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A study of pre and post impact of enactment of Securitization Act 2002 on asset classifications of public sector banks

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Abstract
Commercial Banks are playing a very important role in the financial system and payment systems. Banks are 'special' as financial intermediaries critical for mobilizing public saving and for deploying them to provide safety and return to savers. The introduction of economic reforms gives greater flexibility and autonomy to banks in increasing their profitability, productivity and efficiency. There is large contribution made by the Public Sector Banks (PSB's) in Indian economy, such as agriculture, various industries, trade and employment and infrastructure. Borrowers are not bounded to repay what he took away from the Bank loan. So, the NPA increased in the alarming level due to the willful defaulting on the part of the borrowers. NPAs have not only affected the efficiency and the profitability of the Banks, but also the overall performance e of the banks. The asset quality is a main parameter to assess the performance and overall functioning of banks. The reduction in asset quality results increased the level of standard Assets. Mounting NPAs is a major problem in a public sector bank with comparative to private sector banks. In this present research paper an attempt made to analyze the trends in asset classifications and trends in NPAs of SCBs Recovered through SARFAESI Act 2002. Statistical techniques like arithmetic mean, standard deviation and T-test have been employed for the analyses of data.

Keywords: Standard assets, sub standards assets, NPAs, SARFAESI Act, PSBs

Introduction

Despite various correctional steps administrated to solve and end this problem, concrete results are eluding, it is like a virus which effect universally on banking and financial institutions. The severity of the problem is, however acutely suffered by Nationalized Banks followed by SBI group and All India Financial Institutions. The concept of Asset Quality on the books of Public sector Banks and FIs came into being when RBI introduced prudential norm of asset classification on the recommendations of the Narasimham Committee in the year 1992-93.

The concept of Asset Quality on the books of Public sector Banks and FIs came into being when RBI introduced prudential norms on the recommendations of the Narasimham committee in the year 1992-93.

The loans given by the Banks are classified into performing and non-Performing assets on the following basis:

- ✓ **Performing Assets:** also known as standard assets are the assets which do not disclose any problem and which do not carry more than the normal risk attached to the business. Performing asset is one which generates income for the bank. It is an asset where the interest and or principal are not overdue beyond 180 days (modified to 90 days w.e.f. Mar 2004) at the end of the financial year.
- ✓ **Non-Performing Assets:** An amount is to be treated as non-performing asset when it ceases to generate income for the Bank. An asset may be treated as Non-Performing Asset (NPA), if interest and /or installment of Principal remain overdue for a period exceeding 180 days (modified to 90 days w.e.f. Mar 04) and Banks and FIs should not take into their Income account, the interest accrued on such NPAs, unless it is actually received/recovered. NPAs are further classified into:

a. **Substandard Assets:** Loans which are non-performing for a period not exceeding two years, where the current net-worth of the borrower or the current market value of the security, against which the loan is taken, is not enough to ensure full recovery of the debt.
b. **Doubtful Assets:** Loans which have remained nonperforming for a period exceeding two years and which are not classified as loss assets by for the management or the internal/external auditor appointed by RBI.
c. **Loss Assets:** Assets where loss has been identified by the internal/external auditor of the bank or the RBI, but the amount has not been written-off wholly or partly. These assets are considered unrecoverable and are of little value to the lending institution.

Review of literature

Rajaraman Indira and Vasishtha (2002) [1] this paper was an attempt to study the relationship between non-performing Assets and inefficiency of the borrowers. This study makes more sense for India as India suffers from inefficiency problems. The study was based on the secondary data. In their empirical study proved that significant bivariate relationship exists between non-performing loans of public sector banks and the inefficiency on the side of the borrowers. Being a closed economy for so long, India still lacks the operating efficiency to push its manufacturing sector like China has done so successfully. High inflation is also affects to the Indian economy and banks overall performance, especially NPAs. This is because when RBI takes some actions related to interest rates to control inflation, the defaulters list also grows longer for banks with rising interest rates.

Mukherjee (2003) [3] pointed out that there were broadly two ways to financially restructure a banking system out of the NPA situation. One can either follow the Asset Management/Reconstruction Company (AMC/ARC) approach to clean the balance sheet of banks of their NPAs (at a discount) and use the greater efficiency of the (government-funded) specialized AMCs in realizing the bad debts. Alternatively one could follow the creditor-led reconstruction approach. Both channels have been tried out by countries around the world with mixed results.

Awasthi and Singh (2008) [2] examined the position of NPAs in Indian public sector banks during recent years and found that at the end of March2007, net NPAs in relation to net advances for a majority of public sector banks were below the level of 2 percent. Further the study pointed out that lok adalats, debt recovery tribunals (DRT) and scheme of corporate debt restructuring have provided special thrust to banks to contain their NPAs. And also, Securitization and Reconstruction of financial assets and enforcement of security interest (SARFAESI) Act has been able to reduce the NPAs with full vigor.

Vikrant Vig (2011) [4] this paper revisits the positive link between greater creditor protection and expansion of credit and asks whether there are situations in which strengthening creditor rights could lead to a decline in credit usage by firms. Specifically, the paper exploits a quasi-natural experiment in India, the passage of a mandatory secured transactions law, the SARFAESI Act(Securitization and Reconstruction of Financial Assets and Enforcement of Security Interests Act 2002), to investigate the effect of law on corporate debt structure. Prior to the SARFAESI Act, the slow and rigid judicial process created severe bottlenecks in the recovery of security interests. To liquidate the firm, secured lenders would have to go through a prolonged judicial process, during which the value of collateral considerably depreciated in value. The reform significantly increased the rights of secured creditors by allowing them to bypass the lengthy and judicial process and seize and liquidate the assets of the defaulting firm, thus improving the ability of lenders to access the collateral of the securities.

Research Methodology

Research methodology is a way to solve the research problem systematically. While designing the research work the following methodology will be adopted.

Objectives of the Study

The specific objectives of the present study are given as:

1. To study the trends in the asset classifications of NPAs before and after the enactment of SARFAESI Act 2002 in Indian public sector banks.
2. To analyze the trends in the NPAs recovered through SARFAESI Act 2002.

Hypothesis of the study

H_0: (There is no significant difference between the level of asset classifications of NPAs in public sector banks before and after the enactment of SARFAESI Act 2002.)

H_1: (There is a significant difference between the level of asset classifications of NPAs in public sector banks before and after the enactment of SARFAESI Act 2002.)

Research design

This research by and large is descriptive in nature. This research used secondary sources in order to explain the impact of the enactment of SARFAESI Act 2002 on the asset classifications of public sector banks in India.

To achieve the stated objectives, data are collected from various sources and include;

Research reports, published articles, news reports and conference proceedings available in both national and international level related to NPA. The information obtained from these sources is used for critical evaluation of the subject and identify research gaps in the area of study. These secondary sources are part of different chapters in this report.

Sampling Unit

For Secondary data the sampling unit constitutes the public sector banks to analyze the trends in asset classifications and recovery of NPAs through SARFAESI Act 2002 after the enactment of the Act.

Tools of Analysis

In order to achieve the various objectives mentioned, the data collected were entered, arranged and presented using Microsoft Excel and SPSS 13.All information collected for the purpose of the study has been arranged in cross sectional tables, depending upon the requirements of the analysis. The tabulation encompasses absolute figures supported by simple percentage and subjected to statistical analysis through the use of Average, Standard Deviation, CAGR and Independent T-test.

