NPA Management in Regional Rural Banks

A case study of Manipur Rural Bank

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ABSTRACT

The present study is an attempt to analyze the Non Performing Assets (NPAs) of Manipur Rural Bank (MRB). Adequate credit availability to the rural masses is also one of the main objectives of the Government of India. It will bring the socio-economic development of the country. To obtain this objective, Regional Rural Bank (RRBs) were established (first five RRBs established in 1975) to provide loans and advances to the common people who lived in rural areas. Manipur Rural Bank (MRB) has also been taking its role for the economic development of the rural people since its inception in Manipur (1981). Unfortunately, this bank is now facing the problem of NPAs. Non recovery also affects the profitability of banks. In fact, it is the level of Non-Performing assets which to a great extent, differentiate between a good and a bad bank.

1. INTRODUCTION

The economic development of a nation mainly depends on the availability of adequate credit facility to the various needy people. It is by providing credit to agriculture laborers, rural artisans, landless laborers, marginal farmers, industrialist, traders and businessmen etc. which can be achieved economic progress. The new economic liberalization measures initiated by the Government of India in the year 1991-92 which made many changes in the financial sector including revamping of the banking industry by transforming it into a strong, efficient and self-sustaining system. In these new norms, it also introduced the classification of bank loan assets based on their quality and these were expected to reflect the efficiency of the banks in managing their loan sections. Accordingly, with the commercial banks and Regional Rural Banks (RRBs) have also advised by the Reserve Bank of India (RBI) commonly to adopt prudential and more realistic norms for the purpose of classification of assets, income recognition and provisioning. These not only profitability but equity of the RRBs is also going to be affected considerably by the extent of NPAs brought by these banks. Therefore, there must be immediate and urgent need of due attention be paid by the RRBs for controlling or minimizing NPAs for improving financial health of these banking institution in future.

In accordance with the Regional Rural Banks Act, 1976, the Manipur Rural Bank (MRB) was established on 28th may, 1981 as a join undertaking of Government of India, Government of Manipur and United Bank of India (Sponsored Bank) by contributing share capital at the ratio of 50:15:35 respectively.

The bank started its operation with an objective of economic development of the rural people of the state, particularly the weaker sections by participating in different poverty alleviation programmes of Central and State Government. The bank is one of the 49 RRBs restructured in the 1st phase by the Government of India and has been operating with a network of 27 branches spread over in all nine districts of the state (Manipur).

2. REVIEW OF LITERATURE

The importance of MRB is an institution for financing the rural masses has been increasing since it came into existence. It provides loans and advances under the different categories like long term, medium

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term and short term to rural artisans, agriculture laborers, landless laborers, marginal laborers, traders and industrialists etc. However, MRB is now facing the problem of NPAs. A many studies have been conducted hitherto by various researchers to examine the role of bank finance in uplifting weaker section of the rural people. But no study relating to NPAs management in MRB has been done so far in this region. The related literature has been scanned and reviewed under here.

Tripathi (1986) observed on the basis of his study that the recovery percentage had never been more than 33.3 percent. In fact, it was decreasing and overdue were mounting. It would be desirable to take some effective effort to improve the recovery position.

Singh &Tiwari (1989) examined the diversion loans for other purpose is one of the important causes of poor repayment of agriculture loans. The coefficients of multiple determination (R2) suggest that five variable (size of land holding, consumption expenditure per family member, credit gap, time gap and membership of non-village level organization) together explained 80% of the variation in percentage loan diversion and 70% of the variation in the amount of loan diversion. Therefore, there variables can serve as effective instruments for controlling the problem of diversion.

Sikidar (1992) in his study on "Rural Banking – An Infrastructural Input for Hill Area Development" has critically evaluated the role of bank finance in the development of Hill area in North-East. He has suggested for a practical approach towards recovery of bank loan from the tribal population in Hill areas.

Rangaranjan (1994) found that the major task before the Indian public sector banks is to improve their financial performance. To improve profitability, he suggested that banks have to reduce costs, improve in productivity and ensure better recovery performance of loan. He identified NPAs as the major drag on the profitability of

bank.

Kaveri V.S (2001) studied the non performance assets of various banks and suggested various strategies to reduce the extent of NPAs. In view of the steep rise in fresh NPAs advances, credit should be strengthened. RBI should use some new policies/strategies to prevent NPAs.

