7.1. Summary

The banking sector exercises an imperative role in economic growth of a country. By way of providing services, the banking sector becomes an integral part in creation, allocation, trade and utilization processes in the economic system. It fosters the flow of funds in an economy and fuels economic growth. Thus, the efficiency and effectiveness of banking system determines the swiftness of advancement of an economy. Alike any other business enterprise, the competence of a bank is evaluated based on profitability and quality of assets it possess.

On an assessment of Indian banking industry during the pre-liberalization era, it has been observed that the banking sector suffers from several shortcomings which in turn lead to reduction in productivity, deterioration in asset quality and efficiency and increased cost structure due to technological backwardness. Maintenance of the asset quality is a prime concern for a bank as it impacts various performance indicators, i.e. profitability, intermediation costs, liquidity, credibility, income generating capacity and overall functioning of banks. This reduction in asset quality results in accumulation of Non-Performing Assets (NPAs) which mounted so high causing a threat to the existence of banking industry. The NPAs has far reaching implications on the financial health of the banks. The banks are required to make adequate provisions in their financial statement to account for the losses expected to arises from non performing assets. This dents the profitability of the banks for considerable period of time. Besides that, it also involves allocation of significant task force in managing, monitoring and recovering the funds tied up in NPAs.

The banking sector reforms in India during the post-liberalization period primarily aimed at improving the efficiency of the banking sector by incorporating prudential
norms for income recognition, asset classification and reduction in the level of NPAs. The alarming level of NPAs has been recognized as one of the major problems which demands structural changes and reform measures in the banking sector during this period. For this purpose, many committees were set up from time to time to make suitable suggestions to avert this kind of problem in banking sector. The prominent among those, Narsimham Committee, need special mention. The committee was set up and many prudent suggestions were made. Among the major suggestions and recommendations which are being followed nowadays by banks are gradual reduction of Statutory Liquidity ratio (SLR) and Cash reserve ratio, directed credit programme, issuing more banking licenses, autonomy to banks, removal of banks from the concept of nationalizations, facilitating foreign banks operations in India, liberalizing interest rate regime and structural issues of banks, etc. The reduction in SLR and CRR requirements enables banks to lend more as they are required to hold less cash to meet the mandatory requirement specified by Reserve Bank of India. It is estimated that 25 basis point reduction increases availability of money to the extent of Rs 30,000 crores in the system. The committee recommended allowing foreign banks to set up their own branches fully owned by them and not necessarily in alliance with banks in India. This facilitated banks like City Bank to start its operations in India and provided a competitive field to public sector and private sector banks in India. In order to ensure continuity of various rural industries like cottage industry, handloom and textile industry, the committee suggested lending under direct credit programme which has helped in protecting employment of various unskilled workers in rural part of our country. The committee suggested that the banks shall have the liberty to decide their lending and deposit rate and Reserve banks of India shall provide base rate. This suggestion has significantly enhanced the operations of the banks and ensuring their profitability besides adding competition among them. With regard to the autonomy of the banks in the recruitment process, the banks have not been given full autonomy as suggested by the committee as the test are conducted in coordination with Government agencies to find suitable candidates for appropriate post. One major development, however, in this regard has been appointment of directors in the board of banks which is
now through the shareholders in the Annual General meeting. The process of dual
control on Banks through Ministry of Finance and the Reserve Bank of India was also
recommended to be removed. Since, most of the time the directions issued by the
Ministry of Finance were found inconsistent with the policies to be adopted by the
Reserve Bank of India. Another noteworthy development that took place in the banking
sector in India was the concept of Banking Ombudsman through a notification issued
by the Reserve Bank of India under section 35A of the Banking Regulation Act, 1947.
Under this provision if any customer has any complaint against the bank, he can directly
approach to the Banking Ombudsman for resolution of his complaint. However, before
approaching the Banking Ombudsman, the complainant has to approach the concerned
bank and submit his complaint in writing. In case the bank does not reply within one
month of the receipt of complaint or the complainant is not satisfied with the solution
given by the bank, he can then file his complaint before the Banking Ombudsman, who
act as Arbitrator between the concerned bank and the complainant. The Banking
Ombudsman is either the chief General Manager or General Manager of the Reserve
Bank of India. Thus, various steps have been taken in the banking system to make it
attractive proposition for the general public to avail its services through lending and
deposit money and accessing other services. Apart from the recommendations of
Narsimham Committee which tremendously changed the role of Banking system in
India, another committee at the international level i.e. BASEL committee of Banking
Supervision also led to phenomenal change in the functioning and adding to the
strength of the banks besides inculcating financial discipline habits in their lending
norms. BASEL committee has issued three different norms at different point of time,
the latest one in the year 2010. These norms are to be abided with all the banks in the
world. The main focus of these norms were to strengthen the capital adequacy of the
banks and linking the same with the amount of risk being undertaken by the banks
while granting loans for different purpose. As we know, banks earn their income from
the spreads available on the deposit rate and lending rate. The higher the value of the
spread or the difference between the deposit and lending rate, more will be the income
of the banks. Further, the risky proposals are financed at higher rate whereas less risky
proposals are financed at lower rate. With these conditions at the background, banks are normally tempted to finance high risky areas so that their profitability will be more through higher difference in spreads. But in such a case, the banks are likely to add more Non Performing Assets if the proposal for which the loan has been granted gets into any kind of problem and the borrower fails to repay the interest or principle money.

