# NON-PERFORMING ASSETS OF SCHEDULED COMMERCIAL BANKS IN INDIA: ITS REGULATORY FRAME WORK

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## ABSTRACT

*Bank plays a vital role in the economic development and growth of a country. In a developing country like India, there is a need of efficient and healthy banking system. But from past few decades NPA has become a big threat for the growth of banking sector. In the present scenario, the core financial problem for banks is NPA. Proper recovery of loans can boost the performance of banks. Therefore, an attempt is made in this paper towards examining the effectiveness of NPA recovery measures. Selected recovery measures like Lok Adalat, Debt Recovery Tribunal and SARFAESI Act are taken to study the effectiveness of NPA recovery. From the study it is inferred that recovery of NPAs is still a measure concern for commercial banks in India. One of the reason for the poor recovery from NPAs is that, the mechanism created for this purpose are not effective that's why banks are not able to derive full benefits from these.*

***Key words:*** *Economic development, Non-Performing Assets, Recovery Measures, Lok Adalat, Debt Recovery Tribunal, SARFAESI Act.*

## INTRODUCTION

Economic development of a country depends upon an efficient financial system.

In a developing country like India the commercial banks plays a major role for the economic development in the financial

system. The primary function of a commercial bank is to channelize the surplus savings of the people to the deficit sector in the form of credit for their growth and development. The efficiency of a bank is determined by its profitability and the quality of asset it possesses. Before 1991 asset quality was not a major worry for the Indian commercial banks rather the importance was on widening the banking network, priority sector lending and employment generation. After the recommendation of Narasimham Committee in 1991, it was found that Indian banks are burdened with huge amount of Non-Performing Assets due to which banks had gone financially weak. When RBI issued prudential norms in the year 1992-1993, the concept of Non-Performing Assets evolved as a present day issue. Before implementation of this norm an asset is considered as non-performing if the interest or installment or both is unpaid for a term 180 days or more, but after prudential norms the period of 180 days is lessen to 90 days beginning from 31st March 2004.

The Reserve Bank of India to accelerate the NPAs recovery has designed several debt recovery channels such as Debt Recovery Tribunals (DRTs), Lok Adalats and SARFAESI-Act, 2002. Every now and then the government of India is also taking various necessary steps for minimizing the non-performing assets.

## REVIEW OF LITERATURE

**Sahni & Seth (2017)** made a study on NPAs in Indian commercial banks and they opined that for improving financial performance in the banking sector, the NPAs have to be organized. Government has taken different measures to reduce the NPAs. It is in the part of banks to be careful while giving loans. They must be very much careful and also ensure the credit worthiness of various customers.

**Banana & Chepuri (2017)** in their study stated that the growth rate in advances is decreasing and growth rate in NPAs is increasing, which is not desirable to the bank. Sufficient and strict stapes are needed to be taken before sanctioning of the loans and effectiveness must be there in the supervision of disbursed loans.

**Singh (2016)** stressed on recovery aspect of NPAs in the Indian banking sector. Though different measures have been taken by government to reduce the NPA level, but still there is a needed of strong measures. No bank can make its NPA level at zero. The internal authority must take necessary steps to speed up the recovery process.

**Garg (2016)** in his research paper concluded that the problem of NPA impacts profitability, liquidity and results in credit loss. Proper remedial measures are needed to be taken to reduce the quantity of huge NPA.

**Dubey & Kumari (2016)** in their study opined that if MCAP of banks is taken as a reflection of stock market performance of banks then advances and indicator in the post crisis period of the Indian

economy remaining equity MCAP of market may be taken as a good enough and may be used for picking bank stocks.

## RESEARCH GAP

Looking at the literatures it is found that a lot of study has been done to find out the reasons of NPAs in Indian banking sector, impact of NPAs on banks performance, measures to control NPAs, NPA management and overall efficiency. But very less number of studies has been made on the recovery mechanism of NPAs in Indian banking sector. Therefore, this gap has been identified and explored in our study.

## PROBLEM STATEMENT

The banking sector plays a key role in the financial system of a country, as it directly contributes to the GDP and by bringing forward the savings and spreading the investments. But after managing all kind of challenges, NPAs has been a biggest challenge for them, and its recovery is one of the hardest tasks for the commercial banks. As the increasing amount of NPA adversely affect not only the banking sector but also to the Indian economy. Proper recovery of loans can boost the performance of banks. Therefore, an attempt is made in this paper towards examining the effectiveness of NPA recovery measures.

