A STUDY ON NON PERFORMING ASSETS AND ITS IMPACT ON PROFITABILITY WITH REFERENCE TO SELECTED PUBLIC SECTOR BANKS IN PUNE

A DISSERTATION PRESENTED BY

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UNDER THE GUIDANCE OF

DR.G.V.N.RAO

IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE AWARD

OF

MASTER OF PHILOSOPHY

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TO

TILAK MAHARASHTRA VIDYAPEETH
PUNE

DECLARATION BY STUDENT

FORM 'A'

I hereby declare that the dissertation entitled "**A study on Non Performing Assets and its impact on profitability with reference to selected Public Sector banks in Pune"** " completed and written by me has not previously formed the basis for the award of any Degree or other similar title upon me of this or any other Vidyapeeth or examining body.

Research Student

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C E R T I F I C A T E

This is to certify that the dissertation entitled **"A study on Non Performing Assets and its impact on profitability with reference to selected Public Sector banks in Pune"** which is being submitted herewith for the award of the Master of Philosophy (M.Phil) in **Management** of Tilak Maharashtra Vidyapeeth, Pune is the result of original research work completed by ~~Shri~~ / Smt. **Nadar Ambika Lachhekumar** under my supervision and guidance. To the best of my knowledge and belief the work incorporated in this dissertation has not formed the basis for the award of any Degree or similar title of this or any other University or examining body upon ~~him~~ / her.

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Date :

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CDR: Corporate Debt Restructuring

CIBIL: Credit Information Bureau Ltd

DRAT: Debt Recovery Applet Tribunal

DRT: Debt Recovery Tribunal

GNPA: Gross Non Performing Asset

L&A: Loans and Advances

MSME: Micro, Small and Medium Enterprises

NNPA: Net Non Performing Asset

NPA: Non Performing Asset

NPS: Non Priority Sector

OTS: One Time Settlement

PCR: Provision Coverage Ratio

PS: Priority Sector

RBI: Reserve Bank of India

SARFAESI: Securitization and reconstruction of financial asset and Enforcement of Security Interest

CHAPTER 1: AN INTRODUCTION TO NPA – CONCEPT

1.1 Introduction

The core business of bank is to accept money as deposit and lend it to others in the form of short term or long term loans. These loans are treated as assets of banks as it generates income and it covers the major and crucial part in the asset portfolio of the bank.

Banks play a vital role in national economic development by extending loans to the potential sectors for their own as well as country's development. The risk involved in this lending activity is known as credit risk which when not managed properly causes NPA.

'NPA' is a threatening term for banking sector and all financial institutions today as it weakens the financial position and becomes a hindrance for its survival.

1.2 Definition

A **Non-performing asset**(NPA) is defined as a credit facility in respect of which the interest and/or installment of principal has remained 'past due' for a specified period of time. (Ref https://en.wikipedia.org/wiki/Non-performing_asset)

1.3 Meaning of Non Performing Assets

Loans are assets of banks which produces income in way of interest and it becomes non performing asset when it stops generating income for the bank.When a payment is late for a short period it is classified as "past due" and when it crosses a specific period, usually 90 days, it is said to be Non Performing Asset. . Thus non-performing assets are basically non-performing loans and advances.

In the initial years, NPA was classified with overdue period of 4 quarters in March 1993, which was later on reduced to three quarters in March 1994 and then two quarters in March 1995.

In order to comply with the international standards and as per the recommendation of the committee, the time period for identifying the asset into non performing was declared as 90 days from March 2004.

RBI has set guidelines for classification and provisioning of advances. According to the guidelines, an asset shall be declared as non performing when -

i. interest and/ or installment of principal remain overdue for a period of more than 90 days in respect of a term loan,

ii. the account remains ‘out of order’ in respect of an Overdraft/Cash Credit (OD/CC),

iii. the bill remains overdue for a period of more than 90 days in the case of bills purchased and discounted,

iv. the installment of principal or interest thereon remains overdue for two crop seasons for short duration crops and for one crop season for long duration crops.

v. the amount of liquidity facility remains outstanding for more than 90 days, in respect of a securitisation transaction undertaken in terms of guidelines on securitisation dated February 1, 2006.

vi. in respect of derivative transactions, the overdue receivables representing positive mark-to-market value of a derivative contract, if these remain unpaid for a period of 90 days from the specified due date for payment.

1.4 Classification of Asset

1.4.1 Standard / Performing Assets

Definition

Loan or Advances for which bank is receiving interest or principal amount regularly from the borrower as specified by the bank and / or due period is not exceeding more than 90 days in a financial year is categorized as Standard Assets or Performing Assets.

Provisioning for Standard Assets

1) Agriculture and Small and Micro Enterprises (SMEs) sectors at 0.25 per cent;
2) Commercial Real Estate (CRE) Sector at 1.00 per cent;
3) Commercial Real Estate – Residential Housing Sector (CRE - RH) at 0.75 per cent
4) all other loans and advances at 0.40 per cent.

Disclosure

Such provisions made for standard assets should be shown separately as Contingent Provisions against Standard Assets' under 'Other Liabilities and Provisions Others' in balance sheet and not to be considered while calculating Net NPA.

1.4.2 Non Performing Assets

Non Performing Assets are the one for which due period exceeds more than 90 days. It is further classified into three sub categories.

RBI has given guidelines to banks for classifying NPA, based on the period of their non performing and realisability of due.

1) Substandard Assets

a substandard asset is one in which the asset has remained non performing for a period not more than 12 months. Such an asset will have well defined credit weaknesses that jeopardise the liquidation of the debt and are characterised by the distinct possibility that the banks will sustain some loss, if deficiencies are not corrected.

2) Doubtful Assets

an asset would be classified as doubtful if it has remained in the substandard category for a period of 12 months. A loan classified as doubtful has all the weaknesses inherent in assets that were classified as sub-standard, with the added characteristic that the weaknesses make collection or liquidation in full, – on the basis of currently known facts, conditions and values – highly questionable and improbable.

3) **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.

1.5 Types of NPA:

Gross NPA

Gross NPAs are the sum total of loans and advances that have been converted into non performing because of defaulting borrowers. It comprises of substandard, doubtful and loss asset, which is classified as per the guidelines issued by RBI. Gross NPA determines the quality of bank's loans and advances portfolio

Computation of Gross NPA for the financial year -

Gross NPA = (Opening Balance of Gross NPA (+) additional NPA of the year (-) (Upgradations / Recoveries (excluding recoveries made from upgraded accounts) / Technical/ Prudential Write-offs / Write-offs)

Net NPA

Bank makes provision against non performing assets which includes specific provision as per the type of asset, provisioning guidelines are issued by RBI. After deduction of such provision from Gross NPA we may arrive at Net NPA.

Computation of Net NPA for the financial year -

Gross NPA – (Balance in Interest Suspense account + DICGC/ECGC claims received and held pending adjustment + Part payment received and kept in suspense account + Total provisions held).

1.6 Provisioning

Banks must make provisions and capital buffers while its earning a good profit which it can utilize for managing losses in future. This practice will ensure the stability of financial sector.

Therefore banks were advised to maintain 70% PCR, consisting of specific provisions against NPAs as well as floating provisions.

Floating Provision

Floating Provision is made for contingencies against extra ordinary situation which are categorized into General, Market and Credit. The policies related to level of floating provision and circumstances which can be treated as extra ordinary, is to be approved by the Board. These provision can be deducted from Gross NPA to arrive at Net NPA. It is to be disclosed under "notes on accounts" to the balance sheet, disclosing the opening balance, additional provision made in the year, utilized provision and closing balance at the end of the year.

Provision for NPA

It is the responsibility of the bank management and statutory auditors to make provisions for the non performing assets. Provisioning of NPA is based on the classification of NPA that is

- Period for which it has remained non performing,
- Availability of security and
- Realisable value.

Provision against each category of NPA is given below:

	Unsecured Portion	**Secured Portion**
Substandard assets	**25 %, in some cases 20 %**	**15 %**
Doubtful assets	**100 %**	**Up to 1 Yr – 25%** **1 – 3 Years – 40%**
Loss assets	**100 %**	**100 %**

The above applies for Leased Asset as well.

1.7 Valuation of Security

Tangible securities

It is mandatory to do valuation of security by external agency, as per the guidelines issued by board, in order to avoid any deviation arising at the time of realization of security.

- Stock Valuation should be done annually
- Collateral security should be valued once in three years

Intangible securities

The disclosure of the advances with their estimated value of intangible securities such as charge over the rights, licenses, authority, etc. should be made by the bank separately under "Notes to Accounts".

(Ref: https://rbi.org.in)

CHAPTER 2: METHODS FOR RECOVERY

2.1 Introduction

Banks and Financial institutions were experiencing troubles in recovering their outstanding credits and enforcement of security charge with them. This emerged the need for an effective debt recovery mechanism to assist banks and financial institutions in recovering their outstanding dues.

The Financial committee decided upon setting up of special tribunals to be empowered with rights to decision making. The committee examined the legal and other difficulties in recovering and based on the findings and recommendations "The Recovery of Debts Due to Banks and Financial Institutions Act" was passed by the government in the year 1993.

2.2 Definition –

"An Act to provide for the establishment of Tribunals for expeditious adjudication and recovery of debts due to banks and financial institutions and for matters connected therewith or incidental thereto."

2.3 Debt Recovery Tribunal (DRT)

Prior to 1993, banks had to file a suite in civil court and go through the legal proceedings to deal with the defaulters, it involved a long process and it took on an average of 5 to 7 years for courts verdict ion. Therefore special court "Debt Recovery Tribunals were set up under Section 3 of the Recovery of Debts Due to Banks and Financial Institutions

Act,1993, to enable fast recovery of debt. DRT is headed by a Presiding Officer and has two recovery officers.

Banks can approach DRT Under the Recovery of Debts Due to Banks and Financial Institutions (RDDBFI) Act, 1993 also, under Securitization and Reconstruction of Financial Assets and Enforcement of Security Interests (SARFAESI) Act, 2002 borrowers, guarantors, and other any other person aggrieved by any action of the bank can approach the Debts Recovery Tribunal.

Further appeal can be made in Debt Recovery Appellate Tribunal (DRAT)

At present there are thirty three Debts Recovery Tribunals and five Debts Recovery Appellate Tribunals across the country.

(Ref: http://www.bankdrt.net/index.php)

2.4 SARFAESI

Over the years, DRT got overburdened with cases. Further to bring an alternative option for speedy recovery of NPA, The Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 was formed to regulate securitization and reconstruction of financial assets and enforcement of security interest by secured creditors.

This act enables realization of financial assets by the secured creditors without the intervention of court or DRT.

Under SARFAESI Act, the bank may

1) Issue notice to the borrower

2) Recall the loan and advances

3) Auction the pledge assets.

In case the borrowers fails to clear dues within 60 days of issue notice by the Bank under SARFAESI Act, the bank is empowered with the following rights -

1) Take possession of the securities and right to lease / sell / transfer of rights of asset for the purpose of recovering NPA.
2) Change the management of the company
3) Person, who has purchased assets which is provided as security by the borrower to the bank, is liable to pay bank the outstanding credit of the borrower.

SARFAESI applies only to mortgaged/secured loans above Rs.10 Lakhs and where the outstanding amount is more than 20% of the principal and interest.

2.5 Sale to Securitisation and Reconstruction companies

Securitisation and Reconstruction companies are also set up under the SARFAESI act which allows the company to purchase the NPA from banks and financial institutions and recover NPA from borrowers through realization of its securities. It acts as an agent in recovering the debt from the default borrower thus enabling banks to clear their bad debts from books and focusing on their core banking activity.

This act has been successful in enabling the lenders to recovery its outstanding credit in an easy and rightful way.

RBI has laid down norms for SC / RC with regards to registration, prudential norms for acquisition of NPA from banks and financial institutions etc.

2.6 Lok Adalat

Lok Adalat is a system of alternative dispute resolution developed in India. It roughly means "People's court". These are usually presided over by retired judges, social activists, or other members of the legal profession. (Ref: https://en.wikipedia.org/wiki/Lok_Adalat)

Lok Adalat is one of the recovery mechanism where NPA cases are settled avoiding legal proceedings . It acts as a mediator between the bank and borrower to meet and arrive at a mutual settlement.

According to the guidelines issued by RBI, bank may approach Lok Adalat for recovery of NPA in doubtful and loss category with amount upto Rs 20 Lakhs, both suit filed and non-suit filed cases.

Lok Adalat is best suitable for speedy recovery of small bad debts.

2.7 Corporate Debt Restructuring

Corporate Debt Restructuring is a non statutory mechanism through which corporate debts of viable entities are restructured. Corporate Debt Restructuring System was formed based on Debtor-Creditor Agreement (DCA) and Inter-Creditor Agreement (ICA) under the guidance of RBI on August 23, 2001.

At certain occasion corporate are in financial crisis due to certain uncontrollable external or internal factors. Hence to lend a support to such corporate and also to protect the money lenders such as banks and financial institutions, CDR was formed.

Objectives of CDR

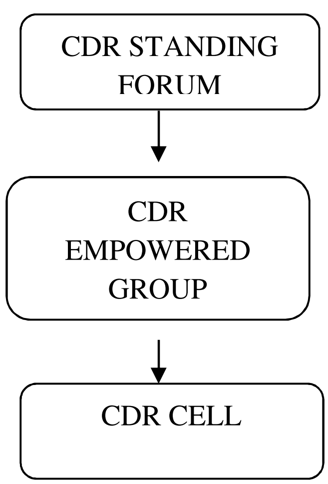
1. To ensure timely and transparent mechanism for restructuring

2. To aim at preserving viable corporate that are affected by certain internal and external factors.
3. To minimize the losses to the creditors and other stake holders

Restructuring involves modification of any terms and conditions which was agreed upon by the lender and borrower initially while sanctioning loan such as rescheduling of payment schedule, installment, interest rate. It also includes financing additional loan, as per the norms.

For E.g. – Project is not completed as per the targeted date because of some reason or unit established is sick because of less demand in the market for the product and is unable to generate projected revenue etc. In all such cases, after sufficient scrutiny of the situation, a second change is given to the borrower by way of restructuring their loan.

Structure of CDR System



Applicable – only for multiple banking accounts, syndication/consortium accounts, where all banks and institutions together have an outstanding aggregate exposure of Rs.100 million and above.

2.8 One Time Settlement (OTS)

One Time Settlement is a non legal method of recovery of NPA. In comparison with legal proceedings, OTS offers easy way to settle an NPA. OTS scheme is offered by banks to its borrowers when the reason for nonpayment is genuine or due to some external un controllable factors and recovery is doubtful.

Bank assesses whether compromise settlement would be beneficial by considering the realisable value and sacrifice on the basis of current situation and future losses.

RBI had laid down certain guidelines which the banks are required to observe at the time of OTS.