The Basel norm therefore divided loans of the banks in different categories and assigned risk weights to different loans ranging from 0% to 125% and so on. The banks are required to examine their asset in the form of loan considering the risk weights and accordingly required to maintain 8% of the minimum capital, as per the first norms recommended by Basel committee. Gradually, the norms were further improved to account for operating and market risk apart from credit risk as advocated in the first set of norms. Besides the minimum capital, the banks were also required to maintain capital conversion buffers so as to prevent themselves from any kind of unforeseen economic shocks or risk in the financial system. The procedure of stress test was also specified and conducted to examine the financial health of the banks at any given point of time and to check their ability to endure any kind of worse economic event.

Almost two decades have completed since the banking sector initiated measures to uplift the banking sector in line with international standards and to improve productivity and efficiency of banks. But even today, NPAs still pose a significant threat to the banking sector and continues to damage it. Many researches on NPA depicted the relationship between asset quality and financial distress and considered management of NPA as a major prerequisite to counter the recessionary pressures and foster economic development. With this backdrop, the current research attempts to conduct a study on reduction of non-performing assets in commercial banks. This research is an attempt to examine the impact of NPA on bank performance with special reference to Alwar district and also to evaluate and understand in detail the intensity and propensity of NPA in commercial banks. Initially a small survey study was conducted in Alwar district to examine the presence and utility of banking services in Alwar alongwith the customers’ profile and their perception towards the banking services. Two different questionnaire – one meant for customers and the other meant for Bank professional...
were designed and the convenience/judgemental sampling technique was employed to select the respondents. Different aspects relating to customers such as extent of their borrowing, purpose of borrowing and commitment to repay was assessed along with their satisfaction level from the available banking services. The bank professionals/employees were also served with a questionnaire to seek their opinion with regard to frequency of transaction, method of selection of borrowers, amount of loan applications, profile of borrowers, time taken to disburse the loan, etc. The questionnaire was designed after having insight of the economic and industrial activity in Alwar over last one decade. The study concluded that the bankers are optimistic about the increasing trend of economic and industrial activity in Alwar and offers good scope of business for them as the large segment of society after seeking education is gradually transforming their traditional lifestyle. This is leading to transformation of their entire lifestyle and gradual shift from their previous profession of earning their living through animal husbandry, cattle feeding, agriculture, etc to work in industries and corporates. At present, the majority of the account holders in Alwar district are individual and very few corporates are having their accounts in Alwars. Consequently, the total exposure in the loan portfolio of any bank through corporate borrowers or individual borrowers is very nominal and offers little scope for turning out to be non-performing assets. The study has therefore been conducted taking into perspective the total loan portfolio of banks and seeking the opinion of bankers in Alwar district on that perspective. The study besides discussing the causes and trend of NPAs of different kind of banks in India also describes various legal recourses, such as One time Settlement Scheme, Debt Recovery Tribunal, Lok Adalats and SARFAESI Act, 2002, etc. were also enacted to facilitate the banks in dealing with the problems of NPAs. Though, NPA issues in banking offers one ample scope of research, but this study has been conducted with a view to examine following issues:

i. History and development of Banking system in India
ii. Reforms in Banking sector in India
iii. Generation of NPAs
iv. Causes of Non Performing Assets
v. Trends of Non Performing Assets
vi. Sectors mainly contributing to Non Performing Assets
vii. Legal remedies available with banks for recovery of NPAs.
viii. To see whether different types of banks have significantly different NPAs. This objective is obtained by using a one-way ANOVA analysis.
ix. To extrapolate the trend in the movement of NPA over time and across different types of banks which are divided into four broad categories viz. Scheduled commercial banks, public sector banks, old private sector banks and new private sector banks. This objective is obtained by drawing a trend line for various types of banks for various NPA measures.
x. To examine the relationship between NPA of banks and macro economic variables. For the purpose of current study, three macro economic variables are taken i.e. inflation, GDP and industrial production.

