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MANAGEMENT OF NPAS IN DCCBS IN INDIA – AN EMPIRICAL ASSESSMENT

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ABSTRACT

In the present paper, an attempt has been made to analyse the NPAs position and growth of District Central Cooperative Banks (DCCBs) in India. Gross NPAs of DCCBs in India stood at Rs.18,728 crores (20.50) per cent of total Gross Advances) and Net NPAs at Rs.6,653 crores as on March 31,2008(8.39 per cent of total Net Advances).These figures pose a severe threat to the profitability of these banks. The NPAs hit banks in several ways. Not only banks lose income on these assets, but they are bad for the economy.

KEYWORDS
Doubtful Assets, Loss Assets, Non-Performing Assets, Standard Assets, Sub-Standard Assets.

INTRODUCTION

In line with the international practices and as per the recommendation made by the Committee on financial system under the chairmanship Shri M. Narasimham. The RBI has introduced, in a phased manner, prudential norms for income recognition, Asset Classification and Provisioning for the advances portfolio of the Banks so as move toward greater consistency and transparency in the published account.

The introduction of prudential norms has ushered in a new era in the reform process of banking industry as a whole. The identification of the NPAs as per the prudential norms specified by the RBI is a pre-requisite for the proper management of the NPAs. As per the guidelines of the RBI, the State Co-operative Banks and the Central Co-operative Banks started implementing the prudential norms from the accounting year 1996-1997. One of the major reasons cited for the introduction of the norms has been the persistence of Non-performing Assets (NPAs) in banks.

Loans or advances given by banks become Non-Performing when the interest and /or instalment of principal remains overdue for more than 90 days. Advances which do not generate any income and which are doubtful affect the very vital function of banks viz. intermediation (mobilizing savings and providing finance for investment).

Loans and advances given by banks are classified as standard assets, sub-standard assets, doubtful assets and loss assets. Sub-standard assets, doubtful assets and loss assets together are called Non-Performing assets. Where assets are Non-performing a provision is required to be maintained.

A PROFILE OF DCCBs

There are at present 371 District Central Cooperative Banks serving 31 states in India, By end of the year 2007-08 the total deposits of the banks stood at Rs.1,02,986 crores. During the year, the total investments of the banks amounted to Rs.44,419 crores. The Gross NPAs to Gross Advances ratio also was considerably high from 17.85 per cent in 2001 to 20.50 per cent in 2008. NPAs affect the liquidity, profitability and equity of the banks hence, the present study elucidates the magnitude of NPAs and their relationship with other category of Assets such as standard assets, sub-standard assets doubtful assets and loss assets.

MEANING OF NPA

NPA is defined as an advance for which interest or repayment of principle or both remain outstanding for a period of more than one quarter. The level of NPA act as an indicator showing the bankers credit risks and efficiency of allocation of resource.

ASSET CLASSIFICATIONS

The RBI has issued guidelines to banks for classification of assets into four categories.

1. STANDARD ASSETS

These are loans which do not have any problem are less risk.

2. SUB-STANDARD ASSETS

These are assets which come under the category of NPA for a period of less than one year.

3. DOUBTFUL ASSETS

These are NPA exceeding one year.

4. LOSS ASSETS

These NPA which are identified as unreliable by internal inspector of bank or auditors or by RBI/NABARD.

REASON FOR NPAs

The major reasons for high NPAs are:

- The slow, inefficient and decrepit legal system.
- Diversion of funds and diversification of business.
- Demand recession.
- Depressed capital market.
- Changes in government policy.
- Environment and pollution control measures.
- Fear psychosis among banks for compromise settlements.
- Industrial sickness and labour problems.
- Improper and inadequate credit appraisal.
- Poor post loan supervision and follow up (Policing of assets by banks).
- Product /marketing /Business failure.
- Inefficient management.
- Inappropriate technology.
- Changes in Macro Economy /Resources.

- Time /Cost overrun of projects implementation.
- Inadequate supervision.
- Delay in sanction of loan.
- Wilful default.
- Siphoning of funds.
- Frauds.
- Misappropriation.
- Political compulsions and corruption etc.

The Indian legal system had been more geared to project borrowers and not lenders. The legal system in India which had been long-drawn and ineffective has definitely affected the recovery climate in banks.

