# CHAPTER – I

## RESEARCH AND METHODOLOGY

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1. RESEARCH METHODOLOGY

1.1 INTRODUCTION

Banks are in the business of accepting deposits for the purpose of lending, and act as financial intermediaries between depositors with surplus funds and borrowers who are in need of funds. From the income received or generated from such advances, expenses of management are met.

The banks are using the deposits in lending and investment business. The risk of business loss is equally associated with the lending activities as in other business. The primary role for Govt. and RBI is to limit the risk & loss to depositors and thus maintain public confidence as well as prevent collapse of the banking system. The RBI as a regulatory authority form time to time issues guidelines to the banks and financial institutions for proper credit administration.

Tandon Committee\(^1\) (1975) recommended slotting of borrower’s accounts into four bands as –

a) Excellent
b) Good
c) Average and
d) Unsatisfactory / bad and doubtful accounts.

Accordingly RBI introduced ‘Health Code’ system\(^4\) (1994) for credit administration. Under health code system, the bank loan assets were classified under eight categories such as-

- H C – 1 : Satisfactory
- H C – 2 : Irregular
- H C – 3 : Sick but Viable
- H C – 4 : Sick but Non – Viable
- H C – 5 : Recalled
- H C – 6 : Suit –filed
- H C – 7 : Decreed
In respect of loans which were categorized under health code No 5 to 8, interest on loan not separately charged was booked to profit & loss accounts. However, charging of interest provisioning and also paid tax and dividend on the income were left to be decided by the bank. These guidelines were subjective & did not reflect the true picture of the bank health.

Pendharkar Committee\(^2\) (1981) was set up, “which recommended the classification of advances in different categories, to index the overall quality of the assets portfolio”. It was starting point for the introduction of the health coding system of categorizing bank loan portfolio by the RBI in 1985.

Further the Reserve Bank of India being an authority for bank supervision felt the need to introduce more objectivity in the assessment of the bad debts of the banks and introduced standard relative accounting norms as per international standards for maintaining sound banking system in the country.

As new norms to define the implementation of Narsimham Committee\(^3\) (1991) the above objective norms and desperate accounting practices were given up, and were replaced by objective and more scientific criteria based on prudential norms of income recognition, assets classification, provision and capital adequacy. The Committee submitted its report in November 1991.

Since 1992, the banking sector reforms were introduced which faced new challenges in the ever changing scenario. The challenges were many amongst them vital challenges were “4 Cs” i.e. Credit, Customer, Computer, and Capital Restructuring. In the changing scenario, the banks are under tremendous pressure to redefine their priorities, in order to manage these challenges effectively for their survival and growth.

### 1.2 STATEMENT OF THE PROBLEM

In a fast changing banking environment of today the very survival of a banking organization depends on level of the income generated through optimum use of assets after paying the cost of funds for acquiring them and other administrative costs involved therein. Once the assets cease to contribute the income, they are termed as Non Performing Assets, which not
only have cost of funds involved but also require to be operated as per prudential norms.

One of the major problems being faced by banks and financial institutions in India is that of bad debts termed as “Non Performing Assets” (NPA). There are many reasons for the sorry state of affairs and major among them are 1) Political interference, 2) Poor low enforcement, 3) Archaic laws and procedures, 4) Corruptions at various levels and competition in various banking institution, 5) Flow of Funds.

As after considering the importance of such a strategic affairs in Indian banking industry it is felt necessary to carry out a study entitled “A Critical Study of Non Performing Assets of Commercial Banks in Maharashtra - An Intersectoral Comparison”

After the Nationalization of banking sector, the Indian banking and financial system has made commendable progress in extending in geographical spread and financial reach. The banking industry in India is also undergoing rapid changes with the introduction of financial sector reforms and follow-up actions by Reserve Bank of India based on the Narasimham Committee recommendations.

However before 1990 the Indian banking business was on the way to dismal performance. Most of the nationalized, private and co-operative sector banks outwardly were sharing profits, but in reality they were fictitious. As a result the basic elements of the banking system were getting shattered.

M. Narasimham committee was to examine all aspects relating to the structure, organization, functions and procedures of the Indian financial system. Narasimham Committee gave preference to the prudential norms of income reconstruction, assets classification and provisioning for the advance portfolio of the banks and recognition of non performing assets and gradually strengthening the financial position of banks. Hence, RBI issued strict adherence to the norms suggested by Narasimham Committee and that the same have been implemented in almost a decade by now.

