

RECOVERY MECHANISM OF NON-PERFORMING ASSETS IN INDIAN BANKS

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ABSTRACT: A country's economic strength is determined by the strength and efficiency of its financial sector, that is determined by a strong and debt-free financial sector. An intact banking sector effectively mobilizes capital in productive sectors, while a debt-free banking system assures that the financial institutions can meet its depositor obligations. Non-performing assets (NPAs) are considerable origin of trouble for the banks in Indian financial sector. NPAs in banking sector can only be reduced with efficient recovery mechanism and proper credit assessment. In country's banking system most of the recovery pathways by which banks recover money are discovered to be unsatisfactory. This research work will basically focus on four major recovery channels i.e. Lok Adalat's, Debt recovery Tribunal, SARFAESI Act and the IBC. The functioning of recovery pathways will be summed up for a period of 10 years from 2012 to 2022.

Keywords: NPA, Recovery Mechanism, Financial system, Economic, SARFAESI Act, Credit Assessment, Lok Adalat.

1. INTRODUCTION

Banking sector is essential for survival of every contemporary economy of the country. It is a critical financial pillar belongs to financial sector, which is important for the smooth operation of an economy. For economic success of a country, it must handle its financial demands for commerce, industry, and agriculture with most enthusiasm and responsibility. Non-performing assets (NPAs) are a vital cause of trouble for banking in India. As per RBI India's Financial Stability Report, asset quality has deteriorated and leads to consequence of rise in unrecovered loans. In this subject, reducing non-performing assets (NPAs) has emerged as the primary goal of any bank. A credit is considered an asset by a bank since the interest payments and principal repayment produce a steady liquidation of cash flows for the institution. The interest payments received by a bank generates profits. Banks sometimes designate assets as bad-debts when they are not converted into cash for a prolonged period of time. Payments that are due for short length of time are considered past due, but late payments for an extended period (approx. 90 days or more) are considered non-performing. The severity of the issue, on the contrary, it is most acutely felt by nationalized banks and thus banks desired for a strong recovery channel.

The problem of non-payment of debts and recovery of money owed passes through effective mechanisms for assessing and managing recovery. If the financial sector experiences excess liquidity an economic boom, banks tend to lend which compromises the quality of assets, which

raises concerns about their adverse selection and the possible to increase the pool of non-performing loans. When the assets of a business become non-assets the turnaround services begin their activities. The execution of various recovery channels of loans in the Indian financial sector has proven adequate so far .It is possible that inadequate due diligence, capabilities linked to macroeconomic characteristics and insufficient legislation against defaulters are the main reasons for the ineffective recovery mechanism process.

2. REVIEW OF LITERATURE

Fatima& Ashraf (2020) in their paper discussed on recovering of the assets they explained When it comes to a healthy financial system, financial institutions are the backbone since they frame a major role in the growing & expansion of an economy by providing loans to an extensive sector of the economy. It is critical for the long-term development of a growing country like India that its banking industry be strong and able to fulfil the capital requirements of all parts of the population. However, throughout the previous several years the bank profitability is majorly affected by the increasing numbers of NPA's, since banks are subjected to make provisions for bad debts. To enhance their financial performance, banks must employ effective resolution strategies to recover large amounts of non-performing assets (NPA's) as quickly as possible.

Alamelumangai & Sudha (2019) in analysed that in recent years NPA has proven as the major issue for the banking sector in Indian region. When it comes to Scheduled Commercial Banks, the counting of uncleared loans has increased, and the course of NPA recovery has remained slow (SCBs). Specifically, as per the report published by RBI named as TPBI (2016), "the annual recovery rate of non-performing assets (NPA's) of scheduled commercial banks has been steadily declining for the past 12 years and reached its lowest level of 20.8 percent trendy 2016-17."

Chepuri & Banana (2021) in their paper explained the concern of nonperforming asset (NPA), which was a contributing factor to the current global financial crisis, has attracted the attention of policymakers and academics alike. Following the implementation of financial sector reforms, the country's financial system has experienced tremendous transformation. It is implementing worldwide best practises with the aim of enhancing the financial sector's stability. The incrementing nonperforming assets (NPA's) has an immediate influence on bank profitability. They are pressuring banks to increment efficiency and reduce nonperforming assets (NPA's) in a way to build up the financial position of the institutions.

