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A STUDY ON IN-DEPTH UNDERSTANDING OF THE NON-PERFORMING ASSETS IN INDIAN BANK SECTOR

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ABSTRACT

The extent of the bad debt crisis in India was not taken seriously. Following the recommendations of the Narasimham and Verma committees, various efforts have been made to address the problem of old nonperforming assets in bank balance sheets. The fact that there has rarely been any systematic study of the best strategy to address the problem continues to be raised from all sides. Non-performing assets (NPAs) in banks have become a major concern in India, with a very common occurrence of large-scale loan defaults/frauds contributing to the already massive levels of NPAs in banks (particularly public sector banks). The article identifies and examines the factors that impact non-performing assets (NPAs), as well as the causes and implications, and makes recommendations for effective solutions.

Keywords: Asset, Liability, Reforms, Public, Banking.

I. INTRODUCTION

Any financial system's foundation is the banking sector. The seamless operation of the banking sector guarantees the overall health of an economy. Loan banks build credit by taking deposits and lending money. The monies collected from borrowers in the form of interest and principal repayments are recycled to raise cash. However, the accumulation of non-performing assets (NPAs) undermines this credit flow. It stifles credit expansion and has an impact on bank profitability. NPAs are the key indicators used to assess the banking sector's performance. According to Reserve Bank of India (RBI) reports from November 2018, the gross amount of bad loans has surpassed Rs 9 lakh crores, demonstrating the severe impact it has on banks' lending practises and liquidity positions. This growth has quadrupled in the last five years, demonstrating banks' poor lending practises. The interest received on loans and advances, as well as the return of the principle, are the primary sources of income for banks. These assets are regarded as nonperforming assets if they do not produce income (NPA). NPA is defined by the Reserve Bank of India as a credit facility for which the interest and/or principal instalments are "past due" for a set period. The asset is designated as a nonperforming asset if the loan payments have not been made for a period of 90 days.

The proportion of net non-performing assets to net advances (NPAs) is a good indicator of a bank's credit quality. In general, a negative relationship between the dimension of efficiency and NPAs is expected because a lower of this proportion encourages higher efficiency levels for Indian banks, and despite what might be expected, an increase in NPAs consistently makes issue for the banks' successful tasks over time, and there is no quick fix for this. The RBI has taken a number of effective and timely actions to address the problems associated with nonperforming assets (NPAs). For example, the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, as well as the Asset Reconstruction Company foundation, were introduced to deal with the difficulties identified with NPAs quickly and efficiently by banks. Previous investigations have linked that bank in many economies have experienced collapse due to a higher presence of NPAs, and have thus defined the dissatisfaction of financial foundations through time. As a result, the board estimates for banks over time suggest that the dimension of financial efficiency diminishes as the proportion of non-performing resources for net advances drops. It has been discovered that there is a positive and measurably critical relationship between nonperforming assets and cost inefficiency and related components, i.e., the higher the proportion of nonperforming assets for net advances, the higher the dimension of inefficiency among Indian banks managing an account. As a result, banks must recoup bad assets as soon as possible, keep a constant eye on non-performing assets, and orient themselves toward better and sound risk management practises that assist account managers in successfully maintaining their financial records and having a low likelihood of NPAs over time. The money is kept with weak corporate governance and executive quality, which might lead to an increase in operating expenditures and no performance credits. As a result, banks must consider all board efforts to address the issue of non-performing resources. The findings of our investigation are comparable to those of previous studies, which found that the dimension of cost inefficiency was high due to the proximity of more non-performing resources, and the proportion of issue advances was higher, demonstrating the proximity of banks in various economies working outside of best practise outskirts.

II. CONCEPT OF NPA

Banks contain a variety of assets in their records, including cash on hand, balances with other banks, investments, loans and advances, fixed assets, and other assets. The idea of a non-performing asset (NPA) is limited to loans, advances, and investments. It is classified as a performing asset as long as it delivers the expected income and does not reveal any unique risk other than standard commercial risk, and it is treated as a non-performing asset when it fails to create the expected revenue. In other terms, a loan asset becomes a Non-Performing Asset (NPA) when it has not generated income for the bank for more than 90 days, i.e., interest, fees, commission, or any other dues. A non-performing advance (NPA) is one in which interest or principal repayment, or both, has gone unpaid for two quarters or more and has become 'past due.' When an amount owed under any of the credit facilities is unpaid for 30 days beyond the due date, it is considered past late.

Non-Performing Loans are another term for non-performing assets. A bank or financing business makes it when repayments or interest payments are not made on schedule. For a bank, a loan is an asset since the interest payments and principal repayment provide a stream of cash flows. A bank's earnings are generated by interest payments. When assets are not serviced for an extended period of time, banks consider them non-performing. A loan is defined as past due if payments are late for a short period of time, and it is labelled as non-performing if payments are late for an extended period of time (typically 90 days). When compared to similar lenders, a high percentage of nonperforming assets might indicate a concern.

