

A Review on the Existence of Non-Performing Assets in the Indian Banking Sector

P. Aruna Devi¹ and Dr. Satvinder Singh Gill²

¹Research Scholar, Department of Management

²Assistant Professor, Department of Management
Sunrise University, Alwar, Rajasthan

Abstract: *A country's financial system has a significant impact on its economic development. By providing a range of services, a strong financial system boosts economic expansion and raises a nation's level of life. An essential component of the Indian financial system, the banking industry provides services that aid in the nation's development goals. One of the main responsibilities of all banks is to transfer money from savers to borrowers for beneficial uses. By engaging in priority lending and job creation, banks carry out social services. But lending money to debtors has grown to be a significant problem. Gaining additional assets does not always translate into more profitability. The issue of borrowers not repaying principal and interest is one that banks are now grappling with. The banks' operating efficiency and profitability have been severely impacted by the non-repayment of loans and interest. Because they are essential to the expansion of the banking industry and the economy as a whole, banks must preserve the quality of their assets and provide stability in their profitability. Therefore, by referencing previous research, the study attempts to provide a solid conceptual understanding of non-performing assets and thoroughly tackles the problem of non-performing assets in the banking industry. Future research on non-performing assets in the banking industry will have a theoretical foundation thanks to this work.*

Keywords: Asset Quality, Financial Stability, Credit Risk, Loan Defaults

I. INTRODUCTION

By providing a range of services, a strong financial system boosts economic expansion and raises a nation's level of life. These services include clearing and settling mechanisms to support both local and international commerce, as well as the collection and channeling of money between depositors and borrowers (Bollard, Hunt, & Hodgetts, 2011). In order to guarantee prompt loan repayment, banks specialize in assessing borrowers' credit worthiness and closely monitoring their actions. The marginal difference between the interest rates that banks charge borrowers and pay depositors is how they get compensated for their services.

A bank now serves a variety of purposes and provides a range of financial products in addition to its primary and most important function of lending and borrowing. Apart from their core services, banks also serve as the government's agent, offer mutual fund products and insurance policies, accept bills of exchange, sell and purchase securities, issue letters of credit, function as referees and underwriters, deal in foreign currency, transmit money, and provide merchant banking, among other services. Bank serves as a go-between for savers and borrowers. Accepting money from those who have extra and lending it to others who need it are the main duties of all banks.

While lending money to borrowers carries a risk due to the possibility of non-repayment, accepting money from savers carries no risk. Due to the rising amount of non-performing assets, or NPAs, banks are becoming more cautious when making loans (Narula & Singla, 2014). Because it impacts the banks' ability to operate, the growing amount of non-performing assets is concerning. Bank-led developing nations like India are worried about the rising number of non-performing assets (NPAs). The presence of non-performing assets has a negative influence on the economy's development in addition to impeding the banks' operations and profitability. Therefore, determining the causes of non-performing assets and creating appropriate policies to reduce NPAs are crucial.

CONCEPT OF NON-PERFORMING ASSETS

A bank's records include a variety of assets, including cash on hand, investments, balances with other banks, loans and advances, fixed assets, and much more. The notion of non-performing assets is limited to loans, advances, and investments. An asset is regarded as a performing asset when it produces the anticipated amount of revenue while revealing no extraordinary risk, even in the face of typical commercial risk. An asset is classified as non-performing when it stops producing income in the form of fees, interest, or commissions.

When principle repayment or interest payments are not made for at least two quarters after they are due, the advance is considered a non-performing asset, or NPA (Selvarajan & Vadivalagan, 2013). Stated differently, non-performing assets are referred to the banks as non-performing loans. It is a bank advance for which the interest or installment payment is not made on schedule. For banks, a loan or advance is an asset as it creates a flow of cash for principle repayment and interest payments. Because banks charge greater interest rates on loans and advances than they are willing to give depositors on their deposits, they typically make money from interest revenue.

