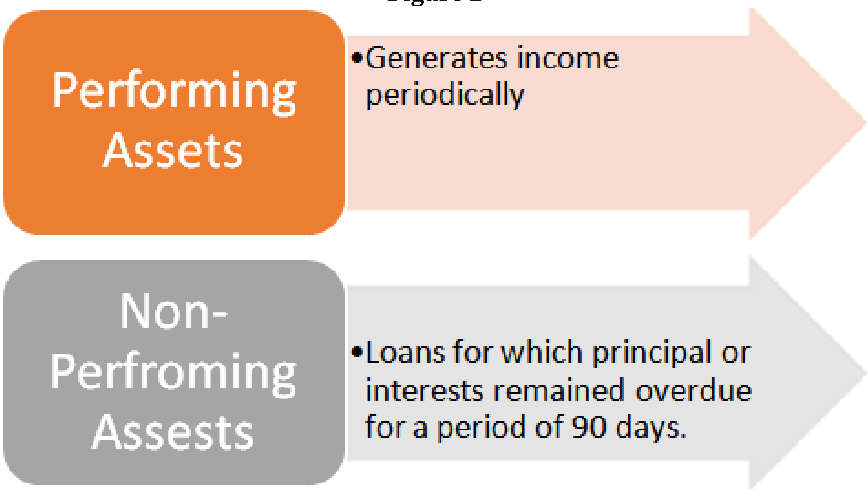
Veerakumar.K (2012) described the serious implications of non-performing assests.He emphasised on the growing NPAs in the banking sector since nationalization and their serious implications on the economy'sliquidity, mis-management of assets-liabilities and thereby affecting the overall profitability of the banking sector.

Debarsh and Sukanya Goyal (2012) in their study stressed on the stricter compliances during loans disbursement, usage of technology tools for recovery procedures.
Kumar (2013) in his study 'A comparative study of NPA of old private sector banks and Foreign Banks ,stated the serious implications of NPAs on the economy ,and described them as headaches for Indian banking sector.
Chatterjee C and Mukherjee J.and Das (2012) in their study on Management of NPAs also pointed towards the guarantor's credibility together with the borrower's to lessen the risk of non-repayment

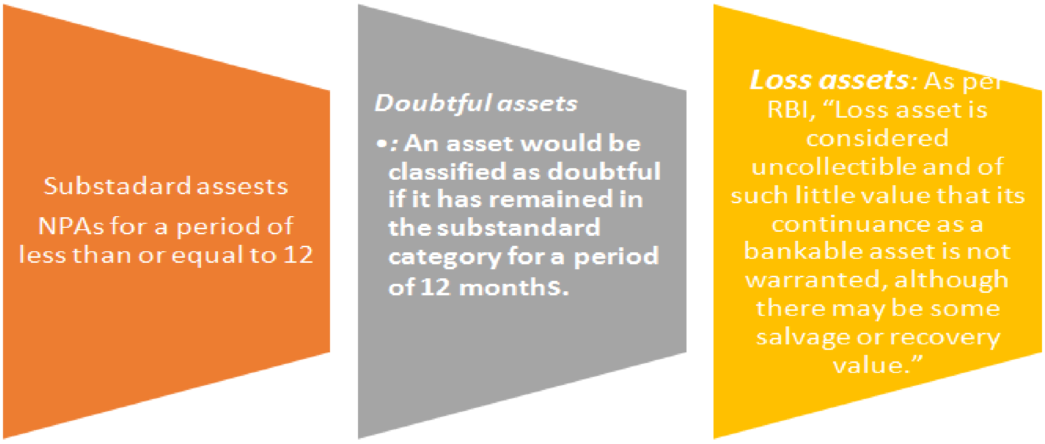
IV. CLASSIFICATION OF ASSETS:

A) Performing Assets and
B) Non-Performing Assets.

