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# A Descriptive Study on Non-Performing Assets of Indian Banks

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## Abstract
*Banking Industry is one of the rapidly growing industries in India and is expanding very fast; it is the industry which requires larger amount of workforce, better technological and infrastructure facilities. There has been tremendous increase in the credit flow to various sectors of the economy such as infrastructure, industry, services and agriculture. Even though there is market growth in all the sectors of the economy the quality of assets is deteriorating day by day. NPAs have direct impact on the profitability and the net worth of the banks. The banks have to focus on the problems on NPAs in detail. The balance sheet of the bank is not always based on its balance sheet but it is also based on the level of return on its assets. The level of NPAs best indicates the soundness of banking industry of the country. A healthy financial sector focuses on the growth of the economy, and for the healthy financial sector we need to maintain the financial soundness of the bank. But the bank is overburdened with problem of rising NPAS. The present study focuses on various issues and future impacts of NPAs in Indian Banks. The problem of losses and lower profitability of NPA depends on how risk is managed in their business.*
***Keywords:*** *Non-Performing Assets, Banking Industry, Balance Sheet, Income statement, Profitability.*

## 1. Introduction
In 1993, RBI issued guidelines based on the recommendations of the Narasimham committee in which it was mentioned that identification and reduction of NPA to be treated as 'National Priority'. Loans and Advances is an important source to make the judgement about financial soundness of the bank. It has direct impact on the profitability, liquidity and overall performance of the banks [1-3]. The level of NPAs indicates the efficiency and effectiveness of banks.There should be some measures incorporated to measure and manage NPA. These measures can be precautionary and curative. Precautionary measures focus on strengthening credit risk management system and continuous risk assessment systems of the bank. All these measures will help in reducing NPAs that have been generated. Even though banking contributed significantly to support government in achieving its performance objectives, banks performance in terms of profitability was not satisfactory. Indian banking sector has changed tremendously over the past few years. With the adaptation of LPG (Liberalisation, privatisation and Globalisation) era in 1991, the Indian Banking industry has adapted with quick changes. Now the banks are becoming much more competitive in terms to have a global presence. Asset quality is considered as one of the most important criterion in determining the overall functioning of the banks. Management spent a lot of their time, efforts and resources in administering their assets in order to minimise risk associated with it. If bank is in condition of stress it will lead to less money and less attention on to the other projects. Banks are the major part of this economy they play an important role as financial intermediary in growing economies along with some additional responsibilities of satisfying government with achievement of social goals, this will ultimately lead to development of the economy and improvement of overall health of the banking sector.

## 2. Non-Performing Assets: An Overview
A non performing asset (NPA) refers to a classification for loans and advances that are in arrears or in default. A loan is said to be in arrear when principal or interest payments are missed and it is said to be in default when the debtor is unable to meet the obligations. Non-Performing assets are

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recorded on bank's balance sheet after a long period of non payment of the loan amount by the borrower. This created a huge amount of burden on lender and it affects the financial soundness of the bank. In this case lenders have the options to recover their loss by taking possession of any of their collateral security [4-7]. The assets that generate income are called performing assets but the assets which do not generate income are called Non Performing Assets. A Non performing asset is elucidated as credit facility in which interest or principle has remained due for a stipulated period of time.NPAs are inescapable burden on the banking industry. In today's era of banking industry success of the bank relies on administration of NPAs [8]. The definition of NPAa is given as below:

**A non-performing asset (NPA) is a loan or advance were**

- Interest and/or instalment of principal remain overdue for a period more than 90 days in respect of a term loan [9].
- The account remains 'out of order', in respect of an overdraft/cash credit.
- The bill remains overdue for more than 90 days in case of bills purchased and discounted [10].

Asset means anything that is owned. For banks, a loan is an asset because the interest we pay on these loans is one of the significant sources of income for the bank. When customers or corporates are not able to pay the interest, the asset becomes 'non-performing' for the bank because it is not earning anything for the bank. Therefore, RBI has defined NPAs as the assets that stop generating income for the [11-13].