2.9 Recovery Agent

Some Bank outsources the recovery activity by appointing external agent for recovering their outstanding due from borrowers. Utilization of services of Recovery Agent helps bank to strengthen their recovery position in all types of NPA account and to concentrate more on its core activity.

RBI has set guidelines to Banks for **Engagement of Recovery Agents.** Similary Recovery agents are required to undergo training formulated by Indian Institute of Banking and Finance (IIBF). Bank can appoint only those agents those who are certified by IIBF.

The Fee or service charges are paid as agreed upon depending on the number and nature of account to the Recovery Agents on the realization of outstanding due.

2.10 Conclusion –

At present, banks have three legal ways to resolve its NPA - SARFAESI Act, DRT and Lok Adalat. Out of which SARFAESI is considered to be the fastest and powerful method as it empowers creditors with rights on securities.

CHAPTER 3 REVIEW OF LITERATURE

3.1 Introduction

Evaluation of various aspects of the bank has been carried out at every phase by the RBI, Indian government, financial institutions, committees' and research scholars. Some of the literatures which are relevant for this study are reviewed below.

3.2 Literature Review

3.2.1 Kajal Chaudhary and Monika Sharma (2011)

International Journal of Innovation, Management and Technology, Vol. 2, No. 3, June 2011

Banking industry had witnessed major changes only after Liberalization, Privatization and Globalization in the country. This evolution brought in cut throat competition, technology advancement, innovation in product and services and eradication of all social barriers in the sector. Public sector banks had a major challenge to face with the introduction of new players like private and foreign banks in market.

This paper attempts to examine the efficiency in performance of public and private sector banks. The Performance was examined with the help of stock price as it is said that ratio analysis of financial statement would have not shown accurate result because of incomplete disclosure of NPA in the books. The findings reveal that -

1) Public sector banks can survive in the market despite heavy competition from private sector banks.

2) It further suggests that listing on the exchanges, commercial goals and functioning as an independent entity improves performance and ownership was not a critical factor. Therefore suggested that government must refrain from having control on bank as it does not help in improvement of performance.

This paper also does an empirical study on the Non Performing Assets of public and private sector banks. NPA is the key factor to assess the financial health of the bank. It is written that the level of NPA is one of the drivers of financial stability and growth of the banking sector.

This study identifies expectations from the customer on modern banking. A well trained staff, better services and accessibility and a reasonable interest rate is what the customers are demanding for.

The author have given some good recommendations which, if observed strictly, can help in reduction of NPA. It includes –

1) Periodical monitoring of loans and advances to ensure proper utilization of fund, for the purpose it was sanctioned.
2) Developing the entrepreneurial skill of the borrower in his business, this will help in building strong banker- borrower relationship.
3) Use of statistical tool to assess the borrowers and sharing of credit history of the borrower among lenders.
4) Ethical way of recovery

5) Standard financial acquisition policy and guidelines for asset recovery companies.

6) Tax benefit for ‘qualified institutional borrower’

7) Replacing traditional documentation with technology and reduce cost to the company.

8) More transparency required in settlement of NPA

This paper was helpful in understanding the changing needs of the customers and the concerns in management of NPA, which contributed to my research topic.

3.2.2 Banking Industry in India, Prem Mohan, Axis, 178-200 (2012)

Author has reviewed the transformation of role, objective and functioning of banking sector in India from the pre independence period to the post liberalization period. The changes in trend is considered to be profitable and enhancement in productivity and efficiency. Indian banking sector has proved to be one of the healthier banking sector in the world with its consistent increase in total asset, return on asset. Indian banking industry includes public, private and foreign ownership and out of which commercial bank plays a dominant role, relatively co-operative and regional rural bank shares a low market segment. The objective of Indian banking sector reforms post liberalization were more focused towards building effective operational system, flexibility, to encourage fair competition in the industry and to set prudential norms and practices in line with the international standards. In today’s 21st century emphasis is given on restructuring, human capital development, technology advancement, structural development which facilitated in achieving universal benchmark.

In Chapter 12, the study deals with the Priority Sector lending which changed the lending pattern of the banking industry. Before nationalization, the banks were more urban based and profit oriented. With the nationalization of 14 commercial banks in India in 1969, there were change in policy which insisted on expanding banking facilities for rural and semi urban area and to provide specific portion of credits to agriculture, small scale industries, micro credit, education, housing etc which were termed as Priority Sector by RBI. This was fundamentally for the purpose of overall development of the economy and to bring in social responsibility in banking sector. Banks not only provided financial support to these sectors but also helped them to make efficient use of credit in their respective fields through various measures such as village adoption scheme in Agriculture sector and provided counseling and guidance in the area of marketing and management for small scale industries .

This chapter illustrates the changing trend in Priority Sector lending and problems faced due to it. More stress on poverty alleviation programs and problems faced such as issues in facilitating large number of borrowers wherein account is small and scattered which lead to issues in monitoring, follow up, mishandling of credit. Lack of entrepreneurship skills in borrowers and poor recovery mechanism had further lead to bad debts. Declined quality services had led to decrease in profitability.

Author here emphasis on having trained staff, infrastructure etc to reduce frauds and to avoid assets converting to non performing. Commercial bank besides having a social responsibility should also work as a commercial organization and maintain its profitability in effective and efficient ways.

During 1990's, NPA was the major focus for all banks globally. In India NPA was very high in the beginning. With the government's financial reform, major revolution was brought in to the credit monitoring and recovery laws in banks and financial institutions, which helped in considerable decline in the NPA.

Initially in India, the time period for classifying the asset as NPA was 180 days as compared to 45 days to 90 days of international norms. This was later changed to 90 days from the year 2004 in order to comply with the international standard.

3.2.3 Madan Mohan Jana and Manas Kumar Thakur, An Overview of Non-Performing Assets Management And Banking Performance – An Empirical Analysis, International Journal of Advance Research in Computer Science and Management Studies, Volume 2, Issue 1, January 2014 pg. 42-50

This paper aims to study the trends of NPA in weaker section in selected nationalized banks for the period 2008-12. It also involves a comparative study by examining the Gross NPA and Net NPA of selected banks in order to evaluate the quality of NPA management.

It is observed that Public Sector banks show more exposure towards weaker section as compared to private sector banks. Author further says that directional credit to weaker section is the major concern for bulging NPA in nationalized banks.

Authors concluded that constructive management of NPA is much required due to its invigorative, agglomerative, multi dimensional impact and affect on the risk mitigation, operations performance, positions in competitive advantages and overall performances of bank.

The study reveals that on an average both Gross and Net NPA shows an upward trend while the growth rate varies from each other. Through statistical test it is interpretated that nationalized banks are efficient in management of NPA.

Author recommends the following SLP principle while sanctioning loan which are –

1) Principle of **S**afety – Proper valuation of primary and collateral securities
2) Principle of **L**iquidity - check on physical condition of the assets, receivables and stocks.
3) Principle of **P**rofitability

Also to use updated technology. This will help to take corrective measure effectively and efficiently.

This article was useful in understanding the method to do a comparative analysis and interpretation with the help of statistical analysis.

3.2.4 Banambar Sahoo ,Non Performing Assests in Indian Banks: Its Causes, Consequences &Cure, ,The Management Accountant, ICAI,VOL 50 No.1, January 2015, Pg no.30-32 :

The author in this article has highlighted that if NPA is not managed effectively and quickly it will affect the financial inclusion and infrastructure development of the country. This study is about the causes, consequences and curative measures on rising NPA.

Author has broadly categorized the causes of NPA into three categories - Business Environment, Borrower and Banker, further elaborated its various reasons under each category.

While discussing the consequences, author states that like any other business bank too has its business risk which cannot be removed completely but needs to be managed on time to avoid big loss. Its major consequences involves fall of profitability which was by 26.8% in public sector banks by the end of March 2014 compared to last year's record, not only that banks also incurs huge maintenance expenses and also the provisions made affects the capital of the bank. These in turn becomes hurdle in providing credit to the needy people and sector. Due to all these reasons banks are more reluctant to lending.

Three curative measures have been recommended which are Preventive, Corrective and Punitive at various stages of NPA.

1) Preventive measures are considered to be precaution measures from forming NPA. These measures include – framing of cohesive & conducive regulatory norms, to inculcate a habit of loan repayment by avoiding unwarranted loan waiver scheme, improve skills and techniques in every stages of loan. The important thing highlighted here is to take strict action against the bank and other

professionals like Chartered accountants, legal advisors who manipulate the system to favor the borrower .

2) Corrective measure is one which needs to be adopted at the alarming stage. The 3 important measures are Rectification, Restructuring and Recovery as recommended by RBI. The Author recommends having the RBI's guidelines (Joint Lender's Forum & Corrective Action Plan) for all categories of NPA, which is as of now applicable only for Special Mention Account 2 (payment overdue between 61-90 days).
3) In Punitive Measures author insist on strict action against the non-cooperative and willful defaulters. Two punitive legal measures available are DRT Act & SARFAESI Act but it has lot of loopholes which needs to be structured for an easy and well-timed recovery process.

This article illustrates the various practical issues related to NPA which further helped in gaining the depth knowledge about the topic.

3.3 Conclusion

This chapter helped to gain insight on the revolution of concept, norms and cause-and-effect relationship of NPA over the years, through the study of various Research Scholars. Also from this research papers, learning is gained about the research design adopted by the researcher, the methods of analysis and interpretation of data and finding and recommendation which helped in gaining more understanding about the conduct of research.

CHAPTER 4: RESEARCH METHODOLOGY

4.1 Introduction

Banking Sector plays a dominant role in determining the national economy. Its major role is supporting the economic activity, agriculture, industrial, infrastructural development of the country and meeting the financial needs of all the sections of society. Non performing advance does not only have adverse affects on banks financial position and its stakeholders, but it also badly affects the country's economy.

4.2 Statement of Problem

Non performing advances reflect the overall quality of the bank's loan book and most important indicators of its financial health. Rising NPA over the years has become major concern of banking sector. According to a study by the Associated Chambers of Commerce and Industry of India, India's banking sector could witness tough times ahead with its non-performing assets.

As per RBI's annual report Gross NPA ratio has risen from 3.42 per cent to 4.10 per cent by March 2014 and to 4.45 per cent in FY15.

Stressed assets ratio, which is GNPA plus restructured standard advances, stood at 10.9 per cent at the end of March, 2015 as compared to 10 per cent in March, 2014 and 10.7 per cent in September 2014. (Ref: http://www.business-standard.com/article/finance/banks-gross-npa-ratio-rises-to-4-45-from-4-1-in-1-year-rbi-115050601332_1.html)

Public sector banks shows highest Gross NPA ratio compared to other banking sectors which holds 70 % of the banking business. Gross NPAs for public-sector banks stood up to 5.17 of their total outstanding loans in March'15 wherein Gross NPA of all private sector banks were 2.05% in September'15.In a report issued by DNA it shows that out of 26 public-sector banks (nationalized Banks and SBI and its associates), 19 reported Gross NPAs of 5% or more in the latest quarter.

Non Performing Advances affects banks in several ways. Bank loses its income earned through these advances and also bears heavy expenditure to maintain NPA in its account. (This NPA account is written off with banks reserves and capital, which is considered to be the financial strength of the bank). It also affects banks stakeholders in various ways, increase in the rate of interest on loans and other products & services, low rate of interest on deposits, less dividend to share holders and also halts the development of the national economy with poor projects. Though several researchers attempted to study the NPAs, there appears to have several gaps in identification of relevant sectors affected by more NPAs and the reasons for sickness which if identified properly can be effectively used for possible correction by proper management.

Hence there is a need to conduct a research on management of NPA to reduce it occurrences and strengthen the profitability of banking sector.

4.3 Objective of the Study

1) To analyze the trends of 'loan and advances' and 'non performing asset' sector wise, in selected public sector bank's branches in Pune.
2) To evaluate the effect of NPA on profitability of the bank.

3) To gain insight on lending, monitoring and recovery policies of respective bank.

4) Identify and analyze the factors responsible for NPA

5) To suggest measures for NPA management.

4.4 Hypothesis

1) Banks lends maximum to Priority Sector

2) Priority Sector Lending contributes maximum towards NPA.

3) Non performing assets affect the profitability of the bank.

4.5 Limitation of the study

Study is based on primary data which has its own limitations. Study is majorly focused only on NPA's of selected Public sectors bank's branches in Pune. Data collected only from three bank's three branches for the period of three financial years i.e. from 2011 - 2014.

4.6 Research Methodology

Descriptive type of research is undertaken involving relevant literature review from RBI reports, published books, articles and internet and a comparative study of financial data of selected Public sector Banks Branches in Pune for analyzing the various aspects of NPA.

Bank's policy related information on Loans and Advances and NPA and its management are collected from bank's officers through questionnaire and interview method.

Tabular and graphical representation of data is made to analyze and interpret the data collected.

4.6.1 Secondary Research

External

1) Concept of NPA and guidelines is studied on RBI website.
2) Literature review on relevant topic in books, articles, journals, other's thesis, and internet has added value to this research.

Internal

1) Branches financial data is collected and analyzed to evaluate the trends of Loans and Advances and Non Performing Assets and its effects on financial health.

4.6.2 Primary Research

Information related to management of NPA and banks policies and procedure for lending, monitoring and recovery will be collected from the bank's officers through **-**

- Questionnaire
- Structured and Un structured Interview

4.7 Instrument

Questionnaire is used as an instrument for data collection. It consist of two parts –

1) First section is Data Section wherein figures related to Loans and Advances, NPA and financial ratios were asked.
2) Second section consists of closed-Ended questions - Scaled questions, Multiple choice question, Dichotomous questions and Open-Ended Questions.

   This section is divided into five stages. It deals with the general policies, procedure, challenges of the bank with respect to the following stages -

   - Loan Appraisal

- Disbursement of Loan
- Monitoring
- Recovery
- NPA Management

4.8 Sampling Plan

Three branches of three Public sector banks in Pune are taken in this study. Samples were collected at random. Three banks are Vijaya Bank, Corporation Bank and Third Public Sector bank's name undisclosed on banks request and named as PS1 Bank in this study.

4.9 Data Collection

Stage I. Pre Survey Interview

This was basically done to test the instrument used in collecting data.

Sample

The initial stage of data collection started with Pre Survey Interview with the Deputy Manager of two public sector banks, one relationship manager of a renowned private sector bank and two chartered accountants.

The samples taken for this pre survey interview were directly or indirectly related with the topic.

The above mentioned people were not part of the original sample taken for the study.

Objective of this pre survey interview was to understand whether -

1) the questions were focused on the research topic
2) the questions framed could be understood by the respondent

3) any questions to be deleted or added or modified

4) the question were ordered in sequence

Method

1) Deputy Managers were given the questionnaire and were asked to answer and give inputs for each and every question. They discussed about the protocol, practical method of processing the loan and recovery of debts, the challenges faced by them and gave some useful recommendations and suggestions out of their experience. The options given in this closed ended questions were refined with this interview. It took approximately 90 minutes per respondent to cover all the questions.