Figure 2



NPAs are further classified into:



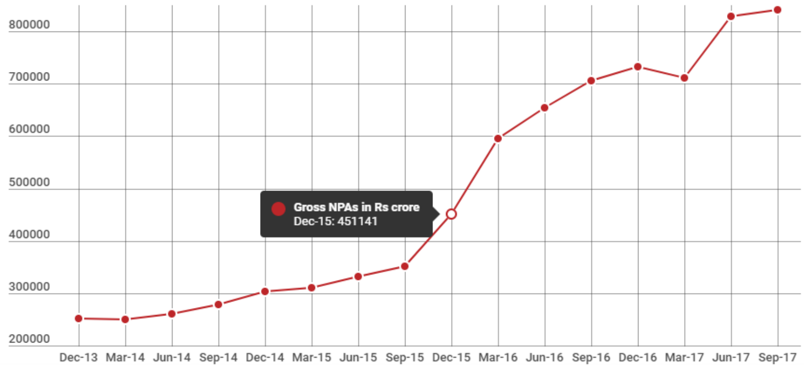
V. COMPOSITION OF NPAS:

Status of NPAs in the Financial stability report 2017 ,released by RBI states that the gross NPA stands at 9.6% .It represents the sum of all stressed assets held by financial institutions in the country including cooperatives ,private banks.A break-up of the NPAs shows that 21 PSBs, or public sector banks, saw their bad loans remaining flat at Rs 7.33 lakh crore compared with June 2017 figures while that of 17 private banks surged by 10.5 percent to Rs 1.06 lakh crore in September from Rs 96,201 crore.

The fig below shows the combined status of Public and Private sector banks

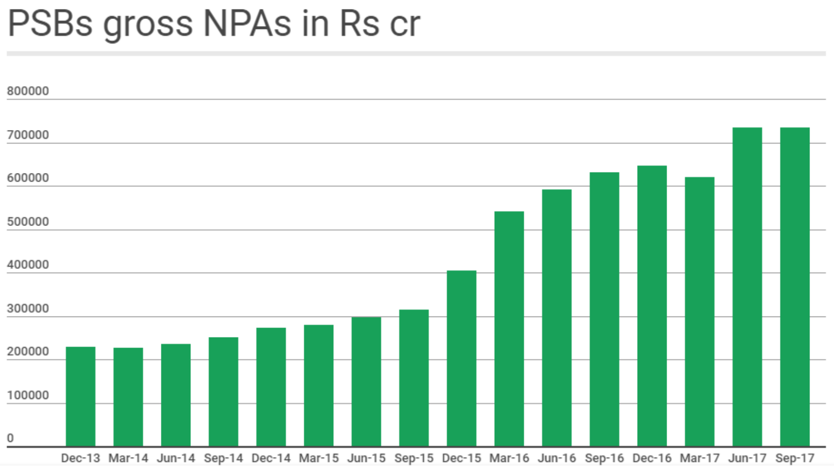
Figure 4

Gross NPAs in RsCR: Combined figures for public and private banks



Data source: CapitalinePlus

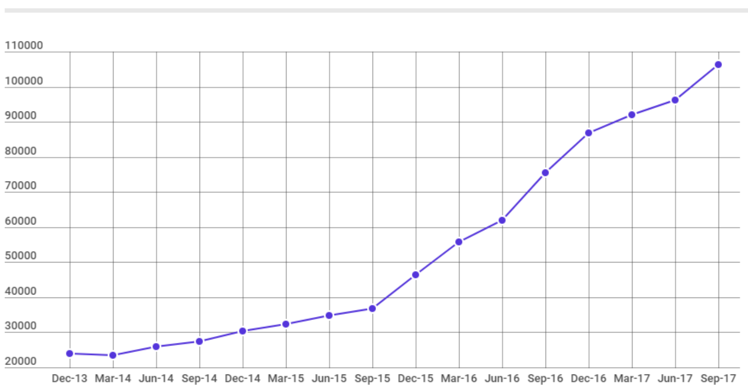
Figure 5:The fig below reveals the picture of growing NPAs in both public sector banks (PSBs) and Private sector Banks .The trend shows considerable increase in stressed assets from December 2013.



