

## Non-Performing Assets in India Banking Sector – A Trend Analysis

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**ABSTRACT:** In bank-based economy like India, sound health of banking system is crucial for sustained development and financial stability. In the post 2008 crisis period Indian banking system has suffered growing impairment of assets quality. Banks loan portfolio is the main source of income generator. The successful resolution of non-performing assets requires effective utilisation of NPA recovery channels. This paper tries to understand the trend in NPA and performance of NPA recovery channels and evaluates its performance along with a discussion on the challenges and limitations present in the resolution mechanism. The past performance study shows that efficacy of various NPA recovery channels is very low in India. Further tension in asset quality could emerge given the subdued growth prospects and global uncertainties due to Covid-19 pandemic. The amount of un-recovered loan is very high which also provides a banks and government an opportunity to strengthen the NPA recovery channels. This research article tries to explain about the performance of NPA recovery channels from past 17 years and provided with the proper suggestions suitable for the NPA recovery channels operating in India.

**KEY WORDS:** NPA, Recovery Channels, Lok Adalat, IBC, DRT, SARFAESI Act, RBI

### INTRODUCTION

Banks play crucial role in economic development of the country. A well-established banking system supported by proper regulatory mechanism is pivotal for study growth of the country. Banks are link between depositors and creditors. Banks give interest for depositors and collects interest from loans. The line breaks when borrower fails to repay principal and interest as per the agreed terms. To mitigate the repayment risk bank collects collaterals and surety for the loans. Holding the collaterals is not sufficient to discharge obligation towards the depositors. The security or collaterals has to be liquidated. For this purpose, well established recovery mechanism supported by recovery laws are very important.

“An asset, including a lease asset, becomes non-performing when it ceases to generate income for bank. A NPAs is defined as a credit facility in respect of which the interest or instalment of principal has ‘past due’ for a specified period of time” (RBI). If the interest or instalment of principal remains due for a period of more than 90 days, the asset is considered as NPAs. On the basis of duration of NPAs banks requires classifying the NPA into 3 categories.

- **Sub-standard asset:** if the loan has been remained NPAs for the period of less than or equal to 12 months;
- **Doubtful asset:** if the loan has been NPAs for more than 12 months;
- **Loss asset:** loans where loss has been identified by bank or auditors or RBI inspector but loan amount has not been fully written off.

NPAs create serious problem to banks, highlight few of them are reduces profitability and solvency of banks, NPA restricts the capacity of the banks to give fresh loans for needy people, NPA reduces the profitability of the banks and Escalating NPA requires bank to make higher provision for losses in their books. To overcome the problem government and RBI established various committees. Narasimham Committee I and II and Andhyarujina Committee was constituted by the Central Government for the purpose of examining banking sector reforms have considered the need for changes in the legal system to effective recovery. Based on recommendation of many committees’ government set of recovery channels to recover NPAs with the minimum intervention of courts.

### LITERATURE STUDY

Banking sector is the one of the most important sectors in Indian economy, which is responsible for all the financial activities taking place in the country and acting as a supporting hand in terms of financing, credit, transaction, collection, payment etc. any disturbance in banking industry will affect the entire economic activities of the country (Ambrish M, 2020). Maintaining the assets quality is important for growth of the banking sector. In the resent year’s asset quality in banks especially in public sector banks continuously deteriorating and creating a lot of stress in financial sector. Over the period of few years Gross NPAs and Net NPAs increased sharply and adversely impacting asset quality so it’s necessary to take steps to reduce the NPAs and improve the recovery mechanisms (Arasu B, 2019).

Indian financial and banking institution will most likely have trouble in maintain momentum, the main reason for that is Non-performing Assets is expected to see a jump, according to the estimate 15% of banks loan are weak and gross non-performing assets will be going to shoot up in upcoming years. Banks credit cost measured by annualized loan provision as a percentage of gross loans will remain high. (Ranina, 2020) COVID-19 pandemic also impacted India’s fragile economy and its banking sector. Effect of virus is more in six major financial and economic hub states, which accounts for roughly 45% of total banking sector loans in India. Any disruption in economic activities in these key states would pose a threat to a flimsy business sentiment. The operating environment for banks will most likely remain grim against the backdrop of pandemic. Banks also facing assets quality concerns since banks financial results are yet to fully disclose impact of stringent lock down which affected common man and MSMEs which depend heavily on banking sector for financials. (Saswata, 2021). Profitability of banking industry became a cause of concern for the Indian economy. Bank based Indian economy is under tremendous stress due to rising NPAs, bad loans persistently draining profits of the banks and hampering the ability of the banks to give fresh loans. NPAs are considered as the major detractor of banks profit. An increase in the portion of bad loans in the total loan portfolio of banks leads to decline in credit quality and hinders the banks performance. Thus, it is very important for banks to handle their loan portfolio carefully. The problem of NPAs if dragged for long time may endanger the financial stability of the county (Dolly Gaur (Ambrish M, 2020)&Dipthi Rajan, 2020).