Analysis and interpretation

Table 1: Trends in Classification of Loan Assets before the SARFAESI Act 2002 (From year 1995-96 to 2001-02)

Year	Standard Assets		Sub-standard Assets		Doubtful Assets		Loss Assets	
	Amount in crores	%	Amount in crores	%	Amount in crores	%	Amount in crores	%
1995-96	189660	82.0	24707	10	4,391	1.9	9299	4.00
1996-97	200637	82.2	26015	10	6,509	2.1	12472	5.1
1997-98	239318	84	25819	9.1	5,371	1.9	14463	5.1
1998-99	273618	84.1	29252	9	6,425	2	16033	4.9
1999-00	326783	86	30535	8	6,398	1.7	16361	4.3
2000-01	387360	87.6	33485	7.6	6,544	1.5	14745	3.3
2001-02	452862	88.9	33658	6.6	7,061	1.4	15788	3.1
Mean Value	295748.3	84.97	29067	8.6	6,100	1.78	14165.8	4.2
CAGR	0.1324	.0116	.0452	-0.576	.0702	-0.042	0.0786	-.035

Source: (RBI) Report on Trend and Progress of Banking in India, RBI.

Table 2: Trends in Classification of Loan Assets after the SARFAESI Act 2002 (From year 2003-04 to 2013-14)

Year	Standard Assets		Sub-standard Assets		Doubtful Assets		Loss Assets	
	Amount in crores	%	Amount in crores	%	Amount in crores	%	Amount in crores	%
2003-04	610435	92.2	28756	4.4	5,876	0.9	16909	2.5
2004-05	830029	94.6	30799	3.5	5,929	0.7	11068	1.3
2005-06	1092607	96.20	25028	2.20	5,636	0.50	11453	1.00
2006-07	1425519	97.30	19873	1.40	4,826	0.30	14275	1.00
2007-08	1656451	97.80	19083	1.13	4,018	0.20	16846	1.00
2008-09	2237556	97.99	20708	0.99	4,296	0.19	19521	0.93
2009-10	2673534	97.81	24679	0.98	5,750	0.21	27685	1.10
2010-11	2455147	97.7	31955	1.04	6,463	0.19	33612	1.10
2011-12	3437900	97.6	47075	1.33	6,000	0.10	60376	1.7
2012-13	3899985	96.8	73485	1.8	6,834	0.10	76589	1.8
2013-14	3546782	95.5	63456	1.7	5,543	0.9	55436	1.4
Mean	2169631	96.5	34991	1.86	4,437	0.39	31252	1.3
CAGR	0.1735	0.0032	0.0746	-0.828	-.005	.0000	0.1140	-.0513

Source: RBI handbook of statistics on the Indian economy2014-15

Table 3: Analysis of classification of Loan Asset

	Secu_Act	N	Mean	Std. Deviation	t	df	Sig. (2-tailed)
Standard Assets	Before	7	84.9714	2.63357			
	After	11	96.5000	1.79433	-11.102*	16	.000
Sub-Standard Assets	Before	7	4.2571	.83238			
	After	11	1.3482	.48181	9.455*	16	.000
Doubtful Assets	Before	7	8.6143	1.27073			
	After	11	1.8609	1.11871	11.857*	16	.000
Loss Assets	Before	7	1.7857	.26095			
	After	11	.3900	.30874	9.895*	16	.000

Note: * significant at 5 percent.