Source: Data source: CapitalinePlus

Figure 6

Gross NPAs of private sector banks



Source: Data source: CapitalinePlus

VI. GENESIS OF NPAS:

1. Repaying inability of both the priority sector and non-priority sector

Banks are the instrument of economic growth .The performance of the economy is directly related to the strength of its banks. The banks credit facility is directed to both the priority and non-priority sectors. Priority sector includes:

a) Agriculture
b) Micro and Small enterprises.

c) Education
d) Housing
e) Export credit
f) And others which include extending credit facilities to weaker sections.

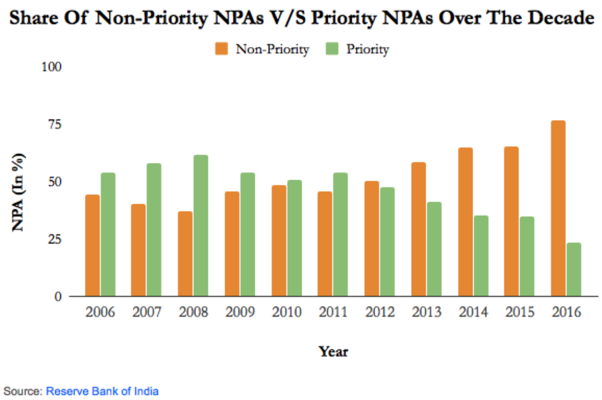
According to priority sector norms, scheduled commercial banks have to give 40 per cent of their loans (measured in terms of Adjusted Net Bank Credit or ANBC) to identified sectors. Within this, for agriculture 18 per cent target is given to banks. And within this 18 per cent, a target of 8 per cent of ANBC is prescribed for small and marginal farmers. According to National Sample survey office (NSSO), 90 % of the Indian farmers have less than two hectares of land. An average farmer makes less than Rs 6500 a month from all sources.

Distressed farming as a result of fragmented land holdings, high dependence on erratic monsoon's, lack of mechanization, has deteriorated the repaying capacity of small and medium farmers.

Similarly the there has been whooping decline in repayment of educational loans**. .** According to data from Reserve Bank of India (RBI) education loans outstanding showed a year-on-year decline of 3.5 per cent.

Non-priority sector includes –mainly corporate lending, car loans, personal finance, credit card dues. A according to the findings of Standing Committee on Finance NPAs in the corporate sector are far higher than those in the priority or agriculture sector. . Latest report given by the Government of India is that leading corporate houses and companies accounted for approximately 77% of the total gross NPAs from domestic operations for the banks.

Figure 7: Shows the comparison of share of NPAs between the priority sector and non-priority sector



2) Corporate Indebtedness

Business models have also gone wrong in recent years due to the over-exuberance of the economic conditions. Study shows that the increase in non-performing assets (NPAs) is contributed more by the industry than the agriculture sector. According to a study report by Anand Rathi, in terms of contribution to overall bank NPA, industry accounts for two-thirds and services nearly 20 percent. Today, banks are struggling with a total bad loans worth Rs 7.7 lakh crore, largely arising from large corporate defaults.

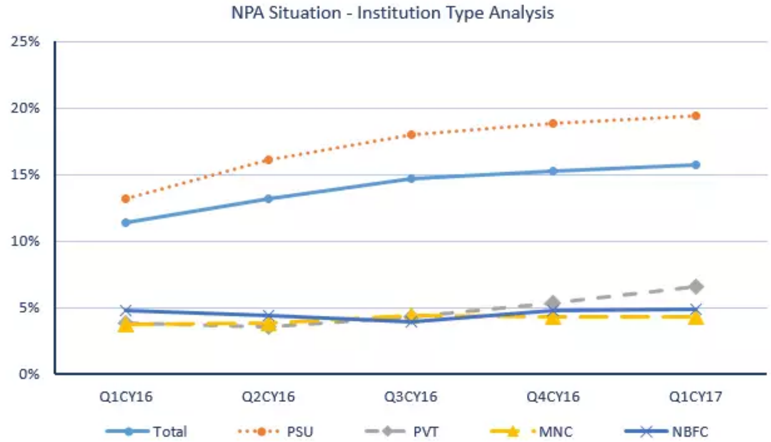
The roots of this stems from the period of 2005-2008 ,when the growth rate reached 9%.Indias investment-GDP ratio moved from 26 % in Financial year 2004 to 35% in year 2008.There was a huge credit flow to the corporate houses and to long term infrastructural projects as a result of the strong macro-economic indicators. The corporate indebtedness increased to almost 9% of GDP in FY 08.

