

Analysis of Composition of NPA's - A Case Study of BDCC Bank, Belagavi

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Abstract

In the present paper, an attempt has been made to analyse the composition of NPAs and the aging pattern, to find out the implications of NPAs on the financial position and stability of the bank. Since NPA problem is a burning issue in the banking field as well as in the nation's economy, the topic commands importance in the banking field, in general and to the BDCC Bank in particular. The study may bring some important points to the notice of the concerned Bank and help to find the key areas to focus and improve in the days to come.

Key words: NPA, BDCC Bank, Financial position

Introduction

The introduction of NPA norms in the banks in India in the year 1991-92 as a result of the recommendations of the Narasimham Committee Report resulted into great changes in the banking field. NPA norms are considered to be the major highlights of the banking reforms which took place after the introduction of LPG in Indian Economy. The banks earlier to these reforms and NPA norms, treated the interest accrued as income without bothering about the receipt of such interest in cash. They conveniently adopted the double entry system of book-keeping and credited the loan accounts with interest due (whether it is received from the borrower or not). This actually led to increase in the loan balances on the one hand and false profit on the other. Both were dangerous and could prove fatal to the banks.

A bank's loan portfolio includes various types of loans categorized as per the RBI guidelines, term of the loans, security provided, the purpose for which they are sanctioned etc. These categories are made for various statutory and administrative purposes. Therefore when the loans are categorized as Non-Performing Assets, these classifications also continue.

In which category NPAs are more or less, will guide us as to whether the recovery is possible or not. For example, if NPAs are more in Cash credit loans, it means recovery of such loans is difficult. If NPAs are more in long-term housing loan category, then it means bank has got the backing of solid security to resort to recovery, but it entails a lengthy legal process. Same way, If NPAs are more in unsecured doubtful assets category or in Loss category, the chances of recovery of loans is almost a remote possibility. Bank may have to write off these loans.

Thus the quality of the assets and the possibility of their recovery is revealed by the composition of NPAs. The analysis of composition of NPAs of a bank guides us in determining the quality of the loan portfolio, recovery chances, impact of NPAs on cost, profitability, and credibility of a bank, impact on its financial feasibility etc. That's why the study of composition of NPAs becomes important as well as relevant.

Statement of the problem

Every bank is facing a major problem of monitoring the loans, avoiding them from slipping into NPA category. Despite all the measures taken to lend only to good and creditworthy borrowers, defaults cannot be avoided 100%. The problem starts once the loan jumps into Non-performing asset category. As it is, such loan will not produce any income to the bank, the bank has to make a provision on such loan which results into further reduction of profit. Banks with severe NPA problems are not allowed to declare dividends without the permission of the RBI. Further the asset quality will speak about the financial position of the bank and further, its capacity to honor the demands of the depositors in time. Hence banks are very keen in controlling their NPA levels and further to reduce them.

This study will try to analyse the composition of NPA loans to find out the problems involved with different categories of NPA loans, the problems and possibilities of recovery of such loans.

Objectives of the study

1. To study the composition of NPAs purpose-wise and category-wise.
2. To study the trends in composition of NPAs of Belgaum DCC Bank
3. To study the impact of composition of NPAs on the BDCC bank's financial position

Research methodology

Only the secondary data have been collected and used for this study. The secondary data have been collected from the BDCC Bank's Annual reports of 10 years from 2005 to 2014, and the NPA reports which are submitted by the Bank to the RBI. The absolute figures, percentages and averages are used for analysis.

Scope of the study

The scope of the present study is limited to the Belgaum District Central Co-operative Bank Ltd, Belgaum. For the purpose of the study, we have made a detailed analysis of the composition of the NPAs of the said bank for last 10 years from 2004-05 to 2013-14. The study includes a detailed analysis of composition of Gross NPAs purpose-wise and category-wise.

Review of literature

A review of literature on the subject reveals that some researchers have made empirical as well non-empirical study on the NPAs of different DCC banks either individually or the DCCBs of a state or of the entire country to find out the impact of such NPAs on the financial stability, profitability and cost of the banks.

