"Managing NPA's in Public Sector Banks in India & Measures to Eradicate the Same"

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Abstract

The current situation of NPA's in Indian Banks is around 4.2% of total loans amongst which Public Sector Banks have a disproportionately higher share. Total stressed assets, comprising gross NPAs and standard restructured assets, are estimated at over 11% of total loans extended by the lenders.

At the same time India's public sector banks (PSBs) continue to face several challenges in raising capital and meeting the higher Basel III requirements. This includes insufficient market appetite to fill the regulatory requirement, which has raised the dependence on the state-owned Life Insurance Corporation (LIC) for private placement of PSBs' Basel III-compliant capital instruments.

We are proposing a solution here to give a one point injection of removing NPA from bank's balance sheet in efficient manner as follows:

Step 1 Removing NPA's from bank balance sheet.

Step 2 Transferring the NPA's to a centralized ARC of government.

Step 3 Efficient recovery and also comparison and real situation analysis for recovery and better performance.

Step 4 Going away with NPA and provisioning culture.

Benefits include reduction in recovery time, and more efficient recovery in terms of percentage recovered. Government's stake will improve as the share price will go up due to removal of NPA's. Bank's credit rate will improve so it will be easier to raise capital.

Objective

- To find relation between bad assets in PSB's with net worth and advances.
- To prove significant relation between share price and Net NPA.
- To estimate percentage increase in bank's equity capital after writing off NPA from their balance sheet.
- To propose BIC(Banking Investment Company) as a centralized ARC(Asset Restructuring Company) also
- Optimum utilization of Govt. funds through ARC rather than investing in PSB's for Basel III requirements

Keywords

Gross NPA, Net NPA, Provisions, Basel III Norms and Public Sector banks.

Introduction

"The SBI chairperson has recently conveyed that we need an urgent intervention from the Centre and the states in short future to pre-empt a surge in banks" bad loans that could severely dent confidence in some public sector banks."

The NPAs of the Indian banks are pegged at 4.2% of total loans with public sector banks having a disproportionately higher share. Total stressed assets that comprise of gross NPAs and standard restructured assets are about 11% of total loans extended by the lenders.

At the same time India's public sector banks (PSBs) are facing challenges in raising capital they need and in meeting the higher Basel III requirements.

Indian banks have until March 2018 to be fully compliant Basel III norms. But the weakening profitability of the PSBs, in particular, is constraining their retained earnings (due to NPA's and provisioning) and raising their overall capital requirement. This need would increase further if loan growth in the system were to resume close to 20% year-on-year from the current 14%-15% rate.

Equity market access has proven tough despite steady capital injection from the government. PSBs need to source approximately INR1.16trn (USD 19bn) from the equity market by 2018, according to recent official estimates. But, in contrast to their private-sector counterparts, PSB's have proven far less successful in raising equity market capital, Even if the market valuations are deeply discounted. Limited market access highlights their worsening credit fundamentals, in particular, the continuing pressures that are mounting on asset quality and earnings.

Looking for solution to curb these twin problems:

- Ever increasing NPA
- Capital Requirements for meeting Basel III norms

We are proposing a solution here to give a one point injection of removing NPA from bank's balance sheet. We will be finding a correlation between NPA percentage growth and share price growth percentage and then we will comment on how effective this solution for the Indian Public sector banks is.

Current Situation of NPA in Public Sector Banks

A NPA (Non-Performing asset) is a loan or an advance where;

- The Interest amount or an instalment of the principal remain overdue for a period of more than 90 days or more in respect of a term loan granted,
- The account remains "out of order" in the respect of an overdraft or cash credit
- The bill presented remains overdue for a period of more than 90 days
- The instalment or interest remains overdue for two or more crop seasons in case of short duration crops and for one crop (or more) season in case of long duration crops

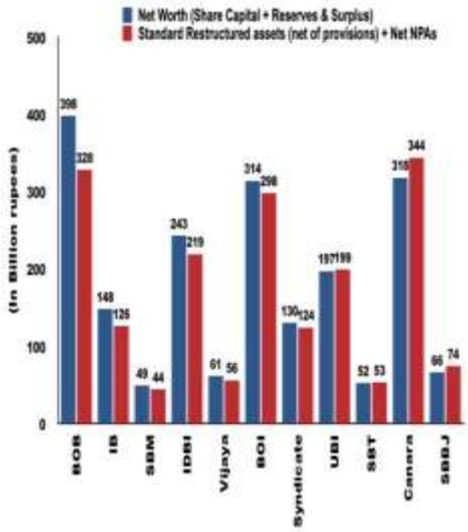
The banking industry is having very high level of non-performing assets (NPAs) to contend with. High NPAs tend to raise the cost of banking operations and thereby the spread and the efforts are needed to bring these down. However, we need to have a balance between the reduction in NPAs on one hand and ensuring adequate supply of credit remains in place to the economy on the other. High pressure on banks to reduce NPAs will make banks highly selective in the credit disbursal process and consequently, will result in reduction of the total level of credit as dictated by the growth of deposits. The rate of reduction of NPAs (non-performing assets) will therefore have to be gradually reduced keeping in mind the growth and notional lending risks associated with the Indian economy and the pace at which debt recovery and settlement processes operate.