**NEED FOR THE STUDY:**

Above literature study clearly shows that Indian banking system is facing serious problem of ever increasing NPA. The quantum of non-recovered loan that need to be recovered is very high, so it’s important to study the performance of recovery channels used by banks to recover NPA, which will help to understand the challenges and opportunities in NPA recovery.

**RESEARCH OBJECTIVE**

The objective of this paper is to evaluate the performance of Non-Performing Asset (NPA) and recovery channels of commercial banks.

**RESEARCH METHODOLOGY**

The data collected for the paper is through secondary data available through various reports, websites, and articles of RBI, Word Bank, S&P Global, Fitch Ratings etc. and data is presented using pictorial tools like tables and graphs.

**DATA ANALYSIS**

**Non-Performing Assets and recovery channels**

India is facing problem of increasing Non-performing Assets, Gross Non-performing Assets is increasing year after year. Since 2012 amount of NPA is increasing rapidly in commercial banks. RBI and government of India introduced several policy measures like introduction of IBC, formation of bad banks and increasing number of Assets Reconstruction Companies (ARCs) etc. as a result NPA started to decline but because of COVID-19 pandemic government provided lot of credit and other concession to boost the economy which is resulting in increase in NPA. Below table shows trend in Gross Non-performing Assets from 2012

**Table 1.1**

<b>Gross NPA as per the RBI Report</b>	
<b>Year</b>	<b>Gross Non-performing Assets</b>
2012	3.37
2013	4.02
2014	4.34
2015	5.88
2016	9.18
2017	9.98
2018	9.46
2019	9.23
2020	8.2
2021	7.3
2022 RBI projection)	9.5

**Interpretation:** The above table reflects the gross NPA of India over the years from 2012 to 2022 (projected), as per the RBI report. We can see that, there is gradual increment in the gross NPA of the country from 2012 to 2017. But, from 2017, it is reducing slowly year on-year. But because of COVID-19, the RBI and the central government were forced to provide the financial assistance and relief to maintain liquidity in the economy, and its negative impact already started to reflect in Gross Non-performing Assets ratio. The RBI’s Financial Stability Report (FSR) projected those loans given to MSME sector has the highest chance of default in repayment. The 24th Financial Stability Report indicated that Gross Non-performing Assets (GNPA) ratio of Scheduled Commercial Banks may increase from 7.3 per cent in March 2021 to 8.1 per cent by September 2022 under the baseline scenario and to 9.5 per cent under a severe stress scenario. The gross NPA that need to be recovered is very high and for that, there are four recovery channels existed in India. They are;

**1. Lok Adalat**

Lok Adalat is similar to a civil court can be organised by the State Authority, the District Authority, The Supreme Court Legal Service Committee or High Court Legal Services Committee at such intervals and places as deemed appropriate. It is created under Legal Services Authority Act 1987. Lok Adalat is off the court settlement of recovery dues and it is one of the disputes redressed mechanism where the cases pending in the court of law or at a pre-litigation stage are compromised or settled outside the court amicably. RBI issued guidelines vide notification LEG.BC.114/09.06.2000-01 dated 20-5-2001 for implementation of Lok Adalat as recovery mechanism. The Lok Adalat’s can be utilised as a method of recovery of Debt up to a ceiling limit of 20 lakhs. The performance of Lok Adalat from past 17 years are mentioned below;

**Table 1.2**

**(Amount in Crores)**

<b>Performance of Lok Adalat since 2005</b>				
<b>Year</b>	<b>No of Cases Registered</b>	<b>Amount Involved</b>	<b>Amount Recovered</b>	<b>Percentage</b>
<b>2005</b>	2,68,090	2144	265	12.36
<b>2006</b>	1,60,368	758	106	13.98
<b>2007</b>	1,86,535	2142	176	8.22
<b>2008</b>	5,48,308	4023	96	2.39
<b>2009</b>	7,78,833	7235	112	1.55
<b>2010</b>	6,16,018	5254	151	2.87
<b>2011</b>	4,76,073	1700	200	11.76
<b>2012</b>	8,40,691	6600	400	6.06
<b>2013</b>	16,36,957	23200	1400	6.03
<b>2014</b>	91,31,199	88700	4300	4.84
<b>2015</b>	29,58,313	30979	984	3.17
<b>2016</b>	44,56,634	72000	3200	4.4
<b>2017</b>	35,55,678	36100	2300	6.3
<b>2018</b>	33,17,897	45728	1811	4
<b>2019</b>	40,87,555	53484	2750	5.1
<b>2020</b>	59,86,790	67801	4211	6.2
<b>2021</b>	19,49,249	28084	1119	4.0

**Interpretation:** In comparison with all the recovery channels Lok Adalat has highest number of referred cases. Amount involved in this channel is less and the recovery percentage is consistent since 2005. The rate of recovery through this channel is very less i.e., below 8% and its working is also not appreciable. There is less significant improvement in NPA recovery through this channel.

