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..... in Commercial Bank with Special Reference to State Bank  
..... of India.

  
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**A Study on Management of Nonperforming Assets In Commercial Bank  
With Special Reference To State Bank of India**

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## **Abstract**

Bank plays a vital role in Indian financial system. In present fast changing competitive global economy, survival of a business is depends on the best practices followed by management in using its resources. In the same manner banks should also follow best management practices for generating optimum income by using its assets, after paying the cost of funds for acquiring them and other administrative costs involved therein. The sound financial position of a bank depends upon the recovery of loans or its level of Non-performing assets (NPAs). Reduced NPAs generally gives the impression that banks have strengthened their credit appraisal processes over the years and growth in NPAs involves the necessity of provisions, which bring down the overall profitability of banks. The Indian banking sector is facing a serious problem of NPA. In this paper we will try to find out what is the impact of NPA on the profitability of the banks.

## **Keywords**

Net NPA, Gross NPA, Bank, Provision, Advance, Profitability

## **Introduction**

After a big recession and slowed down in world economy, now world economy is in the up word changes. According to the Conference Board Global Economic Outlook 2.9 percent global growth will be there in 2017. For the betterment of business we need to focus on strengthening qualitative growth factors, such as technology, innovation, and skills, possible disruptive forces from trade and immigration policies. The incidence of Non-Performing Assets is affecting the performance of the Bank both financially and psychologically which has been reflecting ultimately on the balance sheet of the Bank. With increased concern towards Non-Performing Assets, this study was undertaken to the Management of Non-Performing assets.

After 2008 Lehman brothers crisis most of the policies of bank has been changed in the worldwide. In India also lot of changes have done so far and recently cabinet approved a new policy for Banking Regulation Act (section 35A), for the certain provision of Bankruptcy Code. These changes will empower RBI to give directions to banks to effectively resolve NPAs.

According to Reserve Bank of India, An asset, including a leased asset, becomes non-performing when it ceases to generate income for the bank. A 'non-performing asset' (NPA) was defined as a credit facility in respect of which the interest and or installment of principal has remained 'past due' for a specified period of time.

## **Impact of NPAs on banks profitability**

Non-performance asset reduces profitability by creating provision on NPA. And it increases carrying cost also. All these reasons will results in excess & avoidable management attention and impact on banks profitability. Apart from this, a high level of NPA also puts stress on banks net worth because, banks are under pressure to maintain a desired level of Capital Adequacy. Banks eventually look towards their internal financial strength to fulfill the norms thereby slowly eroding the net worth.

## **Objectives of the study**

The following are the important objective of the study

- To analyze the magnitude of NPA of SBI.
- To identify the factors responsible for the causes of NPA in the banks.
- To examine the level of NPA in SBI and to study the effect of NPA for profitability of banks.



## **Hypothesis of the study**

- There is no significant correlation between Gross NPAs and Gross Advances in respect of Non Performance Assets.
- There is no significant correlation between NPAs and profitability of the bank.

## **Need of the study**

The efficiency of a bank is not always reflected on its balance sheet, but it reflects on the level of returns on its assets. Managing the Non-performing assets is a biggest challenge in the today's competitive banking sector. Because bank should follow the law which is passed by the government and it should also concentrate on debt recovery tribunals, LokAdalat, the legislations enacted by the State Governments and one-time settlement schemes. The banks should not only take steps for reducing present Non-Performing Assets (NPAs), but necessary precaution should also be taken to avoid future Non-Performing Assets (NPAs). NPA will directly impact on Credit risk management of the banking system.

## **Statement of the problems**

Bank plays a vital role in Indian financial system. In present fast changing competitive global economy, survival of a business is depends on the best practices followed by management in using its resources. In the same manner banks should also follow best management practices for generating optimum income by using its assets, after paying the cost of funds for acquiring them and other administrative costs involved therein. Once the assets stop contributing income, they are termed as NPA, which not only involved cost of fund, but also it should be operated as per prudential norms of banking act. The NPAs are the most important factor that will impact on the performance of the banks. The problem of NPA has reached the magnitude of the national level.

The problem is selected to study the non-performing asset in State Bank of India. Hence study is to be conducted to evaluate the level of NPA in SBI and how bank will manage NPA and to study the elective measures taken by the banker to reduce the level of level of NPA to minimum level.

## **Limitation of the Study**

The study is limited to the functions of State bank of India, pertaining to its management of NPAs and profitability. Thus, the important limitations are as follows;

The study on management of non-performing assets is limited to the State Bank of India. The data are collected from SBI during 2012 to 2016. The basis for identifying non-performing assets is taken from the Reserve Bank of India circulars.