However the boom came to end in the FY-08 as a result of financial crises globally .This was soon followed by stringent policy of the RBI with regard to Repo-rate to curb the inflationary trend in the economy. Rupee depreciation from the low of mid-40s to mid 6os in FY08 adversely affected the debt servicing ability of the corporate houses

NPA crises: Current situation:

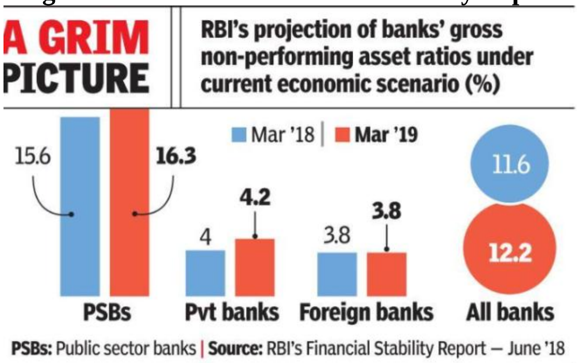
Figure 8

The figure below shows that public sector banks are facing larger NPAs **f**rom 13.2% in 1Q16 to 19.4% in 1Q17.



Source:Trans Union CIBIL

Figure 9:RBIs recent Financial Stability Report



Source :The times of India dated 27thJune

4. Banks and the legislative pressures:

There is strong linkage between Monetary and Fiscal policies of the nation. Fundamentals of economics states that there should be harmony between the two to meet the objectives However it is time and again seen that the banks are forced to deliberately follow the steps which suit the needs of one political party or the other. The case of wilful defaulters, loanwaivers, have added to the woes of the banking sector. There are times when thegovernment wants the liquidity needs to be met with lower interest rates. This again leads to excessive amount of stressed assets.

Frequent changes in government policies like changes in Export /import duties, pollution control orders, administrative delays in clearances of long term capital projects also contributes towards NPAs occurrence's. Growing protectionist policies of the government is crimping the India's export prospects even more. The private sector being shy of providing huge capital for supporting the growth needs, it is the public sector which is bearing the burden of meeting the capital needs.

4 Inherent policies:

Defective lending policies: Foundation of strong Banking sector depends on the principles of safety, Principle of liquidity, Principles of profitability. Principles of safety mean that the borrower is in a position to pay back the loan, including both principal and interest. The refund of loan depends upon the borrowers, Capacity to pay and Willingness to pay. Nationalisation gave banks the mandate "to further control the heights of the economy, to meet progressively, and serve better, the needs of the development of the economy and to promote the welfare of the people in conformity with the policy of the State," according to Reserve Bank of India's (RBI) chronology of public sector banking. And with nationalization the government was able to dictate their own terms, leading to aggressive lending to unviable long term projects. Furthermore during structuraltransformation of the economy from 1990', RBI relaxed norms of the banks to realize the growing need of the economy. This inevitably led to scrupulous lending by banks especially to large corporate houses without giving much attention to the credibility's of repayment**,** much of the NPA problem arose when commercial banks lent aggressively, for long durations, to the non-priority sector in the early 2000s, when the economy reached a growth rate of over 9 percent in 2005-06, 2006-07 and 2007-08.

VII.IMPACT OF NPAS:

The constant rise in NPAs would generate a vicious circle of credit crises in the economy, thereby affecting the overall investments and demand .Banks facing perennial problem of NPAs would face with reduction in their revenue generating capacity. This will bring in scarcity of funds in the financial markets and hurt the shareholders of the banks. Banks facing liquidity crunch would be wary of lending further.