1. A Dharmendran (2011) in his paper finds that the NPAs both gross and net were relatively high in all DCC banks in India. He finds that the main problem arises due to the Government policy of liberal credit to farmers and other weaker section under priority sector advances. He concludes that the overall performance of DCCBs in India is a mixed one. Their main weaknesses are heavy overdues, inefficient funds management, inadequate and untrained staff, lack of adequate supervision etc. But the researcher has not given any suggestions to the DCCBs as such.
2. Dr. B.S. Bhatia, Dr. SukhmaniWaraich and VandanaGautam (2013) find that the overall position of NPAs against loan outstanding in DCCBs of Punjab (9percent) was much better than the DCCBs on all India basis (13 percent) but the position is really grave they say, when compared with commercial banks on all India basis (1.75 percent). The researchers find that the DCC banks are not using the legal weapon for recovery. They also opine that the staff of

DCC banks lack training and expertise to deal with new and various retail loan products. The staff needs proper training and professionalism towards retail lending, they say. They also suggest that these DCC banks need advance technology for banking activities. Representation of professionals on the board is another important suggestion they make. Credit counseling for the debt trapped borrowers is another important suggestion by the authors.

3. Kawale.Pushpalata.G. and SagarPandhari N. (2014) in their paper find that the Latur DCC Bank, Latur has a decreasing trend in the Gross NPAs whereas they have provided increasingly for such NPAs, hence the Net NPA was NIL. They find that the analysis of Gross NPAs, Net NPAs and the provisions made mark satisfactory financial performance of LDCC Bank. The CRAR level is also more than the prescribed levels. And the authors have not made any suggestions, since they find the position quite satisfactory.
4. Lakshmanan.C. and Dharmendran. A. (2007) in their article said that the NPA problem is less in the Chennai Central Co-operative Bank as compared to the other CCBs in Tamil Nadu. They also focus on the impact of NPAs on Net profit, investments, legal expenses and spread of the bank. The study concludes that the effective NPA management is essential to strengthen the financial position of the bank.

The studies already done have not gone deep in to the problem of slippage of NPAs from one category to the next worst category and the impact of such slippage. They have not even brought to light the risk involved in having NPAs concentrated in a single category or component. Most of the studies have even concluded that it is the Government directed agriculture loans that is the main cause of NPA problem. But the researchers try to establish the truth far away and contrary to the general belief. We have observed and convinced that it is not the small farmers' loans which go bad pose the real problem, but it is the big borrowers who are the real culprits endangering the financial position of the banks. With this background, the present study has been to find out the causes of slippage of NPAs from one category to another category, analyse the composition of NPAs and its impact on the financial position of the bank.

Belgaum D.C.C Bank

Started in the year 1919, the Belgaum DCC bank is now at the verge of celebrating its glorious centenary within 3 years from now. The bank has 85 branches spread all over the district of Belgaum catering to the needs of the farmers, primary agriculture co-operative societies, and other co-operatives, businesses and individuals. As on 31st March, 2014 the bank has a share capital of Rs 72.04 crores with a membership of 2,412 co-operative societies, 282 individuals and 206 associate members. The deposits of the Bank touched Rs 1710.31 crores and the loans disbursed amounted to Rs. 1525.69 crores as on 31st March, 2014. The net profit amounted to Rs 19.40 crores. The Bank has registered a remarkable growth in these 96 years and has earned a reputation in the district. Of late it has become more alert about the NPA problem and has made all efforts to tackle it. The provisions made against NPAs (Rs.102.52 crores where as the GNPA is Rs. 47.64 crores) are far above the RBI requirements, thus ensuring the profitability and financial stability.

Analysis of the NPA's- purpose-wise

If we analyse the NPAs according to the purpose for which they are lent we will come to know about the degree of risk the bank has because of such NPA loans. We may make an interpretation as to the possibility of recovery, the problems involved in realizing the securities, the legal complications etc.