## **Literature Review**

A large number of researchers have been studied to the issue of Non-Performing Asset in banking sector.

Dr. ADharmendran (2012), examine the position & growth of standard assets, substandard assets, loss assets, gross non-performing assets provision for non-performing assets & net non-performing assets with the help of percentage analysis method & compound growth rate for all the state Co-operative banks in India.



Namita Rajput, Monika Gupta, Ajay Kumar Chauhan(2012), they analyzed that there is a diminishing trend in the ratios of non-performing assets as GNPA's and NNPA's. There is a high degree of negative correlation between NPA Ratios with ROA. Multiple Regression model has also repetitive the results that there can be an enhancement in profitability of the banks if the NPAs has decreasing trend continuously. The assessment would help to improve the assets quality of banks, so that, provisioning requirement would automatically come down and it added to the profits directly which led to increase the overall performance of the banks. It may spill over the banking system and contract the money stock, which may lead to economic contraction and affect its liquidity and profitability.

Ratikantha Ray (2013), had compared the non-performing assets of commercial and cooperative banks by selecting the banks in Pune. For study researcher selected two bank viz. Bank of Maharashtra from commercial bank sector and JanataSahakari Bank Ltd from co-operative bank. The study concluded that occurrence of NPA affects the profitability and health of a Bank adversely.

VivekRajbahadur Singh (2016), in his research he found that NPAs has a direct impact on profitability of the bank as Indian banks are highly dependent on income from interest on funds lent. And also extent of NPA is comparatively very high in public sectors banks. Although various steps have been taken by government to reduce the NPAs but still a lot needs to be done to curb this problem. The NPAs level of our banks is still high as compared to the foreign banks. It is not at all possible to have zero NPAs. The bank management should speed up the recovery process. The problem of recovery is not with small borrowers but with large borrowers and a strict policy should be followed for solving this problem.

### **Concept of Non-Performing Asset**

After the 1991 Indian economic crisis, to avoid future crisis and increase the growth of economy, Finance Ministry of Government of India set up various committees with the task of analyzing India's banking sector and recommending legislation and regulations to make it more effective, competitive and efficient. In that two expert committees were set up under the chairmanship of M. Narasimham. After that, as per the recommendations made by the committee Reserve Bank of India has introduced new guidelines for advances. According to new guidelines advances should be grouped into performing and non-performing assets. Income is recognized only in respect of performing assets further depending upon the quality of asset and real ability of asset have been designated as standard asset, sub-standard asset, doubtful asset, and loss assets for the purpose of provisioning.

### **Meaning of NPA (As defined by RBI)**

An asset, including a leased asset, becomes non-performing when it ceases to generate income for the bank.

A non-performing asset (NPA) is a loan or an advance where;

Interest and or installment of principal remain overdue for a period of more than 90 days in respect of a term loan. The account remains out of order in respect of an Overdraft or Cash Credit. The bill remains overdue for a period of more than 90 days in the case of bills purchased and discounted. The installment of principal or interest there on remains overdue for two crop seasons for short duration crops. The installment of principal or interest there on remains overdue for one crop season for long duration crops. The amount of liquidity facility remains outstanding for more than 90 days, in respect of a securitization transaction undertaken in terms of guidelines on securitization dated February 1, 2006. In respect of derivative transactions, the overdue receivables representing positive mark-to-market value of a derivative contract, if these remain unpaid for a period of 90 days from the specified due date for payment.



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## Categories of NPAs

Non-performing assets should be classified into 3 categories and are as follows,

- **Substandard Assets** - With effect from March 31, 2005, a substandard asset would be one, which has remained NPA for a period less than or equal to 12 months. Such an asset will have well defined credit weaknesses that jeopardize the liquidation of the debt and are characterized by the distinct possibility that the banks will sustain some loss, if deficiencies are not corrected.
- **Doubtful Assets** - With effect from March 31, 2005, an asset would be classified as doubtful if it has remained in the substandard category for a period of 12 months. A loan classified as doubtful has all the weaknesses inherent in assets that were classified as substandard, with the added characteristic that the weaknesses make collection or liquidation in full, – on the basis of currently known facts, conditions and values – highly questionable and improbable.
- **Loss Assets** - A loss asset is one where loss has been identified by the bank or internal or external auditors or the RBI inspection but the amount has not been written off wholly. In other words, such an asset is considered uncollectible and of such little value that its continuance as a bankable asset is not warranted although there may be some salvage or recovery value.

## Methodology

Type of research – Descriptive research was carried for this research.

For this study we are considered secondary data. Secondary data is the information that already exists. Secondary data was collected through various sources such as, internet, books, journals, newspaper and reference from libraries.