The banks' revenue is the difference between the interest they charge borrowers and the interest they commit to pay depositors. Advances are categorized as non-performing assets if they are not paid within 90 days of the due date, but they are considered past due if they are not paid within a short period of time beyond the due date. The banks are concerned about a startling increase in the amount of non-performing assets. Therefore, the problem must be resolved, and strategies to stop non-performing assets from happening must be found. As a result, by consulting previous research, the current study thoroughly examines the problem of non-performing assets in the banking industry.

Gaining a solid conceptual grasp of the subject of nonperforming assets is the study's main goal. Additionally, it seeks to draw attention to the causes of non-performing assets, the part banks play in making the issue worse, the potential effects of NPAs on bank operations, and, lastly, the investigation of ways to reduce the issue of NPAs. To achieve the aforementioned goals, the descriptive study heavily draws on previous research on non-performing assets. The paper helps to develop a theoretical framework for future empirical research that could be done to measure how NPAs affect banks' operational efficiency, how the central bank's prudential and provisional rules affect the state of non-performing assets in the banking industry, etc.

REVIEW OF EXISTING STUDIES

The occurrence of non-performing assets in the banking industry is the subject of a large number of studies. They look at the causes of them as well as how banks handle these assets. A few of the research (Reddy, 2002; Malyadri & Sirisha, 2011; Collins & Wanjau, 2011; Srinivas, 2013) are thoroughly evaluated. In their research, Malyadri & Sirisha (2011) look at the evolution of non-performing assets in public and private sector banks that belong to India's weaker segments during a seven-year period (2004–10). The quality of the assets of both kinds of banks has increased in recent years, according to the data analysis taken from the Report on Trends and Progress of Banking in India. Public sector banks have outpaced private banks in terms of penetration when compared to weaker sectors during the course of the research period.

A notable decline in the NPA ratio indicates that both public and private sector banks are managing their non-performing assets (NPAs) better. It also emphasizes how regulatory authorities' actions, such as prudential standards and provisioning, have forced banks to keep an eye on their operations and reduce non-performing assets (NPAs) in order to strengthen the Indian financial system as a whole. Examining NPA trends in the Indian banking sector is the goal of another research conducted by Balasubramaniam (2011). Despite high interest rates and operational expenses, the Indian banking industry has shown continuous progress in terms of profitability and performance. Higher credit growth, return on equity, and greater return on assets all show the increased performance.

It also implies that improved credit evaluation procedures and efficient internal control systems may lower greater levels of non-performing assets. In order to meet Basel III standards and the capital adequacy and provisioning requirements, banks would have to raise money. An investigation on the state of non-performing assets in the Indian banking industry is conducted by Singh (2016). According to the trend research, public sector banks have more non-performing assets (NPAs) than private sector banks. The percentage of non-performing assets (NPAs) in the Indian

banking industry remains greater than that of international banks, even after a number of reforms were implemented. It claims that although NPAs have an effect on banks' profitability, having 0% nonperforming assets is also impossible. As a result, banks had to enhance their debt recovery systems. Easy loan recovery requires credit evaluation and post-lending monitoring. One effective strategy to monitor the debtors is to cultivate positive relationships with them by offering them business advice. The research finds that large borrowers are more likely than small borrowers to have trouble recovering their loans. Therefore, the RBI needs to try to update the current credit appraisal changes. The development of a conceptual understanding of non-performing assets is another goal of Mishra & Pawaskar (2017). The report outlines the sectoral distribution of non-performing assets (NPAs) in the Indian banking system and offers strategies for prompt loan recovery.

A four-year period from 2011–12 to 2015–16 is used for ratio analysis, which demonstrates an increased trend in the amount of non-performing assets. According to the report, banks should exercise caution when choosing which consumers to provide credit to since loan recovery is crucial to the expansion of both the banking industry and the overall economy. It also emphasizes how a strong legal system and judicial system may aid in stock loan recovery. Khanna (2012) conducted a similar analysis that examines the patterns of non-performing assets in Indian banks during a five-year span, from 2005 to 2010. For analytical purposes, the research divides the Indian banking industry into three groups: private banks, nationalized banks, and SBI and its affiliate banks. According to the report, the existence of non-performing assets (NPAs) has a detrimental effect on the banks' profitability and net value.