Patel A.R (2001) in his article "Rural Credit System Need for Restructuring" appreciated the present status of rural credit structure in respect of credit disbursal, recovery performances and building up NPAs etc. However, he suggested that an appropriate policy paper should have to be prepared by the Union Government in consultation with the concerned Ministries, RBI, NBARD, IDBI and State Government and after through discussion, strategy to implement the plans and programmes should be formulated so that credit institutions can simultaneously support area based development projects.

The report of the Expert Committee on Rural Credit (2001) under the chairmanship of V.S. Vyas highlighted that RRBs have gradually improved their recovery performances and brought down their level of NPAs.

The above cited studies have concentrated in one part or another in India and have no discussed/analyzed about the NPAs management in MRB. Therefore, the present study is an endeavor of NPAs management in MRB in the state (Manipur).

3.   MEANING OF NPA

RBI has advised banks to move to the 90 days norms for recognizing loans as non-performing, with effect from March 31, 2004. With a view to moving towards international best practices and to ensure greater transparency, it has been decided to adopt the 90 days overdue norm for identification of NPAs (from the year ending 31st March, 2004). Accordingly, an advance will be classified as an NPA where in the

case of:

- Term Loan the interest and /or installment of principal remain overdue for a period of more than 90 days,
- Overdue/Cash Credit, the account remains out of order,
- Bills purchased and discounted the bill remains overdue for a period of more than 90 days,
- Advances granted for agricultural purposes interest and/or installment of principal remain overdue for two harvest seasons but for a period not exceeding two half years and
- Other accounts any amount to be received remains overdue for a period of more than 90 days.

In the light of the Narasimhan Committee Recommendation, RBI has redefined NPA and advised the banks to classify their advances into the following four categories.

- **Standard assets**: It does not make any problem while paying interest or installment of the principal and usually carries more than normal risk attached to the business. These assets do not require provision. Hence, it is not NPAs.
- **Substandard assets**: It is treated as NPA for a period of not exceeding 1 year w.e.f. March 2005.
- **Doubtful assets**: These assets are treated as NPA when a period of above 1 years w.e.f. March 2005.
- **Loss assets**: These assets have been identified either by the bank or its auditor but not written off.

4.   ZERO NET NPA

Recently, the concept of "Zero net NPAs" also emerged. However, it does not mean that these loans have been recovered. But they simply indicate that capital or profits has been set aside as a cover for these bad loans banks have been able to enhance provisions for bad loans because of windfall profits that a plunge in interest rates bestowed on them. Four banks have already achieved the ideal "zero net NPAs" for the fiscal ended March 2004.

5.   REASONS FOR NON-PERFORMING ASSETS

An RBI study of 800 top NPA amounts in 17 banks reveal that the single most prominent reason for units becoming sick and amounts turning NPAs is the diversion of funds by promoters.

In respect of the RRBs, the problems identified relate to the inherent structural weakness, such as, restricted clientele, limited area of operation, and small size of loans, progressive hike in salaries and allowances of the employees etc.

Classification of loan assets of MRB and Schedule Commercial Banks is highlighted in table-1 and 5 (Appendix).The percentage of standard assets to total advances of MRB went up consecutive fours years i.e. from the year 1999-00 (48.07), 2000-01 (54.25), 2001-02 (58.96) and 2002-03 (64.97), came down in 2003-04 (61.68), increased in 2004-05 (66.62) & 2005-06 (74.40), again declined in 2006-07 (55.07) and came up very slightly in 2007-08 (55.98). In case of substandard assets, its percentage share to total advance was very fluctuating however it increased from 1999-00 (5.07 percent) to 2007-08 (9.25). Doubtful assets reduced subsequent four years from 1999-00 (46.71) to 2002-03 (4.66) and increased consecutive four years i.e. from 2003-04 (7.30) to 2007-08 (34.71). Loss assets enhanced from .14 percent (1999-00) to 23.68 percent which was the highest percentage occurred in the year 2001-02 and reduced to .04 (2007-08). The total advances over the years increased from Rs. 72798 (1999-00) to Rs. 380910 (2006-07) consecutively and came down to Rs. 328257 (2007-08). However, the percentage of standard assets to total advances in most of the years was not favorable position.

The position of NPAs in MRB is

highlighted in table-2. The opening balance of NPAs over the years are trend of increasing from Rs. 37,800 (2000-01) to Rs. 1, 71,127 (2007-08). Additional NPAs during the years (from 2000-01 to 2007-08), was fluctuating however it increased from Rs. 4,059 (2000-01) to 29,104 (2007-08).

