

Impact of Recovery Mechanism on Management of Non-Performing Assets of Public Sector Banks

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Abstract - The Indian banking sector is facing a serious problem of mounting NPAs. Increased NPAs affect the profitability and liquidity of bank. . Eliminating the peril of non-performing assets remains a daunting task. The solution of NPAs lies with proper credit assessment and recovery mechanism. Performance of recovery tools have not been satisfactory. This article is based on secondary data base gathered from various authentic sources of Government of India, Reserve Bank of India and Commercial banks. This paper critically analyses the recovery mechanism of NPAs with its three important wings i.e. recovery through Lok Adalat, DRTs and SARFAESI and its impact on NPA covering the years from 2013 to 2016.

Key word: Recovery management, Lok Adalat, DRTs, SARFAESI, NPA

I. INTRODUCTION

A well organized and developed financial system beholds the key to the development of an economy. Banks are the one of the important integral and vital part of the financial system. The basic function of a bank is to accept deposits and provide loans and advances. The difference between interest on loan and deposits is known as spread. So, borrowers has to repay the loan amount (Principal) along with interest on agreed contract. If the loan amount is not recovered on time ,the problems arises for banks. The loan which is an assets to the bank ceases to generate any income to the bank, gets converts into NPA .The concept of NPAs comes to existence. The NPAs is an asset which does not generate income for the banks. NPAs not only affects the liquidity and the profitability but also the efficiency of a bank .

It should be to remembered that recovery of fresh loans or old loans, is basis to NPA management.Recovery mechanism is a process of planning, testing, implementing the recovery procedures and standards required to restore financial assets in the event of failure of the firm. Mainly recovery is done through three major tools as are discussed below:

II. THREE MAJOR RECOVERY MECHANISM FOR NPAS

LOK ADALAT

For cost effective and quicker disposal of cases, banks are now approaching the legal system. Lok Adalats are organized under Legal Services Authority Act, 1987 by the state and or district and taluka Legal Services Committee. Branches have to consult Local Legal Services Committee and IBA chapter, if necessary for organizing Lok Adalats.

Without resorting to courts, banks can now administer justice through the process of Lok Adalat .

DEBT RECOVERY TRIBUNALS (DRTS)

The low rate of loan recoveries is one of the biggest problems faced by bank. This has a bearing on the accounting standards as well as on current operations of banks. It is in this context the „Recovery of Debts“ due to Banks and Financial Institutions Bill, 1993“ was passed in August 17, 1993 that facilities establishments of Debt Recovery Tribunals for expeditions adjudications and recovery of debt due to any bank or financial institutions.

SARFAESI ACT

SARFAESI ACT was formed in Dec' 2002 based on recommendations of a) Committee on Banking Sector reforms (Narasimham Committee Report II) and b) Restructuring of Weak Public sector Banks (Verma Commtee). This Act was formed with the objective of rapid recovery of defaulting loans and to minimize the mounting levels of Non-performing Assets of banks and financial institutions. This Act allows banks and financial institutions to auction properties (commercial/residential) when there is no repayment of loans by the borrower. It empowers the lending bank to issue demand notice to the borrower along with his/her guarantors for repayment of loan.

The Act enables the bank to recover loans through:

- Securitization
- Asset Reconstruction
- Enforcement of Security without intervention of the court

Objectives

1 To know about most commonly used recovery methods in public sector banks.

- 2 To measure the importance of recovery channels in terms of recovery
- 3 To provide suggestions for improvement in recovery mechanism of public sector banks.

Data Source

The data required for the study is purely secondary in nature, collected from secondary source:

- a) Annual reports of the bank
- b) RBI Report on Trend and Progress of Banking in India
- c) Manual of instructions on loans and advances
- d) Research Papers and Published Articles

III. LITERATURE REVIEW

Ahmed, J.U (2008) studied the NPA recovery management and explained that the debt recovery tribunals and SARFAESI Act are the most effective recovery channels in terms of the amount recovered among the various channels of recovery.

