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   REVIEW OF LITERATURE

   NEED/IMPORTANCE OF THE STUDY

   STATEMENT OF THE PROBLEM

   OBJECTIVES

   HYPOTHESES

   RESEARCH METHODOLOGY

   RESULTS & DISCUSSION

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- Bowersox, Donald J., Closs, David J., (1996), "Logistical Management." Tata McGraw, Hill, New Delhi.
- Hunker, H.L. and A.J. Wright (1963), "Factors of Industrial Location in Ohio" Ohio State University, Nigeria.

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- Sharma T., Kwatra, G. (2008) Effectiveness of Social Advertising: A Study of Selected Campaigns, Corporate Social Responsibility, Edited by David Crowther & Nicholas Capaldi, Ashgate Research Companion to Corporate Social Responsibility, Chapter 15, pp 287-303.

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ONLINE RESOURCES

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- Garg, Bhavet (2011): Towards a New Natural Gas Policy, Political Weekly, Viewed on January 01, 2012 http://epw.in/user/viewabstract.jsp

A STUDY ON MANAGEMENT OF NPAS AND IMPACT OF SECURITIZATION ACT, 2002 ON REDUCTION OF NPAS IN BANKS

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ABSTRACT

Banking sector plays an indispensible role in economic development of a country through mobilization of savings and deployment of funds to the productive sectors. During the past decade, a burning issue in the financial arena of the Indian economy has been the accumulation of Non-Performing assets (NPAs) in the banking sector. The profits of the bank came under pressure due to rise in Non-Performing assets. The Securitization Act is a fine, comprehensive piece of legislation which has been a panacea to the entire problem of NPAs. The Legal framework for Securitization in India was enforced with the enactment of "The Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Ordinance 2002(SRFAESI Act). Its purpose is to promote the setting up of asset reconstruction/Securitization companies to take over NPAs accumulated with banks and public financial institutions. This paper makes an attempt to find out the opinion of bankers on the impact of Securitization Act in reduction of NPAs in Public Sector banks.

KEYWORDS

NPA, Securitization Bank, Standard Asset, Gross NPA and Net NPA.

INTRODUCTION

Banking sector plays an indispensable role in economic development of a country through mobilization of savings and deployment of funds to the productive sectors. Bank lending is very crucial for it makes it possible, the financing of agricultural, industrial and commercial activities of the country. It is an established fact that a fragile banking system can, not only hamper the development of a particular economy but also it can deepen the real economic crisis and impose heavy social costs. So the health of the banking system should be one of the primary concerns of the government of each country.

Currently the Indian banking sector is not in a good health. The symptoms of the disease are vastly apparent viz. rising NPAs, high labor costs, competition from mutual funds, bureaucratic hurdle and redtapism. Most of these symptoms have been present in the Indian banking system since independence but it is the post reform era that they have become more ostensible.

The problem of NPA became apparent following the introduction of internationally accepted prudential accounting norms. Prudential norms were adopted with regard to income recognition, asset classification and provisioning norms put severe pressure on the profitability of PSBs.

Banks have so far been able to meet their requirements of additional capital by infusion of funds by the government or by accessing the markets. However, a stage has been reached where further efforts at restructuring some of these banks cannot be confined merely to infusion of capital and giving certain targets for improvement in performance. But major restructuring has to be done to improve the asset quality of the banks. Moreover, Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 was passed by parliament, which is an important step towards elimination or reduction of NPAs.

CONCEPT OF NPA

According to RBI guidelines with effect from 31st March 2004, a Non performing asset has been classified according to the market segments, which shall be a loan or an advance, where:

1. Interest and/or an installment of principal remain overdue for a period of more than 90 days in respect of a Term loan.
2. The account remains "out of order" for a period of more than 90 days, in respect of overdraft/cash credit.
3. The bill remains "out of order" for a period of more than 90 days in the case of bills purchased and discounted.
4. Interest and/or installment of principal remains overdue for two harvest seasons but for a period not exceeding two and half years in the case of advance overdue for a period of more than 90 days in respect of other accounts.

GROSS NPA AND NET NPA

Gross NPAs are the total outstanding of all the borrowers which are classified as non-performing assets (viz., sub-standard, doubtful and loss asset). Net NPAs are the Gross NPA minus gross accounts.

WHAT IS SECURITIZATION?

Securitization is a process whereby the 'originator' of the various financial assets including loans which are illiquid can transfer such assets to special purpose vehicles which issues the tradable securities against these loans and these are issued to the investors. It is an acquisition of financial asset by any securitization company from 'qualified institutional buyer' or by issue of security receipts representing undivided interests in such financial assets or otherwise.

