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Recovery management of non-performing assets in scheduled commercial banks in India

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Abstract

Providing financial assistance to the needy is an essential function of a banker. By meeting the financial requirements of various segments of the society, banks contribute to the economic development of our nation. Banks and financial institutions have heavily financed industries both corporate and individual. Large sums remain unrecovered and the normal process of recovery of debts through the courts is lengthy. Institutions face considerable difficulties in recovery of dues and enforcement of securities charged to them due to delay in legal processes. A significant portion of their funds are thus blocked in unproductive assets, the values of which deteriorate over the period of time. Banks and financial institutions also spend substantial amounts on legal charges, which add to their overheads Recovery of debt is a difficult task and involves a lengthy process. The recovery process begins with issuing notices to the borrowers and ends with sale of property and recovery of debt. Recovery of bank dues is attained by legal and non-legal measures. The legal measures include recovery of debt through DRTs, SARFAESI Act, Lok Adalath, ARCs and the like. The non-legal measures consist of the reminder system, recovery camp, rehabilitation of sick units, restructuring of debt, compromise, reschedulement, and write-off, etc. The adoption of proper methods depends upon the amount of loan, type of security offered, nature of default and the like. It is evident from various studies that majority of the banks recovered the loan amount through OTS/ Compromise settlement. The provisions of the other recovery mechanisms will work well if it is effectively used. Because of the loopholes in the legal and non-legal measures followed by the banks, they find difficult in recovery and delay in recovery of dues.

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The success of lending and recovery is possible only through the proper attention and concerted efforts by all stakeholders like regulators, policy makers, banks and bank customers.

Key words:*NPAs, Recovery, legal and non-legal measures, SCBs and RBI*

Introduction

Diversion of funds for more profitable business other than the original one expansion, modernisation, undertaking new projects and for helping associate concerns are the major factors contributing to NPAs. It is well known that bulk of the amount locked up in NPAs has been caused due to snags in legal system. Banks provide working capital finance by hypothecation of movable properties. But it is to note that neither Indian Contract Act nor transfer of Property Act contain any provision for defining hypothecation, rights and obligations of the hypothecator or hypothecate. Now, as a consequence of default in payment of bank dues, right to take hypothecated security is not available to banks and in case borrower refuses to give possession of hypothecated property, banks have no right to take forcible possession except through the court, even if the hypothecation agreement so provides. There are also instances where the banks find that the borrowers have sold the hypothecated property but neglected to deposit the sale proceeds as a part of repayment of loan. But normally court considers such conduct as a breach of contract and not as a crime. Experiences also show that in the matter of other securities like immovable properties, guarantees, banks do not have any right to enforce the securities on their own and have to obtain recovery from courts. It takes a long time to settle the suit since suits filed by the banks do not get priority in courts and by the time the securities deteriorate in value and the recovery becomes impossible **(Lodh1991)**.

From the branch manager's angle, many difficulties are faced in management of NPAs. Difficulties in keeping a close supervision and effective follow up mechanism at branches arise due to increasing routine work load, shortage of staff and lack of co-operation from the borrowers in submitting the stock statements, balance sheets and the like**(Narayanan 2000)**

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The repayment rationale irrespective of the category of borrowers is based on the assumption that the beneficiary implements the techno economic terms/conditions of the loan sanction, makes judicious use of the loan, generates incremental income and repays the loan from the surplus generated.

Debt Recovery Process and Debt Recovery Mechanisms

Providing financial assistance to the needy is an essential function of a banker. By meeting the financial requirements of various segments of the society, banks contribute to the economic development of our nation. Banks and financial institutions have heavily financed industries both corporate and individual. Large sums remain unrecovered and the normal process of recovery of debts through the courts is lengthy. Institutions face considerable difficulties in recovery of dues and enforcement of securities charged to them due to delay in legal processes. A significant portion of their funds are thus blocked in unproductive assets, the values of which deteriorate over the period of time. Banks and financial institutions also spend substantial amounts on legal charges, which add to their overheads **(Singh2012).** An attempt has been made below to explain the debt recovery process and various debt recovery mechanisms followed by the commercial banks.

The debt recovery policy of the bank is built around dignity and respect to customers. The policy is built on courtesy, fair treatment and persuasion. The banks believe in following fair practices with regard to recovery of dues from borrowers and taking possession of security (properties / assets charged to the bank as primary or collateral security) and thereby fostering customer confidence and long-term relationship. The repayment schedule for any loan sanctioned by the Banks will be determined by taking into account the repaying capacity and cash flow pattern of the borrower. The banks will explain to the customer upfront the method of calculation of interest and how the Equated Monthly Instalments (EMI) or any other mode of repayment will be appropriated against interest and principal due from the customers. The banks would expect the customers to adhere to the repayment schedule and approach the Bank for assistance and guidance in case of genuine difficulty in meeting repayment obligations.