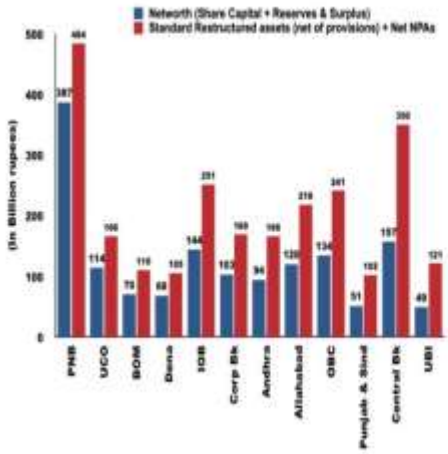
RBI disclosed that while the amount of bad debts stood at Rs 15,551 crore for the financial year which ended March 2012, they (bad debts) had shot up thrice to Rs 52,542 crore by the end of March 2015. While bad loans of public-sector banks (PSB's) grew at a whopping rate of 4 per cent between 2004 and 2012, in financial years 2013 to 2015, they rose by about 60 per cent.

Reserve Bank Governor has repeatedly expressed concern over the health of public-sector banks, and advocated strongly to banks to classify certain stressed assets as NPAs and then make adequate provisions in order to strengthen their balance sheets. At the same time they may look at other alternatives like merger. Public sector banks are sitting on about Rs 7lakh crore of stressed assets, including NPAs and restructured loans. He also emphasized that some banks would have to merge to optimize their use of resources. Gross NPAs of public-sector banks rose to whopping 6.03 per cent as of June 2015, up from 5.20 per cent in March 2015.

Comparison of Net worth Vs. Bad Assets in PSB's

Figure 1 & 2

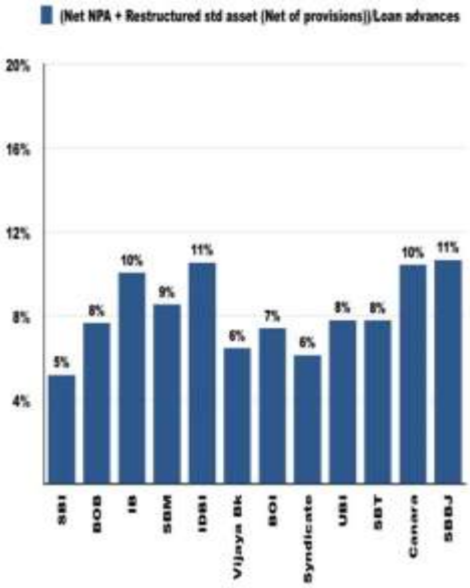


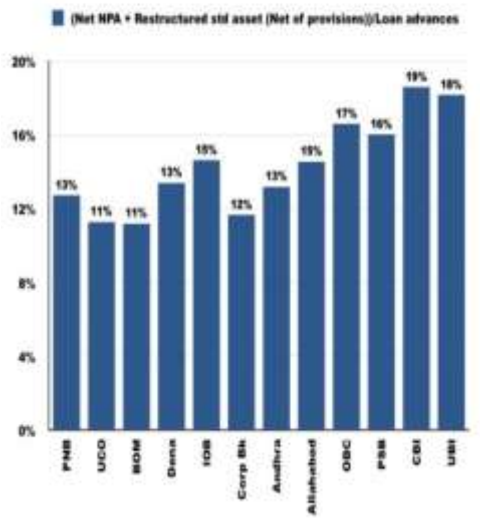


Source for 4.1 & 4.2: Annual reports of banks

Comparison of Bad Assets vs. Advances in PSB's

Figure 3 & 4





Comparison of Gross NPA vs. GDP

Figure 5

Basel III Implementation and its Effects on the Capital

As per the stringent RBI guidelines about Basel III, Indian banks need to plan their capital requirements in advance. If Indian government carries out its responsibilities towards public sector banks (PSB's) properly then not only they (PSB's) will be able to meet their high capital requirements but will also be able to strengthen their position among international banks. The Bank for International Settlements (BIS) has set a deadline for complete implementation of Basel III as 2019 whereas RBI has schedule which states 2017 as deadline which is highly demanding. According to RBI, the full regulatory requirement of total capital (tier 1 and tier 2) is 9% which is higher than BIS norm of 8%.

Basel 3 will impact both Indian and western banks differently. In India, banks are raising capital from different sources to finance their growth whereas their counterparts the western banks are raising capital in a different manner by shrinking their balance sheets.