Thus there will have to be some sort of understanding between the QIBs and the securitization company which can be 'originator' in the case of the banks and the Financial Institutions which has extended the financial assistance to the 'obligator' who is supposed to repay the financial assistance in installments on some future dates as per the agreement entered into by it with the bank. This can be referred to as the 'security interest' is created in favor of the secured creditors including the creation of the mortgage by the deposit of the title deeds with the secured creditors.

SECURITIZATION ACT, 2002

The need for the setting up an asset reconstruction company for acquiring distressed assets from banks and Financial institution with a view to develop market for such assets was being felt, since long, Narasimhan Committee 1&2 and the Verma Committee on restructuring of weak Banks has strongly recommended the setting up of Asset Reconstruction Companies(ARCs).

The business of Securitization and Reconstruction is primarily meant for more than one purpose:

- To regulate the business of securitization and reconstruction of the financial interest.
- To regulate enforcement of the security interest and for the matters connected therewith or the matters incidental thereto

The debt securitization is a new concept in the Indian financial markets and is primarily meant for enhancing the liquidity of the banks an had Financial Institutions which have extended financial assistance to the borrowers for various purposes.

The debt securitization makes available with these institutions the security papers against the financial assets which have been created out of the financial assistance sanctioned and disbursed by these institutions and in the case of a default by the borrowers the secured creditors can have a recourse to either the securitization of the financial asset or the reconstruction of the same.

LITERATURE REVIEW

Rao, Suryachandra and Krishna mohan (2007) in their article "Management of NPAs in Scheduled Commercial Banks" states that the phenomenon of NPAs in financial institutions came during 1990's study, identified specific reasons for NPAs in priority and non-priority sectors and explained the strategies adopted by banks.

Pillai, Manoj (2007) in his article "ARCIL and management of NPAs of Indian Banks" states that presence of NPAs had an adverse impact on the productivity of Indian banks and it resulted in erosion of profits. The research during last 4 years found that aggregate advances increased by 104% but NPAs has reduced over the year. This credit goes to establishment of ARCIL.

Mehalwant, Seema and Singh, Sumanjeet (2010) in their article "Problem of NPA in Indian Public Sector Banks" states that the problem of NPA is not only limited to developing or poor nations, but also in developed nations. Public Sector Banks are worst affected. Ineffective Project appraisal, political favor managing and incorrect projection of future demand in the industrial sector, coupled with the recession in the last few years, resulted in default of loan accounts, resulting NPA.

Sensarma, Rudra and Jayadev (2011) in their article "Are banks stock sensitive to risk management?" states that the risk management capabilities of banks have been improving overtime except for its last two years. The return through stocks is sensitive to risk management capabilities of banks. To tackle the issue various steps have been taken by RBI/Government of India on the lines of the recommendations of two reports of Narasimhan Committee on arresting and containing the growth of NPAs. The process initiated so far was provided with a further fillip with the introduction of the SARFAESI Act 2002 – a law permitting securitization and reconstruction of financial assets and providing for speedy enforcement of security interests. This new law has strengthened creditor's rights through foreclosure and enforcement of securities by banks and financial institutions.

The Reserve Bank of India has also conducted a study to ascertain the contributing factors for the high level of NPAs in the banks covering 800 top NPA accounts in 33 banks (RBI Bulletin). The study has found that the proportion of problem loans in case of Indian banking sector are very high. Loans of these banks formed 17.91 percent of their gross advances. This proportion did not include the amounts locked up in sick industrial units. Hence, the proportion of problem loans indeed was higher. The study revealed that the major factors contributing to loans becoming NPAs include diversion of funds for expansion, diversification, modernization, undertaking new projects and for helping associate concerns. This is coupled with recessionary trend and failure to tap funds in the capital and debt markets, business failure (product, marketing, etc.), inefficient management, strained labor relations, inappropriate technology/technical problems, product obsolescence, recession input/power shortage, price escalation, accidents, natural calamities, Government policies like changes in excise duties, pollution control orders, etc. The RBI report concluded that reduction of NPAs in banking sector should be treated as a national priority issue to make the Indian banking system stronger, resilient and geared to meet the challenges of globalization.