The rising NPA level necessitates changes and provisions in loan issuance and credit management. When approving loans, the banks need to exercise caution. The primary prerequisites for reducing or avoiding the accumulation of new non-performing assets (NPAs) are the loan's purpose, timely delivery of the amount, and appropriate use of funds. A research by Garg (2016) aims to provide a conceptual framework about non-performing assets and their function in the banking industry. According to information gathered from bank annual reports, loan and advance instruction manuals, and the RBI's report on the development and trends of Indian banking, non-performing assets (NPAs) have an impact on bank profitability and liquidity as well as cause credit loss.

Additionally, it establishes preventive measures to lower non-performing assets (NPAs), such as lending to borrowers who are truly in need of a loan; promptness and sufficiency of response are also important; and efficient management practices are crucial for monitoring the borrower and loan amount's timely repayment. All things considered, the research predicts that appropriate corrective actions and procedures must be implemented in order to see a decrease in the number of non-performing assets. Using the case study technique, another research seeks to comprehend the idea of non-performing assets (NPAs) and the connection between NPAs' net advances and loans (Chatterjee, Mukherjee, & Das, 2012).

According to the paper, the existence of non-performing assets (NPAs) has an impact on the banking system's reputation, money deployment, mobilization strategy, and capital adequacy level. Excessive NPA, personnel, and government equity constrain public sector banks. Therefore, by implementing policy changes, the RBI should assume responsibility for reducing non-performing assets. It also makes the case that public banks have to put the advancement of the Indian financial system ahead of the concept of societal benefit. In an effort to close the gap between Indian and foreign banking standards, the time it takes to designate an asset non-performing is being shortened.

This would ultimately lower the amount of non-performing assets and enhance the quality of banks' assets. According to Selvarajan & Vadivalagan (2013), despite their remarkable accomplishments, Indian banks have been unsuccessful in their attempts to integrate with global banking in recent years because of innate flaws. Although banking is seen as an essential tool for economic growth, particularly in developing countries, the issue of non-performing assets (NPAs) has rendered banks a burden on the economy. The cost of managing credit is raised by non-performing assets. NPAs have a negative effect on banks' liquidity, profitability, competitiveness, and financial institution growth. Regarding loan delivery and growth, it also has an impact on bankers' psyche.

Banks must set aside money from their current earnings for non-performing assets (NPAs). The amount of non-performing assets held by banks is one of the key metrics to be taken into account when assessing their performance and overall financial health. NPAs are seen to be one of the factors influencing the banking industry's stability and

financial development (Kaur & Singh, 2011). In contrast to commercial lenders, government-controlled lenders use distinct criteria for allocating loans, according to study conducted by Fotak (2012).

By offering loans under lax legal guidelines or during banking or financial crises, state-owned lenders alleviate financial restraints, which has a detrimental effect on economic development. Srinivas (2013) did research that provides guidance to bankers on how to reduce the growing issue of non-performing assets (NPAs) in the banking industry. According to the study's findings, a lender should keep a close eye on the borrower's actions to ensure that the approved loan is being used appropriately and for the intended purpose. Having both official and informal feedback on the client's goodwill is crucial. The customer's request for a fresh loan should be denied outright if they have previously been shown to be in default.

The lender should inform the clients about the repercussions of loan non-repayment while approving loans. Bankers would see a significant drop in the amount of non-performing assets held by the banks if they followed these recommendations. According to Reddy's (2002) research, steps have been done to enhance the Indian financial system in a number of areas, including prudential standards, entry barriers, risk-based supervision, reserve requirements reduction, and interest rate deregulation. The clarity of macroeconomic indicators and other systemic concerns pertaining to the banking system and the economy are emphasized in the research.

The NPA issue is allegedly best resolved by a robust legislative, judicial, and administrative framework. The experiences of Asian nations in addressing the issue of non-performing assets (NPAs) are highlighted in the article. It goes on to say that in order to create a customized solution for banks to deal with non-performing assets (NPAs), it is necessary to consult global experiences that are clear of local situations. Jadhav, Gujarathi, and Gawali (2016) conducted research to learn more about the Bank of Maharashtra Nashik district's NPA management. Due to their dominance in India and the fact that they often have more non-performing assets than other commercial banks, public sector banks are the focus of more research. The existence of non-performing assets has a negative impact on the banks' financial standing and profitability.