The government last year announced a revamp plan, 'Indradhanush', to infuse Rs 70,000 crore in PSB's over four years, while they will have to raise a further Rs 1.1lakh crore from the markets and other sources to meet their capital requirements in line with global risk norms Basel III.As per the capital infusion road map which has been set up, PSU banks will get Rs25,000 crore this financial year and the next fiscal.

Implementation Schedule for Basel III

Figure 6

Basel – III: Phase-in Arrangements

(Transition period showed in shaded area) (All dates are effective from 1 January)

	2011	2012	2013	2014	2015	2016	2017	2018	As of1 Jan 2019
Leverage Ratio	Supervisory monitoring		Parallel run 1 Jan 2013 - 1 Jan 2017 Disclosure starts 1 Jan 2015					Migration to Pillar 1	
Minimum Common Equity Capital Raito			3.5%	4.0%	4.5%	4.5%	4.5%	4.5%	4.5%
Capital Conservation Buffer						0.625%	1.25%	1.875%	2.50%
Minimum Common Equity plus Capital Conservation Buffer			3.5%	4.0%	4.5%	5.125%	5.75%	6.375%	7.0%
Phase-in of deductions from CET 1 (including amounts exceeding the limit for DTAs, MSRs and financials				20%	40%	60%	80%	100%	100%
Minimum Tier 1 Capital			4.5%	5.5%	6.0%	6.0%	6.0%	6.0%	6.0%
Minimum Total Capital			8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%
Minimum Total Capital plus Conservation Buffer			8.0%	8.0%	8.0%	8.625%	9.25%	9.875%	10.5%
Capital instruments that no longer qualify as non-core Tier 1 capital or Tier 2 capital			Phase out over 10 year horizon starting from 2013						
Liquidity Coverage Ratio	Obser-vation Period begins				Introduce Minimum standard				
Net Stable Funding Ratio		Obser-vation Period begins						Introduce Minimum standard	

Source: RBI circular on Basel 3 Capital regulations

Comparison of Capital Requirements

Figure 7

Comparison of Capital requirement standards

Minimum Capital Ratios	Basel III of BCBS	Basel III of RBI	Existing RBI norms	PSBs current position	Private Banks current position
Minimum Common Equity Tier 1 (CET1)	4.5%	5.5%	3.6%	7.3%	11.2%
Capital conservation buffer (CCB)	2.5%	2.5%	-	-	-
Minimum CET1+ CCB	7%	8%	3.6%	7.3%	11.2%
Minimum Tier 1 capital	7.0%	7.0%	3.6%	7.3%	11.2%
Minimum Total Capital including buffer	8%	9.0%	6%	8.1%	11.5%
Minimum Total Capital +CCB	10.5%	11.5%	9.0%	12.1%	15.9%
Additional counter-cyclical buffer in the form of common equity capital	0-2.5%	0-2.5%	NA	NA	NA

Source: RBI circular on Basel 3 Capital regulations

Basel III in Public sector banks

Basel III requirements in terms of CAR (Capital Adequacy ratio) are shown below for all the PSB's. CAR is the ability of banks to absorb loss, It is also called Capital to Risk (Weighted) Assets Ratio (CRAR).

$$CAR = \frac{\text{Tier One Capital} + \text{Tier Two Capital}}{\text{Risk Weighted Assets}}$$

Table 1

Banks - Basel III	Mar-13			Mar-14			Mar-15		
	CAR - Total	CAR - Tier-I	CAR - Tier-II	CAR - Total	CAR - Tier-I	CAR - Tier-II	CAR - Total	CAR - Tier-I	CAR - Tier-II
SBI AND ITS ASSOCIATES									
STATE BANK OF INDIA	0.0	0.0	0.0	12.4	9.7	2.7	12.0	9.6	2.4
STATE BANK OF BIKANER & JAIPUR	0.0	0.0	0.0	11.6	9.0	2.5	11.6	9.0	2.6
STATE BANK OF HYDERABAD	11.2	8.8	2.4	12.0	9.3	2.7	11.3	9.2	2.1
STATE BANK OF MYSORE	0.0	0.0	0.0	11.1	8.7	2.4	11.4	8.4	3.1
STATE BANK OF PATIALA	10.4	7.5	2.9	10.4	7.9	2.5	12.1	8.7	3.4
STATE BANK OF TRAVANCORE	10.7	7.9	2.9	10.8	8.5	2.3	10.9	8.9	2.0
NATIONALISED BANKS									
ALLAHABAD BANK	0.0	0.0	0.0	10.0	7.5	2.5	10.5	7.7	2.7
ANDHRA BANK	0.0	0.0	0.0	10.8	8.1	2.7	10.6	8.0	2.6
BANK OF BARODA	0.0	0.0	0.0	12.3	9.3	3.0	12.6	9.9	2.7
BANK OF INDIA	0.0	0.0	0.0	10.0	7.2	2.7	10.7	8.2	2.6
BANK OF MAHARASHTRA	0.0	0.0	0.0	10.8	7.4	3.4	11.9	8.8	3.2
BHARATIYA MAHILA BANK LTD.				0.0	0.0	0.0	193.1	192.8	0.3
CANARA BANK	0.0	0.0	0.0	10.6	7.7	3.0	10.6	8.0	2.5
CENTRAL BANK OF INDIA	0.0	0.0	0.0	9.9	7.4	2.5	10.9	8.1	2.9