2) The same questionnaire was presented to the relationship manager of private sector bank. Since he was more associated with handling loans, discussion were more focused on the problems faced by the customer in repaying loans, how does the bank act in solving their problems, their perception towards the working culture of public sector bank. This interview was also very fruitful.

3) It was an open discussion with the chartered accountants. They shared knowledge about the role, issues and challenges of ARC's in debt recovery. The details were of limited use in this research.

The outcome of this interview was extremely valuable.

1) The work culture of public and private sector banks could be known with this interview.

2) It helped to gain more insight about the topic.

3) More significantly, this helped to modify / reframe the questionnaire with the better quality of questions and options.

Stage II. Main study through Questionnaire and Interview Method

Samples

Zonal Head / Regional Head of Vijaya Bank, Corporation Bank and PS1 Bank were approached for permission to take their bank as a sample and to conduct interview with their bank manager.

Method

With the permission of the head, questionnaire was filled by their designated officers. They provided data of their Metro, Urban, and Semi Urban branch each. Since the data was centralized it was possible for the Zonal / Regional office to provide data of their branches.

Officers also shared their experience on day to day handling, interesting live cases, practical problems involved in each stage with reason.

Outcome

1) Unstructured interview with the officers helped to understand the practical issues and their problem solving techniques.

2) Every bank has their own approach in managing things keeping norms as their base.

3) It was also known that the bank is providing service to their customer with personal touch.

4) Observation strongly reflects that experienced officers are efficient in handling NPA in terms of decision making and they prove to be an asset to their banks.

4.10 Period of Study – FY 2011-12, 2012-13 and 2013-2014

CHAPTER 5: DATA PRESENTATION, ANALYSIS AND INTERPRETATION

I. Ratio Analysis

The following financial ratios are considered important to appraise the financial stability and profitability of the bank.

5.1 Gross NPA and Net NPA Ratio

Gross NPA Ratio helps to identify the bad loans out of the total loans sanctioned by the bank. With the help of following formula, the percentage of Gross NPA against Advances lent can be figured out.

$$\textbf{Gross NPA Ratio} = \frac{\textbf{Gross NPA}}{\textbf{Gross Advances}} \ast 100$$

Net NPA determines the actual burden on bank. It is calculated as follows

$$\textbf{Gross NPA Ratio} = \frac{\textbf{Gross NPA - Provisions}}{\textbf{Gross Advances - Provisions}} \ast 100$$

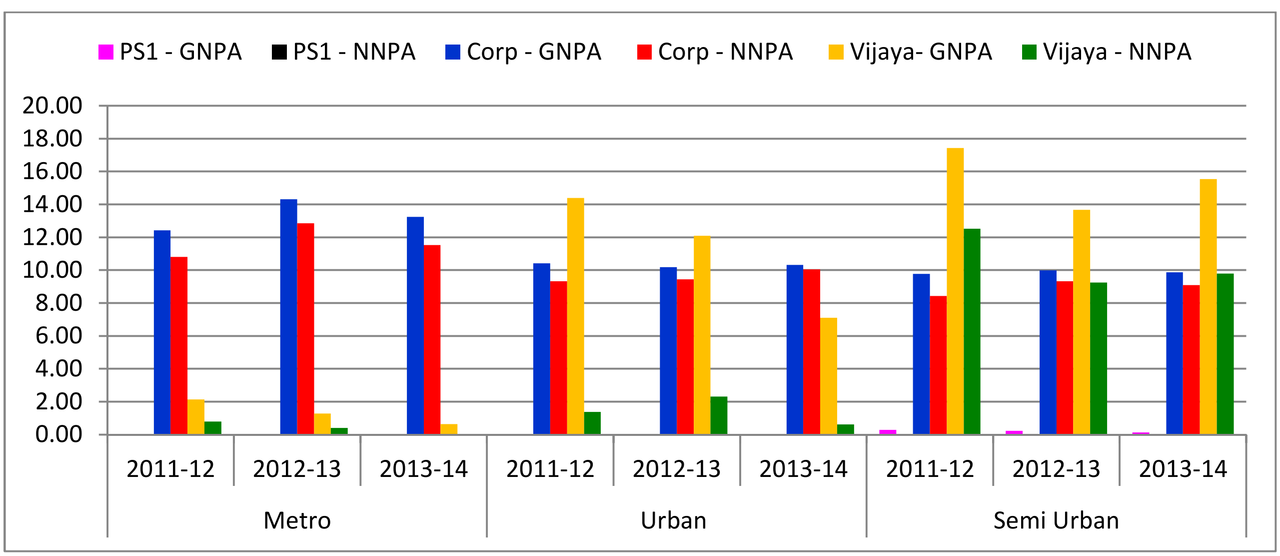
5.1.1 Table: Branch wise Gross NPA and Net NPA

	Metro			Urban			Semi Urban		
	2011-12	2012-13	2013-14	2011-12	2012-13	2013-14	2011-12	2012-13	2013-14
PS1 - GNPA	0.00	0.00	0.00	0.04	0.04	0.03	0.29	0.23	0.12
PS1 - NNPA	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Corp - GNPA	12.42	**14.32**	13.24	10.42	10.18	10.32	9.78	9.98	9.88
Corp - NNPA	**10.80**	**12.86**	**11.53**	9.32	9.45	10.05	8.43	9.32	9.10
Vijaya- GNPA	2.13	1.27	0.64	**14.39**	12.09	7.11	**17.43**	13.68	**15.54**
Vijaya - NNPA	0.79	0.40	0.04	1.37	2.31	0.62	**12.52**	9.24	9.80

5.1.2 Table: Average of Gross NPA and Net NPA

Bank	Metro	Urban	Semi Urban	Average
PS1 - GNPA	0.00	0.04	0.21	0.08
PS1 - NNPA	0.00	0.00	0.00	0.00
Corp - GNPA	13.33	10.31	9.88	11.17
Corp - NNPA	11.73	9.61	8.95	10.10
Vijaya- GNPA	1.35	11.20	15.55	9.36
Vijaya - NNPA	0.41	1.43	10.52	4.12

5.1.3 Graph: Branch wise Gross NPA and Net NPA



ANALYSIS

The graph represents the movement of NPAs in selected public sectors bank's Metro, Urban and Semi Urban branch, in the study.

In a comparative analysis of Metro, Urban and Semi Urban branches of all three banks together, it can be noticed that -

- Among all three Metro branches in the study, GNPA is more in Corporation Bank. And among Urban branches, Vijaya Bank is leading in the year 2011-12 and 12-13 and Corporation Bank has maximum compared to other two banks in the year 2013-14. In Semi Urban branches, Vijaya Bank has maximum percent of GNPA in all three years.
- While Net NPA is more in Corporation bank's both Metro and Urban branch in all three years and in Semi Urban branch in the year 2012- 13. Whereas Vijaya Bank's Semi Urban branch shows maximum Net NPA in the year 2011-12 and 2013-14.

On analyzing the trend of Gross NPA of branches of each bank, it can be noticed that –

- In PS1 Bank, Gross NPA of Metro Branch is nil in the study, and other two branches shows a downward trend.
- In Corporation Bank, there is a decrease of GNPA in its Metro and Semi Urban branch in the year 2013-14. Whereas in Urban branch, GNPA has risen from 10.18 to 10.32 percent in the year 2013-14.

- Gross NPA of Vijaya Bank has been sliding down over the years, except in Semi Urban branch where it shows nearly 2% increase from 13.68 in 2012-13 to 15.54 in the year 2013 -14.

5.2 Provision Coverage Ratio

Is the ratio of provisioning against Gross Nonperforming Assets of bank. It is a key ratio which indicates the fund kept aside by bank by way of provisioning against its risk asset to mitigate losses. It can be calculated as -

$$\textbf{Provision Coverage Ratio} = \frac{\textbf{Gross NPA - Net NPA (Cumulative provisions)}}{\textbf{Gross NPAs}} * 100$$

5.2.1 Table: Branch wise Provision Coverage Ratio

	Metro			Urban			Semi Urban		
	2011 -12	2012-13	2013-14	2011-12	2012-13	2013-14	2011-12	2012-13	2013-14
PS1	-	-	-	100.00	100.00	100.00	100.00	100.00	100.00
Corp	13.0	10.20	12.92	10.56	7.17	2.62	13.80	6.61	7.89
Vijaya Bank	62.89	68.76	94.09	90.46	80.89	91.31	28.16	32.48	36.96

5.2.2 Table: Average of Provision Coverage Ratio

Bank	Metro	Urban	Semi Urban	Average
PS1 Bank	0.00	100.00	100.00	66.67
Corporation Bank	12.05	6.78	9.43	9.42
Vijaya Bank	75.25	87.55	32.53	65.11

ANALYSIS

- PS1 Bank has covered all the risk by provisioning full for the non performing assets.
- Corporation Bank covers minimum risk in all its bank branches, in the study. The average rate of provisioning of Corporation bank is 9.42%.
- Vijaya Bank's Semi Urban Bank covers minimum risk with only 28.16% ,32.48% and 36.96 % of provisioning and maximum risk covered in its urban branch with 90.46%, 80.89% and 91.31% of provisioning, in the period of study. The average rate of provisioning of Vijaya Bank is 65 %.

INTERPRETATION & CONCLUSION

- Overall study reveals that highest percent of Gross NPA is in Vijaya Bank's Semi Urban Branch and highest percent of Net NPA is in Corporation Bank's Metro branch. PS1 Bank shows the lowest percent of NPA in the study. The highest average Gross NPA and Net NPA in the study are in Corporation Bank.
- Low Provision Coverage Ratio means that the bank is at higher risk of gaining losses if uncovered loans turn bad debts. In that case, Corporation Bank is at a greater risk in the study.
- The best bank based on the data in this study is PS1 bank, followed by Vijaya Bank and last is Corporation Bank.

5.3 Non Performing Asset to Profit

Since balance sheet of individual branches are not prepared and only bank's consolidated balance sheet is prepared. Therefore NPA's effect on profitability is shown with the help of Profit and Non Performing Assets taken from respective bank's consolidated balance sheet.

5.3.1 Table: Profit before and after Provisioning for NPA (Rs in Crores)

PS1 Bank	**2011-12**	**2012-13**	**2013-14**
Profit Before Provisioning for NPA	3297.86	3713.45	3802.37
(-) Provision for NPA during the year	1510.73	1555.52	2106.17
Profit after Provisioning for NPA	1787.13	2157.93	1696.20

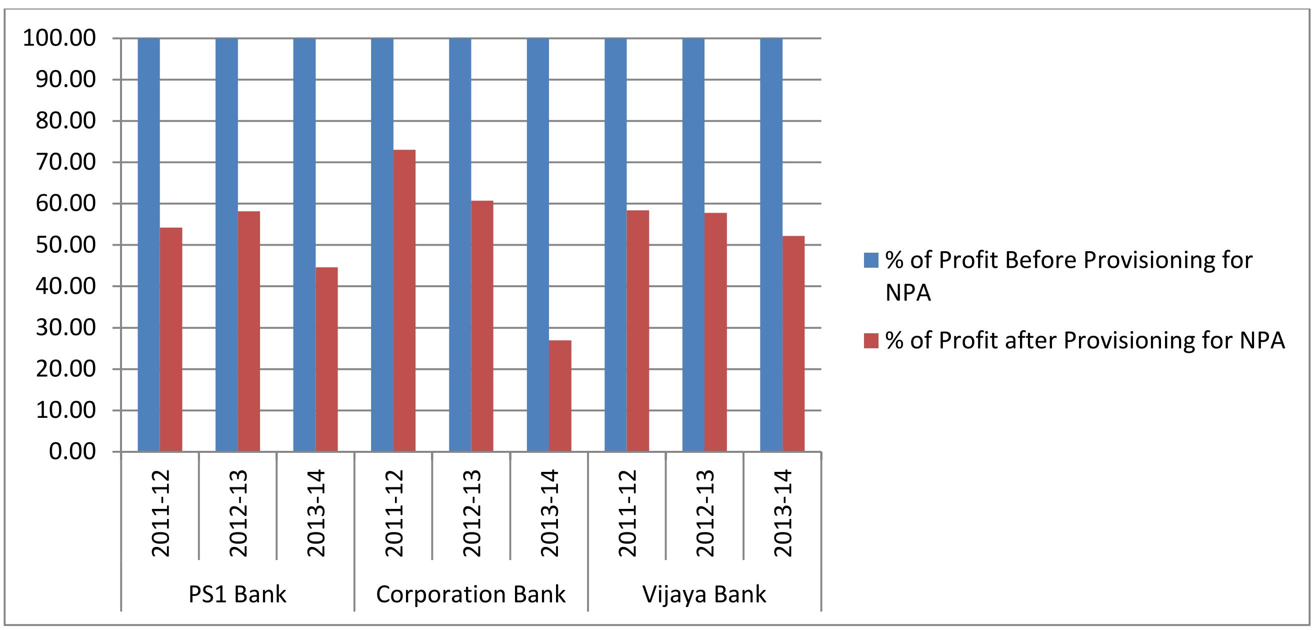
Corporation Bank	**2011-12**	**2012-13**	**2013-14**
Profit Before Provisioning for NPA	2063.24	2362.79	2082.56
(-) Provision for NPA during the year	557.2	928.12	1520.84
Profit after Provisioning for NPA	1506.04	1434.67	561.72

Vijaya Bank	**2011-12**	**2012-13**	**2013-14**
Profit Before Provisioning for NPA	994.93	1013.97	796.73
(-) Provision for NPA during the year	413.94	428.36	380.82
Profit after Provisioning for NPA	580.99	585.61	415.91

5.3.2 Table: Percentage of Profit before and after Provisioning for NPA

BANK NAME	PS1 Bank			Corporation Bank			Vijaya Bank		
YEAR	2011-12	2012-13	2013-14	2011-12	2012-13	2013-14	2011-12	2012-13	2013-14
% of Profit Before Provisioning for NPA	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00
% of Profit after Provisioning for NPA	54.19	58.11	44.61	72.99	60.72	26.97	58.40	57.75	52.20

5.3.3 Graph: Movement of Profit before and after provisioning for NPA (Bankwise)



<u>ANALYSIS</u>

The above graph represents the percentage of Profit before and after provisioning for NPA, of three banks in the study i.e. PS1 Bank, Corporation Bank and Vijaya Bank, for the financial year 2011-12, 2012-13 and 2013-14.

- Corporation Bank's profit has gone down year and year severely from 72.99% to 26.97% and the case is similar with the Vijaya Bank with a slight fall in profit from 58.40% to 52.20%. PS1 Bank's profit has risen from 54.19% to 58.11% in the year 2012-13 but has fallen from 58.11% to 44.61 in the year 2013-14.