Bose (2005) mentioned that, while there have been several schemes in the past to facilitate the recovery from NPAs, but they are not satisfactory in terms of NPAs reduction. It was hoped that SARFAESI Act will help banks to reduce and recover money from NPAs.

Sharma, M (2005) observed that more essential steps needs to be taken to resolve NPA problem is within the time frame In post - liberalization period various measures and recovery mechanisms were initiated in Indian banking system. Problems of NPA cannot be totally eliminated in banking; through proactive and reactive measures it can be controlled. Effective risk assessment, credit evaluation and monitoring techniques are proactive measures while various recovery measures that include Asset Reconstruction

Companies (ARCs), Debt Recovery Tribunals (DRTs), Lok Adalats, SARFAESI Act etc. are reactive measures. The SARFAESI Act 2002 allows banks and other financial institutions to recover NPA accounts without the intervention of the Court. It provided three different methods for recovery of non-performing assets, namely: -

- Asset Reconstruction,
- Securitization,
- Enforcement of Security without the intervention of the Court

Thus it may be observed that SARFAESI helped to toughen the banking sector and allows them to securitize recovery of NPAs.

Kumar (2003) talked about the need, process, summary and pros and cons of the SARFAESI Act. Researcher analyzed that this Act as compared to other recovery tools ,have empowered banks and financial institutions in recovery of NPAs

Muniyappan G.P. (2002) the researcher has presented a very comprehensive picture of NPA management. While NPAs are decreasing in percentage terms, the absolute figure is still going up. RBI has introduced various measures like credit risk management model, compromise settlement methods etc for recovery of loans.

Khan (2000) pointed that banks and financial institutions could convert part of the NPA debt into equity of the defaulting company as a recovery strategy. Researcher advocated usage of credit derivatives and credit default protection contracts as a part of credit risk management and observed that risks associated with economic environment, unforeseen events specific to corporate borrowers are not covered under the present credit risk models.

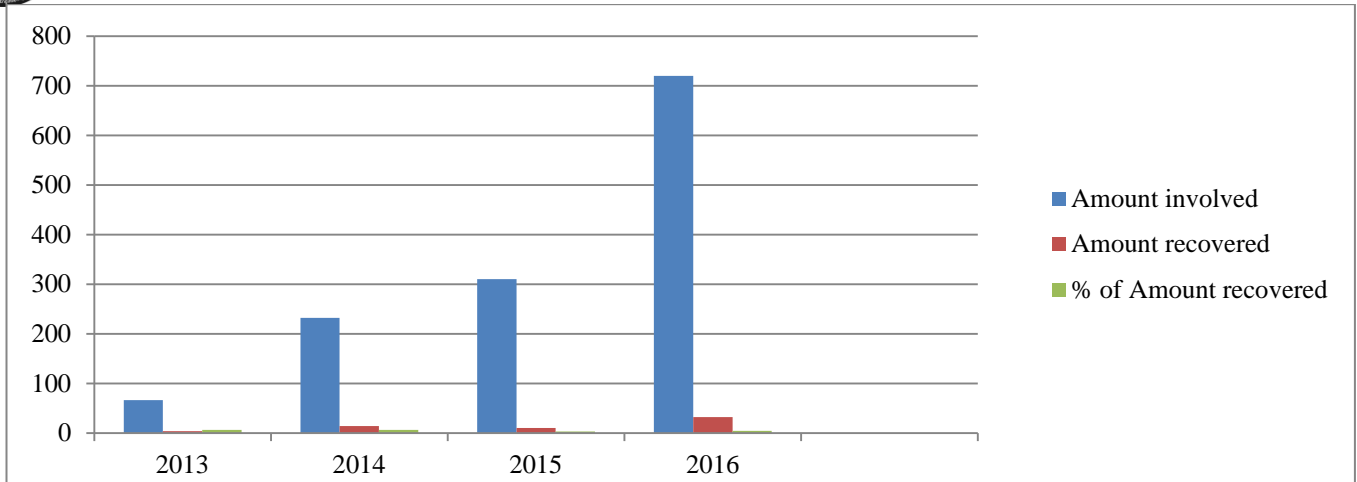
IV. ANALYSIS OF RECOVERY OF NON PERFORMING ASSETS