Vallabh, Bhatia & Mishra (2007) in their study explores an empirical approach to the analysis of Non-Performing Assets (NPAs) of public, private, and foreign sector banks in India. The NPAs are considered as an important parameter to judge the performance and financial health of banks. The level of NPAs is one of the drivers of financial stability and growth of the banking sector. This study aims to find the fundamental factors which impact NPAs of banks. A model consisting of two types of factors, viz., macroeconomic factors and bank-specific parameters, is developed and the behavior of NPAs of the three categories of banks is observed. This model tries to extend the methodology of widely-known Altman model. The empirical analysis assesses how macroeconomic factors and bank-specific parameters affect NPAs of a particular category of banks. The macroeconomic factors of the model included are GDP growth rate and excise duty, and the bank-specific parameters are Credit Deposit Ratio (CDR), loan exposure to priority sector, Capital Adequacy Ratio (CAR), and liquidity risk. The results show that movement in NPAs over the years can be explained well by the factors considered in the model for the public and private sector banks. The co-linearity between independent variables was measured by Durbin-Watson test and VIF characteristic and it was found to be a little for public and private banks. The factors included in the model explain 97.1% (adjusted R-square value of regression results) of variations in NPAs of public banks and 76.9% of the same of private banks. The other important results derived from the analysis include the finding that banks' exposure to priority sector lending reduces NPAs.

M. Karunakar et.al (2008), study the important aspect of norms and guidelines for making the whole sector vibrant and competitive. The problem of losses and lower profitability of NPA and liability mismatch in Banks and financial sector depend on how various risks are managed in their business. Besides capital to risk weightage assets ratio of public sector banks, management of credit risk and measures to control menace of NPAs are also discussed. The lasting solution to the problem of NPAs can be achieved only with proper credit assessment and risk management mechanism. It is better to avoid NPAs at the market stage of credit consolidated by putting in place of rigorous and appropriate credit appraisal mechanisms.

STATEMENT OF THE PROBLEM

During the past decade, a burning issue in the financial arena of the Indian economy has been the accumulation of Non-Performing assets (NPAs) in the banking sector. The presence of NPAs has affected the profitability, liquidity and competitive functioning of banks and finally the psychology of the bankers in respect of their disposition towards credit delivery runs and bank failures that lead to writing off of non-performing loans, restructuring, mergers and acquisitions and even closure of weaker banks. To tackle this issue various steps have been taken by RBI/Government of India on the lines of the recommendations of two reports of Narasimhan Committee on arresting and containing the growth of NPAs. The process initiated so far was provided with further introduction of the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act 2002(SARFAESI) – a law permitting securitization and reconstruction of financial assets and providing for speedy enforcement of security interests. This new law has strengthened creditor's rights through foreclosure and enforcement of securities by banks and financial institutions. Hence the present study is an attempt to study the opinion of the banks towards this act and its impact on reduction of Non-Performing Assets in banks.

OBJECTIVES OF THE STUDY

1. To study the reasons for NPAs and the recovery mechanism adopted by banks.
2. To gain insight into the various provisions of the act with special emphasis on reduction of NPAs in banks.
3. To assess the effectiveness of the act in reduction of NPAs.

RESEARCH METHODOLOGY

The study mainly depends on primary data collected from 25 different branches of Nationalized banks situated in and around Bangalore. Questionnaire based survey method was used to collect data from select bank branches. The Sample bank branches were selected using the Non-Profitability convenience sampling. To analyze the data and to interpret the data analysis simple percentage, ranking and rating method are used. The study period span from July-2013 to Dec-2013. This study is subject to the views expressed by the concerned officials of banks.

OPERATIONAL DEFINITIONS

NPA: An asset is classified as Non-Performing Asset (NPA's) if dues in the form of principal and interest are not paid by borrower for a period of 90 days.
Standard Assets: Such an asset is not a Non-Performing Asset. In other words, it carries not more than normal risk attached to the business.
Sub-Standard Asset: It is classified as Non-performing Asset for a period not exceeding 18 months.
Doubtful Asset: Asset that has remained Non-Performing Asset exceeding 18 months is a doubtful asset.

ANALYSIS AND INTERPRETATION

TABLE 1: REASONS FOR NPAS IN THE BANKS

Reasons	No of Respondents	Percentage (%)
Improper credit appraisal	13	52
Lack of effective follow-up	09	36
Diversion of funds	15	60
Absence of security	03	12
Management failures	05	20
Decrepit legal system	10	40
Cost in-effective legal measures	09	36
Difficulty in execution of decrees	09	36
Willful Default	12	48
Demand recession	03	12
Others	00	00

Source: Primary data

Interpretation
From the above table it is clear that the main reason for NPAs in banks is diversion of funds, improper credit appraisal and willful default by decrepit legal system, cost ineffective legal measures, lack of effective follow up and difficulty in execution of decrees are some of the important reasons.

