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## A study on Non-Performing Assets Management and Its Impact on Profitability With Reference to Karnataka Bank Ltd

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### INTRODUCTION

The banking sector plays an important role in the economic growth of a country. Through its intermediary activities, the banking sector fosters the production, distribution, exchange and consumption processes in the economic system. It stimulates the flow of funds in the economy and fuels economic growth. The efficiency of banking system, thus determines the pace of development of the economy. Similar to any other business enterprise, the efficiency of a bank is evaluated based on profitability and quality of assets it possess. But unlike other commercial ventures, Indian banking has social commitments integrated into its operations. The banking system in India has had to serve the goals of economic policies enunciated in successive five year development plan, particularly concerning equitable income distribution, balanced regional economic growth and the reduction and elimination of private sector monopolies in trade and industry.

To improve the efficiency and profitability of banks the NPA need to be reduced and controlled. In this paper, an effort has been made to evaluate the non-performing assets of the Karnataka Bank since 2004, NPAs. Non-performing Assets are threatening the stability and demolishing bank's profitability through a loss of interest income, write-off of the principal loan amount itself. RBI issued guidelines in 1993 based on recommendations of the Narasimham Committee that mandated identification and reduction of NPAs be treated as a national priority because the level of NPA act as an indicator showing the bankers credit risks and efficiency of allocation of resource.

A strong banking sector is important for a flourishing economy. The failure of the banking sector may have an adverse impact on other sectors. The Indian banking system, which was operating in a closed economy, now faces the challenge of an open economy. The main business of a banking company is to receive deposits and lend money. Receiving deposit involves no risk, since it is the banker who owes a duty to repay the deposit, whenever it is demanded. On the other hand, lending always involves much risk because there is no certainty of repayment. A banker shall be very cautious in lending, because he is not lending money out of his own capital. A major portion of the money lent comes from the deposits received from the public. These deposits are mostly repayable on demand. Hence, while lending money, a banker should follow a very cautious policy. The risk involved in lending business makes it very important as it involves making prominent decisions. Therefore while sanctioning credit the banker should appraise the project reasonably or else it leads to the non-repayment of loans and advances. Most of the banks today in India are facing the default risk wherein some part of the profit is reserved for covering the nonperforming assets.

Historically, in 1997, NPAs were 15.8% of loans for the banking sector, which nosedived to 2.4% in 2008. This figure stands at 2.94% of loans in 2012. In absolute figures, NPAs have doubled from 2009 to 2012 and assets under reconstruction had trebled during the same period. India's biggest lender, State Bank of India, is experiencing an NPA level of 4.99% of total loans. According to a recently published Credit Suisse Group AG report, 10 large industrial houses account for 13% of total assets financed by the Banking system, which means that bank lending is getting increasingly skewed. Further, of the total reconstructed assets, 8.24% belong to the large manufacturing sector, 3.99% are from the services sector while 1.45% are from the agricultural sector.

## **Literature Review**

A large number of researchers have studied the issue of non-performing asset (NPA) in banking industry. A review of the relevant literature has been described as under: -

**Siraj K.K. and Sudarsanan Pillai P. (2012).** Non-Performing Assets engender negative impact on banking stability and growth. Issue of NPA and its impact on erosion of profit and quality of asset was not seriously considered in Indian banking prior to 1991. There are many reasons cited for the alarming level of NPA in Indian banking sector. Asset quality was not prime concern in Indian banking sector till 1991, but was mainly focused on performance objectives such as opening wide networks/branches, development of rural areas, priority sector lending, higher employment generation, etc. The accounting treatment also failed to project the problem of NPA, as interest on loan accounts were accounted on accrual basis.

**Debarsh and Sukanya Goyal (2012)**

Emphasized on management of non-performing assets in the perspective of the public sector banks in India under strict asset classification norms, use of latest technological platform based on Core Banking Solution, recovery procedures and other bank specific indicators in the context of stringent regulatory framework of the RBI. Non-performing Asset is an important parameter in the analysis of financial performance of a bank as it results in decreasing margin and higher provisioning requirements for doubtful debts. The reduction of non-performing asset is necessary to improve profitability of banks

**RESEARCH DESIGN**

Non-performing assets are those which are not been yielding revenue for a long period of time. The bank will always face the problem of NPA because of poor recovery of advances granted by the bank and several other reasons like adopting poor recovery strategies so when the loan is not recovered from the bank effectively and efficiently that balance amount will become the NPA to the bank, it may create some huge problem to the bank's financial status. In order to evaluate the performance of the Karnataka Bank Ltd. it is deemed necessary to undertake the study regarding management of NPAs.