Recovery performance had been varied and not satisfied position over the years. It decreased from Rs. 1,807 (2000-01) to Rs. 1,600 (2001-02) which increased to Rs. 3,978 (2002-03), again declined to Rs. 3,701 (20003-04), went up to Rs. 8,720 (2004-05) & Rs. 11,155 (2005-06) and again fallen down to Rs. 7,302 (2006-07) and rose up to Rs. 17,243 (2007-08). It was very fluctuating recovery performance. NPAs at the end of the years were trend of increasing over the years from Rs. 40,052 (2000-01) to Rs. 1, 82,988 (2007-08). In case of provision held against NPAs was Rs. 32,352 (2000-01) which came down to Rs. 32,014 (2001-02), went up consecutive five years from Rs. 33,816 (2002-03) to Rs. 60,978 (2006-07) and again declined to Rs. 38,118 (2007-08). Percentage of net NPAs to net advance was also very fluctuating. However, it reached to 46.57 percent in 2007-08. MRB is necessary to improve its recovery performance and to take up some effective steps else it would be groaning under the weight of mounting bad debts.

In table-3, it depicts the percentage of gross NPAs to total advances. During the eight years from 2000-01 to 2007-08, the percentage was declining trend up to 2005-06 (25.59) except in 2003-04 (38.31). Reducing percentage which was due to the continued focus of the various policy initiatives taken by the MRB like credit risk management, market risk management and operational management etc. But, the percentage rose up in last two years 2006-07 (44.93) and 2007-08 (44.02) respectively. It requires sustainable policies to become a favorable position for future of the bank. For the purpose of evaluation of performance of

MRB (highlighted in table-4) different parameters have been used selecting total deposit, total demand, total advances, recovery, overdue and credit deposit (C.D) ratio etc. Deposit mobilization is one of the important tasks of any commercial bank and for a RRB too. During these 9 years, total deposit have been increasing continuously from the year 1999-00 (Rs. 2, 10,717) to 2007-08 (Rs. 59, 34,957). It indicates a good performance of the bank in mobilizing the hidden resource of the rural people.

Through the reference period, total demand, total advance and recovery performance also in trends increasing. The credit expansion of the bank is mainly depends upon the level of deposits and other resources along with the demand for it. Disbursement of credit is also one of the main objectives of economic planning and it will meet the financial requirements of rural people. The total demand is increasing from the year 1999-00 (Rs. 52,820) to 2007-08 (Rs. 1,62,913), it means that rural masses need more and more credit and total advance also shows trend of increasing i.e. from the year 1999-00 (Rs.72,728) to 2006-07 (Rs. 3,80,910), it shows rapid increase in credit expansion of the bank however declined in 2007-08 (Rs. 3,28,257). But the recovery percentage of the bank was very dismal during first three years i.e. 33.70 percent (1999-00), 35.04 percent (2000-01) and 44.99 percent (2001-02) respectively. After that, recovery percentage could improve and occurred fluctuating slightly in the consecutive years. The recovery percentage reached to 49.93 (2003-04), 51.80 (2004-05), 50.17 (2004-05), 52.98 (2005-06), 51.24 (2006-07) and 44.08 (2007-08) respectively. However, these recovery percentages were unsatisfactory. Due to poor recovery performance and adverse law and order situation in the state (Manipur), overdue amounts have become in increasing trend i.e. Rs. 35,022 (1999-00) to Rs. 91,102 (2007-

08). It will eat-up the profitability of the bank in the long run. Hence, it becomes automatically NPAs.

The credit deposit ratio is the measuring rode of the bank performances in term of credit disbursement against its deposits. The low ratio indicates low credit disbursement and high ratio implies high and liberal credit policy of the bank. C.D ratio is also growing continuously from 34.55 percent (1999-00) to 74.55 (2006-07) except in the years 2003-04 (52.97) and 2007-08 (55.31). It is generally considered as an important parameter to analyze the performance of the bank.

6.   FINDINGS

The researchers have found out the following points from the present study.

- The percentage of standard assets to total advance was 55.98 in last year (2007-08) and loss assets were .04 percent which was not in favorable position of the bank.
- The level of NPAs of MRB was trend of increasing from Rs. 40,052 (2000-01) to Rs. 88,129 (2006-07). Recovery performance of the bank was not satisfied over the years. Percentage of net NPAs to net advance was also very fluctuating trend. It was 14.50 percent in 2005-06 which reached to 46.57 in last year (2006-07).
- The percentage of gross NPAs to total advances during the eight years was fluctuating trend. However, it reached to 44.02 in last year (2007-08).]