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Objectives of the study

1. To study the causes of NPAs in SCBs
2. To analyse the trends in NPAs in all the SCBs
3. To study the recovery of NPAs through various channels

Research Methodology

The study is descriptive and explorative in nature. Various books and journals were refereed to understand the concept and theoretical base of NPAs and recovery. To analyse the trends in NPAs, NPA classification and Recovery through various channels during 2017 and 2018 the secondary data are used from the publications of RBI.

Review of literature

Shivapuje and Kaveri (1997) in their research book "Management of Non Performing Advance" identified the factors influencing NPAs and their effect on speedy recovery. They revealed that the major emphasis was laid on internal factors over which banks and financial institutions have direct control.Gopalakrishnan (2005) classified the causes for NPA into political, economic, social and technological. Further, he identified that neglect of proper credit appraisal, lack of follow-up and supervision, recessional pressures in economy, change in government policies, infrastructural bottlenecks, and diversion of funds etc. are the major causes for NPA. The reasons for NPA are classified differently; into systematic and situational causes.Muniappan (2002), Misra and Dhal (2011), Khan and Makeen (2012) viewed that the problem of NPAs is related to various internal and external factors. The internal factors are diversion of funds for expansion, diversification, modernization, taking up new projects, promoting associate concerns, business failure, inefficient management, strained labour relations, in appropriate technology or technical problems, etc., while external factors are recession, input/power shortage, non-payment in other countries, price escalation and natural calamities.Jay (2000) discussed about the recovery management, steps to be taken to turn around the loss making branches and whole hearted support of staff at all

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levels. Murthy (2000) discussed the right alternative for arresting the over dues. He highlighted the importance of compromise settlement for recovery of dues. Reddy (2004) highlighted the concept of NPAs and reasons for the growth of NPAs in public sector banks. He also explained the role of DRTs and SARFAESI Act; 2002. He suggested that in order to reduce the NPAs in the banks' balance sheet, proper- evaluation and selection of the borrower accounts, need based financing, post sanction follow up, regular contact with the borrowers, regular monitoring of accounts and holding recovery camps must be given importance.Iyar (2005)observed the ever growing NPAs, a fine euphemism coined to describe the bad loans, passing of Recoveries of Debt Due to the Banks and Financial Institutions Act 1993 whereby a special Debt Recovery Tribunal was set up for the recovery of NPA. Singh (2005) in his paper suggested legal action for recovery of bank dues. Prasad (2006) made an observation about the importance of ARCs and SARFAESI Act 2002 to recover the NPAs.Siraj and Pillai (2012)in their study on "management of NPAs in Indian SCBs: Effectiveness of SARFAESI Act, DRT and Lok Adalath during 2004- 2011" have made an attempt to evaluate management of NPA in Indian SCB's focused mainly on the recovery management measures since 2003- 04. They evaluated the trend in movement of total NPA and recovery of NPA through Lok Adalats, DRTs and SARFAESI Act. They revealed that among the recovery measures, SARFAESI act provided much needed momentum to improve the recovery measures.

The following tables explain the trends in NPAs, classification of loan assets, sector wise NPAs and recovery of NPAs through various channels.

(Amount in Rupees billion)

Item	PSBs*	PVBs	FBs	All SCBs#
Gross NPAs				
Closing Balance for 2016-17	6,847	932	136	7,918
Opening Balance for 2017-18	6,192	932	136	7,265
Addition during the year 2017-18	4,882	1,077	70	6,043

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Table 1: Trends in Non-performing Assets – Bank Group-wise

Recovered during the year 2017-18	823	408	47	1,283
Written-off during the year 2017-18	1,295	308	21	1,627
Closing Balance for 2017-18	8,956	1,293	138	10,397
Gross NPAs as per cent of Gross Advances**				
2016-17	11.7	4.1	4.0	9.3
2017-18	14.6	4.7	3.8	11.2
Net NPAs				
Closing Balance for 2016-17	3,831	478	21	4,331
Closing Balance for 2017-18	4,545	642	15	5,207
Net NPAs as per cent of Net Advances				
2016-17	6.9	2.2	0.6	5.3
2017-18	8.0	2.4	0.4	6.0