**2. Debt Recovery Tribunals (DRTs):**

It is an expeditious adjudication process and recovery of debts due to banks and financial institutions. DRTs are governed by law relating to Recovery of Debt Due to Banks and Financial Institution Act 1993. The act is applicable to the cases where the amount of debt due from banks or any financial institutions is more than ₹20 lacks.

The main objective of Debt Recovery Tribunal (DRT) is to provide the speedy redressal to lenders and borrowers through filing of original applications in Debts Recovery Tribunals (DRTs) and appeal

in Debts Recovery Appellate Tribunals (DRATs). Banks approach the DRT and then it will assist the banks to recover the NPAs. Across India, there are totally 39 DRTs and there are 5 Debt Recovery Appellate Tribunals.

**Table 1.3**

**(Amount in Crores)**

<b>Performance of DRT since 2005</b>				
<b>Year</b>	<b>No of Cases Registered</b>	<b>Amount Involved</b>	<b>Amount Recovered</b>	<b>Percentage</b>
<b>2005</b>	3534	6273	4735	75.48
<b>2006</b>	4028	9156	3463	37.82
<b>2007</b>	3728	5819	3020	51.9
<b>2008</b>	2004	4130	3348	81.07
<b>2009</b>	6019	9797	3133	31.98
<b>2010</b>	12872	14092	3930	27.89
<b>2011</b>	13365	24100	4100	17.01
<b>2012</b>	13408	31000	4400	14.19
<b>2013</b>	28258	55300	5300	9.58
<b>2014</b>	171113	378900	53100	14.01
<b>2015</b>	22004	60371	4208	6.97
<b>2016</b>	24537	69300	6400	9.2
<b>2017</b>	32418	100800	10300	10.2
<b>2018</b>	29345	133095	7235	5.4
<b>2019</b>	51679	268413	10552	3.9
<b>2020</b>	33139	205032	9986	4.9
<b>2021</b>	28182	225361	8113	3.6

**Interpretation:** The above-mentioned table depicts the performance of Debt Recovery Tribunal since 2005. It is identified that, the total amount involved in this channel is comparatively less but the percentage of recovery is aristocratic. The major identification from the table is the time duration between 2005-2008 the recovery rate was reached about 81% but after that the downward trend started and reached 3.6% recovery in the last year. There is a huge gap between amount involved through this channel and the amount recovered.

**3. SARFAESI Act:**

The securitization and reconstruction of financial assets and enforcement of securities interest act 2002, it is an Indian law which allows the bankers and financial Institutions to auction residential or commercial properties of defaulters to recover the loans without the involvement of courts. The SARFAESI act also allows RBI to give licence to Asset Reconstruction Companies (ARCs) which takes over the stressed assets from banks and enforce the security interests without the intervention from the courts. The SARFAESI act is applicable to cases where security interest for any securing repayment of financial assets is more than ₹1 lakh and the amount due is 20% or more of the principal amount and interest thereon. The act is not applicable to any securities interest created against the agricultural land.

Table 1.4

(Amount in Crores)

Performance of SARFAESI Act since 2005				
Year	No of Cases Registered	Amount Involved	Amount Recovered	Percentage
2005	41180	8517	3363	39.49
2006	60178	9058	3749	41.39
2007	83942	7263	4429	60.98
2008	61760	12067	3982	33
2009	78366	14249	4269	29.96
2010	118642	30604	11561	37.78
2011	140990	35300	10100	28.61
2012	190537	68100	18500	27.17
2013	194707	95300	25300	26.55
2014	1241086	470500	115200	24.48
2015	175355	156778	25600	16.32
2016	173582	80100	13200	16.5
2017	199352	141400	25900	18.3
2018	91330	81879	26380	32.2
2019	2,35,437	258642	38905	15.0
2020	105523	196582	34283	17.4
2021	57331	67510	27686	41.0

**Interpretation:** The table 1.4 explains about the performance of SARFAESI act from the past 17 years and it is clearly identified that, there is a consistency in the rate of recovery of NPA amount through this channel from the beginning of its introduction and its performance is highly appreciable. In the year 2007, the highest rate of recovery recorded is 60% and since, it is trying to perform better. In the previous year the rate of recovery reached 41% compare to the year 2020, the rate is increasing.