INTERPRETATION:

It is observed from the study that because of provisioning for NPA,

- In PS1 Bank, profit has fallen by 45.81%, 41.89% and 55.39% in the financial year 2011-12, 2012-13 and 2013-14 respectively. The average loss of profit **is 47.70%** in the year of study.
- With reference to Corporation Bank, profit has reduced by 27.01%, 39.28%, and 73.03% in the financial year 2011-12, 2012-13 and 2013-14 respectively. And the average loss of profit is **46.44%** during the year of study.
- And in case of Vijaya Bank, NPA provisioning has affected the profit by 41.60%, 42.25%, 47.80% in the financial year 2011-12, 2012-13 and 2013-14 respectively. The average loss of profit is **43.88%** in the three years of study.

Overall, it is observed in the study that all three bank's profit is affected by approximately 27% to 73% because of provisioning for NPA.

CONCLUSION

Since profit of the bank has gone down because of provisioning for non-performing assets of the bank, it is therefore concluded that NPA has an adverse effect on the profitability of bank.

II. Loan Portfolio Analysis

5.4 Priority Sector lending

From the year 1968, priority sector lending was given emphasis in commercial banks. Classification of Priority Sector lending and guidelines were formed in the year 1972 on the basis of a study report by RBI.

Although initially there was no specific targets given to the banks, in the year 1974 banks were advised to have 33 1/3 percent of Priority Sector lending in their total advances by 1979.

In the Year 1980 this proportion was further raised to 40 % for the targeted year 1985. Sub targets within the Priority Sector were also given in this year.

Since then, there have been revisions in guidelines, targets and sub targets of priority sector lending based on the recommendations of the committee.

Accordingly, as per the latest revised guidelines set by RBI, Bank needs to lend 40 percent of the Adjusted Net Bank Credit to the Priority Sector.

5.4.1 Table: Branch wise and Sector wise Loans and Advances

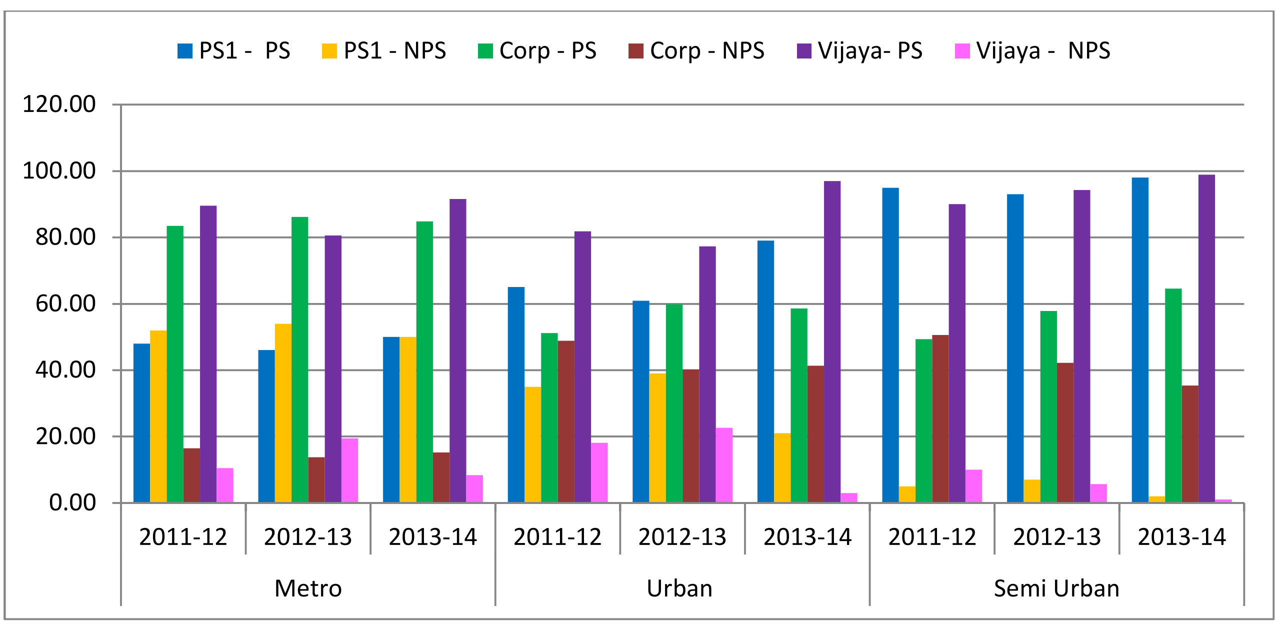
	Metro			Urban			Semi Urban		
	2011-12	**2012-13**	**2013-14**	**2011-12**	**2012-13**	**2013-14**	**2011-12**	**2012-13**	**2013-14**
PS1 - PS	48.00	46.06	50.00	65.03	60.93	79.00	95.00	93.00	98.00
PS1 - NPS	52.00	53.94	50.00	34.97	39.07	21.00	5.00	7.00	2.00
Corp - PS	83.51	86.20	84.79	51.18	59.84	58.62	49.40	57.82	64.60
Corp - NPS	16.49	13.80	15.21	48.82	40.16	41.38	50.60	42.18	35.40
Vijaya- PS	89.53	80.56	91.61	81.89	77.33	97.02	89.99	94.28	98.93
Vijaya - NPS	10.47	19.44	8.39	18.11	22.67	2.98	10.01	5.72	1.07

PS – Priority Sector, NPS – Non-Priority Sector

5.4.2. Table: Average of Loans and Advances in Priority and Non Priority Sector

Bank	Metro	Urban	Semi Urban	Average
PS1 - PS	48.02	68.32	95.33	70.56
PS1 - NPS	51.98	31.68	4.67	29.44
Corp - PS	84.83	56.55	57.27	66.22
Corp - NPS	15.17	43.45	42.73	33.78
Vijaya- PS	87.23	85.41	94.40	89.02
Vijaya - NPS	12.77	14.59	5.60	10.98

5.4.3. Graph: Branch wise and Sector wise Loans and Advances



ANALYSIS

The above graph shows the percentage of Priority and Non-Priority Sectors Lending out of its Total Lending, of three branches of PS1 Bank , Corporation Bank and Vijaya Bank for the financial year 2011-12, 2012-13 and 2013-14.The data collected from 3 branches of three sample banks indicates that -

- PS1 Bank has advanced average percentage of 48.02, 68.32, 95.33 to Priority Sector in its Metro, Urban and Semi Urban Bank respectively.
- Corporation Bank has given 84.83, 56.54 and 57.27 of average percent of loans and advances to Priority Sector in its Metro, Urban and Semi Urban Bank respectively.
- Vijaya Bank has offered maximum percentage of its loans and advances to Priority Sector with 87.23, 85.41 and 94.40 average percent in its Metro, Urban and Semi Urban Bank respectively.

On an average, in the study, PS1 Bank, Corporation Bank and Vijaya Bank has lent 70.56%, 66.22% and 89.02% respectively to Priority Sector.

INTERPRETATION

All the banks under study have met their targets of 40 percent to Priority Sector lending, infact more than the desired percent. Overall in the study, maximum lending is 98.93 % and minimum of 46.06%

CONCLUSION

Banks have lent more to the Priority Sector than Non-Priority sector.

5.5 Non Performing Assets

5.5.1 Table: Branch wise and Sector wise Non Performing Assets

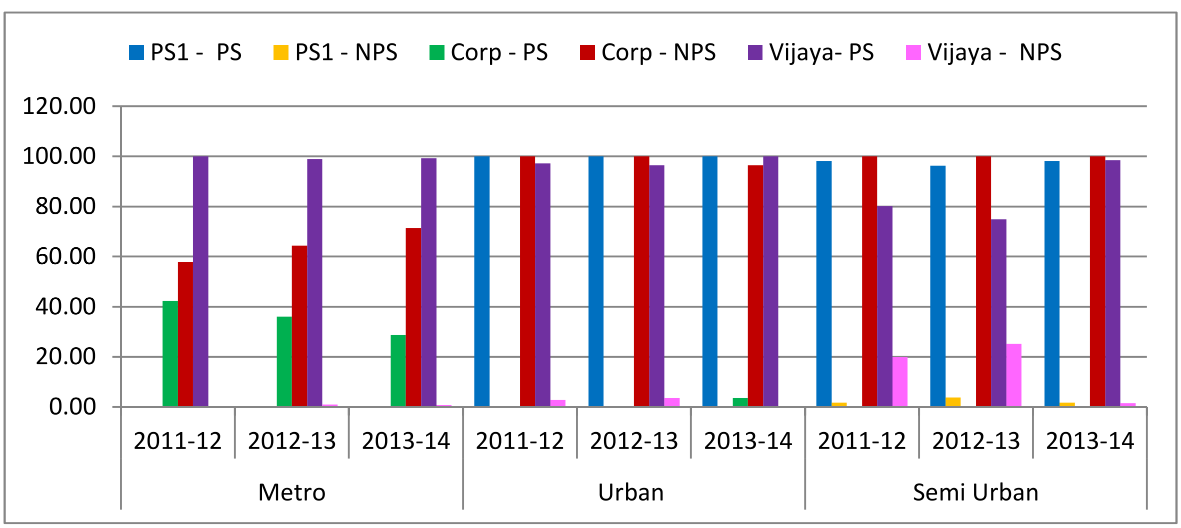
	Metro			Urban			Semi Urban		
	2011-12	2012-13	2013-14	2011-12	2012-13	2013-14	2011-12	2012-13	2013-14
PS1 - PS	0.00	0.00	0.00	100.00	100.00	100.00	98.20	96.25	98.24
PS1 - NPS	0.00	0.00	0.00	0.00	0.00	0.00	1.80	3.75	1.76
Corp - PS	42.28	36.05	28.61	0.00	0.00	3.60	0.00	0.00	0.00
Corp - NPS	57.72	64.36	71.39	100.00	100.00	96.40	100.00	100.00	100.00
Vijaya- PS	100.00	99.03	99.28	97.17	96.43	99.96	80.08	74.82	98.50
Vijaya - NPS	0.00	0.97	0.72	2.83	3.57	0.04	19.92	25.18	1.50

PS – Priority Sector / NPS – Non-Priority Sector

5. 5.2.Table: Average Non Performing Assets in Priority and Non Priority Sector

Bank	Metro	Urban	Semi Urban	Average
PS1 - PS	0.00	100.00	97.56	65.85
PS1 - NPS	0.00	0.00	2.44	0.81
Corp - PS	35.65	1.20	0.00	12.28
Corp - NPS	64.49	98.80	100.00	87.76
Vijaya- PS	99.44	97.85	84.47	93.92
Vijaya - NPS	0.56	2.15	15.53	6.08

5.5.3 Graph: Branch wise and Sector wise Non Performing Assets



ANALYSIS

The above graph shows the percentage of Priority and Non-Priority Sector NPA out of its total NPA, of three branches of PS1 Bank , Corporation Bank and Vijaya Bank for the financial year 2011-12, 2012-13 and 2013-14.The data collected from 3 branches of three sample banks indicates the following trend -

- In PS1 Bank, Urban branch shows 100% of its NPA in priority Sector and more than 96% in its Semi Urban Branch. The average percentage of priority sector NPA in Semi Urban Branch is 97.56.
- Corporation Bank's Metro branch has an average of 35.65% NPA in priority sector and 64.49 in Non-priority sector. In Urban and Semi Urban branch the average percentage of NPA in non priority sector is 98.80% and 100% respectively.
- Vijaya Bank has maximum percentage of its NPA in Priority Sector with 99.44, 97.85 and 84.47 of average percent in its Metro, Urban and Semi Urban Bank respectively.

Bank wise data reveals that PS1 bank and Vijaya Bank's nonperforming assets are majorly in Priority Sector wherein for Corporation bank the case is quite opposite, for them the non performing assets are majorly in Non-Priority sector.

INTERPRETATION

It is observed from the study that not all the banks have maximum nonperforming assets in Priority Sector but NPA occurs majorly in Priority Sector in most of the branches.

CONCLUSION

Thus it is concluded that Priority Sector contributes maximum towards NPA.

5.6 Branch wise Analysis

An attempt is made to analyze the Sub Sectors of Priority Sector and Non-Priority Sector of NPA of all three banks. This is to understand which sub sectors are majorly affected in individual banks.

5.6.1 PS1 Bank

Since the NPA of PS1 Bank is majorly in Priority Sector, sub categories of Priority Sectors are examined here in detail.

5.6.1.1 Table: Sub Sectors of Priority Sector Non Performing Assets of PS1 Bank

Gross NPA	Out of Total %
Agriculture	99.88
Micro and Small Enterprises	0.12
Education	0.00
Housing	0.00
Others	0.00
TOTAL	100.00

ANALYSIS

Out of the total Priority Sector NPAs in PS1 Bank Branches, maximum percent of NPA is in Agriculture sector with approximately 99%, in the study. Second affected sector is Micro and Small Enterprises, but percentagewise it is only 0.12% from the total.

INTERPRETATION

- From the data it can be observed that, Semi Urban Branch lends maximum of around 85% of its total Loans and Advances to Agriculture Sector and very less percent to MSME and other sector.
- And in Urban branch, Agriculture lending is 14% and MSME is 10%, and NPA of these branches are only from Agriculture Sector.
- Unfavorable Climate and Government policy are said to be the major reason for NPA in Agriculture Sector.
- Bank officers in an unstructured interview said that, bank is forecasting NPAs from infrastructural project.

5.6.2. Corporation Bank

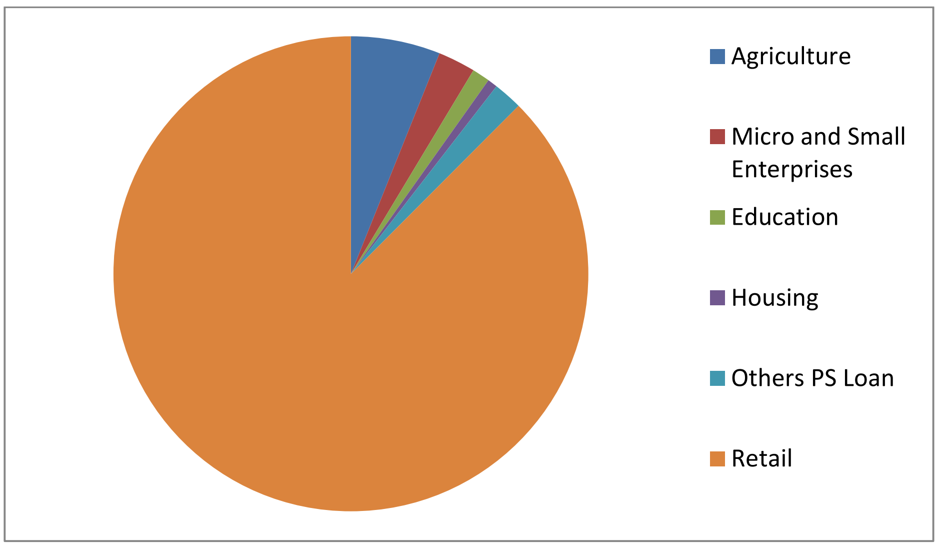
In Corporation Bank, maximum percent of NPA is in Non-Priority Sector, therefore Priority and Non-Priority sector both has been analyzed here.