It is the right time therefore to take a review of the performance of NPAs in various banks. The proposed research is an attempt to go deep into some of
the aspects of this very vital area of banking sector. Banks and financial institutions do not have much control over external factors which may include natural calamities, changes in Govt. policies, adverse effects of cyclical changes, etc. But internal factors are within the reach of these institutions. It is significant to study such internal factors and analyze them carefully so as to formulate suitable strategies to prevent the growth in NPAs.

1.3 OBJECTIVES OF THE STUDY

The beginning of 1990s is seen as a period of dramatic change in the banking and finance world. Changes resulted from Governments led deregulation, liberalization and increasing competition within the industry.

The study basically aims at establishing a linkage between internal efforts of bank and financial institution and growth of NPAs. In other words, growth in NPAs can be checked considerably if bank and financial institutions have suitable internal arrangements. The profitability of the financial institution largely depends upon the level of income generated through optimum use of the assets after paying the cost of funds for acquiring them and other administrative cost involved therein. Once the assets cease contributing to the income, they are termed as Non Performing Assets. The study is related to internal systems, procedures and practices, for monitoring of NPAs and recovery from the same. The research work has undertaken inter sectoral comparison of NPA of selected banks with the specific objectives, they are as follows:

1) To examine the nature and the problem of the NPA position in selected Banks.
2) To study recognized income of the selected banks.
3) To study the classification of assets into different categories of the selected banks.
4) To study the value of security of selected banks.
5) To examine the advances secured against certain instruments.
6) To make an Intersectoral comparison of NPA and other variables in the selected banks.
7) To examine the steps taken for recovery in respect of NPA accounts.
8) To make specific recommendations on the basis of research work carried out.

1.4 HYPOTHESES OF THE STUDY:

1) The loan sanction procedure prevailing in the bank is prominent causing factor for increasing NPA in cooperative and private commercial banks.
2) Increasing NPA has affected on survival of the bank.
3) Asset classification can be modified for minimizing NPA provisions.
4) The management of NPA is done more effectively by private sector banks as compared to cooperative sector banks.

1.5 RESEARCH METHODOLOGY ADOPTED:

1.5.1 Methodology of the work
 Present thesis is outcome of research conducted by researcher adopting survey method. A survey research is usually based on the sample survey or census survey. The present work uses the sample survey method, details of which are given below-

A) Universe
 For the sample survey universe is 27 private sector scheduled commercial banks and 57 urban co-operative banks presently functioning in Maharashtra and three banks from each of the sectors situated in Pune, Satara, and Kolhapur Districts have been selected on the basis of convenience for study in hand.

B) Sampling of banks
 The number of total scheduled commercial banks in India is 57, in which Public Sector Banks are 27 and Private Sector Banks are
There are 73 co-operative scheduled banks in India out of which 30 banks are in Maharashtra. The study covers 3 banks from each of the sectors on convenience basis. Thus the study covers 11.11% private sector banks and 10% cooperative sector banks functioning in Maharashtra.

Table No 1: Sample Size

<table>
<thead>
<tr>
<th>Banks</th>
<th>India</th>
<th>%</th>
<th>Maharashtra</th>
<th>%</th>
<th>Sample</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Private Sector</td>
<td>57</td>
<td>43.85</td>
<td>27</td>
<td>47.36</td>
<td>3</td>
<td>11.11</td>
</tr>
<tr>
<td>Co-operative</td>
<td>73</td>
<td>56.15</td>
<td>30</td>
<td>52.63</td>
<td>3</td>
<td>10.00</td>
</tr>
<tr>
<td>Sector</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>130</td>
<td></td>
<td>57</td>
<td></td>
<td>6</td>
<td></td>
</tr>
</tbody>
</table>

The private sector banks selected are:
1) The United Western Bank Ltd., Satara
2) The Ratnakar Bank Ltd., Kolhapur

The cooperative sector banks selected for the purpose of study are:

1) The Karad Urban Cooperative Bank Ltd., Karad
2) The Ichalkaranji Janata Sahakari Bank Ltd. Ichalkaranji
3) Janata Sahakari Bank Ltd., Pune.

All the banks have their head offices in Western Maharashtra.

While deciding selection of banks, the researcher has also seen that those banks should be large in size and growth, and establishment. All the banks selected have more than 45 years of length of operations and all have received Audit Class ‘A’ for their banking operations. As the head offices of the banks are situated in Western Maharashtra data collection was convenient for the researcher.