STATEMENT OF THE PROBLEM

NPAs affect the profitability of banks on account of non-booking of interest income and provisioning requirements. In addition, the capital adequacy ratio is also affected. NPA levels affect rating by credit rating agencies, which in turn affect the cost of resources mobilised by the Banks. The Gross NPAs of DCCBs in India as on 31-03-2008 stood at Rs.18,728 cores respectively, which represents funds locked and not available for recycling. More over high level of NPAs for Urban and Rural Credit Cooperative Institution continue to be the major area of concern and thus, Cooperative sectors, as observed the Committee on Financial Sector Assessment (CFSA) 2009, remain 'one of the weak links in the Indian financial landscape'. Hence a complete examination into the reasons for higher NPAs would help suggest measures for managing NPAs, improving banking operation and ultimately for reducing NPAs at the DCCBs' level.

REVIEW OF LITERATURE

Literature available on the subject reveals that both empirical and non-empirical studies have already dealt with the problem of NPAs and their impact on the performance of banks from the angle of profitability, liquidity, equity and change in their approach to business. A brief review of these studies is presented here.

A stud by the Office of the Comptroller of Currency (OCC) of the United State in 1988 found that poor asset quality was a major factor responsible for the failure of 98 per cent of the banks. Hence, reduction in gross NPAs was desirable.[1]

Kwan, et al., (1994) also concluded that there is a negative relationship between efficiency and the problem of loans.[2]

Ross Gary (1996) in the study 'Risk Happen, focused on the risk and performance relationship in commercial banking. It is not evident that banks never approved a loan with the intent that the loans would become Non-Performing Assets and that an organisation might learn from its prior decisions as banks continue to accumulate non-performing loans in the normal course of business.[3]

Gupta and Debashish (1997) also concluded that NPAs affect the profitability of banks and lead to liquidity crunch.[4]

According to the comparative study of NPA by Satyanarayana (1998), the NPA in Venezuela, Mexico, Thailand, Brazil, Japan, Taiwan, Colombia, Chile, Korea, Argentina, Intonesia, Malaysia, Hongkong, U.S.A. and Singapore indicated that except in Latin America the NPA levels were in single digit (6 per cent to 7 per cent). India was viewed unfavourably in the international arena, as India has the highest proportion of NPAs (14.45 per cent) among the sixteen countries in 1994-1995.[5]

P.K. Bhattacharjee (1999) in his paper finds that the Indian banking system has an asset backed loan system supported by collaterals and guarantees. The gross NPAs in India are 17 per cent whereas in China it is 25 per cent to 45 per cent.[6]

S.G. Phadhis (1999) justified the Narasimham Committee's observation that asset quality was very poor in directed lending, since around 48 per cent of NPAs were in the priority sector advances group.[7]

Klingebiel and Daniela (2000) discussed the suitability model of asset reconstruction companies to solve the problem of NPAs. Only a few studies have highlighted the impact of NPAs on the performance of banks.[8]

P. Ganesan (2001) in his study with a bearing on NPAs and banks' dealt with administrative measures to improve the profitability of banks. In an empirical study on the determinants of profitability of the public sector banks in India, it has been observed that credit flow into the economy could not produce any positive impact over banks' profitability due to higher NPA when cost incurred on defaulted and other loan assets is high.[9]

H. Srinivasa Rao (2002) in his thesis suggested that the Andhra Pradesh State Co-operative Bank (APCOB) should initiate certain steps like monitoring the spending pattern of loans (indirectly), implementation of the NABARD guidelines, and designing and implementation of collection policies to solve the problems of NPAs, by issuing necessary guidelines to the DCCBs and PACS at the grass root level.[10]

Monica Soni, (2002) in her paper analyses the NPA position of two major components of Rural Banking viz. the Co-operative Banks and the Regional Rural Banks. The situation with regard to NPA management by different co-operative banks is not at all satisfactory. It shows that a large proportion of total NPAs is contributed by RRBs in the current viability category.[11]

A study done by Santi Gopal and Soma Dey (2003) showed that it is a paramount task for the banks to manage their NPAs more efficiently so that they can change their character from NPAs to performing assets. This study makes an attempt to analyse the loan amount-wise, age-wise, head-wise and sector-wise classification of NPAs and to identify the factors responsible for the growth of NPAs of the Khatra People's Co-operative Bank Ltd., UCB, in the district of Bankura in West Bengal.[12]