**Scope of the Study**

The present study of Non-performing assets is confined and restricted to the boundary of Karnataka bank and data is analyzed and the study is descriptive in nature. This research study surely will provide a parameter particular for a better understanding of NPA level in Karnataka bank. This attempt covers the extensive research work on NPA structure. The findings of study present a comparison between selected variables for the past 08 years' since 2008-2009 up to 2014-15.

**Objectives of the Study**

- To study the management of NPA in KARNATAKA Bank limited.
- To investigate the impact of NPAs on profitability of the KARNATAKA Bank limited.
- To suggest measures to manage NPAs in KARNATAKA BANK effectively.
- To analyze the strategies and steps taken by the bank to reduce its NPAs.

### **Need for study;**

Many researchers have attempted to study the non performing assets management and its impact on the profitability of the banking sectors in general and a very few attempts have been made so far

To study on NPAs of Karnataka bank in particular.

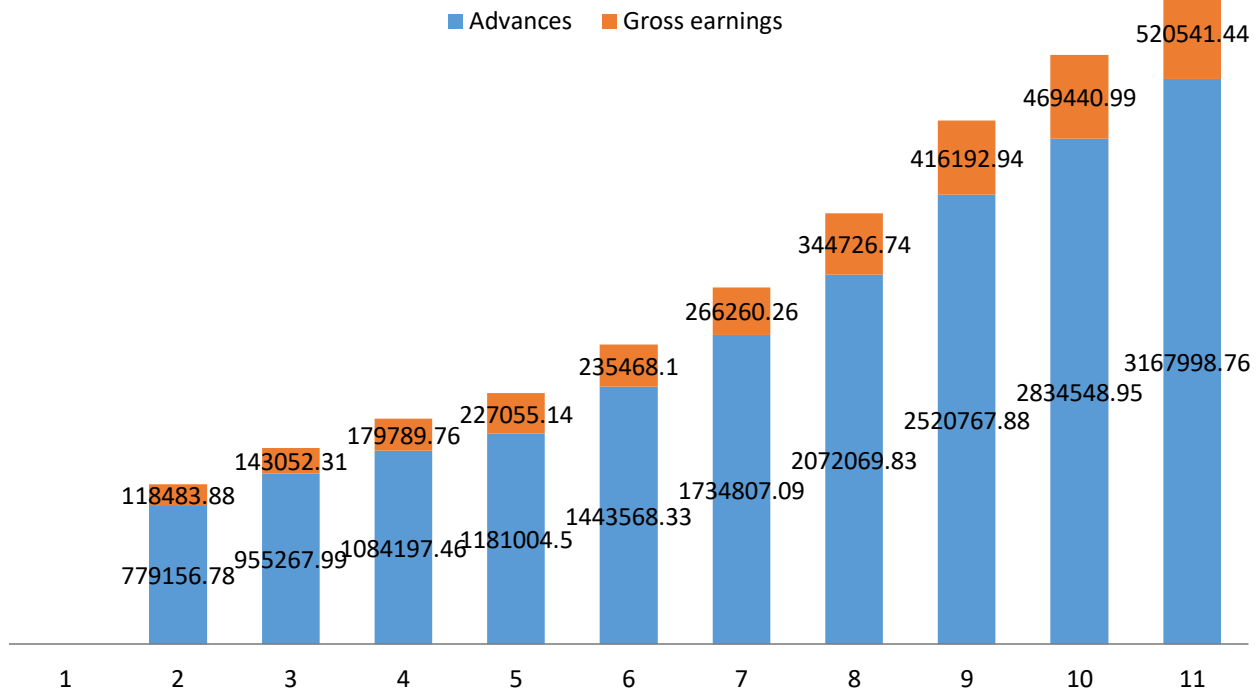
The basic need for this study is to understand, analyze and to investigate the factors that contribute to NPA of Karnataka Bank. There is also a need to suggest some measures in order to reduce the level of NPA.