CORPORATION BANK	0.0	0.0	0.0	11.7	8.1	3.5	11.1	8.1	3.0
DENA BANK	0.0	0.0	0.0	11.1	7.4	3.7	10.9	7.7	3.3
IDBI BANK LIMITED	0.0	0.0	0.0	11.7	7.8	3.9	11.8	8.2	3.6
INDIAN BANK	0.0	0.0	0.0	12.6	10.2	2.4	12.9	10.6	2.3
INDIAN OVERSEAS BANK	0.0	0.0	0.0	10.8	7.5	3.3	10.1	7.3	2.8
ORIENTAL BANK OF COMMERCE	0.0	0.0	0.0	11.0	8.9	2.2	11.4	8.7	2.7
PUNJAB AND SIND BANK	0.0	0.0	0.0	11.0	7.6	3.4	11.2	8.5	2.8
PUNJAB NATIONAL BANK	0.0	0.0	0.0	11.5	8.9	2.7	12.2	9.3	2.9
SYNDICATE BANK	0.0	0.0	0.0	11.4	8.7	2.7	10.5	7.8	2.7
UCO BANK	0.0	0.0	0.0	12.7	8.7	4.0	12.2	9.1	3.1
UNION BANK OF INDIA	0.0	0.0	0.0	10.8	7.5	3.3	10.2	7.5	2.7
UNITED BANK OF INDIA	0.0	0.0	0.0	9.8	6.5	3.3	10.6	7.5	3.1
VIJAYA BANK	0.0	0.0	0.0	10.6	8.1	2.4	11.4	8.2	3.2
Source: RBI circular on Basel 3 Capital regulations									

Budgeted figure for the requirement of capital

To provide greater autonomy to public sector banks (PSB's), Finance Minister himself has said that the lenders would require Rs 2.40 lakh crore capital by the end of year 2018 to meet Basel III norms and there is additional need of additional resources. A large part of this needed fund would be raised through public offers that will be made to retail customers. To enhance the capital, in the interim budget it has been announced to infusion of Rs 11,200 crore in public sector banks (PSB's).

The Financial Stability Board (FSB) has issued the final draft on Total Loss-Absorbing Capacity (TLAC) standard specially for global systemically important banks (G-SIBs) dated November 9, 2015 as part of its reforms agenda set up to deal with 'too-big-to-fail' for banks. The standard has been designed to ensure that the G-SIBs would have sufficient loss-absorbing and recapitalization capacity.

Challenges faced by Public Sector Banks (PSBs) to raise capital

- Timing to approach capital markets is very important. Therefore, the bank has to do planning in advance if they want to raise capital in a time bound manner and at a proper price. Unfavourable markets may result in issuing shares at a higher discount to market price and giving more equity shares, thereby causing dilution of shareholding and reducing earnings per share (EPS). Banks may get impacted by higher costs of capital and lower returns, which will make it difficult to attract and retain investors.
- Capital raising efforts done by PSBs other than the capital infusion by the government, face challenges because of they have relatively low equity valuations compared to their private sector peers. A deteriorating asset quality and a low price to earnings (PE) ratio of the public sector lenders will be additional obstacle for them in raising money. The previous Financial Stability Reports had raised issues about the low valuation of PSBs, despite implicit backing from the government.
- The implicit sovereign guarantee cannot be treated in direct manner because if the value of a firm will fall below the face value of debt, then it is assumed that the compensation given to debtors is made up by the sovereign, but no compensation

will be given to equity investors. Hence, the fortunes of the equity investors are unaffected even by an implicit sovereign guarantee of debt. The improvement in the valuations can only be made from commensurate improvements in asset quality, governance structures and operational efficiency.

- Government has allowed PSBs to raise up to Rs 1.60 lakh crores from markets by diluting government holding stake to 52 per cent in phases so as to align with Basel III capital adequacy norms. All the PSBs need Rs 2.4lakh crores in equity by FY 2018 to meet Basel-III requirements on capital adequacy. Ministry of Finance has sanctioned only Rs 11,200 crores. Further, it has asked lenders to consider other options for meeting their requirements.
- Government has emphasized on allocating budgetary resources to social service sectors such as health and education. The prime factor for the decreasing role of the Government has been the dissatisfaction with the performance of banks.