Singh (2013) in his research explained the issue of non-performing assets that has wracked the whole banking industry, causing it to come crashing down. The primary cause for the high percentage of non-performing loans (NPA's) is a target-oriented approach to lending that degrades the qualitative component of lending. NPAs have a negative influence on the effectiveness, adequacy capital ratio and reliability of the monetary institution. The most significant factors that contribute to the number NPA was discussed by some of top public banks of India and some top

banks from other nation. The paper also discusses the measures required for managing NPAs, such as reformulation of banks' credit assessment methods and the formation of a monitoring department, which are recommended by the authors.

Bajaj, Sanati & Lodha (2021) in their paper explained in accordance with the Basel Committee's recommendations, their research makes major contributions to establishing an extensive pathway and the interplay of different factors in discussing non-performing assets (NPA) and level of restoration for Indian banks. Their study's added contribution is a contrast of banking sectors in value of their quality of assets and their various determinants along their other determinants (such as GDP growth rate and GDP growth rate) as well. A bank with a large amount of net interest income (NIM), a huge percentage of fluid security, and a variation of length of the loans in accordance with the bank's policy followed for asset liability may have the power to effectively manage their portfolio, according to the findings of this study.

Rajbahadur (2016) Singh in his paper discussed the Indian financial sector had been experiencing significant difficulties in raising Non-Performing Assets. Bank profitability is directly affected by increasing NPA's. Non-performing assets (NPA's) are a key source of worry for Indian commercial banks that are a point in the schedule. As a consequence of the Narasimham and Verma committees' guidance, banks have taken action to witness the problem of historical non-performing assets (NPA's). Aims of this paper are to provide an understanding of non-performing assets (NPA's) in banks in Indian region their swings and status also, the factors that donate to NPAs, the causes for the substantial effect of NPAs on India's Scheduled Commercial Banks and the recovery mechanism of NPAS through different channels.

Jha (2019) in her paper discussed NPAs are being ruled out of the banking sector as a serious concern in India. The increase in non-performing assets (NPA's) has evolved out to be one of the most pressing challenges for the banking sector. For the purposes of this study, an interbank contrast of NPA of Punjab National Bank and ICICI bank over the operational period 2011-2018 is being conducted. In all, seven years of data have been gathered through annual reports on the websites of the various banks, spanning the years 2011-12 to 2017-2018. Although the sectors of the economic and the services industry can be compared in between PNB bank and ICICI bank, the banks are not. If we compare the outstanding amount in ICICI bank to the outstanding amount in PNB bank, they saw that ICICI bank is doing much better. Because to their superior NPA management, ICICI Bank has a lower level of non-performing assets (NPA's) than PNB. When contrasted to PNB, the value of non-performing assets (NPA) is significantly smaller at ICICI bank.

Chaki, Chauhan & Daryal (2019) in their paper explained as per the study issued by the Bankruptcy Law Reforms Committee (BLRC) in November 2015, India is among the countries that takes the maximum time to settle bankruptcy cases while also incurring the greatest financial burden on the taxpayer. For India, that have a large concentration of talented entrepreneurs, prompt

resolution of failed corporates is essential in a way to build a climate conducive to credit expansion and investment in the economy, as per the World Bank. It is just as important to address NPAs with suitable recovery mechanisms as this is to mitigate them in the pre stage. After providing a small overview of the present recovery mechanisms, the current paper states the operation of the IBC and reviews its performance since its start, along with discussing the limits and issues that have been identified with the process.

Sahoo & Majhi (2020) in their paper explained the amount of nonperforming assets in a nation is the most reliable indication of the wellness of the banking industry in that country (NPA's). The issue of nonperforming assets has wracked the whole Indian banking industry, causing it to come crashing down. High nonperforming assets (NPA's) are a key source of worry for Indian banks. The only way to resolve the problem of non-payment of debts and recover the amounts owed is through effective credit assessment and recovery mechanisms. When an asset becomes a non-performing asset, the recovery wings begin their activities. The paper examines the mechanism for recovery of performing assets, which includes three important parts: recovery by Adalat, debt recovery courts and through SARFAESI Act, in addition the effect of the recovery mechanism on non-performing assets (NPA's).

Saddy & Kaur (2013) in their paper explained Non-Performing Assets (NPA's) are vital issue for the banking industry. To guarantee that the economy's banking sector is properly operating, we must ensure that NPA levels are maintained low. Banks have never taken prompt recovery and the resulting decrease in Non-Performing Assets (NPA's) as seriously as they are doing now. To handle NPAs, it's necessary to keep in mind that recovery management, whether of new or existing loans, is essential. India's banks are plagued with Non-Performing Assets, which have a bad effect on the bank's financial stability. Debt-recovery lawsuits have taken an extremely lengthy period in civil courts to be resolved and recovered.