## OBJECTIVES OF THE STUDY

❖ To study the concept of Non-Performing Assets in the banking sector.

❖ To study the effectiveness of regulatory framework for recovering debts of Scheduled Commercial Banks.

## RESEARCH METHODOLOGY

**Sources of data: -** Data for this study has been collected from secondary sources. These include data from RBI report trends and progress of banking in India, various published articles, books, journals and research papers.

**Study period: -** Present study covers 9 years, from 2008 to 2016 to compare and analyze the trends of NPA recovery in Scheduled Commercial Banks in India.

**Tools and techniques used: -** Data are analyzed and presented by the help different statistical tools like percentages, tables, graphs, etc.

## ANALYSIS AND INTERPRETATION

### Concept of Non-Performing Assets

An asset becomes non-performing when the borrower is not able to pay either interest or principal or both for a period of 90 days. Reserve Bank of India from year ended 31st march, 2004, to follow global practices and high degree of transparency in a view to move towards international practices and greater degree of transparency, made it applicable for 90 days overdue norm for identifying NPA.

### Asset classification

According to the asset classification norms of Reserve Bank of India, following are the different types of assets of a bank.

1) Standard Assets

2) Substandard Assets

3) Doubtful Assets

4) Loss Assets

**Standard assets:** An asset in which there is no chance of default and which carry only normal risk attached to the banks is known as standard asset. These assets should not be considered as nonperforming asset. Provision for standard asset is made at 0.25% of all type of standard advances.

**Substandard assets:** If an asset remains non-performing for a term up to 12 months then it would be considered as substandard assets. Provision is made at 10% of all type of standard advances.

**Doubtful assets:** If an asset remains non-performing for a period more than 12 months. Provision in these assets are made differently, for a term up to 1 year provision is made 100% of no secured advances and 20% of secured advances, for a term more than 1 year but less than 3 years provision is made 100% of unsecured advances and 30% of secured advances and for term 3 years or more provision is made 100% of both unsecured and secured advances.

**Loss assets:** A loss asset is a type of asset in which an asset remains non-performing for a term more than 3 years. In this type of asset provision is made 100% of unsecured and 100% of secured advances.

As stated by the Reserve Bank of India, in comparison to other Asian countries and U.S., the level of Gross non-performing assets are more than the Net non-performing assets in India. Historically, Indian banks are poor on credit recovery, because of very little legal provision governing foreclosure and bankruptcy, lengthy legal battles, sticky loans made to public sector undertakings, loan waiver and priority sector lending.

## NPAs RECOVERED THROUGH VARIOUS CHANNELS OF SCBs

### NPAs recovered through Lok Adalats of SCBs

Table-1 shows non-performing assets recovery by Indian scheduled commercial banks by the help of lok adalat during our study period. It is found that, the case referred has been increased to a great extent in the year 2015-2016 in comparison to 2007-2008. The trend of NPA recovery by lok adalat is showing an inconsistent trend from 2007-2008 to 2015-2016. Though the amount of NPAs recovery is in an upward trend, but if we see the percentage of recovery then the trend is quit fluctuating. After 2012 the percentage of amount recovered by Lok Adalats shows an inconsistent declining trend. It is recovering 3200 Crore out of 72000 Crore of amount involved in 2016, i.e. only 4.4%. It is much less than other recovery channels. Due to its inefficiency in recovering, the Schedule Commercial Banks searching for other recovery channel.

## NPAs recovered through DRTs of SCBs

Table-2 disclosing recovery of Non-Performing Assets by Schedule Commercial Banks through Debt Recovery Tribunal during our study period of 2007-08 to 2015-16. It is very clear from Table 2 that the referred cases for NPAs recovery to DRTs during the period of study, has been increasingly improved. It recovers highest percentage of involved amount in NPAs i.e. 81.1% in 2008-09 and then it shows the decline trend in recovery percentage in the subsequent years. We can see that the Lok Adalats recovers very less percentage of NPAs in comparison to the DRTs. So the Schedule Commercial Banks has been considered DRTs is best channel of recovery than Lok Adalat.

## NPAs recovered through SARFAESI Act 2002 of SCBs

Table-3 showing the data related to the study period of 2007-08 to 2015-16. This table 3 shows the NPAs recovery by SARFAESI Act 2002 of SCBs. Number of cases referred under Act was 83,942 Crore in the year 2008 and increased up to 1,73,582 Crore in the year 2016. Trend in the number of cases referred increased year after year from 2008 to 2016. The above table exhibited that amount involved was Rs.7,263 Crore in the year 2008 and increased up to Rs.80100 in the year 2016. Data related to amount recovered highlighted that Rs.4,429 Crore recovered in the year 2008 and increasing up to Rs.

