CHAPTER 12

CONCLUSION

12.1 Major Observations and Findings

12.1.1 An analysis of the data pertaining to the 26 PSU banks from 1996 to 2011 shows that the credit risk management in PSU banks in India has gradually improved over the period from 1996 to 2011. The average and median Gross NPA percentages for 1996 were 18.12 and 16.10, respectively which improved considerably over the years so much so that the average and median Gross NPA percentages for 2011 were considerably lower at 2.31 and 1.92, respectively.

12.1.2 The study also tried to find an answer to the question whether the PSU banks in India are a homogenous lot with similarity in credit risk management. The study disclosed that there is a marked divergence amongst the PSU banks inter-se in the matter of credit risk management. There was also evidence that though there is divergence amongst the PSU banks, the degree of
divergence has narrowed and has shown a declining trend over the period from 1996 to 2011. However, the divergence, despite the decline, cannot as yet be said to be insignificant and the PSU banks have not reached a stage where they can be said to be a homogenous lot in the area of credit risk management.

12.1.3 In 1996 the maximum Gross NPA percentage was 38.00 and the minimum was 5.68 with a standard deviation of 7.41 which shows the inconsistency and wide variation in the credit risk management practices of PSU banks at that time. The data compiled in the course of the analysis shows that over the years from 1996 to 2011 the difference between the maximum Gross NPA percentage and the minimum Gross NPA percentage declined considerably and so did the standard deviation. In 2011 the maximum and minimum Gross NPA percentages stood at 3.50 and 0.91, respectively with a standard deviation of only 0.65. This clearly indicates convergence in the credit risk management practices in PSU banks in India.

12.1.4 Despite the growing convergence in the credit risk management practices of PSU banks in India the performance of various PSU banks on the credit risk management front still cannot
be said to have come to a common standard level. Some PSU banks have managed their credit risk very well but there are many PSU banks where there is still a great scope of improvement in credit risk management. An analysis of the Net NPA percentages of the 26 PSU banks in India as on 31\textsuperscript{st} March, 2011 shows that while Bank of Baroda had the minimum Net NPA percentage at 0.35, UCO Bank had the maximum Net NPA percentage of 1.84 which was more than 5 times the Net NPA percentage of Bank of Baroda. Though the average Net NPA percentage came to 1.01 giving the impression that the credit risk management in PSU banks was satisfactory, there were 12 PSU banks with Net NPA percentages above the average signifying lack of proper credit risk management. The 12 PSU banks were the State Bank of India, Canara Bank, IDBI Bank, Union Bank of India, Indian Overseas Bank, UCO Bank, United Bank of India, Vijaya Bank, State Bank of Patiala, Bank of Maharashtra, Dena Bank and State Bank of Mysore. The State Bank of India had a high Net NPA percentage of 1.63. This shows that despite the convergence, credit risk management in various PSU banks inter-se still differs and there is ample scope of further improvement in credit risk management in almost fifty percent of the total PSU banks in India.
12.1.5 The analysis also shows that the credit risk management by PSU banks in India has been more effective at lower lending rates of interest. Gross NPAs in PSU banks have a positive relationship with the lending rates of interest and as the lending rates go up, the Gross NPAs also increase. With lending rates at 12.65% in 1996 the Gross NPA percentage was 18.12. The lending rates lowered gradually from 1996 to 2008 and the Gross NPA percentage also reduced. The lending rates in 2008 were 8.74% and correspondingly the Gross NPA percentage came down to 1.93. After 2008 the lending rates had an upward movement and did the Gross NPA percentage. In 2011 the lending rates increased to 10.50% and correspondingly the Gross NPA percentage in PSU banks in India also increased to 2.31.