K. Rajendran (2004) in his article "Non-performing assets" concluded that increasing NPA exercises a major impact on the DCCBs. DCCBs shall have to educate their employees on NPA and its effect on the bank. Change in NPA norms and credit monitoring and recovery mechanism should be strengthened.[13]

K.C. Chakraborty (2005) in his article pointed out that the banks have to face several challenges in managing NPAs. Besides ensuring better scrutiny of the credit proposals before sanction, banks need to watch closely and monitor the assets from the beginning. In fact, NPA management begins right from the selection of borrowers.[14]

T. Vanniarajan (2006) focused his paper on the problem of NPAs and found that they were more in public sector banks as compared to other banks. NPAs have a direct impact on a bank's profitability, liquidity and equity.[15]

C. Lakshmanan and A. Dharmendran (2007) in their article said that the problem of Non–Performing Assets (NPAs) is less in the Chennai Central Co-operative Bank as compared to the other CCBs in Tamil Nadu. They also focused on the impact of NPAs on the Net Profit, Investment, Legal Expenses and Spread of the bank. The study concludes that the effective management of NPAs is essential to strengthen the financial position of the bank.[16]

N. Ramu (2008) in his article concluded that the NPAs of sample banks chosen for study in within manageable level, but the Thirumangalam Cooperative Urban Bank Ltd (TCUB) have to face severe recovery problems. As per CAMELS rating model the highest weight age (i.e.25 per cent)is given to asset quality component by RBI. The solution to the problem of NPAs lies in strengthening the credit management in banks. Over a period by removing the present deficiencies observed in the standards of credit appraisal, monitoring and improving the overall lending policies of the banks. The process of NPA management does not start after filing at suit, but starts from identification of a right borrower. [17]

Studies so far made on the subject have not come out with any tangible and practical solutions to contain/put up with the problem of NPAs and no lasting solution to arrest/manage the problem and there by strengthening the books of accounts of the banks, has come about. In the scenario, this is an attempt to bridge this gap in solutions and offer a simple, workable and viable remedy to the problem of management of NPAs at least for future.

OBJECTIVE

The objective of this paper is to assess the position and growth of NPAs in DCCBs in India.

METHODOLOGY

The data collected from secondary sources for the eight years from 2001 – 2008. The data published by Reserve Bank of India (RBI) and National Bank for Agricultural and Rural Development (NABARD) is suitably compiled and analysed for the purpose of study. The statistical results are obtained by using SPSS Version 10.

Compound growth rates were estimated for the classification of assets in DCCBs. An exponential function of the following type was employed to estimate the growth rates.

Y_t = abt

Where,

Y_t = Classification of assets

a = Intercept

b = Parameter

t = Years

Compound Growth Rate = (Anti log of b-1) x 100

LIMITATION OF THE STUDY

The present study covers a period of eight years for secondary data from 2000-01 to 2007 -08 for study purpose. Data were available up to 2007- 08 during the field work and accordingly data up to 2007-08 were alone used for analysis. This may not be fully relevant to the later period.

RESULT AND DISCUSSION

TABLE-1: TRENDS IN NPAs OF DCCBs DURING MARCH 2001-2008 (Rs IN CRORE IN PER CENT)