7.   SUGGESTIONS

To reduce the level of NPAs, there may be two steps of strategy i.e. 1) Curative measures for current NPAs management and 2) Maintenance of performing assets.

I)   Curative measures for Current NPAs Management.

- Early warning signals for initiating sickness must be identified and proactive remedial action should be taken up in time.
- Legal and regulatory environment must be created to avoid NPAs.
- Regular contact with borrowers and regular monitoring of the accounts is very necessary.
- There should be recovery camps.
- Increasing the number of debts recovery tribunals.
- Specific guidelines should be issued to the public sector banks (MRB) for settlement of NPAs of small sector.
- No recovery - no loan, such type of rule may be applied and the bank should provide loans and advances only to those borrowers who repaid the earlier loans. If possible, some rebate in interest could be given to the parties who repaid timely.
- The bank must keep close contact and develop regularly with the Government agencies like the Block Development Officers and Village Level Workers should be taken into consideration. Such type of environment will help to control NPAs.
- SWOT(s-strengths, w-weakness, o-opportunities, and t-threats) analysis of current NPAs/Irregular account must be done and an action plan drawn up by each Brach Manager for up gradation of assets and maintenance of the existing standard assets from degradation etc.

II)   Maintenance of Performing Assets.

- Control and regular follow-up of performing assets.
- Loan must be sanctioned timely.
- Proper appraisal of loan proposal leading to better credit decisions and realistic repayment period.
- MRB ought to issue of demand notices or give the information for repayment with the help of media like Radio, T.V, Cable Network and Newspapers etc. in the right time.
- MRB may take assistance of NGOs and Self-Help Groups for collection of

repayment of loan amounts.
- Legal action must be taken whenever necessary.
- There should be adequate staff at the branches.
- Cordial relation between borrowers and bank employees is very must essential.
- There might be rewards to borrowers who have regularly made repayment in time. It should encourage the other borrowers to get them included in the said category. For these purpose, Bank should keep loanee record systematically.
- Sincerity is the most important to become step forwards in both sides (bank employees & borrowers). On the other words, ethics of the masses must be in a good way.

8. CONCLUSION

The Indian public sector Banks have been facing a big problem of NPAs. The main reasons of NPAs were willful default, poor monitoring, business failure and diversion of fund etc. MRB is also one of them. NPAs were an important factor in the analysis of banks financial performance. Reduction in the level of NPAs is very necessary to improve profitability of the bank and comply with adequacy norms. To overcome the problem of existing NPAs, quality of appraisal, supervision, effective recovery and follow-up should be improved. Bank should give loans and advances in an effective way, for this purposes right amounts of credit is given to the right type of client. The MRB (employees) must investigate the borrowers how far they are sincerity and experience regarding the project which they applied for loan before disbursement of loans. The judicial system needs to be renewed to get change of quicker recovery of dues from the defaulters. It is necessary to enforce the securitization Act with more stringent provision to realize the securities and personal assets of the defaulters. The banking secrecy Act must be amended to enable the publication of the defaulter's names as willful default must be treated as criminal offence and hence dealt with seriously.

Table-1
Classification of loan assets of MRB.

(Rs. in thousands)

Years	Classsification of Assets				
	Total advances	Standard assets	Substandard assets	Doubtful assets	Loss assets
1999-00	72798	34998(48.07)	3692(5.07)	34006(46.71)	102(.14)
2000-01	87547	47495(54.25)	6709(7.66)	33208(37.93)	135(.15)
2001-02	114599	67572(58.96)	10365(9.04)	9518(8.30)	27144(23.68)
2002-03	138747	90150(64.97)	12360(8.90)	6471(4.66)	29766(21.45)
2003-04	164880	101706(61.68)	21079(12.78)	12048(7.30)	30047(18.22)
2004-05	239979	159884(66.62)	32309(13.46)	17926(7.46)	29860(12.44)
2005-06	344369	256240(74.40)	25302(7.34)	33209(9.64)	29618(8.60)
2006-07	380910	209783(55.07)	86263(22.64)	56090(14.72)	28774(7.55)
2007-08	328257	183764(55.98)	30375(9.25)	113970 (34.71)	148(.04)

* Given in (   ) is the percentage to total advances of different NPAs.
Source: Annual report of MRB (from the year 1999-2000 to 2007-08).