The Table 1.1 exhibited that amount of Standard Assets was Rs. 189660 and Sub-Standard Assets was Rs. 24707 in the year 1995-96 and then in the year 2001-02 increased up to Rs.452862 and Rs. 33658 and the amount of Doubtful Assets was Rs. 4391 and Loss Assets was Rs. 9299 in the year 1995-96 and then in the year 2001-02 increased up to Rs. 7061 and Rs.15788. Table 4.8 highlighted that amount of Standard Assets increased year on year i.e. 2003-04 to 2013-14 it is good for the bank but Sub-Standard Assets shows fluctuating trends from year 2003-04 to 2013-14. The table 1.2 also highlighted that amount of Doubtful Assets increased year on year i.e. 2003-04 to 2013-14 it is not good for the bank but Loss Assets shows fluctuating trends from year 2003-04 to 2013-14. The result of the table also revealed that percentage of Sub-Standard Assets shows reduction from 10% in the year 1995-96 to 1.7% in the year 2013-14. Table 4.9 revealed that percentage of Loss Assets shows reduction from 4% in the year 1995-96 to 1.4% in the year 2013-14. The difference in the mean scores of Standard Assets (84.9714v/s96.500, t-value-11.102) is significant at 5 percent thereby concluding that bank's Standard Assets has increased after the enactment of securitization Act 2002 and the difference in the mean scores of Sub-Standard Assets (4.2571 v/s 1.3482, t-value 9.455) is also significant at 5 percent which concluding that there is significant decrease in the Sub-Standard Assets after the enactment of the Act. The table 1.3 also exhibited that the difference in mean scores of Doubtful Assets (8.6143v/s1.8609, t-value 11.857) and Loss Assets (1.7857v/s.3900, t-value 9.895) is significant at 5 percent thereby concluding that bank's Doubtful and Loss Assets have decreased after the enactment of securitization Act 2002. There is marginal increase in the CAGR of all the loan assets of pre Act with comparative to post act period except doubtful Assets.

Table 4: NPAs of SCBs Recovered through SARFAESI Act 2002 (Amount in Crores) (from year 20003-04 to 2013-14)

Year	No. of cases referred	Amount Involved	Amount Recovered	Percentage (%)
2003-04	2,661	7847	1156	14.73
2004-05	39,288	13,224	2,391	18.08
2005-06	38,969	9,831	3,423	34.81
2006-07	60,178	9058	3749	41.4
2007-08	83,942	7,263	4,429	61
2008-09	61,760	12067	3,982	33
2009-10	78,366	14249	4,269	30
2010-11	1,18,642	30,604	11,,561	37.78
2011-12	1,40,991	35300	10101	28.6
2012-13	1,90,537	68100	18500	27.1
2013-14	1,94,707	94602	24402	25.8
CAGR	0.4774	-0.1750	-0.1319	0.0523

Source: (RBI) Report on Trend and Progress of Banking in India, RBI.

The Table 1.4 showed that data related to NPAs of SCBs Recovered through SARFAESI Act 2002.Number of cases referred under Act was 2,661 in the year 2003-04 and increased up to 1, 94,707 in the year 2013-14. Trend in the no. of cases referred increasing year on year from 2003 to 2014. CAGR of cases referred is 47.74%. The above table exhibited that amount involved was Rs. 7,847 crore in the year 2003-04 and increased up to Rs. 94,602 crore in the year 2013-14. It also shows increasing trend year on year. Data related to amount recovered highlighted that Rs. 1,156 crore recovered in the year 2003-04 and increased up to Rs. 24,402 crore in the year 2013-14 it also shows increasing trends which is good for all the banks. The result of the table revealed that percentage of NPAs recovered in SCBs through SARFAESI act 2002 shows increase from 14.73% in the year 2003-04 to 25.8 % in the year 2013-14. The result of the table concluded that recovery of NPAs in the SCBs improved after the enactment of the Act 2002.

Conclusion

The analysis highlighted two major aspects (1) trends in the movement of assets classification, (2) trends in the NPAs of SCBs recovered through SARFAESI Act 2002. The amount of Standard Assets increased during the study period it is good for the bank but Sub-Standard Assets shows fluctuating trends. The result of the study also highlighted that amount of Doubtful Assets increased during the study period, it is not good for the bank but Loss Assets shows fluctuating trends from year 2003-04 to 2013-14. There is marginal increase in the CAGR of all the loan assets of pre Act with comparative to post act period except doubtful Assets. The result of the study found that SARFAESI Act 2002 is helpful in the increasing the level of standard Assets. Number of cases referred under Act was also increased during the study period.

Data related to amount recovered also shows increasing trends which is good for all the banks. NPA is closely related to the level of advances and this relationship is mediated and moderated by many bank specific and economy specific indicators. NPA can be reduced to a great extent if banks plan and implement strategies looking into the mediating and moderating nature of bank performance variables.

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