1.5.2 Data Collection:
For the study in hand primary and secondary data have been utilized:

**Primary Data:** The primary data is collected through questionnaire administered to CEOs, AGMs, Branch Managers and NPA borrowers of the banks covered under the study.

**Table No 2 : Break-up of Responses of Sampled Employees**

<table>
<thead>
<tr>
<th>Name of banks</th>
<th>No of employees interviewed</th>
<th>CEO</th>
<th>AGM</th>
<th>Branch Manager</th>
<th>Borrowers And others</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Private Sector</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>The Ratnakar Bank Ltd</td>
<td>12</td>
<td>1</td>
<td>2</td>
<td>4</td>
<td>5</td>
</tr>
<tr>
<td>The United Western Bank Ltd</td>
<td>14</td>
<td>1</td>
<td>4</td>
<td>2</td>
<td>7</td>
</tr>
<tr>
<td>The Ganesh Bank of Kurundwad Ltd</td>
<td>16</td>
<td>1</td>
<td>4</td>
<td>4</td>
<td>7</td>
</tr>
<tr>
<td><strong>Co-operative Sector</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>The Ichalkaranji Janata Sahakari Bank ltd</td>
<td>10</td>
<td>1</td>
<td>2</td>
<td>2</td>
<td>5</td>
</tr>
<tr>
<td>The Karad Urban co-op Bank Ltd</td>
<td>10</td>
<td>1</td>
<td>3</td>
<td>2</td>
<td>4</td>
</tr>
<tr>
<td>Janata Shakari Bank Ltd</td>
<td>9</td>
<td>1</td>
<td>3</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>71</td>
<td>6</td>
<td>18</td>
<td>16</td>
<td>31</td>
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</table>

In the same manner some opinions of the respondents mentioned earlier were collected through personal discussions and their comments on views of the researcher. Some amount of data was also collected from inspection of record.

**Secondary Data:** Since the study is related to financial problem concerning banks it was obvious to rely on the secondary data in the published form which is extensively used for the purpose of the study in hand. Annual Reports from 1998 to 2007, bank publications, circulars, RBI notifications as to NPA Accounts, RBI Publications as to NPA comprising guidelines, NPA Reports, classification of assets by RBI etc. are the published data used. This process is further supplemented by extensive library research reviewing news papers, periodicals, magazines, articles on NPA etc.
From the analysis of annual reports standard assets, sub standard assets, doubtful assets, loss assets, net advances and net NPA amounts of the sample banks covered under study for the period 1998 to 2007 have been calculated and analyzed for the purpose of study.

1.5.3 Statistical Tools Utilized:

Entire data related to NPA is financial in nature which required careful scrutiny for which relevant statistical tools have been utilized as per the need of the study-

1) Percentages and
2) Comparative statements

1.6 SCOPE AND LIMITATIONS OF THE STUDY

The scope of the study is restricted to the selected banks and the area specified in methodology. The geographical limit of the study confined to three districts of Western Maharashtra i.e. Pune, Satara and Kolhapur. Unfortunately some banks were merged into some other banks which has caused a major hurdle in data collection which has hampered the research work. As researcher is a junior level bank employee time remained a major constraint at all phases of the study. Time limit was confined to 31st March 1998 to 31st March 2007.

1.7 CHAPTER SCHEME

The entire research work is divided in Six Chapter

Chapter – I Research Methodology: Introduction, Statement of the Problem, Objectives of the study, Hypotheses of the Study, Methodology, Data Collection, Statistical Tools Utilized, Scope and Limitations of the study and detailed Chapter Scheme.

Chapter – II Conceptual Background and Review of Literature: Conceptual Background, Meaning and Definitions of NPA, RBI Guidelines for
NPA Norms, Suggestion of various guidelines of RBI, Review of Literature, Conclusion.


Chapter – V Analysis of NPA in Selected Sample of Banks: Introduction Gross NPAs to Gross Advances Ratio, Net NPA to Net Advance, Gross NPAs and Net NPAs to Total Assets, Conclusion.

Chapter – VI Inter Sectoral Comparison of Selected Banks: Introduction, Sectoral Comparison of Classification of Assets, Sectoral Comparison of Recovery Mechanism, Sectoral comparison of NPA provision on profit, Conclusion.

Chapter–VII Observations, Recommendations and Conclusion of the Study: Observations of the study, Recommendations made by the researcher, Suggestions offered and Conclusion.
REFERENCES: