

MANAGEMENT OF NON-PERFORMING ASSETS IN VIRUDHUNAGAR DISTRICT CENTRAL CO-OPERATIVE BANK

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ABSTRACT

Banks are one of the financial intermediaries doing the business of borrowing and lending. The borrowing sources of any bank largely consist of deposits received from the public. Funds secured through deposits, interbank loans, etc., are cheap in terms of cost. The banks lend funds on sufficient securities at higher rates of interest. The interest paid on deposits and that received on loan assets constitutes banker's spread. Non-performing Asset is an important constraint in the study of financial performance of a bank as it results in declining margin and higher provisioning requirement for doubtful debts. This paper attempts to study on management of non-performing assets in the perspective of the VRDCC Bank Ltd. The study was based on secondary data which are taken from annual reports of the VRDCC Bank Ltd. Trend percentage and Pearson correlation coefficients were used to analyse the data collected. Trend percentage on loan outstanding has increased tremendously during the study period. It was found that the recovery initiative is not consistent as the recovery ratio fluctuates throughout the period of study. The gross NPA is positively correlated with sub-standard assets and doubtful assets and negative correlated with loss assets. This evidences that the bank tries to achieve efficient management of sub-standard assets and doubtful assets. Rise in loss assets are a sign of weakness of loan assets management.

Key words: Banks, Deposits, Loans, Non-Performing Assets, Provisions.

INTRODUCTION

Banks are one of the financial intermediaries doing the business of borrowing and lending. The borrowing sources of any bank largely consist of deposits received from the public. Funds secured through deposits, interbank loans, etc., are cheap in terms of cost. The banks lend funds on sufficient securities at higher rates of interest. The interest paid on deposits and that received on loan assets constitutes banker's spread. Banks are subject to statutory requirements regarding reserves and surplus, deposits, advances, provisioning, etc. RBI issues directives from time to time in the matter of deployment of funds and management of NPAs in the light of national priorities. This chapter describes the relationship of bank performance indicators on the relationship between advances and NPA of bank. Non-performing Asset is an important constraint in the study of financial performance of a bank as it results in declining margin and higher provisioning requirement for doubtful debts. This paper attempts to study on management of non-performing assets in the perspective of the VRDCC Bank Ltd.

NON-PERFORMING ASSETS

An asset becomes non-performing assets when it ceases to generate income for the bank. Such an asset is known as non-performing assets. This is due to several reasons. A borrower fails to repay the principal along with interest to the bank it is called as non-performing assets. An asset is classified as non-performing assets under the following record of performance of recovery.

- In respect of term loan, if interest and/or installment of principal remain overdue for a period of more than 90 days.
- In respect of running accounts like overdraft/cash credit, if the account remains out of order for more than 90 days. The balance outstanding should not exceed the limit or drawing power, whichever is lower.
- In respect of a bill discounted, if it remains overdue for more than 90 days.
- In respect of short duration crop loan, if it remains overdue for two crop seasons or more.
- In respect of securitization transactions, if the amount of liquidity facility remains over due for more than 90 days.
- In respect of derivative transactions, if the receivables remain overdue for more than 90 days.

CLASSIFICATION OF ASSETS

- **Standard Assets:** Standard assets are those which do not disclose any problems and which do not carry more than normal risk attached to the business. Such assets are not NPA
- **Sub- standard Assets:** These assets are those which have been classified as NPA for a period not exceeding 12 months. In such a case, the current net worth of the borrower/guarantor or the current market value of the security charged is not enough to ensure recovery of the dues to the bank in full. Such assets will have well defined credit weakness that jeopardize the liquidation of the debts and are characterized by the distinct possibility that the bank will sustain some loss, if deficiencies are not corrected
- **Doubtful Assets:** Doubtful assets are those which have remained NPA for a period exceeding 12 months. In the case of term loans, those where installments of principal have remained overdue for a period exceeding 18 months should be treated as doubtful.
- **Loss Assets:** Loss assets are those where loss has been identified by the bank or internal or external auditors or the RBI inspection but the amounts have not been written off wholly or partially. Such assets are considered uncollectable and of such little values that their continuance as bank assets in not warranted although there may be some salvage or recovery values.

PROVISIONS

A bank is required to make a provision for losses in respect of different classes of its advances are as follows:

- **Provision for Standard Assets has to be made as follows:**

Table 1- Provision for Standard Assets

Period of Standard Assets	Rate of Provision
31 st March 2000	0.25
2005-06	0.40
1 st April, 2007	0.25

- **Provision for Sub-standard assets has to be made as follows:**

Table 2 - Provision for Sub-standard assets

Period of Sub Standard Assets	Rate of Provision(%)
Overdue above 3 years up to 4 years	20
Overdue above 4 years but not exceeding 6 years	30
Overdue exceeding 6 years	100

- **Provision for Doubtful assets has to be made as follows:**

Table 3 - Provision for Doubtful assets

Period	Percentage
Up to 31 st March 2010	50
as on 31 st March 2011	60
As on 31 st March 2012	75
As on 31 st March 2013	100

➤ **Provisions on Loss Assets**

The entire assets should be written off obtaining necessary approval from the competent authority and as per the provisions of the Co-operative Societies Act/Rules. If the assets are permitted to remain in the books for any reason, 100 per cent of the outstanding should be provided for. In respect of an asset identified as a loss asset, full provision at 100 per cent should be made if the expected salvage value of the security is negligible.

LITERATURE REVIEW

Some of the main studies selected for review have been discussed below.

The detrimental effects of NPA on the society was providing capital support to banks with high NPA actually a burden on the public exchequer and hence is cost to the society. High NPA reduce earning base and puts much more pressure on the banks to maintain the required capital adequacy ratio. High level of NPA also leads to squeezing of interest spread. There is a need to create industry cells to cope with this menace (Meera Sharma, 2005). As far as banks are concerned; there are several factors that determine the operating efficiency and profitability. They are: Level of deposits, level of advances, number of branches operating, level of capital and reserves, level of customer service and the like. The burden rate should be reduced and spread rate be increased so that profitability can be at higher rate (Raja S, 2005). The Commercial Banks have already realized a strong capital ratio by itself may not ensure profitability in future which depends significantly on the quality of assets (Vasam Anand Kumar, 2006). The financial health of the banks is greatly affected by the NPAs. The high level of NPAs is the greatest impediment to the economic growth of the country and any bottleneck in the smooth flow of credit is bound to create adverse repercussions in the economy, (Karthikeyan K, 2007). High NPAs degrade a bank's credit rating, lowering its creditability as well as the ability to raise fresh capital. Moreover with high level of NPAs, banks are left with less liquidity in hands to handle the day to day operations (Suresh Kumar, 2014).

OBJECTIVES OF THE STUDY

- To assess the current status of Loan Outstanding and NPA
- To analyze the Recovery Performance NPA in VRDCC Bank Ltd
- To analyze the impact of performance variables on Net profit of the bank

DATA

The study is based on secondary data which are taken from annual reports of the VRDCC Bank Ltd. Trend percentage and Pearson correlation coefficients are used to analyse the data collected.

LOANABLE FUNDS AND ACTUAL LOANING

As any other bank, VRDCC Bank Ltd. mobilizes deposits from the public for the purpose of lending and investments. The purpose of investment mainly here is to maintain the liquidity of the bank. It is the loans and advances portfolio of the bank which generates its profitability and helps it to grow. As per RBI suggestions, a bank should have an ideal loan portfolio as follows:

- 100 per cent of borrowings,
- 75 per cent of owned funds, and
- 70 per cent of deposits

According to the suggested norms of the RBI, an exercise is made for the bank to arrive at the loanable funds. Table 4 exhibits the lending performance of VRDCC bank for eleven years.

Table 4 - Loanable Funds and Actual Loaning

Year	Own funds	Loanable 75%	Deposits	Loanable 70%	Borrowings	Loanable 100%	Total Loanable	Actual Loaning	Loaning percentage
2004-05	7363.99	5522.99	21972.9	15381.03	20282.60	20282.60	41186.62	20282.58	49.25
2005-06	6351.93	4763.95	20073.8	14051.66	21430.40	21430.40	40246.01	21430.38	53.25
2006-07	7943.9	5957.93	21883.8	15318.66	20123.20	20123.20	41399.79	20123.22	48.61
2007-08	8547.08	6410.31	26234.6	18364.22	22227.30	22227.30	47001.83	22227.25	47.29
2008-09	10611.5	7958.63	30466.8	21326.76	25531.70	25531.70	54817.09	25531.68	46.58
2009-10	11491.5	8618.63	34506.4	24154.48	31574.30	31574.30	64347.41	31574.27	49.07
2010-11	13241.8	9931.35	40376.6	28263.62	41778.80	41778.80	79973.77	41778.77	52.24
2011-12	13549.5	10162.13	46484	32538.79	51945.40	51945.40	94646.32	46191.06	48.80
2012-13	14258.3	10693.74	52384.5	36669.12	56667.74	56667.74	104030.60	56667.74	54.47
2013-14	16420.4	12315.32	60220.8	42154.55	58656.89	58656.89	113126.76	58656.90	51.85
2014-15	19472.7	14604.50	65843.8	46090.67	62564.21	62564.21	123259.39	62564.20	50.76

Source: VRDCC Bank Annual Reports from 2004-05 to 2014-15

The Table 4 highlights that the VRDCCB follows balanced norms in lending, i.e., the actual loans position never touched or crossed the loanable funds during the entire study period. However the total loans outstanding to loanable funds in the years 49.25% in 2004-05 to 50.76% in 2014-15. The average utility of the loanable funds for actual lending by the bank during the period of eleven years of study is arrived at 46.58%. The parity in actual lending and loanable funds may be considered as non-utilisation of available funds. This is an important factor which results in lower profitability or loss.

LOAN OUTSTANDING

The loans outstanding position of the VRDCC Bank Ltd. provides an insight into the performance of the bank in credit management. For healthy operations of a bank, the turnover of loans and advances must be on the increase. In other words, the disbursement and recovery of loans must be increased every year. Table 5 exhibits the trend percentage loans outstanding of the VRDCC Bank Ltd.

Table 5 - Trend Percentage on Loan Outstanding

Year	Loan Outstanding (₹ in lakhs)	Trend Percentage on Loan Outstanding
2004-05	15642.8	100
2005-06	17030.96	108.87
2006-07	18210.87	116.42
2007-08	20170.02	128.94
2008-09	23463.44	150.00
2009-10	30460.07	194.72
2010-11	40149.45	256.66
2011-12	50249.96	321.23
2012-13	61282.92	391.76
2013-14	68487.33	437.82
2014-15	76175.36	486.97

Source: VRDCC Bank Annual Reports from 2004-05 to 2014-15

From the Table 5, it is observed that the total loan outstanding had registered an increasing trend from ₹.15642.8 lakhs to ₹.76175.36 lakhs continuously from the year 2004-05 to 2014-15 during the period of study. Trend percentage on loan outstanding has increased tremendously from 100% to 486.97% during the study period.

RECOVERY PERFORMANCE

The recovery of loan is indispensable for recycling of funds. In other words, bank's sustained interest in investing loanable resources in loan portfolio depends upon sustained recycling of funds. The health of any credit institution is very much dependent on the continuous flow of funds triggered by recycling of loaned funds. In this backdrop Table 6 evaluates the ratio of recovery to disbursement.

Table 6 - Ratio of Recovery to Disbursement

Year	Outstanding (Previous Year) (₹ in lakhs)	Disbursement (Current Year) (₹ in lakhs)	Outstanding (Current Year) (₹ in lakhs)	Recovery (₹ in lakhs)	Recovery Ratio (Percent)
2004-05	-	-	15642.8	12638.42	-
2005-06	15642.8	15200.25	17030.96	13812.09	90.86
2006-07	17030.96	16272.03	18210.87	15092.12	92.74
2007-08	18210.87	19207.68	20170.02	17248.53	89.80
2008-09	20170.02	20541.95	23463.44	17248.53	83.96
2009-10	23463.44	27432.68	30460.07	20436.05	74.49
2010-11	30460.07	37361.34	40149.45	27671.96	74.06
2011-12	40149.45	48490.4	50249.96	38389.89	79.17
2012-13	50249.96	59273.06	61282.92	48240.10	81.38
2013-14	61282.92	66074.02	68487.33	58869.61	89.09
2014-15	68487.33	69777.1	76175.36	62089.07	88.98
Average Percent					84.45

Source: VRDCC Bank Annual Reports from 2004-05 to 2014-15

Recovery = Previous year outstanding + Current year disbursement – Current year outstanding

The Table 6 reveals the fact that the recovery initiative is not consistent as the recovery ratio fluctuates throughout the period of study. In other words, the average recovery performance of the bank is arrived

at 84.45% for the study period. The recovery in the year 2006-07 was the highest and the percentage was 92.74%. From 2009-10 to 2012-13, the recovery percentages are less than the average (84.45%).

CLASSIFICATION OF ASSETS

The loan asset classification of VRDCC Bank Ltd for the study period has been shown in the Table 7. It is evident from the table that it has been classified into four categories i.e., standard assets, sub-standard assets, doubtful assets and loss assets in the context, hypothesis has been framed. The absolute figure and their respective percentage to the total advances have been shown for the research period. It is patently manifest that standard asset had grown steadily from ₹.16727.96 lakhs (82.47 %) during 2004-05 to ₹.55101.12 lakhs (88.10%) during 2014-15. The percentages of standard assets have been on the increase indicating that the standard assets management by the bank has been consistently good. As far sub-standard assets the percentage to total advances also exhibits a declining trend. It had come down from a high of 8.04 % in 2004-2005 to a low 0.09% in 2014-15. This evidences the efficient management of sub-standard assets. In case of doubtful assets, its percentage share shows an increasing trend from 4.23% in 2004-05 to 9.59% in 2006-07 and the following year of the study it decreased 5.04% in 2006-07 to 0.71 % in 2014-15. As for the loss asset, the performance of bank has been commendable. The size of loss assets is high (12.01%) in 2007-08 and in the following year, it gets decreased and reached 4.78% in 2014-15. An analysis of gross NPAs to total advance has been made separately in the succeeding analysis. The size of total NPAs in terms of percentage had been increased from 17.53% in 2004-05 to 19.01% in the year 2008-09.

Table 7 - Classification of Assets

Year	Standard Assets 1	Percentage	Sub-Standard Assets 2	Percentage	Doubtful Assets 3	Percentage	Loss Assets 4	Percentage	Total Gross NPA 5 (2 to 4)	Percentage	Total Gross Advances 6
2004-05	16727.96	82.47	1629.71	8.04	858.14	4.23	1066.7	5.26	3554.62	17.53	20282.58
2005-06	17555.13	81.92	1266.67	5.91	1235.24	5.76	1373.34	6.41	3875.25	18.08	21430.38
2006-07	16297.27	80.99	636.97	3.17	1929.49	9.59	1260.03	6.26	3826.49	19.01	20123.76
2007-08	18108.87	81.47	328.63	1.48	1120.09	5.04	2669.64	12.01	4118.36	18.53	22227.23
2008-09	21607.22	84.63	237.79	0.93	828.80	3.25	2857.84	11.19	3924.43	15.37	25531.65
2009-10	28686.53	90.49	400.98	1.26	203.14	0.64	2411.13	7.61	3015.25	9.51	31701.78
2010-11	38910.59	93.13	213.07	0.51	110.11	0.26	2545.00	6.09	2868.18	6.87	41778.77
2011-12	49074.19	94.47	131.36	0.25	72.18	0.14	2667.67	5.14	2871.21	5.53	51945.40
2012-13	60044.51	94.98	65.11	0.10	516.04	0.82	2594.41	4.10	3175.56	5.02	63220.07
2013-14	51675.45	88.10	62.78	0.11	485.8	0.83	2872.54	4.90	3560.32	6.07	58656.89
2014-15	55101.12	88.07	58.23	0.09	443.21	0.71	2990.25	4.78	3971.4	6.35	62564.21

Source: VRDCC Bank Annual Reports from 2004-05 to 2014-15

In this context Karl Pearson’s co-efficient of correlation is applied and the following results are obtained.

H₀: There is no significant relationship between Gross NPA and the various categories of loan assets.

Table 8

Classification of Assets - Pearson Correlation Coefficient

Assets	Sub-standard Assets	Doubtful Assets	Loss Assets	Gross NPA
Sub-standard Assets		0.472	-0.902**	0.227
Doubtful Assets	0.472		0.636*	0.711*
Loss Assets	-0.902**	0.636*		-0.141
Gross NPA	0.227	0.711*	-0.141	

Source: Computed Data ** denotes 5% level and * 1% level.

Table 8 depicts the inter-correlation between the various categories of NPA. It is evident from the table that the gross NPA is positively correlated with sub-standard assets (0.227) and doubtful assets (0.711) and negative correlated with loss assets (- 0.141). This evidences that the bank tries to achieve efficient management of sub-standard assets and doubtful assets. Rise in loss assets are a sign of weakness of loan assets management.

SUGGESTIONS

- Loans should be lent to the clients based on their credit worthiness.
- Intensive analysis and proper evaluation of loan proposal should be done while sanctioning the loan. Reason for demand loan amount and required documents for loan proposal should be assessed.
- Property should be evaluated. The pledge for the loan should be adequate, if inadequate pledge is accepted it may create problem in loan recovery.
- Special recovery drive should be launched during the harvest season.
- It is necessary to set up a strong “Recovery cell” in the bank supported by adequate staff and other infrastructure including vehicle support.
- Proper training is important to the staff of the banks at the appropriate level with ongoing process. This is how they should deal with the problem of NPA and what continuous steps they should take to reduce the NPA.
- The defaulters may be names published in the local newspapers, which will help other co-operative banks and credit institutions.

CONCLUSION

Now days the serious problem faced by bank all over the world is the growth of non-performing assets. The value of loan-disbursement process is harmed because of non-recovery of loan installment and the interest on the loan which in turn is the consequence of growth of NPA which adversely affect the lending activity of the bank. Steps need to be taken by the VRDCC Bank Ltd. to recover the loans in time by adopting new recovery mechanism.

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