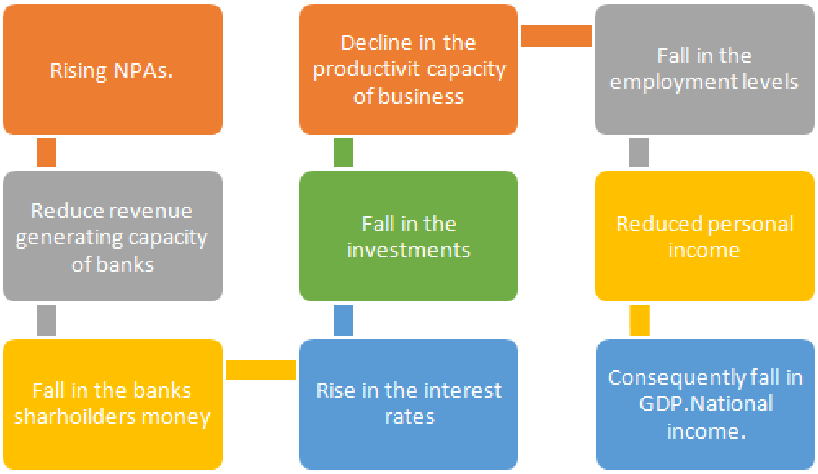
The price of loans or in other words the rate of interest will rise. Rise in the rate of interests will curtail the borrowing capacity of the business houses. There will be either shortfall of production or many small business can face a shut-down. Big industrial and infrastructural projects would further stalled. It will also impact the retail consumers like us, who will have to shell out a higher interest rate for a lot.

This will create an economic downturn with fall in income of business .leading to fall in the employment and consequently fall in the personal disposable income .The aggregate result would impact the general GDP level and the national income consequently.

Thus the Economy gets entrapped in its own inherent factors which eventually affects its competitive capacity .This can be depicted through a figure which demonstrates the cob-web of factors leading to a cycle which affects the economies efficacy and effectiveness.

Figure 10

Vicious circle of NPA



VIII. PREVENTIVE MEASURES

Mere statement of the problem is not enough. Therefore finding the most appropriate solutions and timely implementation of them should be the utmost priority. There have been various interpretations of causes leading to NPAs in India. A pragmatic approach is needed to bring in most probable solutions to this problem. Few of them as given by various planners, academicians as well as bankers can be summarized as follows:

a) Stricter credit appraisals system: basic principles of credit appraisal and monitoring should be followed.
b) Strengthening supervisory capacity of the RBI.
c) Preventing' ever-green policy' of the RBI which led to scrupulous lending's by the banks.
d) Timely action against wilful defaulters by using appropriate technological tools like Fund flow analysis, financial analysis.
e) Loan restructuring schemes integrating with Asset reconstruction companies.
f) Government intervention through amendments in banking sector.
g) Capital infusion into the banks through scheme's like bank recapitalization.
h) Central focus should be around having a strong corporate governance and compliance framework, robust risk management architecture.as suggested by Vishwavir Ahuja, RBL Bank CEO.
i) Investment in trained staff and personnel of banks, incorporation of latest technology and systems will go a long way in achieving tighter controls and supervision, streamlining processes and, most of all, adhering to a culture of checks and balances.
j) Greater transparency and formalisation of the economy will have the right kind of cleaning effect in clearing up the system.

IX. CONCLUSION

The economic health of nation depends on the sound and strong Banking sector. Reliable and strong banking plays a decisive role in enhancing the competitive strength of a country. Therefore slightest lags in operational framework can prove catastrophic for the banks as well as for the economy. It is imperative to constantly focus and monitor the smooth functioning of banks .The root cause of NPAs must be addressed timely to prevent further deterioration in the credit market and thus braking the vicious circle of financial distress. There should be viable regulatory standards to ensure effective Risk management and Credit appraisal. Stricter compliance of procedures in lending, effectivesupervisory steps to tackle the defaulters and management of stressed assets through understanding and cooperation between government and the banking sector would pave for strong financial sector in India.

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