CAUSES OF NPA'S

The following are some of the contributing causes to non-performing assets:

i. Bank Providing Activities: Banks can properly observe the rules and regulations when it comes to lending loans. It is necessary to make an accurate and efficient assessment of the borrowers' creditworthiness. The subprime mortgage crisis of 2008 was blamed on banks' faulty lending practises.

Table 1 Causes for Non-Performing Asset (NPA)

Borrower	Bank	Other
Too ambitious Project	Poor credit appraisal	Lack of infrastructure
Heavy borrowing	Non inspection of unit	Lack of Government support
Poor credit collection	Defective lending process	Government policies
Poor quality management	Lack of trained staff	Changes related to Banking amendments
Willful Default	System overloaded	Natural Calamities
Depend on Single customer	Lack of commitment to recovery	Recession and variation in economic conditions.
Fail to bring required Fund	Lack of technical support	
Lack of Proper Planning	Inefficient recovery system	

ii. Organizational Risk: The organisation encounters issues in its operating environment on a regular basis, resulting in financial loss.

iii. Environment-related risks: Natural disasters such as cyclones, droughts, earthquakes, and floods can leave farmers and agribusinesses without the produce they require.

iv. Borrower's Psychology: In certain cases, the borrower's mentality hinders him from returning the money, despite his ability to do so.

NPA-RELATED PROBLEMS

i. Profitability: Banks gain money from the loans and advances they give out to clients, and they lose money when these loans are not repaid because they can only make money when the loans/advances are repaid.

ii. Liquidity and Goodwill: As a result of lower profitability, banks are unable to freely disburse loans, affecting their liquidity and, as a result, their goodwill.

iii. Economy: The banking industry is critical to a country's economic development. It is the foundation of a nation's financial capital. As a result, if a bank's performance suffers due to a growth in non-performing assets, so does the country's economy.

THE REASONS FOR THE INCREASE IN NPAs

i. The Indian economy was lately growing, and banks, particularly public sector banks, began making large loans to enterprises.

ii. However, as a result of the financial crisis of 2008-09, company revenues collapsed, and mining ventures were forbidden by the government. The situation exacerbated as a result of severe delays in environmental licences, harming the infrastructure sector - power, iron, and steel – and resulting in raw material price fluctuations and a supply deficit.

Another factor is that banks have loosened lending requirements, particularly for large businesses, allowing them to avoid financial and credit checks.

III. IMPLICATIONS OF NPA

For The Economy: The development of strong and healthy financial institutions, particularly banks, is a prerequisite for the country's financial system's overall stability. The high level of nonperforming assets (NPAs) in banks and financial institutions has been a source of public concern, as bank credit is the driving force behind the country's economic growth, and any bottleneck in the smooth flow of credit, one of which is the rising NPAs, is bound to have negative consequences for the economy. When loans are not returned, a large portion of the funds leave the financial system, and the lending-repaying-borrowing cycle is disrupted. Banks must also reimburse their depositors and those who have borrowed money from them. If the borrowers do not pay, the banks will have to borrow more money to pay back their depositors and creditors. As a result, banks are hesitant to lend new cash to new or ongoing projects, strangling the system. The economy suffers greatly when lending to diverse areas of the economy declines. There is a slowdown in GDP growth and industrial output, as well as a drop in corporate profit margins, resulting in market depression.

For banking purposes: The most significant commercial effect of NPAs is that credit risk management takes precedence over other elements of bank operations. Instead of focused on developing business, the bank's whole machinery would be preoccupied with recovery operations. A bank with a high level of non-performing assets (NPAs) would be compelled to bear carrying costs on these assets. Other consequences include decreased interest income, increased provisioning (as banks are required to set aside a portion of their operating profit as provisions, as NPAs rise, banks must increase the amount set aside as provisions, reducing net profits), stress on profitability and capital adequacy, gradual decline in ability to meet steady increases in cost, increased pressure on Net Interest Margin (NIM), reducing competitiveness, and gradual decline in ability to meet steady increases in cost. NPAs create a vicious circle of effects on the financial system's viability and development, and if not managed appropriately, can lead to bank failure.