NPAs of Scheduled Commercial Banks Recovered through Lok Adalats

(Amount in Billion)

Year	No of cases referred	Amount involved	Amount recovered	% of Amount recovered
2013	840691	66	4	6.1
2014	1636957	232	14	6
2015	2958313	310	10	3.2
2016	4456634	720	32	4.4

Source: <http://dbie.rbi.org.in>



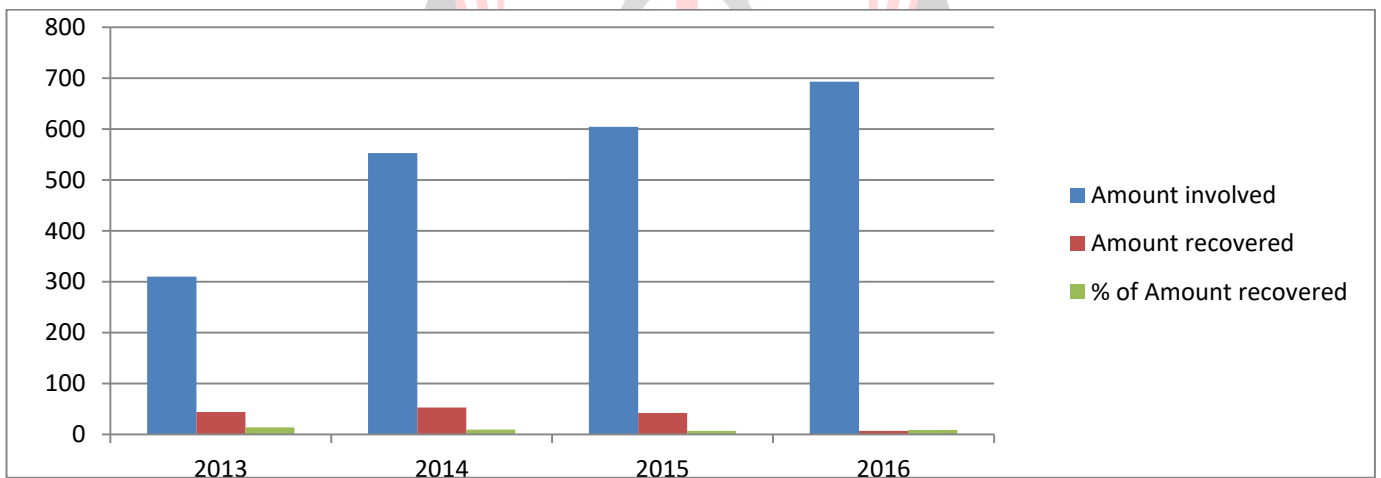
From the above table it is clear that the performance of Lok Adalats has decreased from 6.1% to 4.4 that are from the year 2013-2016

NPAs of Scheduled Commercial Banks Recovered through DRTs

(Amount in Billion)

Year	No of cases referred	Amount involved	Amount recovered	% of Amount recovered
2013	13408	310	44	14.2
2014	28258	553	53	9.6
2015	22004	604	42	7
2016	24537	693	7	9.2