5.6.2.1 Table: Sub Sectors of Priority and Non-Priority Sector Non Performing Assets of Corporation Bank

Gross NPA	Out of Total %
A.	
Agriculture	6.11
Micro and Small Enterprises	2.54
Education	1.21
Housing	0.68
Others	1.99
TOTAL PS	12.28

B.	
Retail	87.72
Corporate	-
Personal	-
Credit Card	-
Others	-
TOTAL NPS	87.72
Total A+B (PS + NPS)	**100.00**

5.6.2.2 Graph: Sub Sectors of Priority and Non-Priority Sector Non Performing Assets of Corporation Bank



ANALYSIS

Out of the total NPAs of Corporation Bank branches, in the study, largest percentage of NPA is from Non-Priority Retail Sector with approximately 87%. Priority Sector contributes very less towards NPA with Agriculture approximately 6%, MSME 2.5%, Education 1.21%, Housing 0.68% and other Priority Sector NPA 1.99%.

INTERPRETATION

- From the data it can be observed that, Urban and Semi Urban branch lends maximum percent of its loans and advances to Non-Priority Retail Sector, NPA is seen only from this sector in these two branches
- In Metro Branch, loans are offered more to MSME and then to the Priority Sector Retail Loans. Here also Retail Sector NPAs are observed maximum.
- Reason is said to be several internal as well as external factors. Internal factors are delay in process, ineffective monitoring, absence of legal mechanism for recovery, high interest rate and external factors are political interferences / scheme, government policies.
- Bank is forecasting to have more NPAs in Agriculture, Education and Personal Loans.

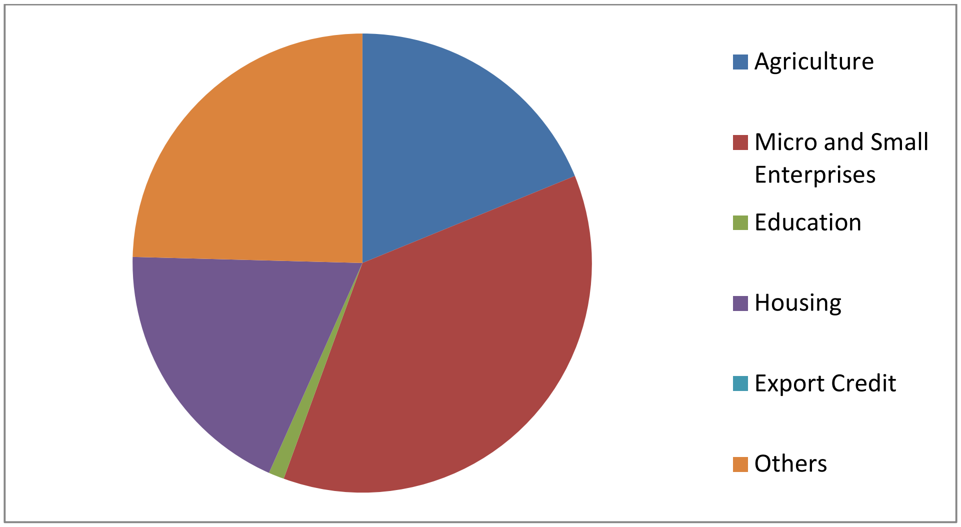
5.6.3 Vijaya Bank

Since the NPA of Vijaya Bank is majorly in Priority Sector, sub categories of Priority Sectors are examined here in detail.

5.6.3.1 Table: Sub Sectors of Priority Sector Non Performing Assets of Vijaya Bank

Gross NPA	**Total %**
Agriculture	18.82
Micro and Small Enterprises	**36.74**
Education	1.09
Housing	18.78
Others	**24.57**
TOTAL PS	100.00

5.6.3.2 Graph: Sub Sectors of Priority Sector Non Performing Assets of Vijaya Bank



ANALYSIS

Out of the total Priority Sector NPAs of Vijaya Bank branches, in the study, majority of NPA is from MSME with approximately 37 percent, next is other priority sector loans with 24.5 %, and then comes the Agriculture sector and housing with close percentage of 18.82% and 18.78% respectively.

INTERPRETATION

- From the data it can be observed that, Metro branch lends maximum percent of its loans and advances to MSME and Housing. Urban branch provides maximum loan to Housing, MSME and other Priority Sector. And in Semi Urban branch maximum lending is in Agriculture, Housing and MSME.
- Overall, maximum lending is in MSME, Housing, Agriculture and other Priority Sector loans.

- Several internal factors like Lack of expertise in analyzing the project, ineffective monitoring and external factors like business failure , diversion of fund, political reason, government policies are said to be the reason for NPA.
- As per Vijaya Bank officers, Bank forecast to have maximum NPA in personal loan because of unavailability of enforceable security. Second is the Agriculture loan since security enforceability is difficult.

CONCLUSION

Overall study reflects that Agriculture, MSME, Housing is the majorly affected sub sectors in Priority Sector and Retail in Non-Priority Sector.

III. Stage wise Analysis and Interpretation

To understand the Lending, Monitoring and Recovery policies of PS1 Bank, Corporation Bank and Vijaya Bank, questionnaire is divided into five stages –

1) Loan Appraisal
2) Disbursement of Loan
3) Monitoring
4) Recovery
5) NPA Management

5.7 .Loan Appraisal

Q.1. As per your opinion, which factors are given more importance while sanctioning loan?

5.7.1 Table: Factors given importance while sanctioning loan

	Character			**Capacity**			**Capital**			**Security**		
	PS1	Corp	Vijaya	PS1	Corp	Vijaya	PS1	Corp	Vijaya	PS1	Corp	Vijaya
Priority Sector												
Agriculture	✓	✓	✓	✓	✓	✓	✓	✓		✓	✓	✓
Micro and Small Enterprises	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	
Education	✓	✓	✓	✓						✓	✓	✓
Housing	✓	✓	✓	✓	✓	✓	✓			✓	✓	✓
Others - Vehicle / Retail		✓	✓		✓	✓			✓		✓	✓ ✓
Non Priority Sector												
Retail	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Corporate	✓	✓	✓	✓	✓	✓	✓		✓	✓		✓
Personal	✓	✓	✓	✓	✓		✓		✓	✓		
Credit Card	✓	✓	✓	✓	✓	✓	✓	✓	✓			

5.7.2 Table: Frequency table for factors given importance while sanctioning loan

	*Character	*Capacity	*Capital	*Security
Priority Sector				
Agriculture	**3**	**3**	**2**	**3**
Micro and Small Enterprises	**3**	**3**	**3**	**2**
Education	**3**	**1**	**0**	**3**
Housing	**3**	**3**	**1**	**3**
Others - Vehicle / Retail	**2**	**2**	**1**	**2**
Non-Priority Sector				
Retail	**3**	**3**	**3**	**3**
Corporate	**3**	**3**	**2**	**2**
Personal	**3**	**2**	**2**	**1**
Credit Card	**3**	**3**	**3**	**0**

*Character includes – Education, Experience, Reference, Cibil Report

*Capacity includes – Skills, Capacity of the business, other sources of repayment

*Capital includes – Working Capital, Net Worth, Cash Flow

*Security includes – Collateral and Guarantee

ANALYSIS

Priority Sector Loans:

Agriculture Loan – Character, Capacity and Security check is given equal importance in all three banks. Capital check is also considered important in PS1 and Corporation Bank.

Micro and Small Enterprises – Character, Capacity and Capital positions equal importance while sanctioning loan. Security is also taken as an important factor in PS1 and Corporation Bank.

Education Loan – Character check is the key criteria in loan appraisal. Security check both collateral and guarantee is also done in PS1 and Corporation Bank and Capacity check i.e. the skills of the candidate is also checked in PS 1 bank.

Housing Loan – Character, Capacity and Security holds important criteria while sanctioning loan.

Others include all other retail loans in which Character, Capacity and Security is a mandatory check before sanctioning loan.

Non - Priority Sector Loans:

Retail Loan - Character, Capacity, Capital and Security is considered equally important in this type of loan.

Corporate Loan – Character, Capacity check is given importance in all three banks. Capital and Security check is also done in PS1 Bank and Vijaya Bank.

Personal Loan – Character, Capacity, and Capital check is given more weightage. Security check is also considered important in PS1 Bank.

Credit Card – Character, Capacity and Capital check is considered important in all three banks.

INTERPRETATION

- From the unstructured interview it could be understood that all parameters have an equal importance in Loan Appraisal.
- From the study, it can also be seen that PS1 Bank insists on security on all types of loan, expect on loans wherever it is not applicable like credit card.
- Overall, Due Diligence Report is the basic and important parameter in Loan Appraisal. Capacity or Capital is the second factor examined to understand the repayment chances and the third factor is the security, which plays as a savior and last option to recover bad debts.

Q.2. What kind of security does the bank receives in each sector?

5.7.3 Table: Security received by the bank in each sub sector

	Pledge			**Hypothecation**			**Mortgage**		
BANK	PS1	Corporation	Vijaya	PS1	Corporation	Vijaya	PS1	Corporation	Vijaya
Priority Sector									
Agriculture			✓	✓	✓	✓	✓	✓	✓
Micro and Small Enterprises	✓			✓	✓	✓	✓	✓	✓
Education	✓						✓	✓	✓
Housing							✓	✓	✓
Others	✓	✓	✓	✓	✓	✓	✓	✓	✓
Non Priority Sector									
Retail	✓	✓	✓	✓	✓	✓	✓	✓	✓
Corporate	✓			✓	✓	✓	✓	✓	✓
Personal				✓			✓		
Credit Card									

5.7.4 Table. Frequency table of security received by the bank in each sub sector

	Pledge	Hypothecation	Mortgage
A – Priority Sector			
Agriculture	**1**	**3**	**3**
MSME	**1**	**3**	**3**
Education	**1**	**0**	**3**
Housing	**0**	**0**	**3**
Others	**3**	**3**	**3**
B – Non - Priority Sector			
Retail	**3**	**3**	**3**
Corporate	**1**	**3**	**3**
Personal	**0**	**1**	**1**
Credit Card	**0**	**0**	**0**
Others	**0**	**1**	**1**

ANALYSIS

- In Agriculture loan and Micro and Small Enterprises loan, hypothecation and mortgage security is received by all three banks. Vijaya Bank also receives pledged security in Agriculture loan and PS1 Bank receives pledge for Micro and Small Enterprises Loan. Normal margin contributed by the borrower for Agriculture loan and Micro and Small Enterprises Loan is 10-25%
- In Education Loan, Mortgage security is received by all three banks. PS1 bank also receives pledge for education loan. Normal margin is 5 – 20% in Education loan.
- Only Mortgage security is received by all three banks for Housing Loan, normal margin is 20%.

- In Other Priority Sector loans like Vehicle Loan, hypothecation is received as 15% margin and for retail loan, all three types of security i.e. pledge, hypothecation and mortgage is received.
- For Retail Loan in Non-Priority sector, all three types of securities are received and margin is 25%.
- In Corporate Loan, hypothecation and mortgage is received by all three banks. Pledge is also received by PS1 bank. Normal margin contributed by borrower is 25%.
- No security charged for Personal Loan and Credit Card in Corporation and Vijaya Bank. PS1 Bank receives hypothecation and mortgage for Personal Loan. The normal margin is 10-25%.
- Other Priority Sector loan include Large and Medium Industry where hypothecation and mortgage is received with normal margin of 25-50%

<u>INTERPRETATION</u>

- Mortgage is received in almost all types of loan except for credit card. In Mortgage, bank takes charge of the immovable property against the loan but the possession lies with the borrower. Bank does not hold right to sell / auction this asset without proper legal proceedings. The entire process takes approximately four months for acquiring the possession and taking action. Eventually, there is loss of money and time.
- Hypothecation is equally accepted like mortgage security, except in Education Loan, Housing and Credit Card. Similar to Mortgage, in hypothecation, bank

takes charge against movable property as a security against the loan given, but the possession lies with the borrower. So in case of bad debts bank has to undergo legal procedure for taking possession of assets and to sell it for realization of its money. This too involves loss of time and money.

- Under Pledge, bank takes charge of right and possession of movable asset. In case of default by the borrower, bank retains the right to sell the asset and recover its outstanding due. This helps in quick and easy recovery of money.

CONCLUSION

In the Loan Appraisal stage, it is observed and concluded that -

- Few bank collects due diligence report through external agency. Since this report plays a very crucial role in determining the acceptance of loan proposal, it is important to have an authentic report.
- Security acts as a life guard and saves bank from loss at the time of bad debts. It is equally important to enforce stringent norms and laws on security.
- Overall in the loan appraisal stage, bank considers certain factors in common for certain types of loan and some banks give more importance to other factors in other types of loans. Thus the importance and preference varies from bank to bank.

5.8 Disbursement

Q.3. Which method bank adopts for payment of loans and advances?

5.8.1 Table: Method adopted by bank for payment of loans and advances

	Directly to Borrowers			**To Suppliers (through RTGS / NEFT)**		
BANK	PS1	Corporation	Vijaya	PS1	Corporation	Vijaya
Priority Sector						
Agriculture				✓	✓	✓
Micro and Small Enterprises				✓	✓	✓
Education				✓	✓	✓
Housing				✓	✓	✓
Non Priority Sector						
Retail				✓	✓	✓
Corporate				✓	✓	✓
Personal	✓	✓	✓			
Credit Card	✓	✓	✓			

5.8.2 Table: Frequency table for Method adopted by bank for payment of loans and advances

	Directly to Borrowers	**To Suppliers (through RTGS / NEFT)**
A – Priority Sector		
Agriculture		**3**
Micro and Small		**3**
Education		**3**
Housing		**3**
B – Non - Priority Sector		
Retail		**3**
Corporate		**3**
Personal	**3**	
Credit Card	**3**	

ANALYSIS

- All three banks, in the study, prefers to make the payment directly to the beneficiary. Only in case of Personal Loan and Credit Card, money is directly given to the borrower.
- In certain cases like in Agriculture Loan, cultivation and harvesting expenses are directly given to the borrower. Similarly in Micro and Small Enterprises Loan and Corporate Loan, money is given to the borrower to meet revenue expenses

INTREPRATAION

Paying money to beneficiary minimizes risk of diversion of fund. In case of personal loan and credit card, there is no control on utilization of fund as the purpose is not specified while acquiring loan, thus bank loses control over such loan.