3. OBJECTIVE OF THE RESEARCH

- Examine the mechanism of recovery of NPAs by different channels.
- Analyse the trend of recovery of NPAs by existing channels.

4. Rationale of the RESEARCH

The financial sector of India, which comprises a large number of institutions, is estimated as one of the most advanced in the developing world. Banks are the most significant of the various organizations in ways of mobilizing the country's wealth and providing loans to investors and households but the incompetency of banks in recovering the loans leads to a debt trap situation for financial sector leading to decrease in profitability of banks and slowdown of economy. So, to cope up with problem of NPAs banks need a strong recovery system. The study is conducted to

find out recovery channels of NPAs and analysis the trend of existing channels.

5. Research Methodology

This research work will specifically focus on four major recovery channels i.e. Lok Adalat's, Debt recovery tribunal (DRTs), SARFAESI Act of 2002 and IBC. The functioning of recovery pathways will be summed up for a period of 10 years from 2012 to 2022. The secondary data will be gathered from Reports on Trend and Progress of Banking, RBI. To draw significant conclusion percentage analysis and trend analysis will be used on selected data.

6. Recovery Channels

6.1 Lok Adalat's

The Legal Services Authorities Act created the Lok Adalat in India. Lok Adalat are non-adversarial proceedings in the state authority, district authority, legal committee of the Supreme Court and premises committee of the High Court convene mock courts. Debt Recovery Courts can now form Lok Adalat to deal with cases involving NPAs Rs.10 lakhs or more. The systems have proven to be more efficient in lending by allowing rapid judgment of their situations. They have mostly assisted in the repayment of smaller debts. Debt Recovery Tribunals were established in India by an Act of Parliament for the recovery of credits owed by the Government of India to banks to financial institutions. The Debt Recovery Tribunal also serves as the authority for appeals filed in under the Secured Creditor Proceedings Act 2002.

6.2 SARFAESI Act 2002

The SARFAESI enables banks and financial sectors to recover non-performing assets without involving a court. The Act defines three possible recovery procedures for non-performing assets:

(i) Securitisation; (ii) Asset Reconstruction; and (iii) Security Enforcement without the participation of the Court.

Act's restrictions apply to NPA loans having a balance of greater than Rs.1.00 lac. NPA loan accounts with less than 20% of the principal and interest are not valid to be considered under this Act. Compromise Settlement: The Compromise Settlement Scheme is a simple recovering NPAs. For loans of less than Rs. 10 crores, the Compromise Settlement Scheme is employed. Cases that are registered in court, along with those that are pending with courts and DRTs, are included.

The SARFAESI Act is sometimes stated as the Securitisation Act. This legislation authorizes banks to issue defaulters with notices that they must pay their liabilities within 60 days. The borrower is not entitled to get rid of the property without the lender's authorization after the statement is issued. The Securitisation Act also empowers banks to seize control of a company's

assets and management. Lenders may recover their losses by selling assets or changing the company's management.

6.3 Debt Recovery Tribunal (DRT)

DRT is adequately authorized to pass inclusive orders and can travel further the obliging process Law to show complete fairness. The Tribunal clear all undecided cases to the District Court under the Recovery of Debts on account of Banks and other sectors like (RDDB&FI) Act 1993. All the cases which involve an amount of 10 lakh and are pending at lower courts get automatically transferred to DRT. DRTs in India is established for immediate and stress-free recovery of credits for banks and institutions.

6.4 Insolvency and Bankruptcy Code, 2016 (IBC)

Insolvency and Bankruptcy Code is constituted under the Ministry of Finance. It is the only law which deals with insolvency and bankruptcy together. According to Crisil, the IBC has moved the power balance from the borrower to the creditor. since the borrower now stands a genuine danger of losing her assets if she does not comply with the stated rules of the agreement. Under the Code, every financial or operational creditor has the right to claim debt collection against a corporation or partnership with the National Commercial Law Tribunal. Afterward, the NCLT selects a Resolution Professional to assume control of the failing debtor's business operations. During the Corporate Insolvency Resolution Process, the Resolution Professional strives to guarantee that the defaulting debtor continues to function while simultaneously attempting to raise cash and collect debts from the creditors involved (CIRP). If the debts cannot be repaid during the CIRP, the procedure of liquidation is triggered. The whole resolution procedure, including any litigation, must be completed within 330 days of the start of the process.

7 Data Analysis and Interpretation

This section illustrates the analysis of data related to different recovery channels and measures which are used for recovering NPAs. It further includes the number of total cases which are referred to different recovery channel and the amount which is being recovered from those channels.