12.1.6 With the economic slowdown setting in 2008 accompanied by rising inflation the Reserve Bank of India took measures to curb money supply with measures like increase in CRR and repo rates. This forced the PSU banks to increase their lending rates. With the increased lending rates the Gross NPA percentage in PSU banks also went up. This shows that intervention in the money market by the Reserve Bank of India also has an affect on credit risk management by PSU banks in India.
12.1.7 The study also showed a recent unhealthy development in the sphere of credit risk management by PSU banks in India. There is a startling growth in corporate restructuring of loans in recent years with PSU banks increasingly resorting to debt restructuring. The ratio of restructured standard advances to gross advances as on 31\textsuperscript{st} March, 2009 stood at 3.03 for PSU banks in India whereas the ratio was 2.73 for all banks in India taken together. The ratio has risen considerably, and the ratio for PSU banks in India increased to 5.73 as on 31\textsuperscript{st} March, 2012 whereas the ratio for all banks in India taken together stood at only 4.68. PSU banks in India are resorting to debt restructuring much more than their private sector counterparts as the ratio of restructured advances to gross advances as on 31\textsuperscript{st} March, 2012 for private banks stood at only 1.61 against a ratio of 5.73 for PSU banks in India.

12.1.8 Non performing assets in some PSU banks in India are at dangerously high level with the State Bank of India alone saddled with around Rs. 50,000 crores of NPAs as on 31\textsuperscript{st} March, 2012. Of the five banks in India having highest level of NPAs as on 31\textsuperscript{st} March, 2012 four were PSU banks – State Bank of India with NPAs of Rs. 49,202.46 crores, Punjab National Bank with NPAs of Rs.
14,023.88 crores, Bank of India with NPAs of Rs. 8,898.60 crores and Central Bank of India with NPAs of Rs. 8,507.37 crores.

12.1.9 The study also attempted to find an answer to the question whether the conventional credit risk management practices followed by PSU banks in India are insignificant. The answer to the question was obtained by using regression analysis with the null hypothesis that the conventional credit risk management practices in PSU banks in India are insignificant and do not have an impact on the efficacy of the credit risk management practices in PSU banks in India. The regression analysis resulted in rejection of the null hypothesis and it was established that the conventional credit risk management practices in PSU banks in India are significant and effective.

12.1.10 PSU banks in India have well defined credit risk management architecture. The credit risk management architecture of larger PSU banks are more elaborate than that of relatively smaller PSU banks. The State Bank of India has a very elaborate multi layered risk management architecture and the framework visualizes empowerment of business units at operating level with
technology as the key driver, enabling identification and management of risk at the place of origination.

12.1.11 The PSU banks in India have migrated to Basel II with Standardised Approach for credit risk. Larger PSU banks, like the State Bank of India and Bank of Baroda, are in an advanced stage of implementing the more complex Advanced Approach under Basel II. Smaller PSU banks are not that well equipped as yet to adopt the Advanced Approach. The State Bank of India has conducted comprehensive risk awareness exercise which has enhanced risk awareness at operational level. In other PSU banks the risk awareness at operational level still needs to be further enhanced.

12.1.12 All the PSU banks in India follow similar guidelines for identification of non performing advances. Such guidelines are notified by the Reserve Bank of India and all the PSU banks follow the guidelines so issued.

In the matter of credit rating also PSU banks in India follow similar practices and follow the guidelines issued by the Reserve Bank of India. All the PSU banks in India accept the ratings of all the
Reserve Bank of India approved External Credit Assessment Institutions (ECAI) namely, CARE, CRISIL, Fitch (India) and ICRA for domestic exposures. For international exposures ratings of Standard & Poor, Moody’s and Fitch are accepted.

12.1.13 Each PSU bank in India has a defined Credit Risk Management Policy in place. The instruments and tools used for credit risk management are more or less similar but due to better awareness and more emphasis on training of staff in larger PSU banks, the use of such instruments and tools is better in larger banks. In the matter of risk measurement the State Bank of India has an elaborate system and there is a large scope of improvement in the area of risk measurement in other PSU banks in India.