Research Methodology

Research design which is used in this study is descriptive research because it deals with statistical tests, regression analysis and correlation analysis to prove our objectives in 3 stages, funneled to reach main objective as follows:

Firstly we have shown by regression and correlation that the variable 1 which is “increase in share price” and variable 2 “increase in net NPA” have been correlated negatively (inversely).

Then we have adopted analysis regarding how much the govt. equity will improve if we wipe out the existing Net NPA’s from the bank’s balance sheet.

Regression Analysis between Gross NPA % & Closing Share Price

We will be illustrating regression model and correlations for few PSB’s, where we show the regression model and negative correlation between the variables: percentage increase in share price and percentage increase in Net NPA. We have carried regression analysis for all the 26 PSB’s, for illustration purpose, regression for 3 banks is shown below.

SBI

Regression Statistics	
Multiple R	0.224324782
R Square	0.050321608
Adjusted R Square	0.02715872
Standard Error	0.214170778
Observations	43

ANOVA

	df	*SS*	*MS*	*F*	*Significance F*
Regression	1	0.099651132	0.09965113	2.17251011	0.14813398
Residual	41	1.880634006	0.04586912		
Total	42	1.980285138			

	Coefficients	*Standard Error*	*t Stat*	*P-value*	*Lower 95%*	*Upper 95%*	*Lower 95.0%*	*Upper 95.0%*
Intercept	-0.032429304	0.032841419	-0.98745137	0.32921324	-0.098753894	0.03389529	-0.098753894	0.033895287
X Variable 1	-0.306150084	0.207708122	-1.47394373	0.14813398	-0.725625146	0.11332498	-0.725625146	0.113324979

%age growth in share price= Y and X = %age growth in net NPA

Correlation -.224324

Bank of Baroda

Regression Statistics	
Multiple R	0.414302472
R Square	0.171646539
Adjusted R Square	0.151442796
Standard Error	0.201770833
Observations	43

ANOVA

	df	*SS*	*MS*	*F*	*Significance F*
Regression	1	0.34587565	0.34587565	8.49577918	0.005744261
Residual	41	1.669170229	0.04071147		
Total	42	2.015045879			

	Coefficients	*Standard Error*	*t Stat*	*P-value*	*Lower 95%*	*Upper 95%*	*Lower 95.0%*	*Upper 95.0%*
Intercept	-0.036943996	0.030773943	-1.20049603	0.23683711	-0.099093234	0.0252052	-0.099093234	0.025205242
X Variable 1	-0.244747508	0.083968553	-2.91475199	0.00574426	-0.414325441	-0.0751696	-0.414325441	-0.075169574

%age growth Y= share price and X = npa net

Correlation -0.41447

Punjab & Sindh Bank

Regression Statistics	
Multiple R	0.72388427
R Square	0.52400843
Adjusted R Square	0.49756446
Standard Error	0.22961604
Observations	20

ANOVA

	df	*SS*	*MS*	*F*	*Significance F*
Regression	1	1.044758591	1.044758591	19.81579607	0.000308301
Residual	18	0.949023424	0.052723524		
Total	19	1.993782015			

	Coefficients	*Standard Error*	*t Stat*	*P-value*	*Lower 95%*	*Upper 95%*	*Lower 95.0%*	*Upper 95.0%*
Intercept	0.0174101	0.05138241	0.338833865	0.738655563	-0.090540337	0.12536054	-0.09054034	0.12536054

X Variable 1	-0.39276078	0.088231234	-4.45149369	0.000308301	-0.578127724	-0.2073938	-0.57812772	-0.20739384

%age growth Y= share price and X = npa net

Correlation -0.72388

Indian Overseas Bank

Regression Statistics	
Multiple R	0.6125743
R Square	0.3752473
Adjusted R Square	0.3600094
Standard Error	0.2957353
Observations	43

ANOVA

	df	*SS*	*MS*	*F*	*Significance F*
Regression	1	2.153770507	2.153770507	24.625962	1.266E-05
Residual	41	3.585833154	0.087459345		
Total	42	5.739603661			

	Coefficients	*Standard Error*	*t Stat*	*P-value*	*Lower 95%*	*Upper 95%*	*Lower 95.0%*	*Upper 95.0%*
Intercept	-0.0276643	0.045106147	-0.61331483	0.5430559	-0.118758	0.0634294	-0.11875798	0.06342944
X Variable 1	-0.7118347	0.143444064	-4.96245523	1.266E-05	-1.0015259	-0.4221436	-1.00152591	-0.42214358

	%age growth Y= share price and X = npa net
Correlation	-0.61257

Similar analysis was done for all PSB's and for 15 PSB's the correlation coefficient was negative, illustrated below:

For 15 Banks the correlation between the percentage increase in share price and percentage increase in net npais negative. This proves significantly that the growth in share price and growth in net NPA has a negative correlation. With Punjab and Sindh bank topping the chart. This substantiates the fact that if we write off NPA's from the books of the PSB's then there will be significant appreciation in their share price and hence the market capitalization.

