

Estimates committee's report on Non-performing assets

Why in news?

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Parliament's Estimates Committee on public sector banks headed by Raghuram Rajan released its report recently on NPA's.

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What are the contents of the report?

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- It says that gross NPAs of banks rose to Rs 10.3 lakh crore in FY18, or 11.2% of advances.

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- **Reasons for rising bad loans -**

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1. **Over-optimism** - Banks extrapolate past growth and performance of the companies that made them to **accept higher leverage** in projects.

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2. **Slow Growth** - Domestic demand slowdown after GFC crisis (2008) affected strong demand projections.

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3. **Government decision-making** - Governance problems as in allocation of coal mines, Project cost overruns etc., made projects unable to service debts.

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4. **Loss of Interest** - Banks' **deceptive accounting** by failing to restructure and recognize losses or declare the loan NPA, to make the business look profitable to the shareholders.

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5. **Malfeasance** - Lack of an independent analysis in the system which multiplies the possibilities for undue influence.

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6. **Fraud** - Increase in the number of of fraud cases in PSBs.

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- **RBI's rationale to introduce schemes**

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1. The **Debts Recovery Tribunals** (DRTs) were set up to help banks recover their dues speedily without being subject to the procedures of civil courts.
2. The **SARFAESI Act** was setup to enable banks a to enforce their security interest and recover dues even without approaching the DRTs.
3. Yet the recovery was only 13% of the amount at stake and only 25% of these cases were disposed off during a year.
4. So **CRILC** was created, that includes all loans over Rs. 5 crores, to identify early warning signs of distress in a borrower such as habitual late payments.
5. **Joint Lenders' forum** was created to decide on an approach for resolution, while giving the opportunity to exit for unconvinced borrowers.
6. 5/25 scheme was created to establish reliability on projects that have long dated future cash flows.
7. Strategic Debt Restructuring (SDR) scheme to enable banks to displace weak promoters by converting debt to equity.
8. All these tools effectively created a resolution system that replicated an **out-of-court bankruptcy**.

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- **Importance of recognising NPAs**

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1. To restructure or write down loans, the bank has to recognize it has a

problem i.e classify the asset as a Non Performing Asset (NPA).

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2. Only then the bank balance sheet will represent a true and fair picture of the bank's health, as a bank balance sheet is meant to.

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• **RBI's role in creation of NPAs**

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1. Bankers, promoters, and circumstances create the bad loan problem.
2. The RBI is just a referee, not a player in the process of commercial lending.

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• **Reason to initiate the Asset Quality Review**

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1. Banks were simply not recognizing bad loans, neither were they following uniform procedures.
2. Hence, Asset quality review was done to ensure every bank followed the same norms on every stressed loan and to look for signs of ever-greening.

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• **Reason for NPAs even after AQR**

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1. Risk-averse bankers
2. Lethargy of promoters before Bankruptcy Code was enacted, hoping to regain control through a proxy bidder, at a much lower price.

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3. The government's delay on project revival etc

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- **Recommendations to RBI**

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1. RBI should probably have raised more flags about the quality of lending in the early days of banking exuberance.

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2. It should have initiated the new tools earlier, and pushed for a more rapid enactment of the Bankruptcy Code.

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3. RBI could have also been more decisive in enforcing penalties on non-compliant banks.

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Source: The Indian Express

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