**Data Analysis and Interpretation;****FINANCIAL INFORMATION NET PROFIT**

Year	Capital Reserve	Deposits	Advances	Gross earnings	N/P	Dividend Paid in %	No of branches	No of employees
2005-06	111113.06	1324316.04	779156.78	118483.88	17603.39	30	395	4346
06-07	123862.77	1403743.54	955267.99	143052.31	17703.44	35	410	4456
07-08	137960.33	1701619.23	1084197.46	179789.76	24174.10	50	431	4677
08-09	156702.70	2033328.53	1181004.50	227055.14	26670.50	60	447	4947
09-10	183274.93	2373064.88	1443568.33	235468.10	16711.97	40	464	5244
10-11	242908.10	2733644.63	1734807.09	266260.26	20461.13	30	478	5795
11-12	259821.05	3160832.43	2072069.83	344726.74	24607.02	35	503	6087
12-13	285708.14	3605622.13	2520767.88	416192.94	34808.21	40	550	6339
13-14	305219.76	4058282.87	2834548.95	469440.99	31103.43	40	600	7185
14-15	338906.05	4600860.55	3167998.76	520541.44	45145.02	50	675	7382

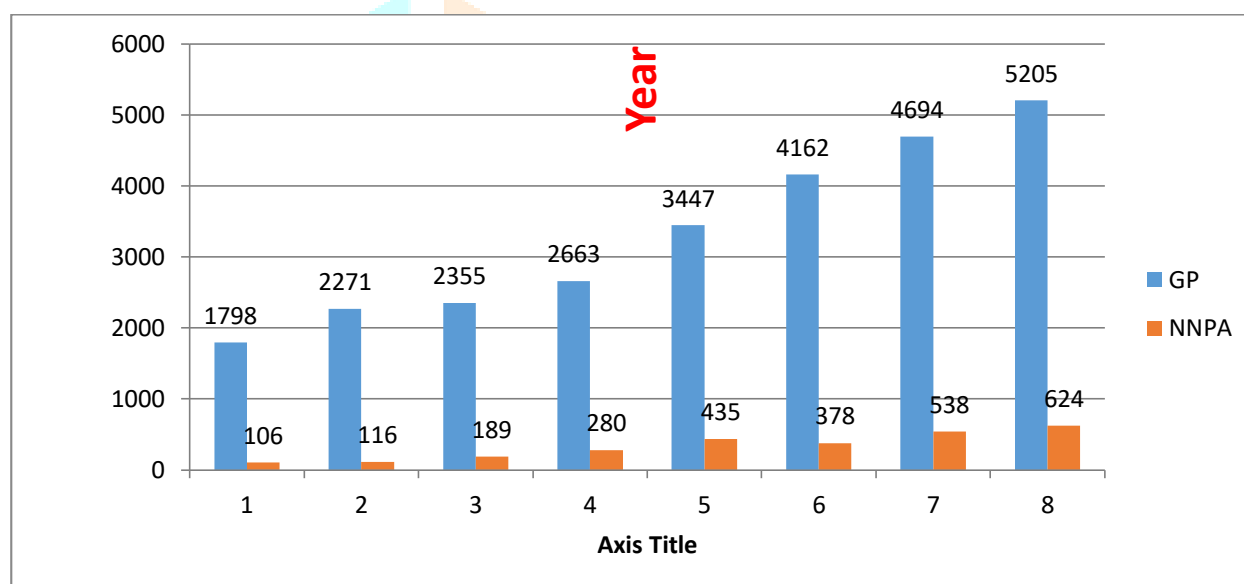
## Gross profit and Advances



This graph shows that there is direct relationship between GP and Advances. This situation is good in banking sector because Bank's main income is interest amount which is collected against loan amount until it becomes Non-performing.

**Profits, Advances and NPAs**

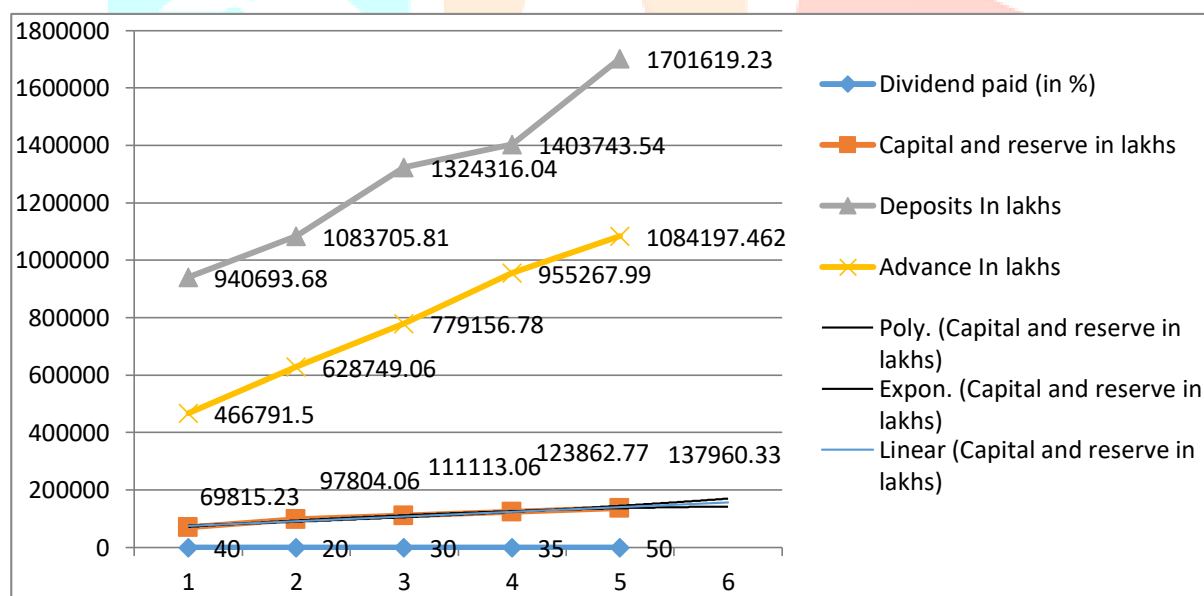
YEAR	GP	GNPA	NNPA	NP	ADVANCES
2008	1798	380	106	242	10842
2009	2271	443	116	267	11810
2010	2355	550	189	167	14436
2011	2663	685	280	205	17348
2012	3447	702	435	246	20721
2013	4162	639	378	348	25208
2014	4694	836	538	311	28345
2015	5205	944	624	451	31680