Source: RBI 2018

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The above table depicts the bank group wise trends in NPAs. It clearly indicates the increase in NPA in all the scheduled commercial banks from the year 2016-17to 2017-18. Gross NPA increased from 9.3% to 11.2% and Net NPA increased from 5.3% to 6 %. During 2017-18, the GNPA ratio of PSBs arising from larger borrowed accounts (exposure of ₹ 50 million or more) increased to 23.1 per cent from 18.1 per cent in the previous year. Similarly, the GNPA ratio of PVBs arising from large borrowed accounts registered an uptick, especially after the implementation of the revised framework of resolution of stressed assets from February 12, 2018. However, the share of special mention accounts, which have a high chance of degrading into NPAs, recorded a decline in case of both bank groups. During 2018-19, NPAs in large borrowed accounts of PSBs and PVBs declined; however, the proportion of loans in total loans recorded an uptick

Table 2: Classification of Loan Assets – Bank Group-wise

(Amount in ₹ billion)

Bank Group	Year	Standard Assets		Sub-standard Assets		Doubtful Assets		Loss Assets	
		Amount	Per cent*	Amount	Per cent*	Amount	Per cent*	Amount	Per cent*
PSBs#	2017	45,012	87.5	1,641	3.2	4,603	9.0	167	0.3
	2018	46,021	84.5	2,053	3.8	5,936	10.9	465	0.9
PVBs	2017	20,310	96.5	244	1.2	429	2.0	65	0.3
	2018	24,506	96.0	272	1.1	700	2.7	52	0.2

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FBs	2017	3,302	96.0	40	1.2	82	2.4	14	0.4
	2018	3,495	96.2	38	1.1	84	2.3	16	0.4
All SCBs**	2017	68,624	90.4	1,925	2.5	5,114	6.7	247	0.3
	2018	74,022	88.5	2,364	2.8	6,720	8.0	534	0.6

Source: RBI 2018

Table 2- reveals bank group wise classification of loan assets, it is apparent that in all the scheduled commercial banks the percentage of standard asset decreased in public sector banks and private sector banks which, is increased in foreign banks during 2017-18 compared to 2016-17. The percentage of substandard asset increased inPSBs and FBs and decreased in private sector banks. Percentage of doubtful debts increased in all the scheduled commercial banks. As for as loss assets are concerned, percentage is increased in public SCBs, decreased in private and FBs. Overall the NPAs in all the banks increasing year by year. Supervisory returns suggest that on top of the elevated level of stressed assets, fresh slippages rose during 2017-18 in respect of PSBs as against a decline in the previous year. This is largely attributable to restructured advances slipping into NPAs and a decline in standard advances. Slippages in respect of PVBs moderated. Quarterly data from supervisory returns suggest a significant decline in fresh slippages across bank groups during 2018-19.

Table3: Sector-wise NPAs of Banks

(Amount in ₹ billion)

Bank Group	Priority Sector		Of which						Non-priority Sector		Total NPAs	
			Agriculture		Micro and Small Enterprises		Others					
	Amt.	Per cent#	Amt.	Per cent#	Amt.	Per cent#	Amt.	Per cent#	Amt.	Per cent#	Amt.	Per cent#
PSBs*												
2017	1,543	24.1	548	8.5	757	11.8	238	3.7	4,868	75.9	6,411	100
2018	1,875	22.2	753	8.9	821	9.7	301	3.6	6,580	77.8	8,455	100
PVBs												

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2017	133	18.0	53	7.2	64	8.7	16	2.2	605	82.0	738	100
2018	184	18.0	78	7.6	80	7.8	26	2.6	840	82.0	1,024	100
FBs												
2017	24	17.8	1	0.5	4	3.1	19	14.3	112	82.2	136	100
2018	12	8.6	1	0.6	6	4.0	6	4.0	126	91.4	138	100
All SCBs (including SFBs)												
2017	1,703	23.4	602	8.3	828	11.4	273	3.7	5,587	76.6	7,288	100
2018	2,076	21.6	832	8.6	910	9.5	334	3.5	7,555	78.4	9,626	100

Source: RBI 2018

Table 3 depicts the sector wise NPAs of banks. It is clear that the percentage of NPAs from non-priority sector is more as compared to priority sector lending. Lending to all the sectors increased from 2016-17 to 2017-18.Sector-wise, industrial sector receives 37.3 per cent of total loans and advances, but it contributes about three-fourth of total NPAs. Asset quality in the industrial sector deteriorated during 2017-18, mainly with better recognition. The agricultural sector posted an uptick in the GNPA ratio possibly reflecting debt waiver by several states. During 2018-19, some moderation in industrial NPAs occurred due to resolution of certain large accounts. At the same time, the asset quality of loans to the agricultural sector worsened further. Loan defaults in retail loans remained at a low level. Size-wise, one-fourth of loans to large industries turned into NPAs by the end of March 2018. Medium sized industries underwent improvement in loan quality during 2017-18, although in 2018-19, these industries were faced with an uptick in the GNPA ratio).