PSU bank's Share price Growth% and Net NPA growth %
Table 2

S No.	Name Of Bank	R square	Correlation
1	Punjab & Sindh Bank	0.524008434	-0.723884268
2	united bank I	0.445918071	-0.667770972
3	IOB Bank	0.375247253	-0.612574284
4	Dena Bank	0.229641722	-0.479209476
5	Vijaya Bank	0.210292269	-0.45857635
6	SBT	0.199024762	-0.446121914
7	Bank of Baroda	0.171646539	-0.414302472
8	Allahabad Bank	0.117249388	-0.34241698
9	State Bank of India	0.050321608	-0.224324782
10	UCO bank	0.043853141	-0.209411415
11	Corporation Bank	0.006085576	-0.078010103
12	Andhra Bank	0.005905871	-0.076849664
13	Central Bank	0.003851287	-0.062058737
14	J&K bank	0.000723446	-0.026896956
15	Bank of Maharashtra	8.91494E-05	-0.009441897

Improvement in Govt. Stake in PSB's after writing-off NPA

Table 3

Name of the Bank	Govt. Holding (%)	Govt. Holding	Improvement after writing-off NPA
Allahabad Bank	60.83	7690.1286	9665.05156
Andhra Bank	61.0183	6140.271529	6494.179882
Bank of Baroda	57.53	22916.5002	30037.27222
Bank of India	64.43	20260.6578	18690.26485
Bank of Maharashtra	79.8	6437.466	6483.052418
Canara Bank	69.91	22272.6269	21395.07009
Central Bank of India	81.46	14219.6576	14881.4981
Corporation Bank	63.33	6638.8839	7027.308911
Dena Bank	59.75	4444.8025	6042.296107
IDBI	76.5	18600.975	16863.62326
Indian Overseas Bank	73.8	11542.32	16845.2163

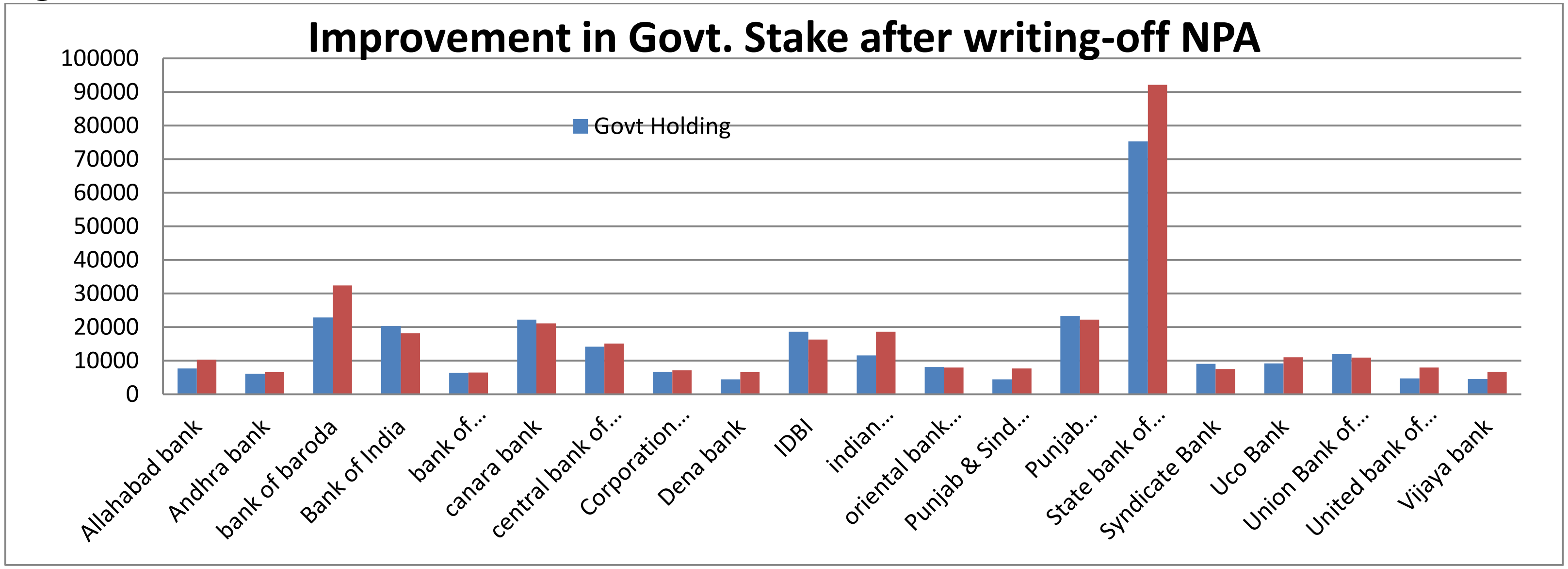
Continues…

Oriental Bank of Commerce	59.13	8146.9314	8026.053721
Punjab & Sindh Bank	79.62	4454.739	6873.275611
Punjab National Bank	59.86	23392.0908	22555.15492
State Bank of India	58.6	75264.082	87926.78106
Syndicate Bank	69.24	9041.3592	7915.468069
Uco Bank	72.83	9138.7084	10574.02079
Union Bank of India	60.47	11948.872	11207.20294
United Bank of India	82	4778.14	7171.167393
Vijaya Bank	74.06	4561.3554	6130.152683