Source: <http://dbie.rbi.org.in>

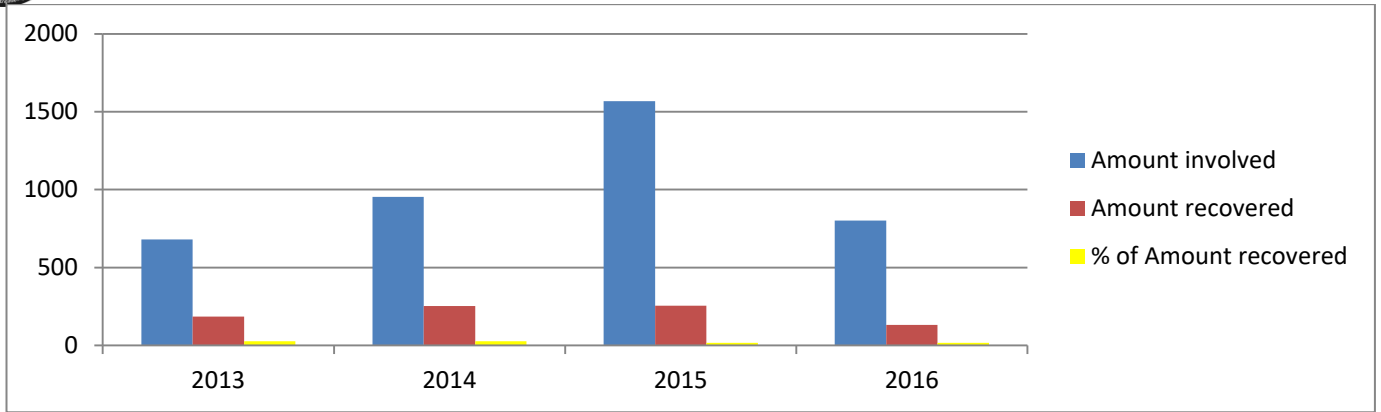


The above table and figure indicates the performance of DRTs with respect to NPAs recovery. The total amount of NPAs increased year by year even though the no of cases referred decreased during the study period that is 2013-2016.

NPAs of Scheduled Commercial Banks Recovered through SARFAESI Act

(Amount in Billion)

Year	No of cases referred	Amount involved	Amount recovered	% of Amount recovered
2013	190537	681	185	27.2
2014	194707	953	253	26.6
2015	175355	1568	256	16.3
2016	173582	801	132	16.5



Source: <http://dbie.rbi.org.in>

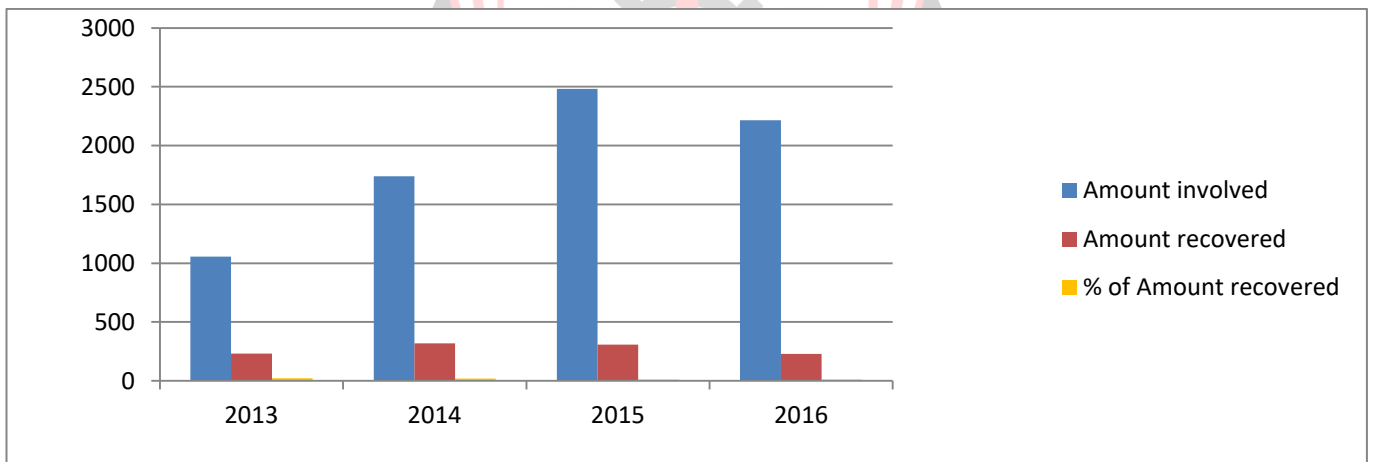
From the table the role of SARFAESI can be understood in NPAs recovery. The performance of SARFAESI is decreasing which is not desirable for growth of banking system.

