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Dr. Kavita Bhatnagar
Associate Professor,
Economics Department,
GDHG PG College,
Moradabad, Uttar Pradesh,
India

Correspondence
Dr. Kavita Bhatnagar
Associate Professor,
Economics Department,
GDHG PG College,
Moradabad, Uttar Pradesh,
India

High level of NPAs in PSBs

Dr. Kavita Bhatnagar

Abstract

The stressed asset that includes the GNPAs and Restructured Advances is a major problem for Banking Industry. The PSBs are the worst hit by growing NPAs in the industry. A comparative study of all the groups of banks reveals that PSBs are the most inefficient sector in the banking industry in dealing with stressed assets. The government has taken many steps to mitigate the NPAs problem by infusion of capital in the PSBs, introducing 'Indradhanush Yozna' for better management, prompt corrective actions to safeguard the interest of the depositors, and enactment of 'The Insolvency and Bankruptcy Code, 2016' for speedy recovery and selling of assets.

Keywords: Indradhanush Yozna, GNPAs, Banking Industry

Introduction

Stressed Assets i.e. Gross Non-Performing Loans (GNPA) plus restructured standard advances in the banking system remained high during the last few years. Though the whole banking industry is suffering from the problem of Non-Performing Assets, the Public Sector Banks (PSBs) are the worst hit by growing NPAs in the industry. The gross NPAs in the PSBs have multiplied from 2.78 lac as of March 2015 crores to 6.84 lac crore as of March 2017 and there is not a single PSB in the list of top five banks with the lowest NPA. It has been revealed that reducing the NPA has a positive impact on the economy of a country on a medium to long term basis. The government and the Reserve Bank of India have taken many certain steps to overcome the problem of NPAs. The enactment of the Insolvency and Bankruptcy Code-2016 and a few amendments to the Banking Regulation Act, 1949 for providing leverage for the IBC mechanism are some of the steps taken by the Government for managing the NPA problem.

As per RBI norms, those advances which fail to generate income for a continuous period of 90 days are classified as NPA. It means advances, where interest and installments of principal or both remain unpaid for a continuous period of 90 days or more, are NPA. Banks are required to identify incipient sickness in the account by creating a Special Mentioning Account Category that is also divided into three sub-categories: i) SMA-0: Principal or interest payment not overdue for more than 30 days but account showing signs of incipient sickness, ii) SMA-1: Principal or interest payment overdue between 31-60 days, and iii) SMA-2: Principal or interest payment overdue between 61-90 days.

The equity capital of a PSB is primarily a means of protection against the losses of a banking business. A high level of capital and so high Capital Adequacy ratio is an absorber of unanticipated losses and it also inspires confidence in its creditor mainly depositors of the bank. Though the depositors are insured up to a certain level, they are not fully insured. The goal of the Basel III norms is to raise the quality, consistency, and transparency of the capital base of the banks to stand erect against these unanticipated losses. The Government considers the minimum capital adequacy ratio as a floor and wants to keep a sufficient buffer for the PSBs. The deterioration in asset quality and the implementation of Basel III requires a higher buffer and so the government has to infuse capital in PSBs through the issuance of recapitalization bonds and budgetary support. The government had so far infused capital of Rs 51,858 crore in Public Sector Banks (PSBs) under its 'Indradhanush Plan' since 2015-16. The government allocated a sum of Rs. 22,915 in 13 PSBs during the FY 2016-17 under the first tranche of capital infusion out of which a sum of Rs. 16,414 (75%) was infused upfront and the remaining amount was to be infused based on the performance of the respective banks.

Not only PSBs but even private banks have been suffered from a high share of NPAs. The gross non-performing assets (GNPA) of all scheduled commercial banks (SCBs) have surged to Rs. 6119 billion in March 2016 and Rs. 7918 billion in March 2017. Further, asset quality and profitability have been deteriorating over time. the stressed advances of banks as a share of total advances of all banks increased from 3.5 percent to 12.1 percent between March 2008 and March 2017, Private banks' better position in NPA management is apparent and now they are at the front seat in the process of credit expansion in the economy. The private sector banks had a 20% share in outstanding credit of all commercial banks which now extends to 29% of the outstanding credit of all commercial banks. The share in incremental credit is more heightened with 75% of incremental credit being disbursed by the PSBs during the last year.