IV. NPAs IN THE CONTEXT OF INDIAN BANKING SYSTEM

In the Indian financial sector, non-performing assets (NPAs) came out of nowhere. Objective and practical business procedures were lacking in the Indian banking sector. Political sway, a lack of competition, and a complete absence of scientific decision-making all contributed to negative consequences. Inadequate accounting practises and impermeable balance sheets were utilised to conceal the flaws, failing to reveal the country's financial institutions' steady deterioration and institutional vulnerability to the public. "Reforms have taken the Indian banking system well ahead of the days of nationalisation," argues Ravi Agrawal. He claims that the NPA's underlying cause was found both inside and outside the banking sector. He says that banks were forced to cover vital industry and company losses in the end. Nonperforming assets (NPAs) increased in size suddenly, and banks were unable to investigate it. Our financial system's lack of preparedness and systemic fragility in responding to the changing circumstances precipitated the catastrophe. It has accumulated detailed information on nonperforming assets (NPA) across a variety of financial sectors, including commercial banks, financial institutions, urban cooperatives, and nonbank financial businesses (NBFCs), among others. Advances to the weaker sections of society below Rs. 25,000 constitute true social banking. NPAs make up about 8% to 10% of the total in this industry. As a consequence, NPA regulation will be automated, including a feature for actively engaged members. It is the responsibility of both business and industry to recognise NPA management transparency. NPA is a widespread national hazard that affects the whole Indian economy. Due to the closure of many lakhs of once-thriving manufacturing enterprises and poor utilisation of expensive industrial infrastructure, the government loses money in the form of taxation and excise. In the end, Ravi Agrawal says, it represents industrial uncertainty. Credit recipients' debts are represented by the NPA, which are subsequently shifted and parked with the ban. Preventive intervention should start with credit receivers and then move to bankers to be dependable. Instead of attempting to repair business and banks, we should offer assistance to both.

V. IMPACT OF NPA'S

1. Profitability: NPA refers to money booked as a bad asset as a result of a poor customer selection resulting in money being blocked. The bank's prodigality is reduced not only by the quantity of NPA, but also by the amount of profit invested in some return-generating project/asset. As a result, NPA affects not just present profits but also future profits, perhaps resulting in the loss of a long-term profitable opportunity. Another consequence of decreased profitability is a low ROI (Return on Investment), which has a negative influence on the bank's present earnings.

2. Liquidity: Money is being blocked, and lower profits result in a lack of cash on hand, forcing the firm to borrow money for a shorter length of time, incurring more costs. Due to a lack of funds, normal payments, and dues, another reason of NPA is difficulty in conducting the bank's activities.

3. Management involvement: Another indirect cost that the bank must incur as a result of NPA is the time and effort of management. Management's time and effort would have been better spent on more productive tasks that would have yielded better results. Banks now have particular workers to deal with and handle nonperforming assets, which comes at a cost to the bank.

4. Credit Loss: If a bank has a problem with nonperforming assets (NPAs), it will have a negative impact on its market credit value. It will lose its goodwill, brand image, and credit, all of which will have a detrimental influence on consumers who deposit money in banks.

VI. THE GOVERNMENT'S RECENT ACTIONS TO CONTROL NPAS IN THE BANKING SECTOR

Willful defaulters and those who are unable to repay the debt owing to economic downturn and other uncontrolled causes, such as loans sanctioned without due diligence by banks, are the two types of loan defaulters. The government has taken a number of steps to address both of these types of defaulters. Steel, textiles, electricity, and highways are just a few of the challenged industries that the government has made steps to restore. In the previous year's Union Budget, the government provided Rs. 25,000 crores for bank recapitalization. The recruitment procedure for senior management positions in public sector banks, such as chairmen and managing directors, has been made more transparent and professional. The government has granted banks complete liberty in making business choices, with no government intervention. To make the recovery procedure more efficient and faster, the SARFAESI Act and the DRT Act have been revised. Where it has been determined that the number of cases in which banks have taken action against guarantors for the recovery of defaulted loans is insufficient, the Government has advised banks to take action against guarantors in the event of borrowers' default under relevant sections of the SARFAESI Act, the Indian Contract Act, and the RDDB & FI Act. The Swachta Mission of banking balance sheets is expected to last for a while longer, which means banks will have to lose even more money in the coming quarters.

VII. CONCLUSION

The correct operation of a country's financial systems, which includes the banking sector, is critical to its economic prosperity. The Indian banking industry has traditionally been plagued by non-performing assets (NPAs). They have a detrimental impact on the banks' earnings. They have an impact not just on the bank's financial success, but also on the financial growth of the economy. Because the financial system is so important to our economic development, banks must focus on NPA management in order to increase profits. An increase in nonperforming assets (NPAs) indicates a large number of credit defaults, which has an impact on a bank's profitability, liquidity, and solvency. Nonperforming assets (NPAs) are an issue that largely affects public sector banks. When deposits become non-performing assets (NPAs) owing to late payments, the capital becomes unavailable, which has a direct impact on the bank's profitability because Indian banks rely largely on interest revenue on borrowed money. As a result, strict policies should be implemented to address this issue. In addition, the government should make additional arrangements to resolve pending cases more quickly. The effective implementation of Debt Recovery Tribunals, LokAdalats, and the SARFAESI Act might help banks manage their non-performing assets (NPAs).

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