IJCRT.ORG ISSN : 2320-2882

INTERNATIONAL JOURNAL OF CREATIVE RESEARCH THOUGHTS (IJCRT)
An International Open Access, Peer-reviewed, Refereed Journal

Effects of Rising NPAs on Profitability of Public Sectors Banks.

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Abstract

Banks play a crucial role in providing the desired financial resources to the needy sectors of the economy. And therefore, banks are considered as the supporting pillar and backbone for the economy. The flow of money from person to person, business to business, country to country just possible due to the efficient banking system. Credit or default risk exists in money lending in the form of short, medium, and long-term advances. When bank or financial institution loans or advances turn out to be non-productive, non-rewarding, or non-paying, they become non-performing assets. Indian banks are in poor shape, with large amounts of bad loans and a sharp increase in gross nonperforming assets (NPAs). The aim of this paper is to examine non-performing assets in major public sector banks and their implications for bank profitability. The study is focused on secondary data from RBI studies, various gazetted websites, and various online research papers and articles relevant to the subject.

Keywords: Public Sector Banks, NPAs, Net Profit, Gross NPA, Net NPA

I. Introduction

The primary function of banks is lending of funds as loans and advances to various sectors. Before liberalisation 1991, the banks did not bother about assets quality instead of they are focused on expansion of their branches, generating customers and lending to priority sector. But the post reform era has changed the whole Indian banking structure. The budding competition had given rise to new challenges for the Indian banks. At the same time, the metrics used to evaluate bank efficiency have shifted. Recently, banks have been judged based on their nonperforming assets (NPAs). Non-performing assets are an unavoidable cost of doing business in the banking industry. Any bank's performance is determined by how it manages nonperforming assets (NPAs) and keeps them within acceptable limits.

As a result, in order to deal with the rising level of nonperforming assets (NPAs), banks should implement an effective monitoring and control policy in accordance with RBI guidelines

II. Concept of Non-Performing Assets (NPA).

Reserve Bank of India has provided guidelines for determining when an asset becomes NPA.

1. If interest/instalment of principal with respect to Term Credit is due for more than ninety days, it is considered as NPA.

2. If Overdraft/Cash Credit (OD/CC) amount is persistently greater than the sanctioned limit for more than ninety days then it is considered as NPA.

3. If the overdue bills purchased and discounted exceed ninety days then it is a non-performing asset.

4. If interest/instalment of principal with respect to agriculture advances is due for two harvest seasons but the duration is not surpassing two terms of six months on account of advance granted, then it is considered as NPA.

5. Any receivable amount that is due for more than ninety days in regard of other accounts, then it is considered as NPA.

III. REVIEW OF LITERATURE

NPA is a major issue for the banking sector and many hence many studies have been conducted to find the solution for the problem of rising NPAs. A number of researches have been conducted and gone through .The present research paper contains the review of some of these researches conducted for various commercial banks in the country.

1. Ranjan, R., Dhal, S.C. (2013) researcher in the research paper uses regression analysis to examine an analytical approach for evaluating the nonperforming loans in Indian commercial banks. The empirical study investigates how three major sets of economic and financial variables, namely credit terms, bank size-induced risk preferences, and macroeconomic shocks, influence the level of nonperforming assets (NPA).
2. Tripathi, L. K., Parashar, A., Mishra, S. (2014) the investigator uses the multiple regression model to inspect the outcome of advances made by banks such as the SBI group and other nationalised banks to priority sector, unsecured advances, and responsive sector advances on gross nonperforming assets (NPAs).
3. Chaudhary, K., Sharma, M. (2011) this paper investigates how effectively public and private sector banks handled their nonperforming assets (NPAs). For the study, a statistical method for trend projection was used.

4. Sharma, Kothari, Rathore & Prasad (2020) From 2006 to 2019, this research paper looked into the effect of gross nonperforming assets on the profitability of various public and private banks. To determine the magnitude of the correlation between two variables, the researcher used the correlation between two variables and the statistical t-test. According to the findings, nonperforming assets (NPAs) have a negative effect on profitability. To determine the magnitude of the correlation between two variables, the researcher used the correlation between two variables and the statistical t-test. Nonperforming assets (NPAs) have a negative impact on not only banks' financial performance, but also the economy's financial growth, according to the report.
5. Chatterjee, Mukherjee & Das (2012) according to the investigators NPAs have a negative impact on the overall economy's capital adequacy, funds mobilisation, banking system reputation, and competitiveness. According to the research report, public sector banks face the greatest challenges in the banking sector due to the social obligations they must meet. The private sector banks have been technologically strengthened and are now capable of managing the growing number of nonperforming assets (NPAs).
6. Narula and Singh (2014), the researcher examined Punjab National Bank's nonperforming assets (NPAs), as well as their effect on profitability and the relationship between total advances, net income, gross and net NPAs from 2006-2007 to 2011-2012. The decline of nonperforming assets (NPA) was found to be critical to the bank's profitability. The study conclued that PNB's Net Profit and NPA have a positive relationship between Net Profit and NPA of PNB. Profit of the bank is increasing on one hand as a result of increased developments, while NPAs are increasing on the other hand as a result of weak follow-up.
7. Singla (2015), The researcher attempted a comparative analysis of Gross NPAs and Net NPAs in various Public Sector Banks, Private Sector Banks, and Foreign Banks in India for this study. Private sector banks had lower risen in gross and net nonperforming assets (NPAs) than public sector banks and foreign banks operating in India, according to the report.
8. Kiran and Jones (2016), The research study examines the effect of nonperforming assets (NPAs) on bank profitability, taking into account gross NPA and net profit. However, each year's Gross NPA involves the previous year's NPA as well as bad loan recovery. As a result of the approach they employed, in which "Lag" was present, the year-by-year difference in NPA should be calculated by excluding the Lag effect from the results.
9. Miyan (2017), The study used a comparative statistical approach to NPAs in India's public and private sector banks. NPAs have been on the decline over the study period, but PSB NPAs are still higher than private sector banks, according to the researchers. As a result, PSU banks performed poorly when compared to private sector banks.