Table 1: Trends in Non-performing Assets – Bank Group-wise (Amount in Rs. Billions)

Items	PSBs	PVBs*	FBs**	All SCBs
Gross NPA as of 2015-16	5400	562	158	6119
Gross NPA as of 2016-17	6847	932	136	7918
% age of Gross Advances as of 2015-16	9.3	2.8	4.2	7.5
% age of Gross Advances as of 2016-17	11.7	4.1	4.0	9,3
Net NPA as of 2015-16	3204	267	28	3498
Net NPA as of 2017-17	3831	478	21	4331
% age of Net Advances as of 2015-16	5.7	1.4	0.8	4.4
% age of Net Advances as of 2016-17	6.9	2.2	0.6	5.3

Source: RBI Annual Report, 2017
*PVBs- Private Sector Banks
**FBs- Foreign Sector Banks

It is evident that the share of large borrowers in the advances of SCBs is 56% but their share in outstanding NPAs is more than 86%. The large borrowers are those borrowers whose credit limit is 5 crore or more. The top 100 large advances account for about 15.2% of the total outstanding advances but their share in non-Performing accounts is 25% of GNPAs of SCBs. The Maximum amount as well as number of NPA has happened in the accounts having outstanding between Rs 20 crores to Rs 50 crores followed by those in the range of Rs 50 crores to Rs 100 crores. The top 100 large exposures (outstanding advances) account for nearly 15.2 percent of gross advances but their share in the top 100 non-performing accounts is 25.6 percent of GNPAs of SCBs.

The PSBs continued to record net losses during 2016-17 although they moderated in relation to a year ago. The State Bank Group also incurred losses in contrast to net profits a year ago whereas nationalized banks reduced their losses year on year.

Private Sector Banks posted a subdued increase in profits, resulting in a decline in return on assets (RoA). Concurrently, their return on equity (RoE) also declined. In contrast, Foreign Banks improved their RoA and RoE over the previous year. A high level of NPAs has also an adverse effect on the health of the PSBs, reflected in their declining Return on Assets (ROA) and Return on Equity (ROE) ratios, which turned negative in 2016 for the first time in a decade. Commercial Banks are negatively affected by a decline in bank credit, low bank profitability, and declining capital adequacy ratio.

Table 2: Return on Assets and Return on Equity of all Scheduled Commercial Banks (SCBs) (Group-wise) % age

Bank Group	Return of Assets		Return on Equity	
	2015-16	2016-17	2015-16	2016-17
Public Sector Banks	-0.07	-0.10	-3.47	-2.05
Private Sector Banks	1.50	1.30	13.81	11.87
Foreign Banks	1.45	1.62	8.0	9.11
All SCBs	0.40	0.35	3.58	4.16

Sources: Reserve Bank of India

A deterioration in the asset quality of Scheduled Commercial Banks adversely impacts their lending capacity with downside risks to overall macroeconomic conditions. ROA and ROE of Private Sector Banks and Foreign Banks have also deteriorated but their position is not alarming.

The Recovery of banks' NPAs is not satisfactory, having declined to 20.8 percent by end-March 2017 from 61.8 percent in 2009. During 2016- 17, Debt Recovery Tribunals (DRTs) made the highest amount of recovery, followed by the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act and Lok Adalats. The significant improvement in the case of DRTs was due to the opening of new tribunals, strengthening existing infrastructure, and computerized processing of court cases.

Indradhanaush Yozna: The government has planned a massive capital infusion of Rs. 2.11 lac crore in the next two years for recapitalization for the PSBs. Undoubtedly the PSBs play a vital role in India's economy but in the last few years, the capacity of PSBs of financing the infrastructure had been severely affected predominantly due to the increase of NPA assets resulting in delayed approval and disbursement. The government has launched its ambitious 'Indradhanush Yojana' to overcome the above deficiencies of PSBs-