**Interpretation:**

This study reveals that over the years the bank has made sufficient efforts to reduce the Non-performing assets, which are a drain on their profitability. Management of non-performing asset is one of the important areas in banks to keep their non-performing assets under control.

## Past trend Source-Annual report of Karnataka bank

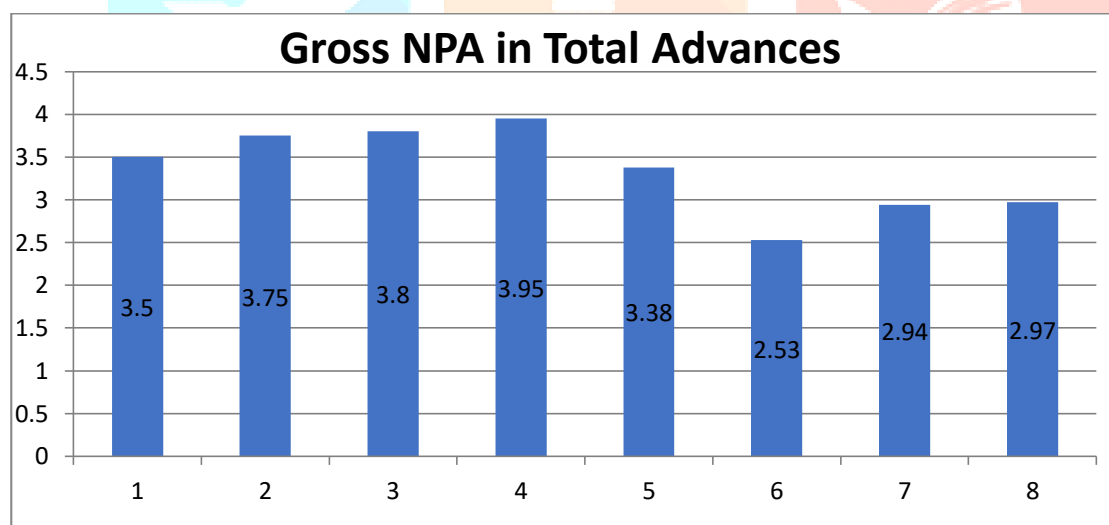
Year	N/p in crores	Dividend paid (In %)	Capital and reserve in lakhs	Deposits In lakhs	Advance In lakhs
2003-04	133.16	40	69815.23	940693.68	466791.50
2004-05	147.14	20	97804.06	1083705.81	628749.06
2005-06	176.03	30	111113.06	1324316.04	779156.78
2006-07	177.03	35	123862.77	1403743.54	955267.99
2007-08	241.74	50	137960.33	1701619.23	1084197.462



This graph represents over all past scenario of Karnataka bank as well as the trend analysis



SL. No	Gross NPA in Total Advance		Gross NPA in %
	GNPA	ADVANCES	
1	380	10842	3.5
2	443	11810	3.75
3	550	14436	3.8
4	685	17348	3.95
5	702	20721	3.38
6	639	25208	2.53
7	836	28345	2.94
8	944	31680	2.97



**Interpretation:** The Above graph reveals the total gross NPA in total advances from 2008. The total gross NPA gradually increased till 2011 after that it gradually reduced because of good credit appraisal policy. Then after this showed a gradual increasing trend.