From Table No 1, we can analyse the composition of GNPA as under;

1. NPAs in loan for agriculture operations and short-term loans constituted major portion of GNPA in the first year of study. It was as high as 47.66% of Gross NPAs in 2005 followed by NPAs in C/C loans to business which stood at 32.83%. But from the second year onwards, the trend has totally changed. NPAs in SAO and short-term have shown a declining trend continuously up to 2012 when they came down to just 2% of the GNPA. In the last two years there was a slight increase in NPA to 2.36% and 4.68% in the year 2013 and 2014.

This trend in NPAs in SOA and S-T shows that the bank has made full efforts to recover the interest and installments in these 10 years. Another major contributor was the state government. Since the state government has been allowing interest waiver on short-term agriculture loans, the recovery of installment amount (principal) is becoming easy for the bank officials.

Still in the last year, the NPAs in SAO and S-T increased to 4.68% which is almost double the previous year figure of 2.36%. Bank needs to give more attention to NPA recovery in this category.

2. The second major contributor to the GNPA in the first year of study i.e. C/C loans to business has turned into the highest contributor to the total GNPA immediately from the second year onwards. From 32.83% in 2005, it increased to 64.09% in 2006, and continued to remain or increase further. In the year 2012, it reached its peak at 88.14% of the GNPA. In 2014, though it has come down to 81.70%, still has remained the highest of all the categories.

As far as the proportion of C/C loans (business) to total outstanding advances is concerned, it has been the second highest contributor to the total advances. It has remained less than 30% always. And in the last year of study, its contribution was only 22.17% to the total advances, whereas the NPAs in the same year are 81.70% of the total GNPA, which is almost disproportionate. Bank has to give lot of attention to these NPA loan accounts, since the major portion of the NPA loans belong to this category.

As the C/C loans are inherently prone to high risk, bank should take care while sanctioning new limits. As far as the existing NPAs are concerned, it is observed that 3 major borrowers contribute 99.33% of total NPAs in this category. Bank should negotiate with these borrowers and initiate a compromise so that the bank's major problem regarding NPAs will be eliminated.

3. NPA in Term-loans was 18.82% of the GNPA in the first year of study, i.e. 2005. It has continuously decreased year after year till 2013, in which year it was 4.74% of GNPA. In the year 2014, it has been on the increase at 5.58% of GNPA. In absolute figures, it stood at Rs 2.66 crores in the same year. The declining trend in NPAs in term-loans as compared to increasing trend in outstanding term-loans to total advances, shows that the bank has sufficient control over this category loans. It has strongly controlled the NPAs, at the same time new loan disbursements must have been done taking all precautions as to the purpose, security and borrower's creditworthiness have been done taking all precautions as to the purpose, security and borrower.
4. NPAs in C/C and O/D loans to individuals have shown a decreasing trend in the initial 4 years from 2005 to 2008. From 0.69% in 2005 it has come down to 0.01% of total NPAs in these years.

But in 2009, suddenly it has increased to 4.66% of GNPA. Even in absolute terms it has gone up to Rs. 4.72 crores from a mere Rs. 2.00lakh in 2008. After 2009, there has been volatility, but it has been in the range of 3.24% to 8.04% upto 2014. It was at its peak in the last year of study i.e. 8.04% of GNPA, though in absolute terms it has come down from Rs 4.79 crores in 2013 to Rs 3.83 crores in the same year (2014).

Bank should take absolute care while sanctioning new limits in this category. Since the borrowers have a common belief that these loans can be renewed every year without having the necessity to pay interest, it becomes very difficult for the bank officials to explain the new NPA norms to convince the borrowers to pay interest regularly. Hence it is better to avoid C/C and O/D limits on the security of NSCs, Insurance policies as well as on gold.

Analysis of aging pattern of NPAs

The analysis of aging of NPA accounts will throw light on the possibility or otherwise of recovery of these loans. The analysis will also describe us the danger position of the bank. It gives an alarming message to the bank to take rigorous steps for recovery, because, the slip of accounts from one category to another will indicate the seriousness of the problem. The more frequently the loan accounts slip into next category, the more remote will be the chances of recovery of such loans.