12.1.14 The techniques used for credit risk mitigation are more or less similar across the PSU banks in India. PSU banks in India mostly resort to the traditional methods for controlling credit risk like credit rationing, credit limits, collaterals, loan pricing etc. Amongst the newer methods PSU banks have adopted some of these methods like asset securitization and loan sales but these methods are being used with a lot of reluctance. PSU banks in India are, however, yet to adopt the recently developed modern methods of credit risk mitigation and
transfer like credit derivatives, credit default swaps, credit options and credit linked notes. Banks abroad have successfully used these modern methods for improvement in their credit risk management.

**12.1.15** Study and analysis of credit risk management by banks abroad shows that there is no evidence that there is any universal set of best practices for credit risk management. Thus there is no assurance that successful credit risk management practices in say, the United States, will succeed in India with different institutional settings and other dissimilarities. The study also shows that the global financial crisis and the European sovereign debt crisis are bound to have an impact on the credit risk management in PSU banks in India. Looking ahead, the current economic recovery is very slow and fragile and there will be more problems ahead and the credit risk management by PSU banks in India has to factor in these problems.

**11.1.16** The study shows that PSU banks in India have achieved most of the computerisation under the Core Banking Solution (CBS) which by itself does not prepare them adequately for the necessary MIS and analytical tools required for efficient credit risk management. In order to upgrade the risk management systems, PSU banks in India need to upgrade their technology proportionately so that the MIS and the
analytical tools for credit risk management are available. This will entail large investment in training of staff and technology, particularly for those PSU banks which have to migrate to the advanced approaches under Basel II.

12.1.17 The study also disclosed that while there is a corporate debt restructuring (CDR) cell for large loans, there is no such CDR cell for small loans with the result that NPAs resolution for small borrowers in the PSU banks in India takes a very long time and there is an urgent need to establish a CDR cell for small loans to improve credit risk management in PSU banks in India.

12.1.18 The study also shows that PSU banks in India have the tendency to specialize in certain industries or geographical areas or business houses due to the convenience in collecting information and the convenience of familiarity. Almost half of the bank loans are concentrated in just two sectors – infrastructure and basic metals and metal products. PSU banks in India need to avoid such credit risk concentration for better credit risk management.

12.1.19 For improvement in credit risk management in PSU banks in India it is imperative that the PSU banks curb the practice of promoting
the financing of politically attractive projects rather than the economically efficient ones.

12.1.20 The study also shows that introduction of Basel II has improved credit risk management and disclosures in PSU banks in India.

12.1.21 There is no effective framework for pooling and sharing of credit information amongst PSU banks in India which if implemented can go a long way in enabling PSU banks to streamline their credit appraisal framework and also instill greater discipline amongst their borrowers. The satisfactory credit risk management in the Chilean banking sector is largely attributed to the good information sharing system. PSU banks in India can substantially improve their credit risk management by adopting an effective framework for pooling and sharing of credit information.

12.1.22 PSU banks in India tend to lay more emphasis on deposits than on advances. Taking the typical financial intermediation role of PSU banks in India, deposits should be taken as an input, but the PSU banks in India tend to covet deposits as an independent output and being risk averse tend to focus more on deposit mobilization than on credit expansion and improvement in credit risk management. Such an
approach and attitude in PSU banks in India needs to change for improvement in credit risk management in PSU banks in India.

12.2 Suggestions for Further Research

The credit risk management in PSU banks in India and in the banking sector in India in general provides a vast area for the researchers. Some of the potential areas that can be investigated in the Indian context are as follows:

1. Investigation into the credit risk measurement by banks in India and the impact of credit risk measurement on the determination of risk premium in the pricing of loan products offered by banks in India.

2. Investigation into the On-Balance Sheet and Off-Balance Sheet credit risk exposures and related credit risk management practices of PSU banks in India.

3. Investigation into credit risk mitigation by PSU banks in India – covering both the traditional methods like loan pricing, credit
rationing etc. and the newer methods like credit derivatives, credit default swaps, credit options etc.

4. Investigation into the credit risk management governance and risk management architecture of PSU banks in India.