Sr.No	Asset type	2001	2002	2003	2004	2005	2006	2007	2008	CGR
1.	Standard Assets	43120 (82.15)	47431 (80.03)	49336 (78.07)	51008 (75.96)	58605 (80.14)	63493 (80.17)	72542 (81.47)	72646 (79.50)	9.82
2.	Sub-Standard Assets	4994 (9.51)	6325 (10.67)	7603 (12.03)	8428 (12.55)	6468 (8.85)	6905 (8.72)	6375 (7.16)	7858 (8.60)	5.80
3.	Doubtful Assets	3466 (6.60)	4245 (7.16)	5060 (8.00)	6068 (9.04)	6053 (8.28)	6699 (8.45)	7648 (8.59)	8210 (8.99)	11.40
4.	Loss Assets	911 (1.74)	1268 (2.14)	1199 (1.90)	1648 (2.45)	1999 (2.73)	2106 (2.66)	2471 (2.78)	2660 (2.91)	14.30
5.	Total Gross NPAs (Total of 2 to 4)	9371 (17.85)	11838 (19.97)	13862 (21.93)	16144 (24.04)	14520 (19.86)	15709 (19.83)	16495 (18.53)	18728 (20.50)	9.00
6.	Total Gross Advances(1 to 4)	52491 (100)	59269 (100)	63198 (100)	67152 (100)	73125 (100)	79202 (100)	89037 (100)	91374 (100)	7.20
7.	Total Provision for NPAs	N.A	N.A	6384	6900	11387	9440	12163	12075*	14.37
8.	Total Net NPAs (5-7)	_	_	7478 (13.16)	9244 (15.34)	3133 (5.07)	6269 (8.99)	4332 (5.64)	6653 (8.39)	-6.00
9.	Total Net Advances (6-7)	_	_	56814	60252	61,738	69762	76874	79299	7.47
10.	Gross NPA Coverage Ratio (7/5)(%)	_	_	46.05	42.74	78.42	60.09	73.74	64.48	_

*Provision,N.A- Not Available

(-)Figures in Bracts at Sr.No.1 to 5 are percentage to respective year's Gross Advances (Sr.No.6) and at Net NPAs (Sr.No.8) to Net Advances (Sr.No.9).

Basic Source: (i) Report on Trends and Progress of Banking in India, 2000 - 01 to 2007- 08.
(ii) NABARD.

Note: CGR – Compound Growth Rate.

Table 1 shows the trends in NPAs during the study period for all the 371 DCCBs in India. Gross NPAs of DCCBs (Table-1) stood at Rs.18,728 crores, as on March end 2008 consisting of Rs.7,858 crores in sub-standard category, Rs.8,210 crores in doubtful and the remaining Rs. 2,660 crores in loss category where the salvage value in negligible. In percentage terms, Gross NPAs amounted to 20.50 per cent of gross advances consisting of 8.60 per cent in sub-standard, 8.99 per cent and 2.91 per cent in doubtful and loss categories respectively. Though in absolute terms the gross NPAs went up from Rs.9,371 crores, as on March end 2001, to Rs.18,728 crores in 2008 growing @ 9 per cent for annum, there was increased in percentage terms 17.85 per cent to 20.50 per cent during the said eight years period due to obvious increase of the denominator at a rate faster than the numerator. As the provision against NPAs went up from Rs.6,384 crores to Rs.12,075 crores during 2003 to 2008 growing @ 14.37 per cent per annum the net NPAs come down from Rs.7,478 crores in 2003 to Rs.6,653 crores in 2008 growing @ -6 per cent per annum. The coverage ratio of provision to gross NPAs was 46.05 per cent in 2003 and went up to 64.48 per cent in 2008.

MANAGEMENT OF NPAs

The level of NPAs in the Indian Cooperative Banking Industry is a concern and thus urgent cleaning up of bank balance sheet has become a crucial issue. Although, a ratio of Gross NPAs to Gross Advances has been reduced to some extent but still it is very high in absolute terms. An effective and prudent management of NPAs consist of:

- To check creation of NPAs in the first place particularly of fresh loans.
- Improvement in the quality of NPAs i.e. to reduce slippage of a low grade NPA to next high level.
- Reduction of NPAs.

So NPAs would have to be reduced drastically and for the same purpose the following strategies for reducing NPAs are:

- Reducing the existing NPAs and curbing their further build up.
- Maintenance and regular updating of client profile. Credit rating of clients.
- Computerisation of loan accounts.
- Strong inters department management information system among loans, operations and recovery departments.
- To establish a system of early warning (EWS) for potentially weak loan accounts. Some key signals are nature of operations in the accounts, persistent default, overdraw, diversion of funds, lowering of rating etc.

- Observance of limitation period.
- Timely extension of period of limitation by-

- acknowledgement of debt
- receipt of partial payment
- renewal of documents.

- General strategies-

- effect recovery
- compromises to improve recovery status of account
- partial write off
- adjustment to collateral securities
- pressure on guarantors
- special recovery drive
- help from revenue authorities.

