NPA - in the Context of Indian Banking Sector

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When a borrower is unable or unwilling to pay the amount of the loan or its interest, then the loan is known as a non-performing asset or NPA.

In other words, when the components of a loan are not serviced by the borrower, as the loan provided by the bank is an asset, so the amount of loan becomes a non-performing asset. The asset that fails to earn a return for the investor for a certain period of time is called NPA. The stipulated time period for an asset to be considered as NPA is 90days.

Classification of NPA-

1. Substandard asset is an asset that is considered as NPA for less than or equal to 12 months.
2. Doubtful asset is an asset that is considered as NPA for 12 months.
3. Loss asset is an asset that is considered as NPA for more than 12months.

Impact of NPA-

- Lenders suffer a lowering of profit margins.
- Higher interest rates by the banks to balance the loss by NPAs
- Investors do not get fair returns.
- NPA related cases add up to the already pending cases that are piled up.

Various steps taken to tackle NPA-

In 1991, Narasimhan committee recommended several reforms to tackle NPA. They are as follows:

The debt recovery tribunal (DRTs)-1993 - The reform is governed under the provisions of banks and financial institution act of 1993. The main motive behind this act was to reduce the time frame for settling the cases of NPA.

1. **Lok adalats-2001-** They are mainly concerned with the recovery of small loans, they are limited to 5lakh rupees only according to RBI guidelines.

2. **SARFAESI act 2002-** The act stands for Securitization & Reconstruction of Financial assets & Enforcement of Security Interest act. The secured assets are acquired and disposed by the banks with the unpaid amount of 1lakh and above without indulging the court under this act.

3. **Asset Reconstruction companies (ARC)-** The motive behind this act was to unlock value from stressed loans.

4. **Corporate debt restructuring 2005-** Under this the rates paid are decreased and the time the company has to pay back the obligation is increased. Thus reducing the burden of the debt on the company.

5. **5:25 rule- 2014-** The 5:25 rule or flexible structure of long term projects loans such as infrastructure. These projects have a longer timeline and they do not get money back for a long time, thus it was proposed to maintain cash flow of such companies.

6. **Mission Indra Dhanush- 2015-** To improve the overall performance and revamp the public sector banks -ABCDEFG nomenclature was used to describe various terms:-

A- Appointments- Separate post of chairman, MD and CEO will be designated.

B-Bank Board Bureau- BBB consists of reputed officers and intellectuals.

C-Capitalization- A buffer of minimum capital is required to be maintained under the norms of Basel 3.

D- Distressing PSBs- To improve the measures of risk control and NPA.

E-Empowerment- The decisions are taken by the bank individually without any consultation from the government.

F-Framework of accountability- Key performance indicators (KPI) are associated with the performance.

G- Governance reforms- Transparent and meritorious appointments in PSBs by BBB.

8. **Asset Quality Review 2015 -** Under AQR, provisions are made for stressed assets to protect the interest of the banks.

9. **Insolvency and Bankruptcy code act 2016-** Under this act, the interest of shareholders are considered and changes are made to improve the credit facility of the banks and their entrepreneurship.

10. Bad Banks 2017- The problem of stressed loans are considered by forming bad banks that are going to be governed by the flexible rules.

Raghuram Rajan's viewpoint on NPA-

Dr Raghuram is a known intellectual in the world of finance. His views are held in financial world with much respect and awe. He taught in an American university for long time before he was invited to took over as the Governor of reserve bank of India.

Dr Rajan, remained in the office as Governor of the Reserve Bank of India (RBI) from September 5, 2013 to September 2016, He discussed NPA ND ITS roots in great detail. Some of the points given by him are:

1) The period of 2006-08 was beneficial for the economy as significant projects were completed within time and budget. These past performances affected the due diligence of future projects.
2) When banks started to write down bank debt and promoters brought in more equity to avoid the threat of losing their project, the bank helped promoters in paying their dues by advancing more loans to them and pretending that it was performing. The profit shown by the bank was illusionary and no interest was actually coming in reality.
3) Initially DRTs and SARFAESI were successful but later promoters found their way to game them.
4) RBI has pulled on their socks and initiated by giving power to the banks. To identify the working of every loan that are above 5crore, a large loan database was formed.
5) To end forbearance, ever greening of projects was stopped by the banks.

What happened in the 2015 Asset Quality Review?

- Banks were not recognising bad loans in order to ever greening the projects and denying the loss they were going through. As different banks were following different norms thus a loan that was non performing in one bank was performing in another.
- It was the need of the hour to clean up the bank as soon as possible to resume credit. But banks have not made enough provisions for the loans that were non performing for a long time.
- During August-November 2015, RBI conducted a balance sheet check of random banks to examine the status of their asset quality. The report generated from these inspections was called Asset Quality Review.
- RBI has given time to banks to classify their assets according to the risk they possess. This helped in bringing out the actual financial position of banks as banks were hiding bad assets with the help of forbearance.

Post effect of AQR-

- After conducting AQR by RBI, losses were piled-up in the banking sector, the aim was to clear the balance sheet of the banks.
- Public sector banks were the most affected whereas in private banks only ICICI bank and Axis banks were affected.
- The losses recorded by large lenders were- Bank of Baroda (Rs 3230 crore), PNB (Rs5367 crore), IDBI (Rs 1376 crore) and many more.
- The impact of AQR was furthermore as provisioning required for standard assets were increased from 0.4% to 15%.

Vijay Mallya's case of NPA-

Vijay Mallya(VM) was a known industrialist of India and owned major manufacturing units. He was also appointed member of upper house because of his credibility and work. He was given a loan of Rs 8040 crore in 2004. The loan was advanced in the name of Kingfisher Airline (KFA) but it was believed that that VM siphoned off the money to buy properties and various teams in Formula 1 track team , cricket team , across the world.

Mallya currently owes more than 9000 crore to 17 banks and major money to SBI who is the leader of this consortium of banks. The loan was advanced to KFA on the basis of the brand name that the company possessed at that time rather than having secured assets on these loans.

Even after this Mallya managed to get 900 crore loan from Industrial Development bank of India in 2009 despite warning from some of its officers. The loan that was taken in 2004 was declared NPA in 2009 and was restructured in 2010.

Today , there are 9150 wilful defaulters of state owned banks that have amounted money to the tune of Rs 85258 crore. Under SARFAESI act, action is taken against 6207 wilful defaulters.

Banks are still making losses despite taking various actions as these steps have led to the recognition of losses that were mounting for a long time. Now the provision is being made for the future projects but that will not compensate for the losses that were made in the past.

CONCLUSION-

The current scenario of Indian banking system is worth our attention. The pandemic and national lockdown has affected the situation of NPA. Private and public banks are expecting a growth in their bad loans and banking industry is expecting a loss of value of financial asset over time. To overcome the situation, they have to provide for the defaulters from their end.

RBI has predicted a gross NPA of 12.5% in the month of march this year(2021). It was expected that the situation will be difficult due to the pandemic but the actual figures are bit higher than the expected figures. The moratorium expected from both private and public banks was quite high. Even NBFCs has given 49% of moratorium to their customers.

Though the situation of public banks was still better than private banks in the initial period of 2019-20, the situation got worsened for both sectors due to covid-19 pandemic.