IV. Objectives of the study

The study's primary objectives are to:

1. Analyse the NPA and profitability positions of the selected banks.

2. To determine the effect of nonperforming assets (NPAs) on the net profit of the selected banks.

V. RESEARCH METHODOLOGY

1. **Sources of data:** The present study "**Effect of rising NPAs on Profitability of Public Sectors Banks.**" is mainly based on secondary data. Secondary data was gathered from a variety of sources, including annual reports from various banks and the Reserve Bank of India, relevant subject matter and related websites from public and private sector banks in India, online blogs, research papers, and e-news, among others.
2. **Sampling Design:** The top 6 public sector banks State Bank of India, Punjab National Bank, Central Bank, Bank of India, Bank of Baroda, Union Bank of India were selected for this study based on purposive sampling method the study period is from 2011-2020.
3. **Statistical tools**: Arithmetic Mean has been used and calculated to know the average performance of the banks and to find out the relationship between Gross NPA and advances, Net NPA and Net profit.

VI. ANALYSIS AND INTERPRETATION

Table 1
Gross NPA to Gross Advance Ratio

Year	SBI	PNB	CENTRAL BANK	BOI	BOB	UNION BANK OF INDIA
2011	3.28	1.79	1.82	2.23	1.36	2.37
2012	4.44	2.93	4.83	2.34	1.53	3.01
2013	4.75	4.27	4.80	2.99	2.40	2.98
2014	4.95	5.25	6.27	3.15	2.94	4.08
2015	4.25	6.55	6.09	5.39	3.72	4.96
2016	6.5	12.90	11.95	13.07	9.99	8.70
2017	6.9	12.53	17.81	13.22	10.46	11.17
2018	10.91	18.38	21.48	16.58	12.26	15.73
2019	7.53	15.50	19.29	15.84	9.61	14.98
2020	6.15	14.21	18.29	14.78	9.40	14.15
MEAN	**5.97**	**9.43**	**11.26**	**8.96**	**6.37**	**8.2**

Source : Annual reports of selected banks (various issues)

The Gross NPA to Gross Advance Ratio of Selected Public Sector Banks is shown in Table 1. Central Bank had the highest mean ratio of 11.26, followed by Punjab National Bank with 9.43, BOI with 8.96, Union Bank with 8.2, BOB with 6.37, and SBI with 5.97. This demonstrates that the Gross NPA to Gross Advance Ratio is consistent.