The data so collected has been tabulated and analyzed by using various ratio techniques the study also examines the trend of NPA in various sample banks. The findings of the study are inconformity with the statistical tables, Pie diagrams and column charts are done to compare the ratios of five financial years & interpret the analysis of the same.

## Data analysis & interpretation

### 1. Net NPA ratio

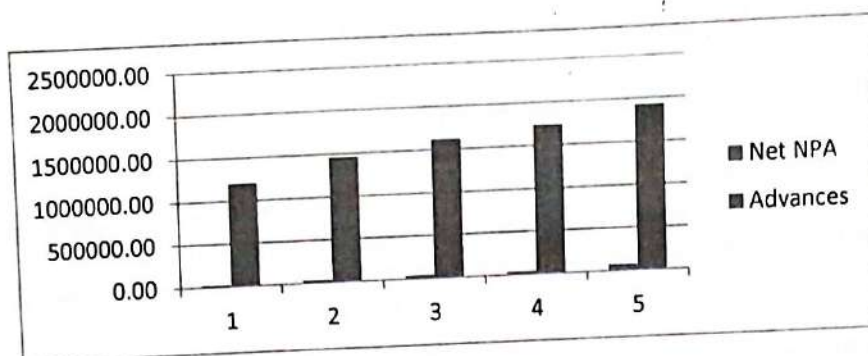
This ratio will help us to measure the overall quality of the bank's loan book.

$$\text{Net NPA ratio} = (\text{Net NPA} / \text{Advances}) * 100$$

### Data Analysis & Interpretation

Year	Net NPA	Advances	Net NPA Ratios (%) (In crore)
2012	21095.09	1199934.94	1.76
2013	28782.38	1459944.79	1.97
2014	42204.80	1623067.34	2.60
2015	37813.96	1737896.30	2.18
2016	69809.03	1928714.97	3.62



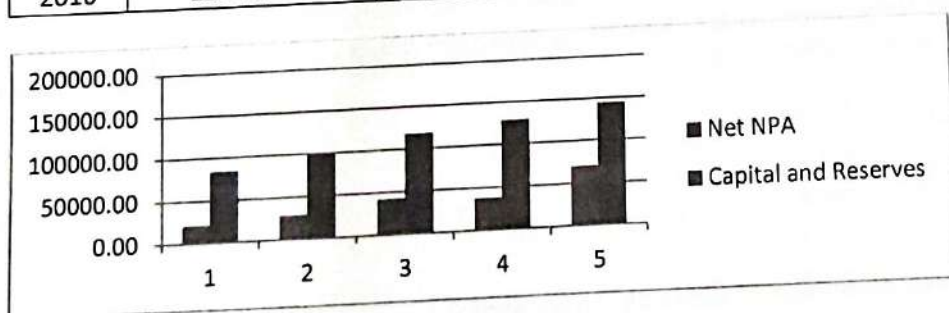


From the above graph we can conclude that net NPA is increase as advances are increasing year by year. But in 2015 net NPA ratio was 2.18%, when we compare this with 2014(Previous year), we can conclude that bank was taken good decision to control net NPA ratio in 2015. When we compare overall net NPA ratio, it is growing year by year. And that concludes, bank had failed to make sufficient provisions against NPA in these years.

## 2. Gross NPA ratio

### Data Analysis & Interpretation

Year	Gross NPA	Advances	Gross NPA Ratios (%) (In crore)
2012	49648.70	1199934.94	4.14
2013	63987.43	1459944.79	4.38
2014	80737.02	1623067.34	4.97
2015	74626.63	1737896.30	4.29
2016	123463.87	1928714.97	6.40



### Analysis & Interpretation

The above table and graph conclude that the average gross NPA is not satisfactory. It is seen that the gross NPA which was 4.14% in 2012 increased marginally every year and finally reached 6.40% in 2016 which is much higher.

## 3. Total Provisions Ratio

Total provision ratio =  $(\text{Total provision} / \text{Gross NPAs}) * 100$

### Data Analysis & Interpretation



## Categories of NPAs

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## Data analysis & interpretation

### 1. Net NPA ratio

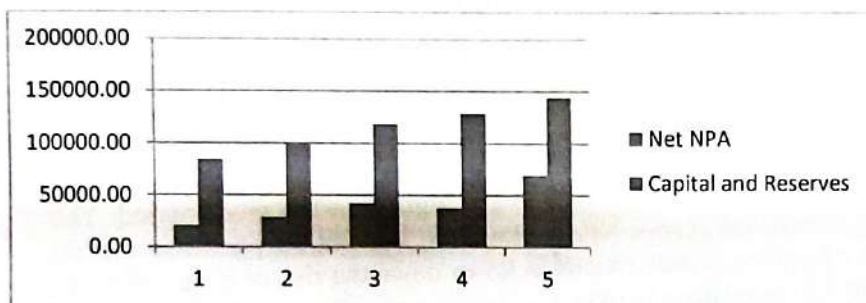
This ratio will help us to measure the overall quality of the bank's loan book.