- Replacement of Loans/Rescheduling of demands.
- Rehabilitation of potentially viable units.
- Compromise with borrowers for final settlements.
- Calling up the advances and filing of civil suits.
- Increasing the number of Debt Recovery Tribunals(DRTs).
- Settlement of claims with DICGC/ECGC.
- Write of the outstanding.
- Do not consider projects with old technology for finance.
- Do not consider financing term loans for maturities longer than 5 years except in case of agriculture, infrastructure and SSI.
- Complete ban on generalized loan waivers.
- Provide financial help to from Asset Reconstruction Fund (ARF).
- Collect interest from clients on a monthly basis instead of quarterly collection.
- Compulsory annual review of borrower accounts with sufficient disclosure in balance sheet. For this purpose, change the review format to analyse both quantitative and qualitative data.
- Train the staff to closely monitor credit worthiness of borrowers and the end use of bank loans to avoid major post-defaults, so finance only for the productive projects.
- At the time of credit appraisal, observe and consider the list produced by RBI of defaulters and suit-filed cases thoroughly.
- Special officer/managing director should visit the branches periodically to monitor timely and preventive action should be taken by the branches.
- Separate credit-monitoring and audit cells should be installed in the banks.
- Eliminate political interference in disbursing loans.

Hence, the above said of strategies should be considered to arrest the trend of ever increasing level of NPAS.

FINDINGS AND SUGGESTIONS

1. NPAs include sub-standard assets, doubtful assets and loss assets. The growth rates of sub-standard assets, doubtful assets and loss assets were positive in all the DCCBs in India with 5.80 per cent,11.40 per cent, and 14.30 per cent per annum respectively. The positive growth rates of these assets would have led to falling profitability and erosion of the net worth of the banks. The banks have to minimise these assets considerably through effective recovery proceedings for earning profit.
2. The growth rates of Gross NPAs and Net NPAs in all DCCBs in India were 9 percent and -6 per cent per annum respectively. The problems of NPAs together (both in gross and net terms) were relatively high during the study period increase in provision for NPAs will lead to decrease in Net NPAs, and vice versa. NPA is not just a problem for banks, they are bad for the economy. The money locked up as NPA is not available for productive use and to that extent the banks seek to make provisions for NPA or write them off. It adversely affects their profit and results in a higher rate of interest to their diligent borrower customers. This also raises the cost of administration. The steps taken at the appropriate time may help in avoiding NPAs. Qualitative appraisal, supervision and follow up should be taken up for the present advances to avoid future NPAs.
3. Positive growth rates of standard assets were found in all the DCCBs with 9.82 per cent per annum. The task of containment of NPAs by arresting slippage of accounts from standard assets to NPAs was a cause of concern for almost all the banks due to the government policy of liberal credit to farmers and other weaker sections under priority sector loan. Relentless monitoring and introduction of loan review mechanism of standard assets may be of some help in containing the slippage to NPAs.
4. The positive growth rates in provision for NPAs in all the DCCBs with 14.37 per cent per annum result in the growing problem of the existence of NPAs. This suggests that the quality of assets must be improved through an effective credit delivery system and an effective recovery mechanism.

CONCLUSION

The DCCBs play a significant role in the economy of India. The overall performance of the DCCBs in India is, however, a mixed one. The heavy overdues, inefficient funds management, inadequate and untrained staff, lack of adequate supervision, poor profit earning, defective loan policies, book-adjustments and inadequate bad and doubtful debt reserves are some of their weaknesses. The accumulation of NPAs has been detrimental to the financial health of the banks. The banks have faced additional burden by creating more provision for management of NPAs. While the profitability of the banks is rather low, the liquidity position warrants strengthening. The depleting solvency is fatal to operational efficiency.

This picture reiterates the need for effective recovery management, particularly of short-term loans. Stringent measures must be taken to control and prevent NPAs; besides, effective credit monitoring and use of effective execution of decrees, and resort to various avenues of recovery, especially compromise settlements, would contain the problem of NPAs effectively.

If the study could help the planners and officials of the co-operative banks in removing the problem of NPAs. It is hoped that this endeavour will provide the basis for further research in other banks of India. The Author has the satisfaction of having undertaken a socially relevant study.

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