TABLE 2: MEASURES FOR RECOVERY OF NPAS ADOPTED BY THE BANKS

Preference	No of respondents	Percentage(%)
Legal Measures	04	16
Non-Legal Measures	02	08
Both Legal and Non-Legal	19	76
Others	00	00

Source: Primary data

Interpretation
From the above table it can be interpreted that 76% of the respondents said that they have taken both Legal & Non-Legal measures for recovery of NPAs while 16% said that they have taken only legal measures and 8% said that they have taken only non-legal measures.

TABLE 3: THE RECOVERY MECHANISMS ADOPTED BY THE BANKS FOR NPAS--PRE-SECURITIZATION ACT

Recovery Mechanisms	No of respondents	Percentage (%)
Lok Adalats	05	20
Civil Courts	13	52
Debt Recovery Tribunal	13	52
One-Time Settlement Schemes	14	56
Others	00	00

Source: Primary data

Interpretation
From the above table it is evident that 56% of the respondents said that they adopted one-time settlement scheme for recovery of NPAs, while 52% of the respondents said both civil courts and Debt recovery tribunals as recovery mechanism and 20% said that they adopted Lok Adalats pre-securitization act.

TABLE 4: THE RECOVERY MECHANISM ADOPTED BY THE BANKS FOR NPAS--POST SECURITIZATION ACT

Recovery Mechanisms	No of respondents	Percentage(%)
Lok Adalats	03	12
Civil Courts	08	32
Corporate Debt Restructuring	04	16
Debt recovery tribunal	13	52
One-time settlement schemes	15	60
ARCs/Securitization Companies	10	40
Others	00	00

Source: Primary data

Interpretation
From the above table it is evident that 60% of the respondents said that they adopted one time settlement schemes as a recovery mechanism for NPAs, 52% said Debt recovery tribunals, 40% said Asset Reconstruction Companies, 32% said Civil Courts, 16% said corporate debt reconstruction and 12% said Lok Adalats after post-securitization act.

TABLE 5: EFFECTIVE MEASURES OF RECOVERY BY THE BANKS

Preference	No of respondents	Percentage(%)
One-time settlement schemes	15	60
Lok adalats	03	12
Debt Recovery Tribunal	03	12
Civil Courts	00	00
Corporate Debt Restructuring	01	04
ARCs/Securitization Companies	03	12
Others	00	00

Source: Primary data

Interpretation

From the above it is evident that 60% of the respondents said that one time settlement scheme is not most effective recovery mechanism, while 12% said Lok Adalats, 12% said Asset reconstruction companies, 12% said debt recovery tribunals and 4% said corporate debt restructuring.

TABLE 6: WHETHER THE SECURITIZATION ACT HAS EMPOWERED THE BANKS WITH ADDITIONAL POWERS OR NOT

Preference	No of respondents	Percentage (%)
Yes	25	100
No	00	00

Source: Primary data

Interpretation

From the above table it is clear that 100% of the respondents said that the securitization act has empowered the banks with additional powers by facilitating the setting up of asset reconstruction companies.

TABLE 7: WHETHER THE ACT REDUCED THE LEVEL OF NPAS IN THE BANK

Preference	No of respondents	Percentage (%)
Yes	22	88
No	00	00
Can't say	03	12

Source: Primary data

Interpretation

From the above table it is evident that 88% of the respondents said that the enactment of the Securitization Act has reduced the level of NPAs in the banks, while 12% said that they can't say whether the Act has helped in reduction of NPAs in the banks or not.

TABLE 8: RATE OF IMPACT OF THE ACT IN REDUCTION OF NPAS ON A SCALE OF 1 TO 10

Rating	No of Respondents	Percentage(%)
Below 5	03	12
5 & Above 5	22	88

Source: Primary data

Interpretation

From the graph it is evident that 88% of the respondents rated the impact of Securitization act in reduction of NPAs as 5 and above 5, and 12% rated below 5. From this it can be interpreted that the act has been successful in reduction of NPAs in the banking sector.