NPAs of Scheduled Commercial Banks Recovered through all channels

(Amount in Billion)

Year	No of cases referred	Amount involved	Amount recovered	% of Amount recovered
2013	1044636	1057	233	22
2014	1859922	1738	320	18.4
2015	3155672	2482	308	12.4
2016	4654743	2214	228	10.3

Source: <http://dbie.rbi.org.in>



The above table & figure showed the performance debt recovery channels. No of cases and amount involved has increased but the percentage of amount recovery has decreased year on year during the study period which bad sign for health of the banking system.

Comparison between Lok Adalats ,DRTs and SARFAESI Act

Year	Sr No.	Recovery Channel	Lok	DRTs	SARFAESI	Total
			Adalats		Act	
2012-13	1	No. of cases referred	840691	13408	190537	1044636
	2	Amount involved	66	310	681	1057
	3	Amount recovered*	4	44	185	233
	4	3 as per cent of 2	6	14	27	22
2013-14	1	No. of cases referred	1636957	28258	194,707#	1859922
	2	Amount involved	232	553	953	1738
	3	Amount recovered*	14	53	253	320

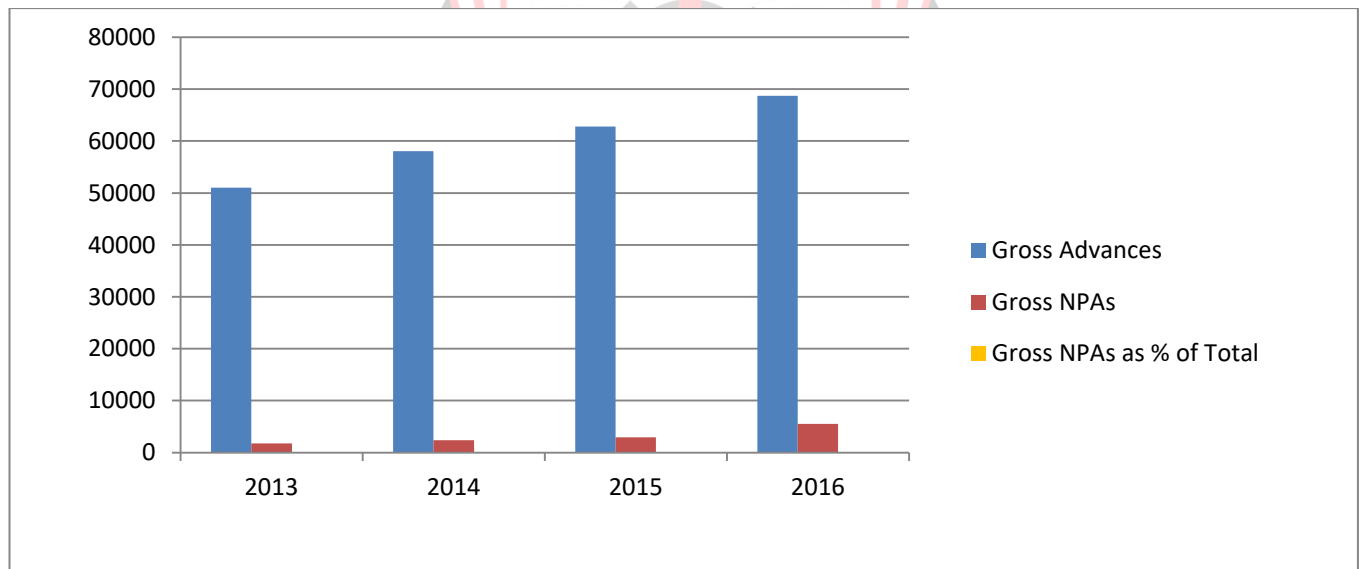
	4	3 as per cent of 2	6	10	27	18
2014-15	1	No. of cases referred	2958313	22004	175355	3155672
	2	Amount involved	310	604	1568	2482
	3	Amount recovered*	10	42	256	308
	4	3 as per cent of 2	3	7	16	12
2015-16	1	No. of cases referred	4456634	24537	173582	4654753
	2	Amount involved	720	693	801	2214
	3	Amount recovered*	32	64	132	228
	4	3 as per cent of 2	4	9	17	10
2016-17	1	No. of cases referred	2152895	28902	80076	2261873
	2	Amount involved	1058	671	1131	2860

Source: <http://dbie.rbi.org.in>

Gross advances and Gross NPAs of Scheduled commercial banks
 (Amount in Billions).