The central bank's implementation of prudential and interim standards, including asset categorization and revenue recognition, has contributed to revealing the actual financial condition of Indian banks. The research emphasizes that the Bank of Maharashtra has a strong loan recovery strategy and credit evaluation system in place. Credit-related transactions are handled by a different department. In spite of these actions, the NPA level rose significantly between 2011–12 and 2014–15. Because agricultural loans have a larger percentage of non-performing assets than other loan categories, banks should focus more on the NPAs that come from this industry. Unexpected rains and other natural disasters are thought to be the potential cause of non-performing assets (NPA) in the agricultural sector.

Singh and Makkar (2014) attempt to investigate the connection between stock return volatility and the crisis in the Indian banking industry. For empirical study, the Bankex stock index which serves as a stand-in for the stock prices of Indian commercial banks is used. Major public and private sector banks that are listed on the Bombay stock market are included in the Bankex index. The research examines closing stock price time series data that was gathered daily between January 1, 2004, and December 31, 2012. The investigation comes to the conclusion that the performance of the Indian stock market is significantly impacted by news of the US stock market's decline.

It has been noted that the volatility and stock returns of Indian banks varies significantly between pre-crisis and post-crisis times. The reasons for the banks' non-performing assets have been the subject of several investigations. Roy (2014) identifies the variables influencing Indian banks' non-performing asset levels. The research uses panel regression using a fixed effect model to investigate how country-related and bank-related variables affect the amount of non-performing assets (NPAs) from 1995–1996 to 2011–2012. The ratio of net non-performing assets to net loans is a dependent variable, while the macroeconomic variables of GDP growth, real effective exchange rate, and inflation, as well as one bank-level indicator, net interest margin, are independent variables.

The frightening thing is that all developed and developing nations have already managed to curb the NPA level from the high of 2008–09 at the time of the global recession, where it is still rising in India. The results show that while the level of non-performing assets (NPAs) in foreign banks has decreased following the global financial crisis, it is still increasing after 2008. Analysis shows that the amount of non-performing assets (NPAs) in the Indian banking industry is significantly impacted by changes in the currency rate, GDP growth rate, and global volatility. According to Zafar,

Maqbool, and Khalid (2013), internal bank issues are to blame for the subpar performance of assets that eventually turn into non-performing assets.

The banks themselves are in charge of limiting the reasons that contribute to non-performing assets (NPAs), and they must reorganize their organization, develop methods for evaluating their credit worthiness, and enhance their overall management and technological efficiency. Examining how well various banks manage their non-performing assets is the main goal of Siraj & Pillai (2013). To assess the trajectory of NPA movements in various banks, a number of indicators are taken into consideration, including Net NPA, additions to NPA, Gross NPA, provisions towards NPA, and reductions to NPA. These characteristics are further contrasted with the banks' micro-performance metrics.

In terms of successfully managing non-performing assets, NB is ranked first overall by the rankings based on NPA indicators, followed by SBI affiliates, foreign banks, and private sector banks. Another research by Rathore, Malpani, and Sharma (2016) looks at Indian commercial banks' non-performing assets (NPAs) as of 2015. It cites a number of external and internal causes that contribute to India's escalating non-performing assets (NPAs). Diverting money for growth or modernization, ineffective credit monitoring and administration, and a lack of cooperation among lenders are some examples of internal issues. On the other hand, external variables include recession, price increases, natural disasters, exchange rate volatility, and more.

The results show that poor management has led to a positive correlation between a bank's net earnings, total loans, and non-performing assets (NPA), which is not a good indicator. It is also shown that one of the causes of the growing NPAs is slow domestic growth. It also makes a number of recommendations for reducing the amount of non-performing assets in banks, including offering compromises to debtors, one-time settlement plans, suing the borrower for non-payment of the loan, and enlisting the aid of debt collection courts and Lok adalats. The study conducted by Narayanan and Surya (2014) identifies the causes of assets becoming non-performing assets and the corrective measures that should be implemented to lower the amount of non-performing assets.