Correlations				
		Net non Performing asset	Net profit	Gross Profit
Pearson Correlation	Net non-performing asset	1.000	.723	.963
	Net profit	.723	1.000	.828
	Gross Profit	.963	.828	1.000
Sig. (1-tailed)	Net non-performing asset	.	.021	.000
	Net profit	.021	.	.006
	Gross Profit	.000	.006	.
N	Net non-performing asset	8	8	8
	Net profit	8	8	8
	Gross Profit	8	8	8

### Interpretation

Net nonperforming asset is significantly positively correlated to Net profit and gross profit. Value of  $R^2 = 94.4\%$  indicates that the model is a good fit. Almost 95% of the variation in the dependent variable Net nonperforming asset is explained by the independent variables Net profit and gross profit.

### Findings

- ✓ Because of mismanagement in bank there is a positive relationship between Total Advances, Net Profits and NPA of bank which is not good.
- ✓ Positive relation between NPA & profits are due to wrong choice of clients by Banks.
- ✓ There is an adverse effect on the Liquidity of Bank.
- ✓ Bank is unable to give loans to the new customers due to lack of funds which arises due to NPA
- ✓ Gross NPA & Net NPA of KBL are increasing every year.
- ✓ Total advances given by KBL and Net Profits are increasing continuously since 2008.
- ✓ The specific findings from the study are that, there is still a need to have controlling devices to monitor NPA system in the Karnataka bank limited

## **Limitations of the study and suggestions for future study**

In the present study, secondary data were used for obtaining the results, and no primary data were used collected and used in the study. The data related 8 years for the NPA in the Karnataka Bank. However this data may not have given conclusive results.

The limitation also show the way for further research in this area. Researchers can obtain primary data to verify whether the NPAs have really risen in the Karnataka bank ltd. If yes, then what are the reasons for the non-payment of the loans by the Karnataka bank members? If the time span of the data is increased, more efficient results can be drawn. After analyzing the reasons for the increase in NPAs, a checklist of preventive measures can be prepared from such results as suggestive measures for the bank.

## **Suggestions**

Advances provided by bank need to be done pre-sanctioning evaluation and post disbursement control so that NPA can decrease. Good management needed on the side of bank is to decrease the level of NPA. Proper selection of borrowers & follow ups required to get timely payment.

**To control the Non-performing assets in Karnataka Bank Limited, some remedial measures are suggested as follows:**

1. There must be an effective follow-up at regular intervals of the customers to watch any diversion of funds.
2. A number of personal visits after sanction and disbursal of credit and close monitoring of the operations of the accounts of borrowed units.
3. Between the Bankers – borrower a healthy relationship should be developed. Many instances reported that the banks uses force in recovery of loans, which is unethical.
4. Managers in charge of non-performing assets should have dynamism and zeal in their work.
5. Frequent discussions with the staff in the branch and taking their suggestions for recovery of NPAs make them feel responsible.
6. RBI needs to take necessary actions against defaulters like, publishing names of defaulters in Newspapers, broad-casting media, which is helpful to other banks and financial institutions.
- 7 The bank should avoid the wrong selection of borrowers. The staff must be additionally trained to assess the borrower's efficiency through proper credit appraisal.

## **Conclusion**

NPAs reflect the overall performance of the banks. The NPAs have always been a big worry for the banks in India. The Indian banking sector faced a serious problem of NPAs. A high level of NPAs suggests high probability of a large number of credit defaults that affect the profitability and liquidity of banks. The extent of NPAs has comparatively higher in public sectors banks. To improve the efficiency and profitability, the NPAs have to be scheduled. Various steps have been taken by government to reduce the NPAs.

This study can conclude that the KBL can avoid sanctioning loans to the non-creditworthy borrowers by adopting certain measures. They are careful appraisal of the project which involves checking the economic capability of the project.

KBL Banker must consider the homecoming on investment on a proposed project.

If the calculated return is sufficiently higher than the credit amount he can sanction the loan.

The banker also has to educate the borrowers regarding the effects and consequences of defaulting. By considering all the above factors the banker can reduce the non-performing assets in bank.

The use of technology like Core Banking solutions in KBL should make more reachable to all borrowers.

The problem of NPAs has been a major issue for the banking industry. The RBI which is the apex body for controlling level of non-performing assets have been giving guidelines and getting norms for the banks in order to control the incidents of faults. Reduction of NPAs in banking sector should be treated as national priority item to make the Indian Banking system more strong, vibrant and geared to meet the challenges of globalization.

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