#### 4. IBC 2016: Insolvency and Bankruptcy code

Insolvency and Bankruptcy code is bankruptcy law in India enunciated in 2016 which seeks to consolidate the existing framework by creating a single law for insolvency and bankruptcy. IBC provides time bound resolution scheme, cases admitted to IBC proceedings need to be solved within 180 days. In IBC insolvency professional is appointed to harmoniously recover the dues from insolvent accounts, he decides whether to restructure the loans or to liquidate the assets of the defaulter to recover the due amount. The Adjudicating authority under IBC for insolvency and bankruptcy of individuals and partnership firm is Debt Recovery Tribunals (DRTs) and National Company Law Tribunal (NCLT) for corporate insolvencies. For individuals and partnership firm to start insolvency proceedings minimum default amount must be not less than ₹1000 and for corporates it is ₹1 crore.

Table 1.5

(Amount in Crores)

Performance of IBC from 2017 to 2021				
Year	No of Cases Registered	Amount Involved	Amount Recovered	Percentage
2017	37	-	-	-
2018	701	9929	4926	49.6
2019	1152	145457	66440	45.7
2020	1986	224935	104117	46.3
2021	537	135139	27311	20.2

**Interpretation:** The table 1.5 depicts that the performance of Insolvency and Bankruptcy Code from the year 2017 to 2021. It is identified that, the number of cases admitted under this channel for NPA resolution is growing year by year and also involvement of amount under this channel is also in terms of lakh crores. In the year 2021 number of cases admitted under IBC reduced drastically

because of hold imposed by Supreme Court on insolvency resolution and change in ceiling limit from 1 lakh to 1 crore to admit the cases under IBC for NPA recovery. IBC is able to recover average of 40.25% in last 4 years, recovery percentage reduced to 20.2% in 2021 due to restriction imposed on NPA recovery during COVID lockdown period.

**Table 1.5**

**(Amount in Billion)**

Year	Amount Involved	Amount Recovered	Amount Unrecovered	% Of Recovery Recovered	% Unrecovered
2021	4561	642	3919	14.1	83.9
2020	7425	1726	5699	23.2	76.8
2019	7261	1186	6084	16.3	83.7
2018	2956	404	2552	14	86
2017	2783	385	2398	14	86
2016	2214	227	1987	10	90
2015	2481	308	2173	12	88
2014	1731	311	1420	18	82
2013	1057	233	824	22	78
2012	394	144	250	37	63

**Interpretation:** The table explains about total amount involved under NPA resolution by the different recovery channels and also the table consists of total amount recovered and unrecovered. Table shows that the total amount of NPAs is increasing year after. On the recovery front there is no notable improvement and recovery in most of the years is below 20%. Table indicates that the percentage of unrecovered amount is very high.

**FINDINGS AND SUGGESTIONS**

Banks are facing over burden of Non-Performing Assets. Despite of the government efforts to reduce the NPAs by strengthening exiting laws and recovery channels there is no remarkable improvement in NPAs recovery. IBC introduced in 2016 shown slightly better recover percentage than other recovery channels. By analysing the data, it is identified that, the recovery channel Lok Adalat’s performance is not good enough to appreciate, but the following suggestions can be done through this research work.

- Ceiling limit for LokAdalat need to be increased so that, the greater number of cases can be accommodated for off the court settlement which will reduce burden on other recovery mechanisms.
- Number of national company law tribunal DRTs and DRATs need to be increased for fast-track time taken to resolve the recovery cases.
- All the recovery channels must try to recover dues in specific time.
- Time taken to resolve the case need to be reduced, since most of the cases exceeding prescribed time limit focus must be given to time bound resolution.
- Laws relating to recovery channels need to be strengthened in a such a manner that cases are solved with the minimum intervention of courts.

**CONCLUSION**

Banking sector plays a key role in the economic development of the country. So, maintaining asset quality is important for stability of banks. The recovery of non-performing loan play’s important role in improving asset quality but recovery channels are struggling to effectively recover non-performing loans. Future outlook for bank also very bleak because of problems created by COVID-19 pandemic. Banks need to be very cautious in managing non-performing assets. The global economic recovery is losing pace because of re-emergence of COVID-19 infections, the new variant Omicron, high rate of inflation, global supply chain disruption. New indications also showing sign of stress in micro, small and medium enterprises (MSME). Spill overs from global crisis and muted performance of industries may lead to the future deterioration of asset quality. Creation of National Asset Reconstruction Ltd (NARC) also known as bad bank that work as ARCs to transfer and recover the NPAs of bank is the welcome move by government. The amount of NPA is very high so, government and RBI need to adopt the good policies to reinforce NPAs recovery channels.

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