From Table No 2, the following analysis can be made

1. The sub-standard loans which were 30.74% of the GNPA in the first year of study, which were also the highest in that year, have shown a declining trend after 2008. Though there is an increase from 18.13% in the year 2006 to 23.63% in 2007 and 36.77% in 2008, thereafter the percentage has declined to 8.20% in 2009. Though there is some increase in the last 2 years of study, the overall trend is of declining one, which is a good sign, as far as these loans are actually recovered in cash. But if they have slipped into the next category, i.e. doubtful, then the position is still worst.
To decide and analyse the effect of decrease in sub-standard assets, we must analyse the trend in doubtful assets category simultaneously.
2. When we analyse the doubtful assets in all three sub categories of D1, D2 and D3, we see that the absolute figures as well as the percentages have declined continuously, which is a good sign again. From 11.05%, 14.85% and 9.01% respectively in the year 2005, they have come down to 0.53%, 1.24% and 4.41% in the year 2014. But along with these numbers, when we study the unsecured portion of doubtful assets, we observe an alarming increase in the category. From 7.22% in 2005, they have shot up to 81.83% of total NPA in the year 2009 and thereafter though they are on the declining mode to come down to 64.53% in 2010, 64.76% in 2011, they have continued to remain a big worry for the bank. Though in the last year of study i.e. 2014 they have come down to 39.90%, the botheration continues because banker is left with no option, but to bring a moral pressure on the borrowers by compromise using all human skills to make the borrower agree to pay the outstanding balance. This is inevitable because the banker is in a vulnerable position due to absence of security for the loan.
3. The loss assets comprise a major portion of the Gross NPA making the position of the bank still worse. Though the absolute figures and percentages have both come down from Rs 48.65 crores (27.13%) in 2005 and Rs 48.61 crores (50.52%) in 2006 to just Rs 3.06 crores (3.35%) in 2007 and to Rs 3.03 crores (2.71%) in 2008 and Rs 2.98 crores (2.94%) in 2009, thereafter they have suddenly surged to a staggering Rs 23.82 crores (24.82%) in 2010 and have continued to remain almost the same in terms of absolute figures. Percentage -wise, they have suddenly shot up to 49.60% in 2014, which shows that there is absolutely no recovery in this category.

If we consider the unsecured portion of doubtful assets and loss assets together, we will be surprised to find that 89.5% of the total NPAs are almost non-recoverable. In both the cases, security-support is not available and possibility of recovery is zero. They are just burdening the bank's portfolio.

The management of the bank should seriously decide the fate of these loans. Because a deeper study in to such accounts shows that it is only 3 big loan accounts which are the crux of the problem. If these loans are either recovered or written off, the bank can clean up the Balance Sheet and trim the loan portfolio. If these loans are totally unrecoverable, then there is no point in continuing them as unsecured doubtful assets and loss assets. Once these loans are eliminated, the major problem is over. Anyway the bank's management has not yet made such hard decision.

We can summarize that the majority of NPA loans are in the category of unsecured doubtful and loss assets and hence are in the worst position, and need immediate and strict action without any personal bias or political interference.

Major findings

1. It can be noticed that the bank has major problem with C/C loans to business, because the NPAs in these loans are the highest contributing 81.7% of Gross NPAs. The bank may find it very difficult to recover.
2. C/C and O/D loans to individuals stand second in terms of percentage of NPAs to GNPA (8.04%). But the bank can take drastic steps to recover these bad loans and must take proper precautions while sanctioning new loans in this category.
3. If we observe the aging pattern of the NPAs, the position of the Bank seems worst, because majority of the NPAs are in the group of unsecured doubtful and loss assets (89.5%) which means that the chances of recovery are very less.

4. The other NPA records (Top 20 defaulters) reveal the fact that only 3 big institutional borrowers are responsible for the major problem of NPA in the bank. If these 3 loans are recovered the major problem is solved.

