CRACKING THE BAD LOANS :
IMPERATIVE FOR THE FINANCIAL STABILITY OF THE BANKING SYSTEM

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With the economic variables moving southwards, the bad loan book or the Non Performing Assets (NPAs) of the banks have started registering growth, much against the wishes of the bankers. As per Reserve Bank of India, Net NPAs to total assets ratio of banks has increased from 1.28% in FY12 (Year ended March 2012) to 1.68% in FY13, whereas Gross NPA ratio of banks increased from 2.94% in FY12 to 3.42% in FY13. This is largely contributed by Public Sector Banks (PSBs). In fact, the private banks have actually reduced their NPA book. Net NPAs of 26 PSBs has increased from 1.53% in FY12 to 2.02% in FY13. The total value of bad loans of PSBs has been established at ` 1,65,000 crore for FY13, which has gone up to ` 1,82,829 crore as on June 30, 2013. Interestingly, the top 30 defaulters of the PSBs accounted for ` 63,671 crore of the gross NPA, which is 34.79% of the bad loan book. In fact, the banking system has written off more than about ` 1,00,000 crore in the last 13 years and 95% of the amount was due to large borrowers. NPAs ail the PSBs more than the private sector banks. SBI has incurred whooping NPAs, especially in the agriculture (9.39% of Gross NPA in FY13) and industrial (16.40% of Gross NPA in FY13) sectors.

NPAs not only reduce the loan book and interest income considerably, but also require incurring a lot of cost by way of resources spent to salvage the recoverable amount, legal expenses, under-recoveries and write-offs. Too much of NPAs can hamper the financial stability of the bank and can constraint its profitability, liquidity and lending capacity significantly. RBI has advised the banks that willful default should be dealt with as a criminal offence and list of defaulters be published publicly. The Finance Ministry has also advised stern action by banks against all bad loans.

A tighter due diligence is required from the PSBs, to reduce the NPAs and improve their profitability. There is a need to maneuver from the existing exposure norms to tighter exposure norms before pledging the money by the lenders. Tightening of exposure norms is necessary considering RBI has advised banks to be Basel III compliant by March 2018. Moreover, transparency of data and easy access to data is required to avoid unnecessary risk taking. Regulatory bodies should make collective and calculated efforts to empower banks, financial institutions and stock exchanges. Awareness amongst the investors and the lenders needs to be created on the existing and the potential defaulters. A stringent example needs to be set to minimize the NPAs. Unless the banking system of the economy is strong, it will be difficult for India to create a healthy investment and growth-oriented environment.