CONCLUSION

In the Disbursement stage, it is observed and concluded that

- Disbursement Method is common in all the banks under study.
- It is advisable to have close monitoring where money is paid directly to the borrower. Also thorough examination of the beneficiary before payment will help to reduce fraudulent borrowers.

5.9 Monitoring

Q.4. What monitoring mechanisms are adopted by your bank after disbursement of loan?

5.9.1 Table: Monitoring mechanism adopted by bank

	Immediate inspection to check on diversion of fund			**Periodic inspection**			**Stock Audit**			**Market trend**		
	PS1	Corp	Vijaya	PS1	Corp	Vijaya	PS1	Corp	Vijaya	PS1	Corp	Vijaya
Priority Sector												
Agriculture	✓	✓	✓	✓	✓	✓	✓					✓
Micro and Small Enterprises	✓	✓	✓	✓	✓	✓	✓	✓	✓			✓
Education	✓		✓	✓								
Housing	✓	✓	✓	✓	✓	✓						✓
Non Priority Sector												
Retail	✓	✓	✓	✓	✓	✓			✓			✓
Corporate	✓	✓	✓	✓	✓	✓	✓	✓	✓			✓
Personal												
Credit Card												

5.9.2 Table: Frequency Table for Monitoring mechanism adopted by bank

Consolidated	Immediate inspection to check on diversion of fund	Periodic inspection	Stock Audit	Market trend
Agriculture	**3**	**3**	**1**	**1**
Micro and Small	**3**	**3**	**3**	**1**
Education	**2**	**1**	**0**	**0**
Housing	**3**	**3**	**0**	**1**
Retail	**3**	**3**	**1**	**1**
Corporate	**3**	**3**	**3**	**1**
Personal	**0**	**0**	**0**	**0**
Credit Card	**0**	**0**	**0**	**0**

ANALYSIS

From the survey it can be found that –

Under Priority Sector

- In Agriculture Loan, immediate inspection and periodic inspection is carried out by all the banks to check on diversion of fund. Vijaya Bank keep an update on market trend as well and PS1 Bank does stock audit periodically.
- In Micro and Small Enterprises, immediate inspection after disbursement, periodic inspection and stock audit is done by all three banks. Vijaya Bank also monitors the market trend.
- For Education Loan, Immediate check is carried out by PS1 Bank and Vijaya Bank. PS1 Bank also does periodic inspection. Corporation Bank does not monitor this type of loan.
- In Housing Loan, check on diversion of fund and periodic check is made by all three banks in the study. Vijaya Bank also keeps an eye on the market trend.

Under Non-Priority Sector

- In Retail Loan, immediate and periodic check is carried out by all three banks. Vijay bank also conducts stock audit and market trend analysis.
- In Corporate Loan, Immediate and period inspection and stock audit is conducted by all three banks. Vijaya Bank also does a market analysis.
- There is no monitoring mechanism for personal and credit card loan.

INTERPRETATION

- It is observed from the survey that Vijaya Bank also keeps them updated on the market condition by doing a market analysis for each type of loan.
- Immediate and periodic inspection is made mandatory by all banks to avoid any slippages.

CONCLUSION

In the Monitoring stage, it is observed and concluded that

- All three banks follows a common mechanism for monitoring but extra initiative should also be taken by the bank like market trend analysis by expert for more close monitoring and detecting warning signal.
- There is a need to develop monitoring mechanism for Credit Card and Personal Loan .

5.10 Recovery

Q.5. Measures adopted to collect the outstanding credit from the borrower

5.10.1 Table: Frequency Table for Measures adopted to collect the outstanding credit

Consolidated	Follow-up mechanism	One Time Settlement	Recovery Agents	Lok Adalat	Filing a case in DRT	SARFAESI Act
30 days due	**3**					
60 days due	**3**					
Sub Standard	**3**	**2**	**1**	**2**	**3**	**3**
Doubtful	**3**	**3**	**1**	**3**	**3**	**3**
II	**3**	**3**	**1**	**3**	**3**	**3**
III	**3**	**3**	**1**	**3**	**3**	**3**
Loss Asset	**3**	**2**	**0**	**2**	**2**	**2**

*Follow-up Mechanism includes -spot visit, frequent calls / emails / notices by the bank officers

<u>ANALYSIS</u>

- Follow up is made at all stages of NPA by all banks in the study.
- Once the asset becomes NPA, if follow up does not work, next method adopted is filing a suit in DRT / SARFAESI.
- Bank prefers Lok Adalat for recovery of small amount.
- Recovery Agent is appointed on banks interest to outsource the activity.

PS1 Bank and Corporation Bank appoints recovery agent at the early stages of NPA wherein Vijaya Bank prefers to involve recovery agent only at the final stages of NPA.

INTERPRETATION

A question was asked to each bank officers to understand the best effective method in recovery and as per their opinion -

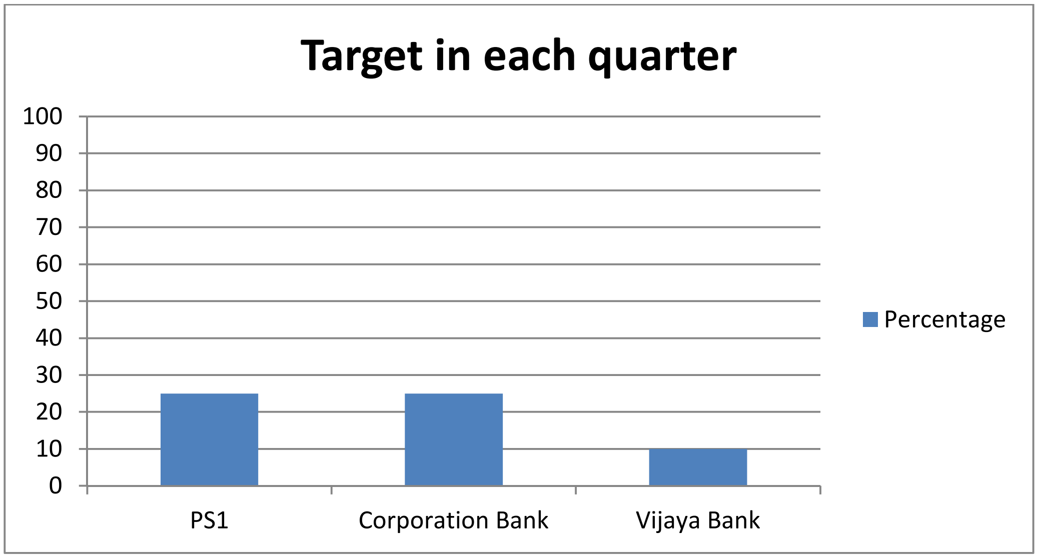
- Follow-up with the borrower is considered to be the most preferable and effective way in recovering outstanding credit at all stages. SARFAESI, One Time Settlement and Recovery Agent are the next dominating option for recovery of NPA.
- During the study period, In PS1 Bank and Corporation Bank, most of the recovery were made through recovery agent and in Vijaya Bank through one time settlement.

Q.6. What % of NPA you expect to recover in each quarter

5.10.2 Table: Target set by bank in each quarter for recovery

Bank	Percentage
PS1	25
Corporation Bank	25
Vijaya Bank	10

5.10.3 Graph : Target set by bank in each quarter for recovery



<u>ANALYSIS</u>

- Even though bank prefers to recover 100% of their outstanding credit, a target is been set to recover the NPA in each quarter taking into consideration the time and efforts invested in the recovery process.
- Minimum target set in each quarter by the banks are 25 % by PS1 Bank and Corporation Bank and 10% by Vijaya Bank.

Q.7. Time period generally taken to recover the outstanding credit from the borrower.

a. Within the deadline

b. Beyond the deadline

5.10.4 Table:Time period taken to recover the outstanding credit from the borrower

	Within the deadline	Beyond the deadline
PS1 Bank		✓
Corporation Bank	✓	
Vijaya Bank	✓	

ANALYSIS

Corporation and Vijaya Bank are in the opinion that targets are met within the deadline however for PS1 bank recovery takes beyond the targeted time.

CONCLUSION

In the Recovery stage, it is observed and concluded that -

- Legal proceeding is not possible in certain type and amount of loan because of restrictions in law.
- From the observation and unstructured interview it can be understood that recovery decision is taken based on “borrower to borrower basis”. Practical thinking is said to be much required for clearing NPA.
- Each Bank sets their individual realistic targets based upon their NPA amount and available resources.

5.11 NPA Management

Q.8. Of the following stages, which stage gives more weightage for loans and advances to become NPA?

5.11.1 Table: Stage which gives more weightage for loans and advances to become NPA

(Score 4 = Highly Responsible, Score 1 = Less Responsible)

	Loan Appraisal	Disbursement	Monitoring	Recovery
PS1 Bank	**4**		**3**	**2**
Corporation Bank	**4**	**1**	**3**	**2**
Vijaya Bank	**4**	**4**	**4**	**4**

ANALYSIS

- Vijaya Bank believes that all stages are of equal importance and for them each and every stage holds equal weightage for an asset to become NPA.
- For PS1 Bank and Corporation Bank, Loan Appraisal holds first rank, second is Monitoring and third is Recovery.
- Corporation Bank also considers Disbursement as last reason for NPA.

INTERPRETATION

- Early stage is considered to be the most crucial stage to determine the quality of loan. Loan Appraisal involves scrutiny of borrower, his proposal and security which are the major factors for Loan and Advances to become NPA.

- The second important stage is regarded as Monitoring. An inappropriate monitoring mechanism would not help in early detection of NPA which in turn increases the risk for an asset to become NPA.
- The third stage of importance is Recovery. An effective recovery process is required to minimize loss, save time and efforts and blockage of fund. Lengthy or inappropriate recovery processes not only postpones the asset to become NPA but also incurs huge loss which can be reduced by taking action at the right time.
- And the last stage contributing to NPA is Disbursement. This stage involves giving out the sanctioned loan. There can be problems if adequate loan amount is not disbursed at the right time.

Q.9. As per your opinion, in NPA, What are the percentage of -

a. Genuine defaulters ☐

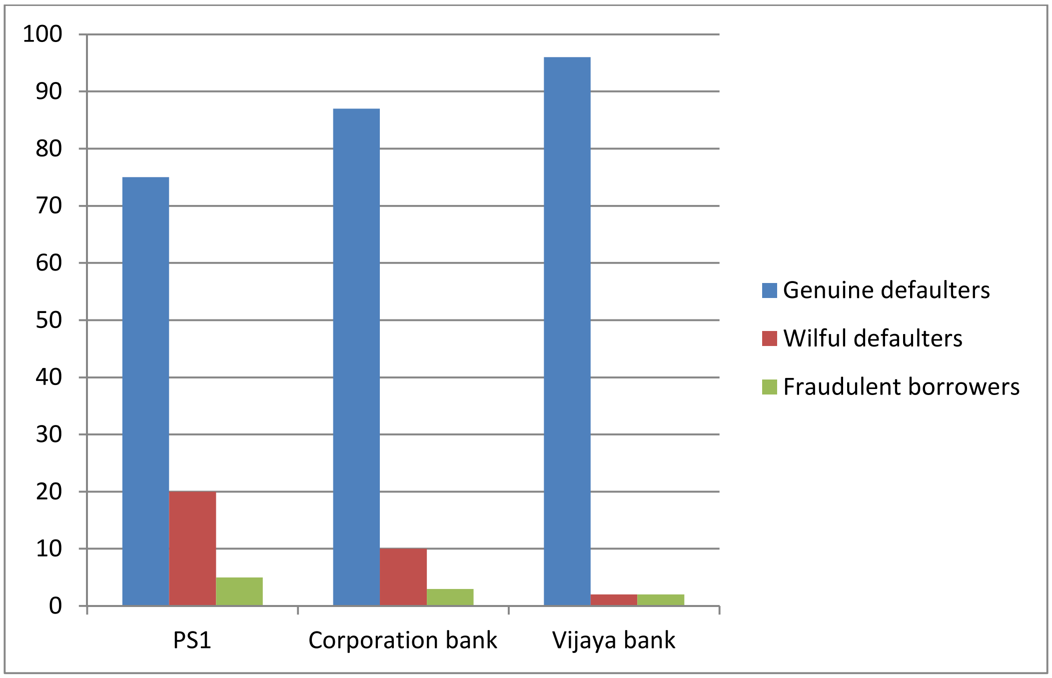
b. Willful defaulters ☐

c. Fraudulent borrowers ☐

5.11.2 Table: Percentage of Defaulters

	Genuine defaulters	Willful defaulters	Fraudulent borrowers
PS1 Bank	**75**	**20**	**5**
Corporation Bank	**87**	**10**	**3**
Vijaya Bank	**96**	**2**	**2**

5.11.3 Graph: Percentage of Defaulters



ANALYSIS

- All the banks under study have stated that out of the entire defaulters, majority of them are genuine. Genuine defaulters are on and above 75% , willful defaulters lies between 2 to 20 percent and comparatively fraudulent borrowers are less between 2 to 5 Percent.

INTERPRETATION

- Genuine categories have been regular in paying the dues, and hold intention to pay the interest and loan on time but are unable to do so due to some unforeseen situation. There are 75% in PS1 bank, 87% in Corporation Bank and 96% in

Vijaya Bank. Vijaya bank holds the highest percent of genuine defaulters compared to PS1 and Corporation Bank.

- Next is the Willful defaulter who holds 20, 10 and 2 percentage in PS1, Corporation and Vijaya Bank respectively.
- Fraudulent borrowers are very less compared to the other two types of defaulters having 5% in PS1, 3% in Corporation Bank and 2% in Vijaya Bank.
- It is observed that Character check is given more importance by all three banks, this helps to identify the fraudulent borrower at the time of loan appraisal.

Q.10. As per your opinion, who should be held liable for non recovery of outstanding credit.

a. Bank

b. Employee

c. Borrower

5.11.4 Table: Liable for non recovery of outstanding credit

	Bank	**Employee**	**Borrower**
PS1 Bank			✓
Corporation Bank		✓	✓
Vijaya Bank		✓	✓

5.11.5 Table: Frequency table for Liable for non recovery of outstanding credit

	Opinion
Bank	**0**
Employee	**2**
Borrower	**3**

ANALYSIS

All three banks are in an opinion that borrower should be held liable for outstanding dues. None of the respondents claimed the responsibility of Bank. According to Corporation and Vijaya Bank employees are equally liable for non recovery of outstanding credit.

INTERPRETATION

- First responsibility holds with the borrower as they have agreed to pay the interest and loan installments on time and agreed to the terms and conditions lay down by the bank. And the borrowers are liable for all the legal actions on nonpayment of the due amount.
- Secondly, the employees involved in the entire process hold responsibility as it is their duty to collect the due amount and take appropriate action on nonpayment. If any of the employees is not performing his role and responsibility in the approved manner, the entire process gets disturbed and becomes one of the reasons for non performing asset.