1. First, the government has decided to separate the post of Chairman and Managing Director and prescribed that in subsequent vacancies, the CEO of the PSB will get the designation of MD & CEO. The executive chairman of the bank will be appointed separately.
2. The Government has created an appointment body Banks Board Bureau (BBB) for the topmost appointment of the Bank administration. The BBB will consist of eminent professionals and officials. The BBB will be responsible for the appointment of Chairman, Executive chairman, whole-time Directors.
3. The growing NPA and its provision have turned many PSBs inadequately capitalized. Some of the PSBs are not able to fulfill the capital adequacy norms of Basel III, whereas for further financing the banks should keep a safe buffer over and above the minimum norms of Basel III and so the government decided to infuse capital by way of budgetary allocation for the next few years. The estimate for extra capital infusion is Rs. 1.80 lac crore, keeping in view the average credit growth of 12% to 15% of each bank, depending upon its size and ability to grow.
4. The government has decided to release any political and administrative pressure on the management of the PSBs, named empowerment, and clarified that there should be no interference in the day-to-day administration and credit decision of the PSB and they have to make the decision on the basis of their

commercial interest and viability.
5. Accountability norms are fixed. The government has announced a new framework of Key Performance Indicators (KPIs) for PSBs management. Strict guidelines were issued for filing and monitoring fraud cases and instructions were given to report these matters on a day-to-day basis.
6. The process of good governance started with 'Gyan Sangam' a joint conclave of PSBs officials and financial institutions in 2015 at Pune. The Prime Minister, the Finance Minister, and the senior officer of RBI have also attended this conclave. The major stress was given to strengthening the risk management practices and each bank has to nominate a senior officer as Chief Risk Officer of the Bank. The main thrust was given to improving HR management practices.
7. It was observed that during the past decade, PSBs have financed many infrastructures and core sector projects. These projects with a large gestation period have also been delayed due to mismanagement and other issues and thus lead burden of NPA on Banks. The problem causing stress in these projects was examined and discussions were held with all the stakeholders to remove the barriers. The central bank has issued guidelines to PSBs for granting flexibility in the restructuring of these loans based on viability and feasibility.

The Insolvency and Bankruptcy Code, 2016: Earlier, India had multiple laws that governed various mechanisms of corporate rescue and/or insolvency process. Before the enactment of the Act, the time is taken for resolving the insolvency issue was quite long. There were many pending litigations for recovery of dues primarily because of overlapping jurisdictions of various laws governing insolvency resolution. The Contract Act -1872, the Companies Act-1956, the Recovery of Debts Due to Banks and Financial Institution Act (DRT)-1993, the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act (SARFESI)-2002 and some other Acts for the speedy recovery of non-performing assets have not yielded the required result. The Presidency Town Insolvency Act-1909 and the Provincial Insolvency Act-1920 have already completed hundred years of their enactment and were not effective. So, A new Insolvency and Bankruptcy Code, 2016 is enacted to provide a single window, time-bound process for resolution of an asset with an explicit emphasis on promotion of entrepreneurship, maximization of value of assets, and balancing the interests of all stakeholders. The IBC repealed two legislation--the Presidency Towns Insolvency Act, 1909, and the Provincial Insolvency Act, 1920--and amended 11 others.

Prompt Corrective Action: Prompt Corrective Action is intended to intervene as early as possible in the lending process of a bank and to take corrective measures in a timely manner to restore the financial health of the bank. Reserve Bank's Prompt Corrective Action framework was originally introduced in 2002 and later reviewed and revised. This revised PCA framework was issued by the Reserve Bank on 13th April 2017. The revised PCA restricted and required to the bank-

a. Distribute dividend/ remittance of profit
b. Bring more capital by promoter/owner
c. Restrict branch expansion
d. Required higher provisional norms
e. Restrict management compensation.

Consolidation of Banks: Narsimham Committee had suggested the merger of banks to create some world-level banks. This agenda is pending for a long but now six SBI associate Banks and Bhartiya Mahila Bank have been merged with SBI. The RBI Governor has said the Indian Banking System could be better off if some Public Sector Banks (PSBs) are consolidated to have fewer but healthier entities, as it would help in dealing with the problem of stressed assets. The merger of more Public Sector Banks is on cards and expected to be finalized very soon. Merging and consolidating the banks is a win-win situation for banks concerned and the government. After the merger, the Banks can manage their liquidity – short term as well as long term – position comfortably and A better and optimum size of the bank would help PSBs offer more and more products and services and help in integrated growth of the sector.

Though there are still many challenges before the Public Sector Banks in terms of their strength and liquidity and the Private Sector Banks and Foreign Banks are competitors, but the PSBs have a lot of faith in the common man. These banks are the places where people trust their hard-earned money with. A good and efficient banking system is the key to relieving the stress from everyone's life.

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