Both secondary and primary data analysis has been used for studying in detail the objectives mentioned above. As a first step, a secondary data analysis has been carried out. To add robustness to the results obtained by secondary data analysis, primary data analysis has been carried out.

7.2. Research Methodology

In the current study, a mixed method approach has been adopted to achieve the above mentioned objectives. For the purpose of adding robustness and reliability to the results, both primary and secondary data analysis has been carried out.

For carrying out secondary data analysis, differential statistics has been used in the current study for two purposes. Firstly, to see if there is any significant difference between various NPA measuring variables amongst different categories of banks over a period of 12 years. For this purpose, one-way analysis of variances (ANOVA) has been used. Secondly, to do a trend line analysis to see the trend of various categories of banks for each NPA measuring variable over a period of 12 years starting from 2002 to 2013.
Besides this, associational inferential statistics has also been used in the current study to see the impact of macroeconomic variables i.e. inflation, industrial production and gross domestic production (GDP) on NPA of various categories of banks. For this purpose, multivariate regression analysis has been carried out.

To understand in detail the intensity and propensity of NPA on commercial banks, a primary data analysis is carried out by using a survey tool - questionnaire. Since the bankers are the best judge to evaluate the various facets of NPA as they are closely involved in lending/advances and its follow-up on a day to day basis, therefore, for this purpose, a primary data has been collected from the staff of the banks, with special reference to officers working with State Bank of India (SBI). The data collected using a structured questionnaire has been analyzed using various statistical tools and techniques and packages like Microsoft Excel, SPSS.

The main findings of the study are summarized below:

i. The size of NPA in Public Sector Banks significantly increased during the period 2007 onwards and the same has been substantiated and proved through various indicators of NPA used in the study. This necessitates an immediate action for developing various control techniques which can resolve the problem and does not allow its further proliferation.

ii. Among the various categories of banks, old private sector banks were observed to have lowest NPAs. This can be attributed to the fact they are not required to undertake the loan approvals with social objective as one of the major objective as in case of Public Sector banks.

iii. The strategies and concern towards reducing and controlling NPAs has proved to be effective as observed from various indicators of NPA in the sample period. The Gross NPA percentage as well as Net NPA percentage was observed to be at relatively higher level in the beginning and at the end of the sample period i.e. 2002 to 2012.
iv. The interrelationship between various NPA indicators – Gross NPA as percentage of gross advance, Gross NPA as percentage of total assets, Net NPA as percentages of gross advance, Net NPA as percentage of total assets and economic indicators GDP, Industrial production and inflation, when measured through multiple regression analysis was found to be statistically significant in case of Scheduled Commercial Bank, Public Sector Banks, New private sector banks and Old private sector banks except two instances where inflation is not statistically significant for Net NPA as % of net advances of public sector banks and new private sector banks.

7.4. Contribution of the Present Study

A well developed banking system is imperative for the economic development of a country. The data analysis revealed a decrease in the quantum of NPAs over the years but still there is a long way to go to enhance the financial prudence of the Indian banking sector. This study realised the need for further reforms in the banking sector and initiate measures to further enhance NPA management. In this regard, following contributions were made by this study:

1. The current study by conducting both secondary and primary data analysis arrives at conclusions which are more robust and reliable.
2. The current study has adopted a triangulation approach by doing ANOVA analysis, trend analysis and regression analysis.
3. Current study by conducted an elaborate study over a span of ten years has very richly augmented the existing relevant literature.

7.5. Limitations and Scope for Further Research

The current research although being extensive in nature, does not cover every researchable area related to NPAs of banks and thus following are a few suggestions for further research:
1. Current research is conducted to see the impact of NPA on bank performances all over India as Alwar being small area, only few bankers could be interacted.

2. Current research is limited to India only whereas research on NPAs across the globe may be carried and comparative analysis may be conducted.

3. In the current study, post liberalisation time period has been taken for the purpose of analysis. Similar research may be conducted in a different time frame.