It also seeks to determine if the bank's operations before and after writing down non-performing assets change in any way. According to the report, some of the factors that have been linked to non-performing assets (NPAs) include inadequate follow-up procedures, embezzlement and mismanagement of money, and inappropriate customer selection for providing loans. In consequence, these non-performing assets raise the cost of capital, decrease interest revenue, and lower return on investment. Banks must act proactively in the current environment to manage and reduce the amount of non-performing assets. The Reserve Bank of India and the Finance Ministry must work together to address the issue of non-performing assets.

Das and Dutta (2014) analyze the incidence of non-performing assets in various Indian bank types during a five-year period (2008–2013) to see whether there are any differences. For analytical purposes, SBI affiliate banks and other public banks are taken into account. The ANOVA results show that the incidence of non-performing assets (NPA) does not significantly vary between banks. Overall, it can be said that banks encounter non-performing assets in a similar way, even if their activities vary. Collins & Wanjau (2011) provide yet another important addition to the banking industry when they assess how interest rate spreads affect Kenyan commercial banks' non-performing assets (NPAs).

The research is descriptive in nature and gathers information on loan non-performance and interest rate spread for 43 Kenyan commercial banks using both quantitative and qualitative methods. It is concluded that the interest rate spread indirectly establishes the loan's cost, which ultimately influences asset performance. Because it raises loan costs, the difference between borrowing and lending interest rates affects asset performance. The study also looks at how banks' credit risk management policies affect interest rate spreads and non-performing assets. Since interest rates are benchmarked against the associated non-performing assets (NPAs) and non-performing loans are a result of higher loan costs, it is discovered that credit risk management policies have a distant effect on the banks' interest rate spread. The research concludes by advising banks to evaluate the borrower's creditworthiness, determine the amount of collateral security given, and adjust interest rates appropriately.

II. CONCLUSION

The current article provides a summary of the research that has been done on non-performing assets, the most significant topic in the banking industry. Understanding the conceptual framework of non-performing assets is the focus

of a significant portion of the literature. Stated differently, non-performing assets (NPAs) are assets that no longer bring in money for the banks. Studies have also examined the prevalence of non-performing assets (NPAs) and the variables that contribute to their rise. Among the frequent causes are ineffective credit management practices and lending money to customers without properly evaluating their creditworthiness or goodwill. These elements raise the cost of capital by causing non-performing assets (NPAs) to arise.

However, research has shown that external variables like GDP growth rate and currency rate volatility also have a big influence on non-performing assets (NPAs), therefore internal causes aren't the only ones that cause them to accumulate. Although it is impossible to have zero non-performing assets (NPAs), the central bank and individual banks should make an effort to reduce the amount of NPAs. The presence of non-performing assets may have an impact on banks' net worth, profitability, and liquidity. Numerous studies have identified a number of corrective and preventive measures to stop non-performing assets (NPAs). These include post-monitoring loans, credit appraisal mechanisms, effective credit management policies, evaluating borrowers' credit worthiness prior to making loans, and building strong professional relationships with borrowers to monitor the appropriate use of the loan amount.

In conclusion, non-performing assets (NPAs) are a significant element that impacts the expansion of the banking industry and ultimately impedes a nation's economic progress, particularly in bank-led countries like India. Therefore, in order to address the issue of non-performing assets (NPAs), banks must implement prudential and provisional standards as periodically recommended by the central bank. Additionally, measures should be taken to avoid the occurrence of non-performing assets.