Q.11. Yearly, what percentage of expenses bank bears for the management of NPA.

5.11.6 Table: Percentage of expenses bank bears for the management of NPA

Bank	Response
PS1 Bank	NIL
Corporation Bank	NIL
Vijaya Bank	NIL

ANALYSIS

All the three banks in the study has same stand that there is no expenses bared by the bank for the management of NPA.

INTERPRETATION

- Bank generally absorbs the expenses incurred in recovery process such as call, travel, courier etc, these are assumed to be standard expenses regardless to the category of asset. The expenses which are occurred in connection with NPA such as expenses in sale of security, legal charges etc are added to the NPA account. Therefore it is not treated as expenses to bank.
- However bank bears the losses which occur while settling the NPA account.

Q.12. Whether restructuring of loan is effective.

a. Yes b. No

5.11.7 Table: Whether restructuring of loan is effective

Bank	Response
PS1 Bank	YES
Corporation Bank	YES
Vijaya Bank	NO

ANALYSIS

PS1 and Corporation Bank agree that restructuring of loan is effective. Vijaya Bank is in the opinion that restructuring of loan is not effective. In its opinion, restructuring is simply postponement of NPA.

INTERPRETATION

It is observed that even though banks have different ideas regarding restructuring, only less than 5% of NPA is restructured by the banks every year. This indicates that restructuring of loan and advances is carried out at a very minimum level. Restructuring of loan has high risk of falling into NPA category in future.

Q.13. Whether your bank follows Risk Management Policy, if yes, how effective it is in early detection of NPA.

a. Low b. Medium c. High

5.11.8 Table: Whether Risk Management Policy in your bank is effective

Bank	Response
PS1 Bank	MEDIUM
Corporation Bank	HIGH
Vijaya Bank	MEDIUM

ANALYSIS

All the banks in this study have expressed implementation of Risk Management Policies in their respective banks. Further PS1 and Vijaya bank are of the opinion that Risk Management Policies has a medium effect in detection of NPA and Corporation Banks opines the effect is high.

INTERPRETATION

There are various types of risk the bank has to take care of. It can be broadly classified into credit risk, market risk, and operational risk. Risk management plays an important role at the time of loan appraisal, this helps in granting loan to the right proposal with minimum risk. It is not considered as a sole factor to decide upon sanctioning of loan but definitely as one of the factors during loan appraisal.

It is agreed upon that risk management gives maximum input however monitoring is considered to be most effective in detecting NPA.

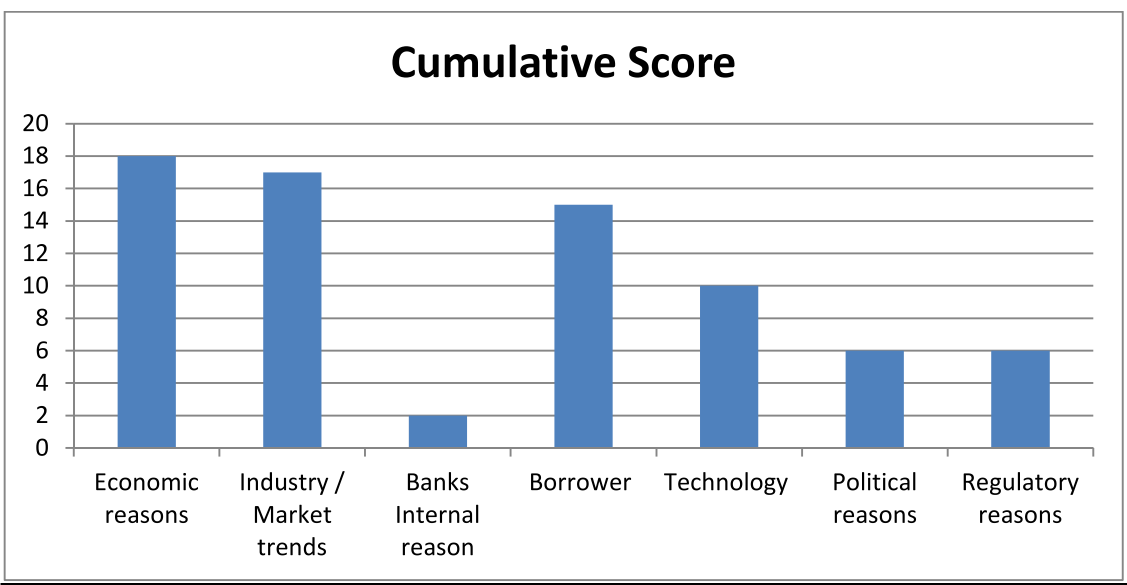
Q.14. Which factors are highly responsible for NPA

5.11.9 Table: Factors responsible for NPA

(Score 7 = highly responsible, Score 1 less responsible)

	Economic reasons	Industry /	Banks Internal	Borrower	Technology	Political reasons	Regulatory reasons
PS1 Bank	**7**	**5**		**6**			
Corporation Bank	**7**	**6**	**1**	**2**	**5**	**4**	**3**
Vijaya Bank	**4**	**6**	**1**	**7**	**5**	**2**	**3**
Cumulative Score	**18**	**17**	**2**	**15**	**10**	**6**	**6**

5.11.10 Graph: Cumulative Score for Factors responsible for NPA



ANALYSIS

- As per the research study, PS1 observes Economic factor as the major reason for NPA followed by Borrower and third being Industry / Market trends.
- Similarly in case of Corporation Bank, Economic is the major reason, followed by Industrial / Market trends, and then the Technology, Political and Regulatory factors, lastly Borrower and Bank Internal reasons.
- Vijaya Bank is mostly similar to Corporation Bank with few different opinion. As per its view, Borrower is the major reason for NPA, and then the Industry / Market Trends, Technology, and Economic reasons is in 4^{th} Place, and lastly the Regulatory, Political and Banks internal factors.
- Cumulative score under the study shows that, Economic factors, Industrial / Market Trends and Borrower are the top 3 reasons responsible for NPA.

INTERPRETATION

- External Factors like Economic, Industry, and Technology are uncontrollable factors and carries a huge effect on all the sectors. Thus they are the major reasons for NPA.
- There are two cases of default by borrower –
    - Borrower is willing to pay but do not have the capacity for repayment
    - Borrower is unwilling to pay but has the capacity for repayment

  The first one is a genuine defaulter who defaults payment due to uncontrollable circumstance and second one is the willful defaulter. Both the situations may arise at any time and bank needs to handle it tactfully.

- Political and Regulatory reasons put pressure on bank's working system.
- Bank's Internal system or resources are also responsible, which if corrected on time can save many future losses of bank.

Q.15. Whether training to staff helps in reduction of NPA.

a. Yes   b.No

5.11.11 Table: Whether training to staff helps in reduction of NPA

	YES	NO
PS1 Bank	✔	
Corporation Bank	✔	
Vijaya Bank	✔	

ANALYSIS

All the banks in the study agree to the factor that training to staff helps in reduction of NPA.

INTERPRETATION

Training helps in upgrading the skill and knowledge of the employees. It is crucial to have regular upgradation to create an efficient and effective working environment. At present, bank is providing required training to their staffs.

Q.16. Any remedial measure adopted by your bank in the following stages to prevent NPA , please specify the measures.

- Loan appraisal
- Disbursement of Loans and Advances
- Post disbursement supervision
- Recovery

5.11.12 Table: Remedial measure adopted by the bank

	Loan appraisal	**Disbursement of Loans and Advances**	**Monitoring**	**Recovery**
PS1 Bank			YES	
Corporation Bank	YES			YES
Vijaya Bank				

ANALYSIS

PS 1 has formed remedial measure in monitoring stage. Corporation Bank has adopted remedial measures in Loan Appraisal and Recovery stage.

INTERPRETATION

PS1 Bank follows Structured Monitoring Policy wherein inspection of every account is done in 30 / 45 / 60 days, quarterly and annually.

Corporation Bank Loan Appraisal stage is outsourced to “Due Diligence Agencies”. They have announced special schemes for repayment of loans and advances for few sectors.

Q.17. Which type of "loans and advances" has high risk of getting converted into NPA? The reason behind it.

PS 1 Bank -

- According to PS1 Bank, Infrastructural Project like power, steel, chemical and Real Estate lending is at high risk due to government policy in Infrastructural Project and prevailing market condition of Real Estate.

Corporation Bank –

- Agriculture sector has high risk of getting converted into NPA because of high dependability on nature and political sensitivity. Fresh loan given to Agriculture Sector even after "One Time Settlement".
- Second is Education sector because of lack of responsibility of the borrower and employment opportunity
- Third is said to be personal loan because of non security, people attitude to change the job frequently.

Vijaya Bank –

- Personal Loan because of unavailability of enforceable security
- Second is Government sponsored scheme, which can be withdrawn due to change in government.
- Third is Agriculture Loan since security enforceability is difficult.

CHAPTER 6: CAUSES AND IMPACT OF NPA

6.1 Causes of NPA

Several studies have been carried out to identify the causes of NPA and to reduce its occurrences. It will be difficult to completely eradicate NPA because of few uncontrollable factors but it is possible to control the rising of NPA by identifying controllable variables.

There are various factors, either jointly or independently, responsible for the causes of NPA. The major reasons which directly or indirectly affects the performing assets of the banks are given below -

1) Economic / Environmental Factor
   - Slow down in country's or global economy
   - uncertainty in the global markets
   - Natural Calamities

2) Political reasons
   - Change in government policy for e.g. – ban in mining projects.
   - Delay in granting permission related to environmental projects such as power, iron, steel sector etc.
   - Political interference in granting loan to any individual / company / project.
   - Political Subsidy Scheme / debt relief policy

3) Industry / Market trends

Industries are witnessing increased stress like aviation, telecom etc for various reasons.

- Since LPG, country is facing tough competition in domestic as well as in global market.
- Sick industry such as aircraft company etc
- Unavailability of resources, Shrinking demand or rapid change in market trend resulting in low productivity or supply.

4) Banks

- Aggressive lending by banks
- Lack of expertise which is required in various stages like appraisal, monitoring and recovering of loan.
- Deficiency of policies in various process
- Delay in process for e.g. loan approval and loan disbursement which sometimes destroys the purpose of loan proposed.
- Inadequate skill for appraisal of loan which leads to wrong lending decision like sanctioning loan for wrong project or rejecting the potential one.
- Lack of accountability since bankers keep getting transferred
- Lack of Centralized Credit Information Mechanism
- High rate of interest
- Unrealistic payment schedule

- lengthy recovery process with the question of uncertainties
- Delay in collection of receivables
- Improper valuation of collateral security which allows bank to lend more than required

5) Borrower
    - Poor Project
    - Mismanagement in various functional areas
    - Poor implementation of projects due to lack of managerial skills or resources
    - Diversion of Fund such as personal use, purchase of unproductive fixed assets, unwarranted expenses.
    - Due to uncontrollable factors like health issue, loss of job, emergency in family
    - Willful defaulter
    - Fraudulent borrower

6) Regulatory and policy reasons
    - Slow & prolonged judicial process
    - Misuse of regulation like restructuring of NPA just to show lesser NPA in books, it only worsens the situation later.
    - Lousy legal system such as no severe action against willful defaulters.

- Existing provision not implemented rigorously for e.g. – if a person wants to appeal against the order in DRT, the person needs to deposit 75% of the loan amount with the court , which is generally waived of by the judge.
- Shortage of staff in DRT's
- The system of rewards and penalties for performance and non-performance is weaker in public sector banks

7) Technology

- Sudden change in technology affects industry badly, it takes time for the industry to cope up with the change and stabilize its business.
- Use of outdated technology further maximizes the risk of failure of business

6.2 Impact of NPA

1) **Profitability**

Return on investment, which is considered to be the current earning of the bank, is affected because of NPA. It also affects the long term profit because of money being blocked in the wrong project thus not allowing the bank to invest in a fruitful return earning project. Also bank needs to do provisioning for NPA at increasing rate with the growing period of NPA; this directly affects the profitability of the bank.

2) **Capital deterioration**

Increasing credit defaulters pulls down the income of the bank, affecting the profitability. Provisioning of loan and loss on loan asset is adjusted from the capital. Thus Banks net worth is severely disturbed with rising NPA.

3) **Mobilization of Money**

Banks core activity of mobilization of fund is hampered because of the fund being trapped as NPA. This halt in recycling of loan results in weak asset position of bank.

4) **Operational Difficulties**

Bank faces lack of money due to rising NPA and lowering of profit. This leads to borrowing of fund temporarily which further leads to additional burden to the bank .It becomes difficult for the bank to function due to cash crisis.

5) **Resources of bank**

Banks resources and time and efforts of management and employees are put in managing NPA which could be dedicated in some prospective activity of the bank.

6) Reputational Risk

NPA adversely affects the banks goodwill. It brings negative rating in the market also builds poor image about the bank and its management. This in turn affects the stakeholders and prospective customers of the bank which hampers banks business.

7) Hinders Country's Development

The Indian banking industry plays an important role in the economic development of the country and is the most dominant segment of the financial sector. Bank extends financial resource to various sectors such as agriculture, infrastructure, industry, services which contributes to the GDP. Since banking and economic development are correlated, any interruption in banking activity that distress the financial health of the bank also hinders the economic development of the country.

CHAPTER 7: FINDINGS AND CONCLUSION

1) Risk Based Loans -

- Agriculture loan is said to have high risk of getting bad because of -
    - its high dependability on nature
    - Politically sensitive as government may announce subsidy and waive off the loan anytime.
    - Fresh loans are issued even after OTS

- Housing Loan –

  Banks are seeing a sudden spurt in bad debt in the home loan segment, a warning that RBI issued last week. (Ref http://timesofindia.indiatimes.com/business/india-business/Home-loans-see-rising-bad-debt/articleshow/45235511.cms)

Housing loans has the second largest Priority Sector NPA in the study, reason being the -

- increasing illegal construction in Pune
- non availability of centralized data in sub registrar office

Complicated process for permission and the lack of mechanism to identify and control the legal construction are the reasons for booming illegal constructions in Pune leading to NPA.

As informed by one of the bank manager during interview, there are 22 sub registrar offices in Pune but they do not have centralized data sharing facility.

- Education Loan is one of the risk based loans in Priority Sector because of
  - no proper employment
  - lack of responsibility or casual attitude among youngsters such as switching over job very frequently
  - Students migrate for employment

- Corporate Loan –

Edelweiss in a recent report has pointed out that major stress to the banking system comes from iron and steel, infrastructure and textile industry. Not only are the NPAs highest in these segments but so are the slippages. (Ref:http://www.business-standard.com/article/opinion/five-pros-and-cons-of-rbi-s-new-npa-takeover-norms-115060900455_1.html)

Corporate loans are affected due to government policies, prevailing market condition.

However, as per the new rule by RBI, bank can acquire 51% of stake of the defaulting company after the loan has been restructured. With the new mechanism to recover, it is expected to cut down the losses on corporate loan.