Net NPA ratio = (Net NPA / Advances) \* 100

### Data Analysis & Interpretation

Year	Net NPA	Advances	Net NPA Ratios (%) (In crore)
2012	21095.09	1199934.94	1.76
2013	28782.38	1459944.79	1.97
2014	42204.80	1623067.34	2.60
2015	37813.96	1737896.30	2.18
2016	69809.03	1928714.97	3.62

Year	Provision	Gross NPA	Total Provision Ratios (%) (In crore)
2012	11546.00	49648.70	23.26
2013	11368.00	63987.43	17.77
2014	14224.00	80737.02	17.62
2015	17908.00	74626.63	24.00
2016	26984.00	123463.87	21.86



#### Analysis & Interpretation

From the above table it can be interpreted that Bank has not made enough provisions for their gross NPAs. From the table we can see that of 5 consecutive years under study, in 2012 the provisions was the highest i.e. 23.26% but after it is being decreased to 17.62% in the year 2014, which is not a good sign for bank. The bank needs to make sufficient provision in order to reduce the level of NPA.

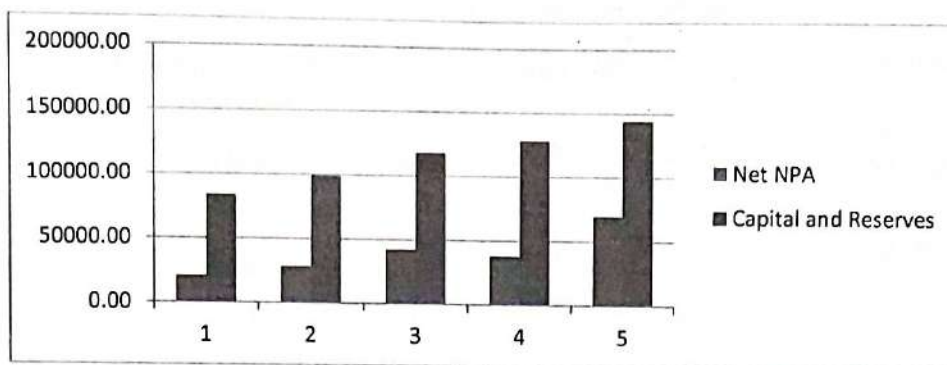
#### 4. Shareholder's Risk Ratio

Shareholder's risk ratio = (Net NPAs / Total Capital and reserves) \* 100

#### Data Analysis & Interpretation

Year	Net NPA	Capital and Reserves	Shareholder's Risk Ratios (%) (In Crore)
2012	21095.09	83951.00	25.13
2013	28782.38	98884.00	29.11
2014	42204.80	118283.00	35.68
2015	37813.96	128439.00	29.44
2016	69809.03	144274.00	48.39





### Analysis & Interpretation

From the table and graph, we can see the position of Bank. The risk ratio was low in the year 2012. After that it is increasing year by year and reached to 48.39% which is the highest in the given period. This indicates the bank has failed in making provisions against NPAs. However, it is not the good sign that the risk ratio is increasing, the bank has to take some instant actions to lower down the risk or it can affect the goodwill, market price of the shares and the competitive market.

### Findings and Conclusion

NPA has been increasing whether gross or net in terms of rupees and percentage too. When we compare overall net NPA ratio and gross NPA ratio, it is growing year by year. And that concludes, bank had failed to make sufficient provisions against NPA in these years. Shareholder's Risk Ratio is also increased by year to year. However, it is not the good sign that the risk ratio is increasing, the bank has to take some instant actions to lower down the risk or it can affect the goodwill, market price of the shares and the competitive market.

The bank seems to have an increasing trend of NPA in last five years. The bank needs to be proactive in the selection of clients and customers while sanctioning of loans. The operation of the bank is wide enough to cater to the needs of broad range of the society and economy of India at large. Bank should take some strict action to avoid NPA.

Bank needs to have better credit appraisal system so as to prevent NPAs from occurring. However, once NPAs do come into existence, the problem can be solved only if there is enabling legal structure, since recovery of NPAs often requires litigation and court orders to recover stock loans. With long-winded litigation in India, debt recovery takes a very long time. Even if the bank is taking necessary measures for recovering the loans, but it needs the support of the system.

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