Suggestions

1. The bank should train the employees properly in the field of credit appraisal and NPA management and NPA recording.
2. Bank should classify the NPA accounts at the branch level itself. The present practice of calculating and recording of NPAs at Head Office level should be done away with, so that the Branch Managers can control their loan portfolio at their levels and get the early warning signals at branch level itself.
3. Bank should modernize its operations by computerizing all the banking operations and MIS so that the information about the defaulters and NPA accounts can be updated and circulated easily among the branches as well as other banks.
4. Bank should become totally professional and come out of the influence of political interference.
5. Bank should recover the 3 big loans which are in C/C loans category so that the bank will come out the problem totally. After that the bank will have less than normal level of NPAs.

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Table 1 Showing composition of NPA loans (Amount in Rs crores)

Year	Absolute figures/ Percentages	NPAs in SAO & S-T loans	NPAs in C/C & O/D to Individuals	NPAs in C/C to business	NPAs in term loans	Gross NPAs
2005	Amt	85.45	1.23	58.87	33.75	179.3
	%	47.66	0.69	32.83	18.82	100
2006	Amt	20.72	0.93	61.69	12.92	96.26
	%	21.52	0.97	64.09	13.42	100
2007	Amt	16.49	0.68	60.11	13.93	91.21
	%	18.08	0.75	65.9	15.27	100
2008	Amt	16.73	0.02	80.94	14.04	111.73
	%	14.98	0.01	72.44	12.57	100
2009	Amt	8.18	4.72	76.96	11.37	101.23
	%	8.08	4.66	76.02	11.23	100
2010	Amt	5.77	3.93	76.96	9.33	95.99
	%	6.01	4.09	80.18	9.72	100
2011	Amt	3.64	3.24	72.77	5.63	85.28
	%	4.27	3.8	85.33	6.6	100
2012	Amt	1.62	4.11	71.26	3.86	80.85
	%	2	5.08	88.14	4.78	100
2013	Amt	1.91	7.79	70.62	3.85	81.17
	%	2.36	5.9	87	4.74	100
2014	Amt	2.23	3.83	38.92	2.66	47.64
	%	4.68	8.04	81.7	5.58	100

Table 2 Showing composition of NPA loans (Amount in Rs crores)

Year	Absolute figures/ Percentages		Doubtful assets				Loss Assets	Gross NPAs
			D1	D2	D3	Unsecured		
2005	Amt	55.11	19.81	26.62	16.16	12.95	48.65	179.3
	%	30.74	11.05	14.85	9.01	7.22	27.13	100
2006	Amt	17.44	4.7	5.04	6.73	13.7	48.61	96.26
	%	18.13	4.88	5.24	6.99	14.24	50.52	100
2007	Amt	21.55	3.38	1.69	2.97	58.56	3.06	91.21
	%	23.63	3.71	1.85	3.26	64.2	3.35	100
2008	Amt	41.08	2.74	3.19	3.06	58.63	3.03	111.73
	%	36.77	2.45	2.86	2.74	52.47	2.71	100
2009	Amt	8.3	1.7	2.95	2.47	82.85	2.98	101.23
	%	8.2	1.68	2.91	2.44	81.83	2.94	100
2010	Amt	6.11	0.8	1.07	2.25	61.94	23.82	95.99
	%	6.37	0.83	1.11	2.34	64.53	24.82	100
2011	Amt	3.58	0.34	0.62	2.17	55.23	23.34	85.28
	%	4.2	0.4	0.73	2.54	64.76	27.37	100
2012	Amt	1.96	0.39	0.26	1.42	53.49	23.33	80.85
	%	2.42	0.48	0.32	1.76	66.16	28.86	100
2013	Amt	2.74	0.21	0.55	1.99	52.03	23.65	81.17
	%	3.37	0.26	0.68	2.45	64.1	29.14	100
2014	Amt	2.06	0.25	0.59	2.1	19.01	23.63	47.64
	%	4.32	0.53	1.24	4.41	39.9	49.6	100