REFERENCES

- [1]. Bollard, A., Hunt, C., & Hodgetts, B. (2011). The role of banks in the economy-improving the performance of the New Zealand banking system after the global financial crisis A speech delivered to New Zealand Shareholders Association Annual Meeting in Tauranga. (August).
- [2]. C.S.Balasubramaniam. (2011). Non-Performing Assets and Profitability of Commercial Banks in India : Assessment and Emerging Issues. Abhinav National Monthly Refereed Journal of Research in Commerce and Management, 1(7), 41–52.
- [3]. Chatterjee, C., Mukherjee, J., & Ratan Das, D. (2012). Management of Non Performing Assets -a Current Scenario. IRJC International Journal of Social Science & Interdisciplinary Research, 1(11), 204–214.
- [4]. Collins, N.J., & Wanjau, Kenneth. (2011). The effects of interest rate spread on the level of non-performing assets: A case of commercial banks in Kenya. International Journal of Business and Public Management.1(1), 58-65.
- [5]. Das, S., & Dutta, A. (2014). A Study on NPA of Public Sector Banks in India. IOSR Journal of Business and Management, 16(11), 75–83.
- [6]. Fotak Veljko (2012), "Why do governments lend?" Paolo Baffi Centre Research Paper Series No. 2012-111.
- [7]. Garg, A. (2016). A study on management of non-performing assets in context of Indian banking system. International Journal of Engineering Technologies and Management Research, 3(11), 15-25.
- [8]. Jadhav, S., Gujarathi, D., & Gawali, R. (2016). A Study of NPA Management at Bank of Maharashtra Nashik District. Abhinav International Monthly Refereed Journal of Research in Management & Technology, 5(1), 26–33.
- [9]. Kaur, K., & Singh, B. (2011). Non-performing assets of public and private sector banks (a comparative study). South Asian Journal of Marketing & Management Research, 1(3), 54-72.
- [10]. Khanna, P. (2012). Managing non-performing assets in commercial banks. Gian Jyoti E-Journal. 1(3), 153-163.
- [11]. Malyadri, P., Sirisha, S. (2011). A Comparative Study of Non-Performing Assets in Indian Banking Industry. International Journal of Economic Practices and Theories, 1(2), 77–87.
- [12]. Mishra, U. M., & Pawaskar, J. R. (2017). A study of non-performing assets and its impact of Banking sector. Journal for Research, 3(1), 1–5.

- [13]. Narayanan, B. B. S., & Surya, R. (2014). A study on non- performing assets in Indian banks. International Journal of Management Research and Business Strategy, 3(3), 144–155.
- [14]. Narula, S., & Singla, M. (2014). Empirical study on non performing assets oh bank. International Journal of Advance Research in Computer Science and Management Studies, 2(1), 194–199. Rathore, D., Malpani, S., & Sharma, S. (2016). Nonperforming assets of Indian banking system and its impact on economy. IOSR Journal of Economics and Finance, 7(6), 21–26.
- [15]. Reddy, P. K. (2002). A comparative study of Non-Performing Assets in India in the Global context- similarities and dissimilarities, remedial measures. Remedial Measures. Retrieved from https://papers.ssrn.com/sol3/papers.cfm?abstract_id=361322
- [16]. Roy, S. G. (2014). Determinants of Non-Performing Assets in India - Panel Regression. Eurasian Journal of Economics and Finance, 2(3), 69–78. Retrieved from <https://doi.org/10.15604/ejef.2014.02.03.005>
- [17]. Selvarajan B., & Vadivalagan, G. (2013). A Study on Management of Non-Performing Assets in Priority Sector reference to Indian Bank and Public Sector Banks (PSBs). Global Journal of Management and Business Research, 13(1), 101- 114.
- [18]. Singh, S., & Makkar, A. (2014). Relationship between crisis and stock volatility: Evidence from Indian banking sector. IUP Journal of Applied Finance, 20(2), 75.
- [19]. Singh, V. R. (2016). A Study of Non-Performing Assets of Commercial Banks and it's recovery in India. Punè Annual Research Journal of Symbiosis Centre for Management Studies, Pune, 4, 110–125.
- [20]. Siraj, K.K. & Pillai, P.S. (2013). Efficiency of NPA Management in Indian SCBs – A Bank Group Wise Exploratory Study. Journal of Applied Finance & Banking, 3(2), 123-137.
- [21]. Srinivas, K. T. (2013). A study on non-performing assets of commercial banks in India. International Monthly Refereed Journal of Research in Management & Technology, 2, 61-69.
- [22]. Zafar, S. T., Maqbool, A., & Khalid, S. M. (2013). Nonperforming assets and its impact on indian public sector banks. International Journal of Marketing, Financial Services & Management Research, 3(2), 68-87