ISSUES OF CONCERN OF THE BANK IN THE IMPLEMENTATION OF THE SECURITIZATION ACT FOR RECOVERY OF NPAs

The issues of concern expressed were as follows:

1. Disposal of securities is difficult without court intervention.
2. Lack of market for such securitized assets.
3. Non-commencement of Asset reconstruction and Securitization companies.
4. Difficulty in seizing the said property with tenants and leaseholders occupying the property
5. Under the act, the bank has to issue a notice and wait for 60 days before proceeding to take possession of the quality of assets and rendering them less valuable
6. Stay from civil courts by the parties against the action initiated by the banks for seizure.
7. Cost of maintenance to the bank of the seized assets
8. Parties delaying the process by contending in court/DTRs
9. Inability to prevent alienation of the said property by the borrowers during the notice period
10. Threats from the borrowers to the bankers

SUMMARY OF FINDINGS

The following are the main findings from the study conducted:

1. It was evident after the analysis as that 100% of the respondents said that the securitization act has empowered the banks with additional powers by facilitating the setting up of Asset reconstruction companies/Securitization companies.
2. It was evident that the Act has helped in reduction of NPAs in the banks as 88% of the respondents said that the enactment of the Securitization Act has reduced the level of NPAs in the banks and they rated the impact of Securitization Act in reduction of NPAs as five and above 5.
3. It was found that the main reason for NPAs in banks is diversion of funds, improper credit appraisal and willful default followed by decrepit legal system, cost ineffective legal measures, lack of effective follows-up and difficulty in execution of decrees.
4. The measures to tackle the NPAs adopted by the bank includes the increasing use of the forum of Lok Adalats, Civil Courts, Debt recovery Tribunal, use of Corporate Debt Re-Structuring, one-time settlement schemes and asset reconstruction/securitization companies.
5. Before the enactment of the securitization act bankers had limited option for recovery which consisted of having an intensive follow-up and interaction with the borrower and initiating legal action either thought courts or Debt recovery tribunals.
6. The securitization Act empowers Bank/FIs to change or takeover the management/possession of secured assets of the defaulting borrowers & sells or lease out the assets without the intervention of the court.
7. Although the Securitization Act empowers banks/FIs to seize the secured assets of the defaulting borrowers without the intervention of the courts, borrowers are still able to get proceedings under the act stayed by appealing in civil court and DRTs.
8. Despite the many issues of concerns in the implementation of the act overall the act has been a boom for the banking community. Majority of the bankers opined that the act was helpful in the reduction of NPAs.
9. At the macro level, NPAs have chocked off the supply line of credit of the potential lenders thereby having a deleterious effect on capital formulation and arresting the economic activity in the country.
10. At the micro level, unsustainable level of NPAs has eroded current profits of banks. They have led to reduction in interest income and increase in provisions and have restricted the recycling of funds leading to various asset-liability mismatches. Besides this, it has led to erosion in their capital base and reduction in their competitiveness.
11. The mounting menace of NPAs has raised the cost of credit, made Indian businessman uncompetitive as compared to their counterparts in other countries. It has made Banks more averse to risks and squeezed genuine small and medium enterprises from accessing competitive credit and has throttled their enterprising spirits as well to a great extent.
12. While the banking industries in India is progressively complying with the international prudential norms and accounting practices, there are certain areas like recovery management in which it does not have a level playing field as compared to other participants in the international financial markets. Our

existing legal frame work relating to the commercial transactions has not kept pace with the changing times, this resulted in slow pace of recovery of defaulting lone & mounting levels of NPA's in banks.

CONCLUSIONS
While the banking industries in India is progressively complying with the international prudential norms and accounting practices, there are certain areas like recovery management in which it does not have a level playing field as compared to other participants in the international financial markets. Our existing legal frame work relating to the commercial transactions has not kept pace with the changing time, this resulted in slow pace of recovery of defaulting NPA's in banks.
It could be concluded that the SARFAESI Act, 2002 holds the promise of reformulating the contours of asset management and of rectifying the imbalance between borrowers and lenders in India, a direct consequence of which has been the colossal accumulation of NPAs. The loopholes and inequalities of in the act need to be ironed out through appropriate legislative measures. The basic structure of the act must not be tampered with, though a few changes like making appeals easier, framing rules and guidelines to prevent misuse of the powers under the Act, making a reasonable distinction between willful and other defaulters etc., can be considered. IT must be said that the Act, by empowering lenders to exercise their right of expeditious attachment and foreclosure for the enforcement of security, has made a beginning in the right direction.
Moreover, if the banks have to survive in the competitive and increasingly globalized market conditions they should be helped both bh the RBI and the government in the form of faster recovery climate, especially for the legal processes of enforcement of contracts. Till such time the banks may be helped by recognizing their provisions against standard assets, additional provisions over and above the prudential norms etc., as tier II capital.

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