- Personal Loans and Credit Card

  Because there is no security charged against the loan and no monitoring being carried out.

2) Loan Appraisal -

   - In loan sanctioning process, big loans are approved by Regional offices wherein small loans are handled by branch itself. This results in lack of accountability by bank Manager.
   - Some bank does the due diligence check by its own staff wherein some prefer to get it done through the outsourced agents. The Bank authorities stated in an interview that the report prepared by the agent cannot be fully authenticated.
   - Cibil reports are not updated. Bank takes time in sending the updated information to Cibil.

3) Monitoring -

   - Loan account is monitored with a long gap and no rigorous monitoring mechanism is available which provides warning signal at early stage.

4) Recovery –

   Bank use the four upayas or approaches " Sāma, Dāna, Bheda, Danda " for recovery.

When a borrower defaults payment, the first action that bank takes is follow-up – gentle reminders to the borrower to clear the due, this is an art of gentle persuasion “Sāma – Respect”

If this doesn’t work, the next step preferred is announcing offers / scheme for payment that is Dāna – Gift / compensation.

If that still does not encourage the borrowers to clear the dues then comes the “Bheda – Division”, the matter is directed to Recovery Agent or taken upon legally in DRT / SARFAESI.

When the money is still not recovered, the last technique used is *Danda* – Punishment, where bank has the power of “seize and desist”.

Till the time bank takes strict action against the borrower, it bears huge losses. It is therefore necessary to scrutinize individual account and take action at the initial period of default.

5) Provisioning –

Provision is derived from the profit which has an impact on the reserves and equity thus hitting overall capital structure of the bank. Rising NPA demands for the need for more provisioning thus it cuts down the profitability of the bank. Therefore to keep the profitability intact, provisioning to be reduced and in view of that there is a need to reduce and control NPA.

6) Restructuring

- Loans which were restructured earlier have come under stressed asset. Under the new scheme of restructuring where bank can restructure its long term loan for every five years, gross NPA is estimated to fall down by next year but such loans have high risk of turning into bad debts. Banks attention gets attracted more towards managing such stressed asset resulting in lesser attention towards boosting credit. Restructuring also affects the profitability of the bank because of lowering interest rate.
- There is lack of expertise and resources to monitor stressed assets.

7) DRT –

The objective of DRT is to help financial institutions in speedy recovery of outstanding dues instead of proceeding in lengthy civil court procedure. The purpose doesn't seem to be fulfilled rather banks are experiencing more pain than gains out of it.

- As per law, cases must be disposed in 6 months timeline but only 1/4th of the cases pending at the start of the year is been disposed during the year. At present there is no mechanism to ensure timely disposal of cases.

(Refhttp://www.business-standard.com/article/finance/debt-recovery-tribunals-more-pains-than-gains-for-banks-114121600139_1.html)

- There are 33 DRT and only 5 DRAT. Over 5,000 cases are pending in western zone and it becomes a matter of concern when the chairperson is on leave or vacant. At such cases only urgent matters are transferred to other region wherein regular appeals are adjourned till the Chairperson is appointment or resumes his duty.

- "*If bankers cannot get their money back, they are not going to give you loans at cheap price. So, making sure debt recovery tribunals work better, making sure that you don't have excess number of stays, excess number of appeals – that is what we need to focus on," RBI governor Raghuram Rajan* (Ref http://www.business-standard.com/article/finance/debt-recovery-tribunals-more-pains-than-gains-for-banks-114121600139_1.html)

Unless the dues are cleared bank cannot make fresh lending, the whole process gets halted here.

8) Technology –

Unavailability of defined process and system for entire loan asset life cycle across banks is one of the problems in early detection and alerting bad loans. Each bank follows their individual system from loan sanctioning to closure of loan account. There is also no database linkage system to monitor the entire stage of loan starting from the loan appraisal, disbursement, periodic monitoring and settlement of account.

9) Willful Defaulter -

From Vindhyavasini group to Winsome, Forever Precious Jewellery, Yash Birla's Zenith Birla and even a government company called NAFED, the list of wilful defaulters is growing at a fast pace.

(Ref:http://indianexpress.com/article/business/business-others/bad-debt-wilful-defaults-on-a-rise-up-90-in-14-to-44465-crore/)

A latest report shows that willful defaulter has raised to 90% from 2013 to 2014, which is nearly 15% of total nonperforming assets of banking industry. Cases filed against the borrower is still pending in the courts and DRT's for many years. Bank has to eventually write off the bad loans which they are unable to recover from the borrower.

10) Competitor -

From the unstructured interview with the bank officers it was found that Public sector banks faces tough competition in the market from the Private Sector Bank. Major key activities are outsourced by the Private Sector Bank which makes them expert in each activity. Customers get lured by the promotional strategies and borrow loan from the private sector bank. Bank loses its potential borrowers.

11) Reluctant to offer fresh loans -

With high NPA's hitting the profitability, banks are now reluctant to lend fresh loans especially to the corporate sector unless their loan books are cleared.

12) Interest Rate -

High interest rates have resulted Retail borrowers especially home and car loans to postpone their purchase and companies deferring borrowing.

CHAPTER 8 - RECOMMENDATIONS

Effectiveness of any industry is measured on the basis of its resources which are man, money, machinery and material. Similarly in banking industry it is judged on its financial statement, employees, technology, product and services. Therefore bank must focus on improvement of all its resources.

1) Loan Appraisal stage –

   - Certification course should be developed by the banking institution for agencies providing due diligence services, wherein agents should be trained and certified by the government for providing services to banking industry.
   - Banks must send information immediately to CIBIL for regular up gradation. Penalty could be levied on banks for delay in updating the data.
   - Bank Manager must initiate more social contacts and display more accountability.
   - Banks must insist on pledge as far as possible to enable easy recovery at the time of bad debts without intervention of legal procedure.
   - In case of Mortgage and Hypothecation, legal process should be made simple and quick for immediate action.

2) Disbursement -

   - Bank needs to make pre and post disbursement supervision to ensure fund goes to the right person and utilized properly.

- Also disbursement of adequate amount and at the appropriate time will help in effective use of fund .

3) Monitoring –

- Stringent and regular monitoring is crucial in capturing frauds at any stage. Necessitate more focus on examining the causes of such frauds and suggest appropriate measures and amendments in norms and policy, in order to avoid possible NPAs.
- Adequate staff must be employed for close surveillance of loan portfolio
- Structured training program should be developed and regular training must be provided to officers about the monitoring techniques.
- Continuous feedback with the officers will help to understand the practical issues involved in the process and suggestions could be given thereof.

4) Recovery –

- Immediate rigorous action should be planned against the defaulter if he ignores the initial calls / reminders like -
  - Visit by group of officers
  - Notice in the main place of the village / city
  - Notice in news paper with photo
- Recovery climate should be free from political interference.

5) Strengthening of Law –

- Law should be strengthened to ensure mandatory time bound disposal of cases.

  Improvement in the functioning of DRT and SARFAESI is required to help banks for speedy recovery of dues.

    - Number of DRAT should be increased
    - Staff and Infrastructure should be made adequate
    - Stringent timeline for disposal of cases

- Willful defaulters should be dealt with severely by registering complaint under criminal law.
- Centralization of Data in respective government sectors should be mandated for easy access of data.
- Banking norms should not get influenced by political interferences.

6) Technology –

- More up gradation required in technology for appraisal and monitoring of loan.
- It is necessary to consolidate or centralize the details of the borrower in terms of credit offered and its security across banks, to prevent banks from offering credit to wrong customer or security.
- Technology can bring in more accuracy, cost and time effectiveness in managing and decision making.

- Moreover this can help in studying various dimensions of NPA which can further assist in policy framing, product design and market analysis.
- Smart use of technology can pave the way for improvement in asset quality.

7) Strengthening Manpower –

- Structured and regular training programs to bank employees across banks should be initiated by RBI to update them with the system and upgrade their skills in handling the loan portfolio.
- Adequate staff should be employed by recruiting young talents through campus recruitment.
- Feedback mechanism should be initiated to take regular feedback from the officers about the challenges faced which can help in correcting or developing new system.
- Performance Appraisal should not only be used as a tool to reflect past performance rather should also be used as a pillar for planning future activities to improve effectiveness of bank.

8) Restructuring –

- Restructuring should be one time phenomenon unless situation continues to remain adverse.
- External experts can be hired to monitor restructured loans to avoid any slip-up.

9) Fair Game –

- Government must take initiative to eradicate unethical ways in banking industry.
- RBI should bring in audit system of Private Sector banks in par with the public sector bank to achieve more transparency and equality.
- Competitive advantages of Private sector bank should be studied such as their way of operation, Central Processing Cell, product and marketing strategy etc and should try to adapt the best effective method in public sector banks.

10) Bank must act as a commercial as well as non-commercial organization. It must operate with an intention to earn profit as well as to support the development of individual and country. In view of that, banks must take adequate security and cover maximum margin for all types of loan other than the weaker section.

CONCLUSION -

To emphasize on profitability, bank must focus more on potential borrowers and finance on viable projects for the development of an individual, its own entity and nation as a whole. Hence stringent loan appraisal for selection of right borrower, adequate and timely disbursement of fund, close monitoring and assisting for the correct use of fund and timely recovery is essential for reducing or preventing NPA and for generating profitability for the bank.

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ANNEXURE I - QUESTIONNAIRE

Name of the Bank: ________________________ Date:
Branch: ___________________________________

1.

	% of Loans and Advances in each sector (from total) (FINANCIAL YEAR)			% of NPA in each sector (from total) (FINANCIAL YEAR)		
	2011-12	2012-13	2013-14	2011-12	2012-13	2013-14
A.						
Agriculture						
Micro and Small Enterprises						
Education						
Housing						
Others						
TOTAL Loan and Advances in Priority Sector						
B.						
Retail						
Corporate						
Personal						
Credit Card						
Others						
TOTAL Loan and Advances in Non priority Sector						
A + B (Total Loans and Advances)						

2. Recovery of NPA through the following channels –

	Recovery Agent	One Time Settlement	Lok Adalat	DRTs	SARFAESI Act
FY 2011- 12					
No. of cases					
Total Amount					
Amount recovered					
FY 2012-13					
No. of cases					
Total Amount					
Amount recovered					
FY 2013-14					
No. of cases					
Total Amount					
Amount recovered					

3. What % of NPA has been written off fully during the FY -

FY 2011-12	
FY 2012 - 13	
FY 2013 - 14	

4. Financial Ratios

	FY 2011 - 12	FY 2012 - 13	FY 2013 - 14
Gross NPA			
Net NPA			
Provision coverage ratio			

STAGE 1 - Loan Appraisal

1. As per your opinion, which factors are given more importance while sanctioning loan?

	Character (Due Deligence Report)				Capacity			Capital			Security	
A.	Edu	Exp	Ref	CIBIL report	Skills	Of the business	Other Sources of repayment	WC	NW	CF	Collateral Security	Guarantee
Agriculture												
Micro and Small Enterprises												
Education												
Housing												
Others												
B.												
Retail												
Corporate												
Personal												
Credit Card												
Others												

Edu – Education
Exp – Experience
Ref – Reference

WC – Working Capital
NW – Net worth
CF- Cash Flow

2. What kind of security does the bank receives in each sector?

	Pledge	Hypothecation	Mortgage
A – Priority Sector			
Agriculture			

Micro and Small Enterprises			
Education			
Housing			
Others			
B – Non - Priority Sector			
Retail			
Corporate			
Personal			
Credit Card			
Others			

STAGE 2 - Disbursement of Loan

3. Which method bank adopts for payment of loans and advances?

	Directly to Borrowers	To Suppliers (through RTGS / NEFT)	Reimbursement
A – Priority Sector			
Agriculture			
Micro and Small Enterprises			
Education			
Housing			
Others			
B – Non - Priority Sector			
Retail			
Corporate			
Personal			
Credit Card			
Others			

Challenges Faced -

____

____

____

STAGE 3 - Monitoring

4. What monitoring mechanisms are adopted by your bank after disbursement of loan? Please tick

	Immediate inspection after disbursement	Check on diversion of fund	Periodic inspection	Stock statement	Market trend	Any other, please specify
A – Priority Sector						
Agriculture						
Micro and Small Enterprises						
Education						
Housing						
Others						
B – Non - Priority Sector						
Retail						
Corporate						
Personal						
Credit Card						
Others						

STAGE 4 - Recovery

5. **Measures adopted to collect the outstanding credit from the borrower**

	Follow-up mechanism including - spot visit, frequent calls / emails / notices by the bank officers	One Time Settlement	Recovery Agents	lok adalat	Filing a case in DRT	SARFAESI Act
30 days due						

60 days due						
Sub Standard Assets						
Doubtful Assets I						
II						
III						
Loss Asset						

B. Best Effective Method -

	Follow-up mechanism including - spot visit, frequent calls / emails / notices by the bank officers	Utilization of credit counselors	One Time Settlement	Recovery Agents	lok adalat	Filing a case in DRT	SARFAESI Act
30 days due							
60 days due							
Sub Standard Assets							
Doubtful Assets I							
II							
III							
Loss Asset							

6. What % of NPA you expect to recover in each quarter ____________

7. Time period generally taken to recover the outstanding credit from the borrower.

   a. Within the deadline
   b. Beyond the deadline

STAGE 4 - NPA Management -

8. Of the following stages, which stage gives more weightage for loans and advances to become NPA? Please specify the rank order.

   a. Loan Appraisal ☐
   b. Disbursement ☐
   b. Monitoring ☐
   c. Recovery ☐

9. As per your opinion, in NPA, What are the percentage of -
a. Genuine defaulters ☐
b. Wilful defaulters ☐
c. Fraudulent borrowers ☐

10. As per your opinion, who should be held liable for non recovery of outstanding credit.
    a. Bank
    b. Employee
    c. Borrower

11. Yearly, what percentage of expenses bank bears for the management of NPA.

    ____

12. Whether restructuring of loan is effective.

    a. Yes b. No

13. Whether your bank follows Risk Management Policy, if yes, how effective it is in early detection of NPA and the reasons.
    a. Low b. Medium c. High

Reasons –

14. Which factors are highly responsible for NPA,

	please specify the rank order	% of their share in NPA
Economic reasons		
Industry / Market trends		
Banks Internal reason		
Borrower		
Technology		
Political reasons		
Regulatory reasons		

15. Whether training to staff helps in reduction of NPA.

a. Yes b.No

16. Any remedial measure adopted by your bank in the following stages to prevent NPA ,.

- Loan appraisal
- Disbursement of Loans and Advances
- Post disbursement supervision
- Early detection of NPA
- NPA recovery

17. Which type of "loans and advances" has high risk of getting converted into NPA? The reason behind it

a. ______________________________

b. ______________________________

c. ______________________________

d. ______________________________