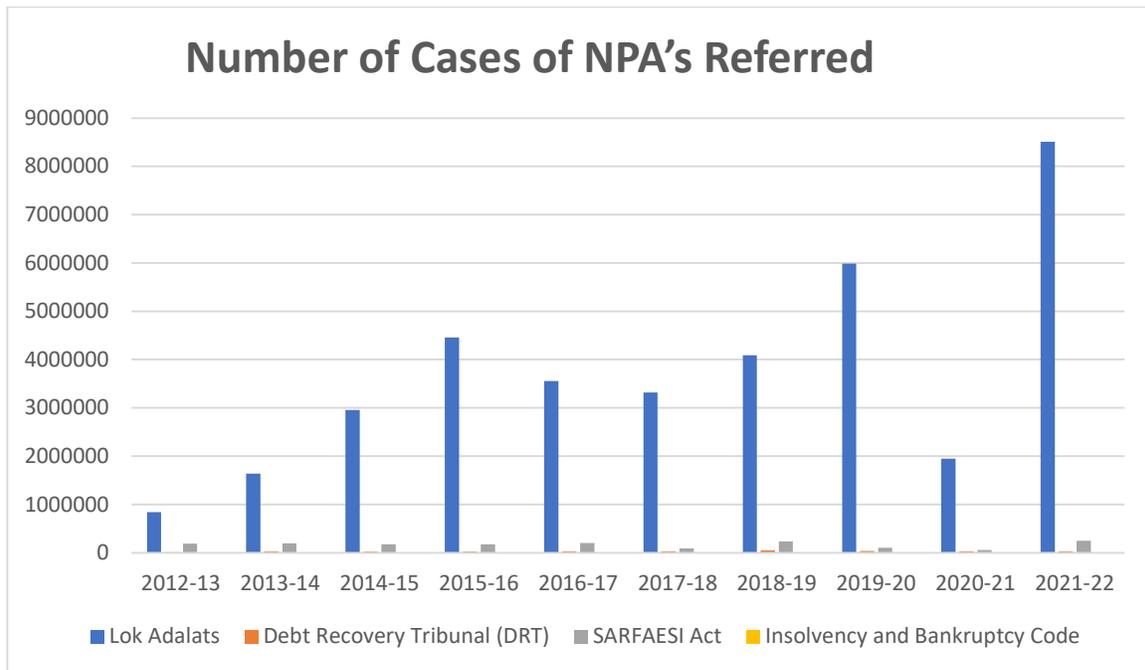
7.1 Total Number of Cases of NPA's Referred

YEAR	Lok Adalat's	Debt Recovery Tribunal (DRT)	SARFAESI Act	Insolvency and Bankruptcy Code
2012-13	840691	13408	190537	0
2013-14	1636957	28258	194707	0
2014-15	2958313	22004	175355	0
2015-16	4456634	24537	173582	0
2016-17	3555678	32418	199352	37

2017-18	3317897	29551	91330	701
2018-19	4087555	51679	235437	1152
2019-20	5986790	40818	105523	1953
2020-21	1949249	28182	57331	537
2021-22	8506648	29487	249475	885

Source- Report on Trend and Progress of Banking in India, RBI, Various Issues

(a)



(b)

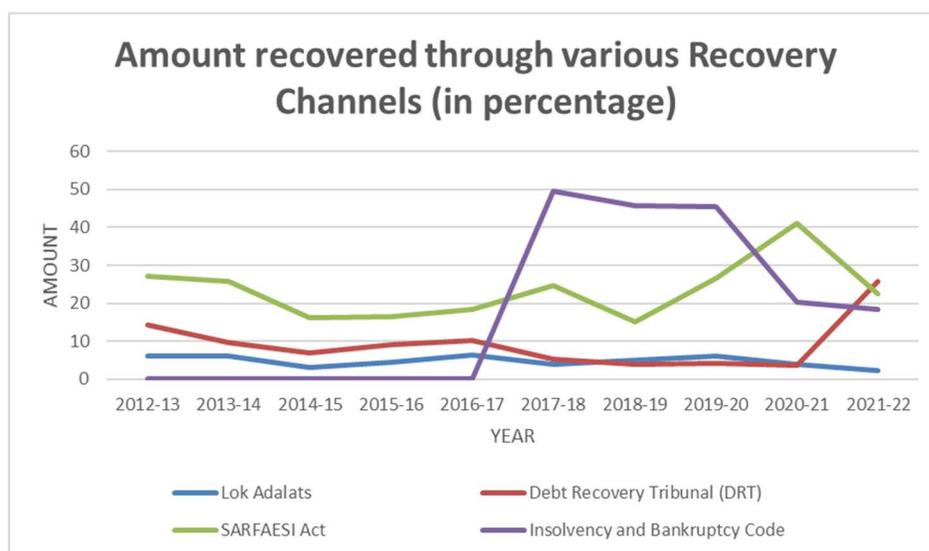
It can be clearly stated from the bar graph stated above that the maximum number of cases related to non-performing assets are allotted to Lok Adalat's as they are considered as the most prominent recovery channels used for NPAs rest three channels have received a least significance when compared with Lok Adalat's. The second most adopted channel is SARFAESI act but when compared with Lok Adalat's the cases which were referred are very low. Insolvency and Bankruptcy Code which came into existence in 2016 but from the till now the cases referred to IBC are lowest till now. In 2021-22 the cases which were referred to Lok Adalat's are maximum as of now.