### 2.1. How Non-Performing Assets Work?

Non-performing assets (NPAs) are loans or advances issued by banks or financial institutions that no longer bring in money for lender since the borrower has failed to make payments on the principal and interest of the loan for at least 90 days. A debt or loan that has been unpaid and due for past predetermined period is known as a Non-Performing Assets (NPAs). When the ratio of NPAs in the portfolio of bank rises, its income and profitability fall. To find out some way for this issue, the government and the Reserve Bank of India have introduced various policies and methods to manage and reduce the amount of NPAs in the banking sector [14].

## 3. Classification of Non-Performing Assets

Banks classify their non-performing assets further following into three main categories and these categories are based on the period for which the asset has remained non-performing and based on their dues [15]:

### 3.1. Standard Assets

It is a performing asset that generates constant income and pays back the loans before the due date. Therefore, these assets have a reasonable risk and are not considered as NPAs [16].

### 3.2. Substandard Assets

Substandard assets has remained NPA for a period less than or equal to 12 months. In this kind of case, the current net worth of the borrower is not enough to ensure recovery of the dues to banks in full. This is also called a loan defaulted for less than a year. Although banks believe that they can get back the money from these loans, they keep a small amount approximately 15% in case they don't get their money back. To get their money back they keep a continuous check on buyers [17-20].

### 3.3. Doubtful Assets

Non-performing assets in the doubtful debts category have been past due for at least 18 months. In this case banks generally have doubts that the borrower will ever repay the full loan or not. This category of NPA seriously affects the bank's own profile. After huge time gap bank starts keeping more money aside, expecting that they might not get the full amount. These loans are very risky, and banks don't expect to get back their money. So bank starts focusing more on these loans and plan accordingly.

### 3.4. Loss Assets

A loss asset is one where loss has been identified by the bank or internal or external auditors. These are non-performing assets that do not pay the interest amount or principal amount for more than three years. With this category bank register as loss to balance sheet. Although the bank counts the loan as total assets, they might still try to get some money back legally, even if the chances are very less.

## 4. Reasons for Non-Performing Assets

Some different reasons and factors lead to NPAs: Some reasons are as follows:

### 4.1. Poor Loan Checks

This happens when banks don't carefully check if someone can pay back the loan or not and the major issue is they don't closely check the borrower's business plans or their past dues. If banks are not working carefully, they end up with unpaid loans.

### 4.2. Business Problems

Many times, it happens buyer don't buy things which are sold for their convenience in the market because of which business are facing problems to upgrade their activities for which they are taking loans.

### 4.3. Money Troubles

Many reasons are there which might lead to money issues. It can be bad planning, disagreements among families, or workers go on strikes. If these issues are not sorted they might not be able to pay back their loans.

### 4.4. Easy Loan Availability

In today's era taking loan has become an easy process less paper work is involved so almost all of them have involved themselves in taking loans which creates more of NPAs.

### 4.5. Bad Economy

People in the economy have started doing so much duplication that even the papers are being duplicated which looks like original which leads to sanctioning of the loans ultimately to NPAs.

## 5. Objectives of the Study

- To study the changes in the banking sector due to emerging NPAs
- To study Non-Performing Assets in detail.
- To study the causes and types of NPAs in detail.
- To maintain the quality of assets in the banking system by creating awareness about sanctioning of loans.
- Reducing and preventing the accumulation of NPAs contributes to overall stability and growth of the banking sector.

## 6. Impact of NPAs on Banking Operations

The level of the bank is not reflected by the size of the balance sheet but it depends on the net income worth on assets of the banks. NPAs don't provide income to the banks but at the same time bank have to provide provisions of NPAs from their current profits.

- Interest income of bank will fall due to NPAs; it will have huge impact on the income statement of banks.
- Return on Investment is reduced due to NPAs.
- It limits the amount of funds because the funds get stuck and it can't be recycled.
- There will be huge mismatch between the assets and liabilities.
- Bad debts will be more which will adversely affect profitability of the banks.
- The economic value addition of the bank will get affected.

It is due to the above factors public sectors are more bulging with lower income and profitability.

## Conclusion

If banks have to get rid of this situation they have to do proper credit assessment and majorly they need to find out the best risk mechanism. Increase in lending money will decrease the quality of the assets. It is essential that banking sector must follow some prudential norms to completely avoid the problems of NPAs. NPA means blocking of money,ultimately decreased profit which ultimately leads to lack of liquidity flow. Time and efforts of bank management and administration which they use for managing NPA would have diverted to some fruitful activities, which would ultimately give higher returns.

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