Table-2

Statement of NPAs in MRB *(Rs. in thousands)*

Years / Items	2000-2001	2001-2002	2002-2003	2003-2004	2004-2005	2005-2006	2006-2007	2007-2008
NPAs at the beginning of the years	37800	40052	47027	48597	63174	80095	88129	171127
Addition during the year	4059	8575	5548	18278	25641	19189	90300	29104
Recovery during the year	1807	1600	3978	3701	8720	11155	7302	17243
NPAs at the end of the year(A+B-C)	40052	47027	48597	63174	80095	88129	171127	182988
Provision Held Against NPAs	32352	32014	33816	34044	39054	44662	60978	38118
Net NPAs(D-E)	7700	15013	14781	29130	41041	43467	110149	144870
Total advance outstanding	87547	114599	138747	164880	239979	344369	380910	328257
Net advance(G-C)	55195	82585	104931	130837	200925	299707	319932	311014
% of net NPAs to net advance(F/H*100)	13.95	18.18	15.09	22.26	20.42	14.50	34.43	46.57

Source: Annual report of MRB (from the year 2000-01 to 2007-08

Table-3

Percentage of gross NPA to total advance.

Years	2000-01	2001-02	2002-03	2003-04	2004-05	2005-06	2006-07	2007-08
Gross NPAs	45.75	41.04	35.03	38.31	33.37	25.59	44.93	44.02

Table-4

Overall performance of MRB.

Years	Total deposits	Total demand	Total advance	Recovery	Overdue	C.D. ratio (%)
1999-00	210717	52820	72798	17798 (33.70)	35022	34.55
2000-01	227618	57958	87547	20311 (35.04)	37647	38.46
2001-02	234948	71867	114599	32334 (44.99)	39533	48.78
2002-03	253969	81856	138747	40870 (49.93)	40986	54.63
2003-04	311250	91310	164880	47301 (51.80)	44009	52.97
2004-05	368394	103745	239979	52047 (50.17)	51698	65.14
2005-06	464979	131535	344369	69690 (52.98)	61845	74.06
2006-07	510945	145571	380910	74596 (51.24)	70975	74.55
2007-08	593495	162913	328257	71811 (44.08)	91102	55.31

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Table - 5
Classification of NPA of Scheduled Commercial Banks
As percentage of Total Gross Advances (in percentage)

Year	Standard Assets	Substandard Assets	Doubtful Assets	Loss	Total Gross NPA
		Scheduled Commercial Assets			
2004	92.9	2.3	4.0	0.9	7.2
2005	94.9	1.2	3.3	0.6	5.1
2006	96.7	1.0	2.0	0.4	3.3
2007	97.5	1.0	1.2	0.3	2.5
2008	97.7	1.1	1.0	0.2	2.3
		i. Public Sector Banks			
2004	92.2	2.5	4.4	0.9	7.8
2005	94.6	1.3	3.5	0.7	5.4
2006	96.2	1.0	2.2	0.5	3.7
2007	97.3	1.0	1.4	0.3	2.7
2008	97.8	1.0	1.1	0.2	2.2
		ii. Private Sector Banks Old - New			
2004	**92.4** - 95.0	**2.0** - 1.6	**4.7** - 3.0	**0.9** - 0.3	**7.6** - 5.0
2005	**94.0** - 96.2	**1.1** - 1.1	**4.0** - 2.4	**0.8** - 0.3	**6.0** - 3.8
2006	**95.6** - 98.3	**0.8** - 0.7	**3.0** - 0.8	**0.6** - 0.2	**4.4** - 1.8
2007	**96.9** - 98.1	**0.8** - 1.1	**1.9** - 0.7	**0.4** - 0.2	**3.1** - 1.9
2008	**97.7** - 97.5	**0.7** - 1.6	**1.2** - 0.8	**0.3** - 0.2	**2.3** - 2.5
		iii. Foreign Banks			
2004	95.1	1.6	1.8	1.5	4.8
2005	97.0	1.0	1.3	0.7	3.0
2006	98.0	1.0	0.7	0.5	2.0
2007	98.1	1.1	0.5	0.3	1.9
2008	98.1	1.2	0.5	0.2	1.9

Source: Report on trend and progress of Banking in India.

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