Data as on 31.05.2015

75% factor is taken to calculate improvement in govt. holding, being conservative

Figure 8



Ease in Comparison in PSB Banks and getting Actual Picture of NPA’s

In all the PSB’s the exact NPA isn’t known. So as we implement this solution, we will be able to fulfil following benefits:

1. The banks will disclose all true NPA’s, so we will get to know exact figure of the NPA’s and we can address the issue.
2. Banks are not able to lend as capital has been wiped out and lending is restricted to maintain the capital adequacy.
3. We can compare actual condition of banks after writing off NPA’s or transferring all NPA’s to centralized ARC, thus cleaning the balance sheets of banks, their actual condition will be clear and we can compare performances in a real manner.

One more recommendation is that in future there will not be any NPA, banks will have to write off full loan from profits if it goes bad (we will eliminate provisioning), so that they may act carefully in risk assessment and lending.

Banking investment Company (BIC) acting as a central ARC

Countries like Singapore, UK and Belgium, have set up investment companies to hold the equity in banks. This resulted in operational distance between the governments from the banks, discouraging direct intervention and suasion, helping to align the governments' role as that of the principal shareholder in the banks which resulted to an enhanced focus on financial returns.

India should aspire to this model, vigilance which is the main criteria is needed to ensure that such a Banking Investment Company (BIC) is not just a bureaucratic layer in a varied style of the Government's control of its public banks. It also depends on how the BIC board is constituted; its autonomy and empowerment conferred on it by the Government plays a crucial role. A professional banker or a private equity investment professional is desirable to be CEO of BIC he should also possess a vast experience of working in financial environments where return on investment is the yardstick of performance, and he/she should be appointed through a search process.

Though Banking Investment Company (BIC) can be constituted as a core investment company under RBI registration and regulation, its business would make it resemble a passive sovereign wealth fund. The non-executive Chairman of BIC would be nominated by the Government, all the other directors is to be independent and expected to bring in the requisite banking or investment skills.

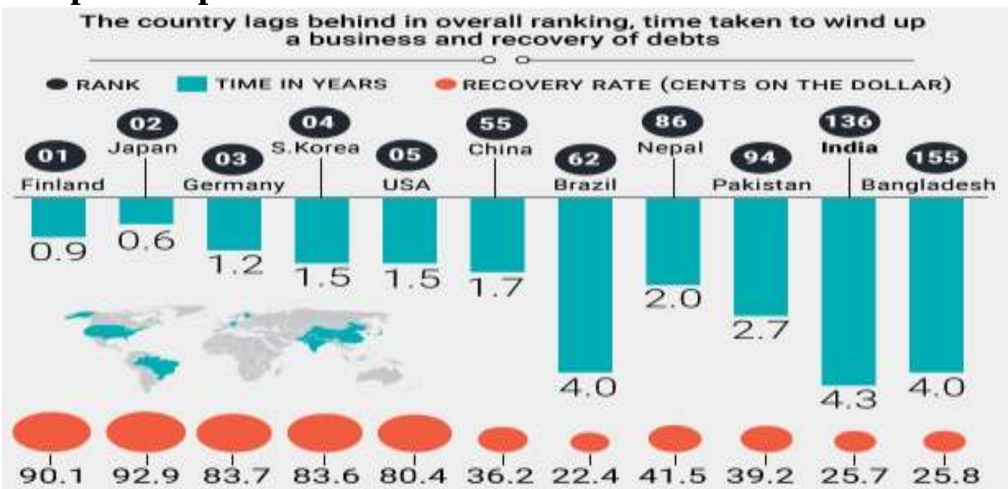
"The vested powers of Government in relation to the governance of banks should also be transferred to BIC". The first phase of PSB reform, until a BIC becomes operational, bank board's bureau (BBB) which comprise of ex- senior bankers should advise on all board appointments, viz. appointment of chairmen and executive directors.