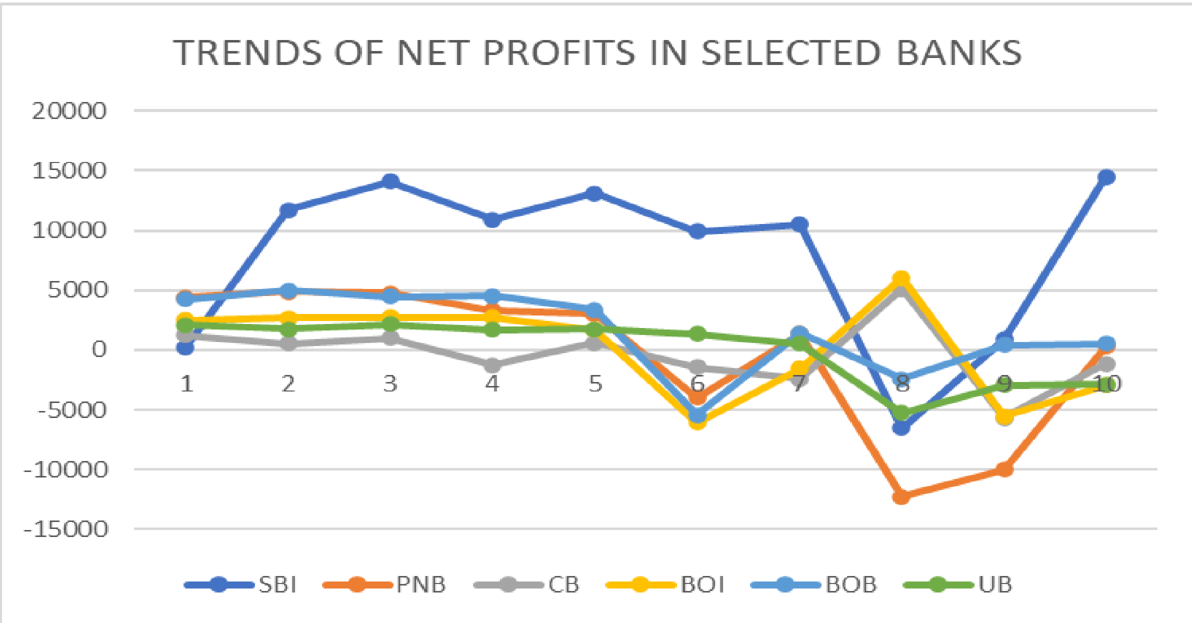
Table 2

Net Profit Position

Year	SBI	PNB	CENTRAL BANK	BOI	BOB	UNION BANK OF INDIA
2011	264.52	4433.50	1252.41	2488.71	4241.68	2081.95
2012	11707.29	4884.20	533.04	2677.52	5006.96	1787.13
2013	14104.98	4747.67	1014.96	2749.35	4480.72	2157.93
2014	10891.17	3342.57	-1262.84	2729.27	4541.08	1696.25
2015	13101.57	3061.58	606.45	1708.92	3398.43	1781.64
2016	9950.65	-3974.39	-1418.19	-6089.21	-5395.55	1351.60
2017	10484.10	1324.80	-2439.10	-1558.34	1383.13	555.21
2018	-6547.45	-12282.82	-5104.91	6043.71	-2431.81	-5247.37
2019	862.23	-9975.49	-5641.48	-5546.90	433.52	-2947.45
2020	14488.11	336.20	-1121.35	-2956.89	546.18	-2897.78

Source : www.moneycontrol.com

Graph 1.



Source : Prepared by Author

Table 2 shows the net profit position of the selected public sector banks. It can be clearly seen that the three major banks Central Bank, BOI and Union bank of India are having net losses, out of the three the position of Central Bank was much serious as the bank was having continuous losses since 2016. In 2018 almost all the banks experienced a negative growth as compared to 2017.

Table 3

Net NPA to Net profit ratio

Year	SBI	PNB	CENTRAL BANK	BOI	BOB	UNION BANK OF INDIA
2011	1.63	0.65	0.55	0.91	0.35	1.19
2012	1.82	1.52	3.09	1.47	0.54	1.70
2013	2.10	2.35	2.90	2.06	1.28	1.61
2014	2.57	2.85	3.75	2.00	1.52	2.33
2015	2.12	4.06	3.61	3.36	1.59	2.71
2016	3.81	8.61	7.36	7.79	5.06	5.52
2017	3.71	7.81	10.20	6.90	4.72	6.57
2018	5.73	11.24	11.10	8.26	5.49	8.42
2019	3.01	6.56	7.73	5.61	3.33	6.85
2020	2.23	5.78	7.63	3.88	3.13	5.49
MEAN	**2.87**	**5.14**	**5.79**	**4.22**	**2.70**	**4.24**

Source : Annual reports of selected banks (various issues)

The Net NPA to Net Profit Ratio of Selected Public Sector Banks is shown in Table 3. The NPA mean ratio of Central Bank was the highest at 5.79, followed by Punjab National Bank at 5.14, as shown in the table above. The NPA of Bank of Baroda is 2.70, which is the lowest among the selected Public Banks. This demonstrates that the concentration of nonperforming assets (NPA) with some of the largest public sector banks rises at a faster rate.

VII. FINDINGS

1. All of the public sector banks selected have nonperforming assets (NPAs) on their balance sheets.
2. Nonperforming assets (NPAs) continue to grow for all banks.
3. While large banks are able to control NPA losses, small banks are unable to do so.
4. Profits have decreased as a result of market expansion and a rise in nonperforming assets (NPAs) on the part of banks.

5. Largest public sector bank SBI is also having NPAs but at the same time also earning high profits.
6. Public sector banks are facing more issues by NPAs as compared to private sector banks

VIII. CONCLUSION

The rising level of nonperforming assets has an effect not only on the bank's financial position, but also on the economy's financial development. The Indian banking sector was beset by nonperforming assets (NPAs). A high level of nonperforming assets (NPAs) indicates a high likelihood of a significant number of credit defaults, which can impact a bank's profitability and liquidity. NPAs must be organised in order to increase productivity and profitability . To tackle the NPA crisis, strict steps must be implemented. Since complete removal of NPA is highly unrealistic, it can only be regulated. Improved recovery management, prompt loan recovery, implementation of new recovery schemes for overdues, tracking of defaulters' accounts, maintaining frequent communication with borrowers, adequate credit appraisals, disbursements, post-sanction follow-up, and need-based credit are some of the areas of credit management that need to be improved in order to minimise NPAs. During the study period, the present study discovered that NPA had a significant effect on net profits in a number of public sector banks.

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