13,200 Crore in the year 2016. It is also shows increasing trends which is good for the all the banks.

## NPAs of SCBs recovered through various channels

Figure 1 depicted that the NPAs recovery percentage by Lok Adalat (8.2%) is very negligible in comparison to the percentage of NPA recovery by DRTs (51.9%) and SARFAESI Act 2002 (61%) in the year 2008. In 2016 the percentage of NPA recovered has been decreasing to 4.4% in Lok Adalat, 9.2% in DRTs and 16.5% in SARFAESI Act. We can clearly conclude that SARFAESI Act recovers highest amount of NPA during the period of study (i.e. 2008-2016). So it is the most favorable NPAs recovery channel.

## Findings

- From our study period of 2008 to 2016 Schedule Commercial Banks has been recovered Rs.2,535 Crores of NPAs by Lok Adalat.

- From the year 2008 to 2016 Schedule Commercial Banks has been recovered Rs.37,831 Crores of NPAs by Debt Recovery Tribunals.

- From the year 2008 to 2016 Schedule Commercial Banks has been recovered Rs.1,16,044 Crores of NPAs SARFAESI Act 2002.

- The basic factors responsible for increasing NPAs are ineffective recovery, willful defaults and defective lending process.

## Table 1- NPAs recovered through Lok Adalats of SCBs

| Year | Cases Referred (in No.) | Involved Amount (in crore) | Recovered Amount (in crore) | Recovered Amount (%) |
|---|---|---|---|---|
| 2007-08 | 1,86,535 | 2,142 | 176 | 8.20 |
| 2008-09 | 5,48,308 | 4,023 | 96 | 2.40 |
| 2009-10 | 7,78,833 | 7,235 | 112 | 1.55 |
| 2010-11 | 6,16,018 | 5,254 | 151 | 2.87 |
| 2011-12 | 4,76,073 | 1,700 | 200 | 11.8 |
| 2012-13 | 8,40,691 | 6,600 | 400 | 6.10 |
| 2013-14 | 16,36,957 | 23,200 | 1,400 | 6.20 |
| 2014-15 | 29,58,313 | 31,000 | 1,000 | 3.20 |
| 2015-16 | 44,56,634 | 72,000 | 3,200 | 4.40 |

*Source: Reserve Bank of India*

## Table 2- NPAs recovered through DRTs of SCBs (Amount in Crore)

| Year | Cases Referred (in No.) | Involved Amount (in crore) | Recovered Amount (in crore) | Recovered Amount (%) |
|---|---|---|---|---|
| 2007-08 | 3,728 | 5,819 | 3,020 | 51.90 |
| 2008-09 | 2,004 | 4,130 | 3,348 | 81.10 |
| 2009-10 | 6,019 | 9,797 | 3,133 | 32.00 |
| 2010-11 | 12,872 | 14,092 | 3,930 | 27.89 |
| 2011-12 | 13,365 | 24,100 | 4,100 | 17.00 |
| 2012-13 | 13,408 | 31,000 | 4,400 | 14.10 |
| 2013-14 | 28,258 | 55,300 | 5,300 | 9.50 |
| 2014-15 | 22,004 | 60,400 | 4,200 | 7.00 |
| 2015-16 | 24,537 | 69,300 | 6,400 | 9.20 |

Source: (RBI) Report in Trends and Progress of Banking in India, RBI.

## Recommendations

- Former credit assessment and observing system should be reconsidered by RBI.
- Strong loan recapture methods should be employed by all Indian banks.
- RBI may take initiative against defaulter through newspaper, media by publishing their name, which will ultimately supports the financial institutions.
- The recovery mechanisms must be strengthened so that the recovery amount can be increased.

**Table 3-** NPAs recovered through SARFAESI Act 2002 of SCBs (Amount in Crore)

| Year | Cases Referred (in No.) | Involved Amount (in crore) | Recovered Amount (in crore) | Recovered Amount (%) |
|------|------|------|------|------|
| **2008** | 83,942 | 7,263 | 4,429 | 61.00 |
| **2009** | 61,760 | 12,067 | 3,982 | 33.00 |
| **2010** | 78,366 | 14,249 | 4,269 | 30.00 |
| **2011** | 1,18,642 | 30,604 | 11,561 | 37.78 |
| **2012** | 1,40,991 | 35,300 | 10,101 | 28.60 |
| **2013** | 1,90,537 | 68,100 | 18,500 | 27.10 |
| **2014** | 1,94,707 | 94,602 | 24,402 | 25.80 |
| **2015** | 1,75,355 | 1,56,800 | 25,600 | 16.30 |
| **2016** | 1,73,582 | 80,100 | 13,200 | 16.50 |

Source: (RBI) Report in Trends and Progress of Banking in India, RBI.