BIC can act as a centralized ARC and can absorb entire NPA from all PSB's and clean their balance sheets, thus aided by bankruptcy code it will help in achieving following objectives:

1. Increase in recovery rate (higher proportionate recovery from the bad debts).
2. Decrease in recovery period
3. Increase in overall ranking, time taken to wind-up a business and recovery of debts

Figure 9

The present position of India is illustrated below



Source: Human development index report, 2015

Double Edged Sword – Raising Capital through Public Issue

Multiple options available to meet the challenges of mobilization of additional capital are through public issues:

i. Divestment of Government's shares in PSBs. Present level of government shareholding in Public sector banks ranges from 58 per cent to 89 per cent, there is enough ground for raising equity from the market without even diluting the public sector character;

ii. PSBs may issue non-voting equity shares to the public, thus while the Government can hold less than 51 per cent of the total equity shares, government still maintaining at least 51 per cent voting rights;

iii. Similarly, the second option of issuance of differential voting equity could also be considered. Issuances like these will allow the Government to maintain their voting rights at the desired level though there resulting to a dilution in the economic interest, i.e., in terms of dividend income to the Government;

iv. By amending the respective statutes governing PSBs, the Government's stake in PSBs can be diluted below Fifty One per cent in conjunction with certain protective rights given to the Government;

v. In this conjunction, the proposals by the Committee to Review Governance of Boards of Banks in India (Nayak Committee) to transfer the share of the Government in PSBs to an investment company viz., Bank Investment Company (BIC), will reduce Government stakes in PSBs to less than 50 percent and provide much required autonomy and professionalism which is need of the hour to PSBs and thus will improve returns on equity resulting in attracting more capital from the market.

Economic Benefits

Benefits for Banks

- Concentrating towards core competencies
- Higher leverage opportunity
- Increase in their equity price resulting to an easier access to capital markets(FPO)
- Seamless alignment towards capital requirements as per Basel III standards

Benefits for Government

- It will boost financial position of economy which attract more investments.
- Improvement in credit ratings which will enable loans at lower interest rate and also attracts FDI's

- Availability of finance at reasonable (lower) interest rate to manufacturing sector which will boost "Make-in-India" initiative.

Benefits for Economy

Following are the Economic Benefits, by Government allocating capital to Social Service Sectors like Health, Sanitation, Housing and Education rather than to corporate:

- Educated children and youth increases the demographic dividend of the country
- A high level of inequality in development of industrial and social sector, with the rich and the poor difference can be reduced.(Insights on India, 2015)
- The negative externalities that have increased with the rising pollution and resulting disease spread; leading to an increased cost of living can be reduced.
- The delays in implementation of schemes like Swachh Bharat Abhiyan and irregular salary received in MGNREGA scheme can be significantly lowered, leading to an increase in faith on the government.
- Attention towards issues related to children will lower child mortality and malnutrition rates.

India is ranked 130 among 188 countries in 2014 in (Human Development Report, 2015). India moved up by five places to the 130th rank in the latest UNDP report on account of rise in life expectancy and per capita income. This ranking can be further improved by Govt. focusing on Social Service Sectors.

Limitations of Study

Some of the limitations faced during this study are:

1. Data collected is for 26 Public sector banks in India.
2. Data is analyzed since 2005-2006 up to 2014-2015(last 10 years).
3. The study covers only one aspect that is comparison of trend and amount of NPA in different public sector banks.
4. Convenience method of sampling has been used so all the units in the universe (all public sector banks) did not have the equal chances of selection.
5. Correlation and regression analysis is used.
6. To calculate government appreciation in stake 75% factor is used as a conservative approach.

Conclusion

The NPAs have created a big problem for the public sector banks in India. Rising NPA's not only impacts Banks but also cripple the economy. The money locked up in NPAs has a direct impact on profitability of the bank as Indian banks are highly dependent on income from interest on funds they lend, also they have to do provisioning for the same. This study shows that extent of NPA is comparatively very high in public sectors banks and percentage growth in NPA results in decrease in share price growth of the banks. Although various steps have been taken by government to reduce the NPAs but still a lot needs to be done to curb this problem. The NPAs level of our banks is still high as compared to the foreign banks. It is not at all possible to have zero NPAs. The bank management should speed up the recovery process. The problem of recovery is not with small borrowers but with large borrowers and a strict policy should be followed for solving this problem.

The government should also make more provisions for faster settlement of pending cases and also it should reduce the mandatory lending to priority sector as this is the major problem creating area. So the problem of NPA needs lots of serious efforts otherwise NPAs will keep killing the profitability of banks which is not good for the growing Indian economy at all. We have recommended writing off NPA's from banks balance sheet in a single go and transferring the same to the centralized ARC under governments control, this will help in appreciating the share price and thus governments stake in the banks so this will reduce the burden of Basel III infusion that government has to do in the banks, also when bank's credit rating will go up due to less or no NPA's, Banks can raise capital at a cheaper cost from public or other sources. The NPA's will be transferred to centralized ARC under BIC (Banking Investment Company) which will speed up the recovery process being a statutory body.

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