Table 4: NPAs of SCBs Recovered through Various Channels

(Amount in ₹ billion)

Recovery Channel	2016-17				2017-18			
	No. of Cases Referred	Amount Involved	Amount Recovered*	Col. (4) as % of Col. (3)	No. of Cases Referred	Amount Involved	Amount Recovered	Col. (8) as % of Col. (7)
1	2	3	4	5	6	7	8	9

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Lok Adalats	3,555,678	361	23	6.3	3,317,897	457	18	4.0
DRTs	32,418	1,008	103	10.2	29,551	1,333	72	5.4
SARFAESI Act	199,352	1,414	259	18.3	91,330	1,067	265	24.8
IBC	37	-	-	-	701	99	49	49.6
Total	3,787,485	2,783	385	13.8	3,439,477	2,956	404	13.7

Source: RBI 2018

Table 4 reveals the NPAs of SCBs recovered through various channels.' During the year 2016-17, only 6.3% of the amount involved in cases referred to Lokadalaths, 10.3% of the amount involved in cases referred to DRTs and 18.3% of the amount involved in cases referred to SARFAESI. Whereas in 2017-18,4.0% of the amount involved in cases referred to Lokadalaths, 5.4% of the amount involved in cases referred to DRTs and 49.6% of the amount involved in cases referred to SARFAESI. There is a increase in cases referred to recovery channels from 2016-17 to 2017-18.

Recovery of stressed assets improved during 2017-18 through the IBC, 2016 and Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interests (SARFAESI) Act, 2002 . Apart from vigorous efforts by banks for speedier recovery, amending the SARFAESI Act to bring in a provision of three months' imprisonment in case the borrower does not provide asset details and for the lender to get possession of mortgaged property within 30 days, may have contributed to better recovery. Recovery through Lok Adalats and Debt Recovery Tribunals (DRTs) declined alongside the number of cases referred partly indicative of growing clout of the IBC mechanism for resolution of stressed assets.Apart from recovery through various resolution mechanisms, banks are also cleaning up balance sheets through sale of doubtful/ loss assets to assets reconstruction companies (ARCs) and other banks/NBFCs/financial institutions by taking haircuts. During 2017-18, the acquisition cost of ARCs as a proportion to the book value of assets increased, indicating better realisations by banks on sale of stressed assets. Bank group-wise, PVBs have been most aggressive on asset sales. PSBs lagged in asset sales mainly owing to large haircuts and various management issues. On the positive side, some PSBs have strengthened in-house

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expertise for recovery of NPAs, spurred by the need for faster resolution. Quarterly data suggests that during 2018-19, sales of stressed assets to ARCs by both PSBs and PVBs witnessed deceleration.

Conclusion

In spite of encouragement and support from the government many industries are facing the problem of finance and many banks are experiencing increase in NPAs. Various debt recovery mechanisms must be strengthened and financial support should be given to industries by following aggressive assessment methods. Furthermore though there are number of institutions and committees which have been formed to protect and safeguard the interest of the SSIs, the success of the SSIs and the reduction in NPAs depends upon how effectively the regulations and recommendations are implemented in true spirit.

Recovery of debt is a difficult task and involves a lengthy process. The recovery process begins with issuing notices to the borrowers and ends with sale of property and recovery of debt. Recovery of bank dues is attained by legal and non legal measures. The legal measures include recovery of debt through DRTs, SARFAESI Act, Lok Adalath, ARCs and the like The adoption of proper methods depends upon the amount of loan, type of security offered, nature of default and the like. It is evident from various studies that majority of the banks recovered the loan amount through OTS/ Compromise settlement. The provisions of the other recovery mechanisms will work well if it is effectively used. Because of the loopholes in the legal and non-legal measures followed by the banks, they find difficult in recovery and delay in recovery of dues. The success of lending and recovery is possible only through the proper attention and concerted efforts by all stakeholders like regulators, policy makers, banks and bank customers.

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