7.2 Amount recovered through various Recovery Channels (in percentage)

YEAR	Lok Adalat's	Debt Recovery Tribunal (DRT)	SARFAESI Act	Insolvency and Bankruptcy Code
2012-13	6.06	14.19	27.17	0
2013-14	6.03	9.58	25.79	0
2014-15	3.18	6.97	16.33	0
2015-16	4.48	9.18	16.45	0
2016-17	6.37	10.22	18.32	0
2017-18	4.0	5.4	24.8	49.6
2018-19	5.1	3.9	15.0	45.7
2019-20	6.2	4.1	26.7	45.5
2020-21	4.0	3.6	41.0	20.2
2021-22	2.3	25.7	22.5	18.4

Source- Reports on Trend and Progress of Banking in India, RBI, Various Issues

(c)



(d)

The above line graph shows the total amount of NPAs which was recovered through various channels. While analysing the data of the recovered amount of NPAs from various channels it is analysed that most the highest percentage of the amount is recovered from Insolvency and Bankruptcy Code but then also least fraction of cases are being transferred to IBC and the least percentage is recovered from LOK Adalat's but when dealing to the total amount of NPAs recovered it is done through Lok Adalat's and the least amount from IBC. The SARFASI Act stood at number second in recovery of NPAs followed by Debt Recovery Tribunal. Even though the study suggested that the percentage of recovered money has decreased from 6.06 % in 2012 to 2.3% in 2022 in the instance of Lok Adalat, from 14.19% in 2012 to 3.6% in 2021 in case of DRTs and from 27.17% in 2012 to 22.5% in 2022 in the instance of SARFAESI Act.

8 CONCLUSION

Indian banks have experienced a remarkable transformation by reason of fast changes occurred due to the progressive financial sector reforms. The current transformation activity should be seen as a chance to change Indian banking into a steady, robust, and dynamic sector capable of carrying out its responsibilities efficiently and effectively without placing the government at risk. According to the study banks have made every effort to reduce non-performing assets via various legal channels such as Lok Adalat rulings, Debt Recovery Tribunals (DRTs), and SARFAESI activation. Even though the study indicates that recovery trend is downward when discussed about recovery channel and it is a significant decline in some cases which indicates a drastic increase in NPAs of Indian banking sector thus declining the productivity and profitability of the banks. The recovery slowed primarily due to a reduction in recovery through the SARFAESI channel. Banks also reduced stressed assets by selling them to asset recovery companies (ARCs). RBI along with Government of India should focus on strengthening of recovery channels which can lead to improvement in the overall efficiency of the financial system and the effectiveness and efficiency of individual institutions. Consequently, it is mandatory to examine the efficiency of banks in India and the recovery measures followed by those banks to take remedial action to enhance the banking system's health.

9 Limitations of the Research

- The study is basically limited to a time span of 10 years i.e. from 2012 to 2022.
- Only four major recovery channels are being used in the research and the rest are being ignored.
- The data is restricted to use of published data for analysis and primary data is not considered.

10 FUTURE SCOPE OF THE research

Research in future can be most precisely conducted on working mechanism of all the recovery channels. In order that limitations can be easily discovered in recovery process and the preventive measures can be adopted for smooth functioning of the recovery tribunals. Primary data can be collected from each bank to know about the recovery tribunal used by that bank.

11 ABBREVIATIONS

NPA- Non-Performing Assets, RBI- Reserve Bank of India, DRT- Debt Recovery Tribunal, IBC- Insolvency and Bankruptcy Code, SARFAESI Act- The Securitization and Reconstruction of Financial Assets and Enforcement of Security Interests Act of 2002, ARCs- Asset Recovery Companies

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