**Table 4- Percentage of NPAs Recovery through various channels of Schedule Commercial Banks (Amount in Percentage)**

| Channel\Year | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 |
|------|------|------|------|------|------|------|------|------|------|
| **% of Amount Recovered by Lok Adalat** | 8.2 | 2.4 | 1.55 | 2.87 | 11.8 | 6.1 | 6.2 | 3.2 | 4.4 |
| **% of Amount Recovered by DRTs** | 51.9 | 81.1 | 32 | 27.89 | 17 | 14.1 | 9.5 | 7 | 9.2 |
| **% of Amount Recovered by SARFAESI Act 2002** | 61.0 | 33.0 | 30.0 | 37.78 | 28.6 | 27.1 | 25.8 | 16.3 | 16.5 |

*Source:self-compiled*

**Figure 1-Showing Recovery percentage of NPAs of Schedule Commercial Banks through various channels (Amount in Percentage)**
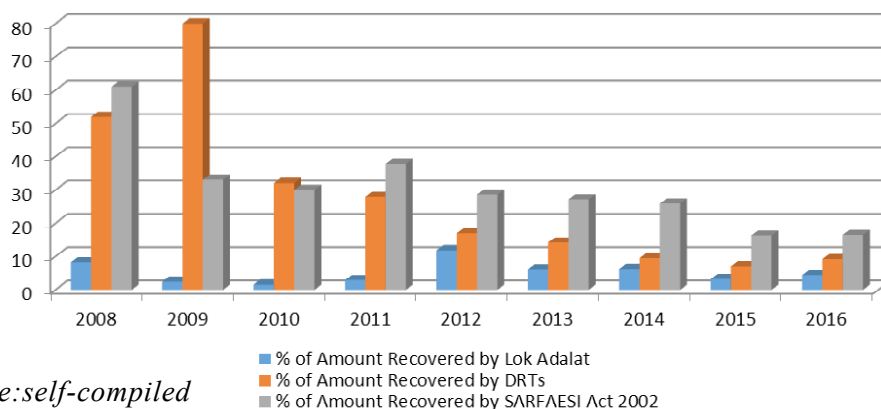


*Source:self-compiled*

## CONCLUSION

The major problem in Indian banking industry is the increasing level of NPAs. As the interest on funds lent is the major source for Indian banking sector. So money blocked as NPAs has a significant influence on effectiveness of banks. The study reflects that the Indian Schedule Commercial Banks suffering from high level of NPAs. The government has been taken diverse steps to minimize the NPAs level but still a lot of efforts are to be executed to curb this problem. From our study it is inferred that among different mechanisms made by the government, SARFAESI Act-2002 is the most effective reform measure in the Indian banking industry for NPA recovery. But if we compare the amount involved and the amount recovered then the amount recovered is very negligible in comparison to amount involved. One of the reasons for the poor recovery is that, the mechanisms created for this purpose are not effective, that's why banks are not able to derive full benefits from these.

## LIMITATIONS OF THE STUDY

In this study we have certain limitations, that are- this study is limited to only lok adalats, debt recovery tribunals and SARFAESI Act. The data for the study is confined to all scheduled commercial banks during 2008 to 2016. If more years of data were added then more accurate results could have been obtained. The analysis can further be done on the basic of categorization of the banking sector on the basis of ownership structure.

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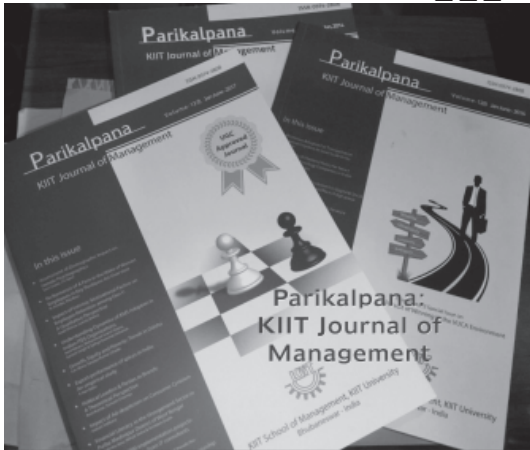
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