Year	Gross Advances	Gross NPAs	Gross NPAs as % of Total
2013	51025	1759	3.45
2014	58022	2395	4.13
2015	62826	2943	4.69
2016	68738	5504	8.01

Source: <http://dbie.rbi.org.i>



The above table explains that though the gross advances but gross NPAs and the percentage of gross NPAs to total gross advances have also increased of Scheduled commercial banks, which means the performance of banks is not satisfactory.

V. CONCLUSION

The NPAs have always created a big problem for the banks in India. It is just not only problem for the banks but for the economy too. Profitability, liquidity and efficiency of banks is adversely effected due to growth in non-performing assets. This study shows that various mechanisms have

been introduced by government to control NPA. Lok Adalat has not shown considerable success in recovery of NPA i.e percentage of recovered amount to total has not touched even double figures .SARFAESI Act and the Debt Recovery Tribunals (DRTs) have proved to be most effective in terms of amount recovered among the various channels of recovery. There is need to broaden the scope of SARFAESI act so that recovery mechanism could be speedy. However, Indian Bank has slippages during the period of study in controlling of NPAs in the early years of the decade.. Though, there is a progress, bankers are struggling (particularly Public Sector banks) to reduce their

NPAs level to maintain the stability and profitability in the business. Amidst rising non-performing loans, the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act (Sarfaesi Act) was the most potent tool in the hands of banks for recovering bad loans. The Sarfaesi Act empowers banks and financial institutions to recover their non-performing assets without the intervention of courts.

According to the RBI's Report on Trend and Progress of Banking in India, 2012-13, banks have recovered Rs 18,500 crore through the Sarfaesi route. Also, in terms of efficiency, the Act has proved to be more effective than the debt recovery tribunals (DRTs) or mediation by Lok Adalats.

VI. SUGGESTIONS

- **Less Government Interference** Government interference in credit distribution system should be minimised. Government interference hinders credit process.
- **Non availability of Appropriate Information** Non-availability of timely and sufficient information about the defaulters leads to delay in identification of potential NPAs and executing timely remedial measure. Timely identification of NPAs may upgrade potential NPAs to standard assets.
- **Computerisation of the Branches:** Branches are not well equipped with adequate facilities to counter NPAs problem. Due to vast network of branches, computerization of banking activities is not available in all the branches.
- Customers training and awareness are the most effective way to improve recovery..
- Proper identification of borrower and the purpose of loan, careful scrutiny of the project, repayment capacity, close follow up and monitoring.
- Government assistance and help in case of genuine defaulters.
- Priority to those borrowers who have repaid their loans promptly.
- Concession in interest for prompt repayment.
- Communication with Bank about Problems Faced:

More than half of the customers do not communicate their problems to the bank. However, those who approached the bank with their problems/difficulties got solution to their problem or relief in repayment.

Radical changes have been made in the Indian Banking Sector after the liberalization and globalization emerged in the year 1991. The reforms were like interest rate regulation, reducing of reserve, prudential norms etc. Prior to 1991, the legal process to recover the bad loans was tiresome, since it takes several years' legal civil proceedings for getting decree.

Indian Banks improved their business and technology to meet the requirement of the customers at ease and made the banking systems as friendly user. Though, there is a progress, bankers are struggling (particularly Public Sector banks) to reduce their NPAs level to maintain the stability and profitability in the business.

The increase in the ratio of Non-Performance Assets (NPA) affects the profitability and of the banks, as they have to allocate provisions for the settlement of NPAs. Under the Recovery of Debts to Bank.

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