



Securitization Act 2002 and NPAs of public sector banks

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Abstract

The banking sector in the India plays an important role in the growth of an economy. Through its intermediary activities, the banking sector fosters the production, distribution, exchange and consumption processes in the economic system. Similar to any other business enterprise, the efficiency of a bank is evaluated based on profitability and quality of assets it possesses. The Bank has created Non- Performing Assets (NPA's), when the amount of bad and doubtful Assets increased in the banks. When the amount of the loan is due, they neither recover the capital nor earn income in real terms. Such NPA's affects the performance and profitability of the bank. This leads to drain on the social resources. The issues of 1 lakhs crore NPA's in Indian Banking system and need for augmenting necessary capital as per prescribed Basel norms, were strongly deliberated between Banking department of (GOI) Government of India, RBI and (G o M) Group of Ministers in the central cabinet. After seriously pondering over the said issue, the Government of India emerges with the consensus to present a bill in the parliament giving substantial autonomy to the management of PSB's in releasing the blocked funds in the NPA's account by lawful recovery means as formulated in the forms of Securitization Act of 2002. For the first time Banks management were equipped with sharp result orienting tools of the Securitization Act to realize long term NPA's. Under the Act Banks were authorized to attach immovable properties of the defaulting borrowers and sale through auction of such property, the proceeds of which were directly receivable by the Bank for appropriation in borrowers NPA's account. The enactment of the securitization Act 2002 is very helpful in the recovery of the NPAs and credit management. The Main feature of the Act is that no need to go court. Keeping in mind the above views & importance of the Act, a modest attempt made to carry out study in respect of trends in the NPAs of public sector banks and SARFAESI Act 2002.

Key words: Gross and Net NPAs, PSBs, SARFAESI Act.

Introduction

Securitisation Act 2002

The Securitization and Reconstruction of Financial Assets and Enforcement of Securities Act, 2002 [SARFAESI] Act, 2002 was enacted to regulate securitization and reconstruction of financial assets and enforcement of security interest and for matters connected therewith or incidental thereto. The Act encompasses the areas of: securitization of financial assets; reconstruction of financial assets; recognition to any security interest created for due repayment of a loan as security interest under the Securitization Act, irrespective of its form; banks and financial institutions have the power to enforce the security without intervention of the courts; setting up the Central Registry for registration of the transaction of securitization, reconstruction and creation of security interests.

The need for the setting up an asset reconstruction company for acquiring distressed assets from Banks and FIs with a view to develop market for such assets was

being felt, since long. Narasimham Committee 1 &2 and the Verma Committee on restructuring of weak Banks has strongly recommended the setting up of Asset Reconstruction Companies (ARCs) The business of Securitisation and Reconstruction is primarily meant for more than one purpose:

- To regulate the business of securitization and reconstruction of the financial interest
- To regulate enforcement of the security interest and for the matters connected therewith or the matters incidental thereto

Review of Literature

Shakuntalamani (2001) highlighted the magnitude of NPAs in banks, reasons for mounting NPAs, the impact and the measures adopted for reducing NPAs in the banking system so far. The study was based on the secondary data. The information had been retrieved from Report on the trend and progress of banking in India, various books and journals. The study found that the percentage of NPAs to gross advances had a downward trend over the year of study (1993 to 1999) which indicated better

management techniques in banks. Further, legal framework, political interference, competition and liberalization were identified as reasons for mounting of NPAs. The study concluded that recovery efforts had been redoubled upon within the framework of the guidelines.

Sanjai Singh Rathore and Alka Singh (2004) in their study found the relationship between NPAs and capital adequacy. Relationship was analyzed by considering the case study of Avadh Gramin Bank, Lucknow. The study was based on the secondary data. The NPAs was Rs.3200.29lacs in year 1996-97 which increased to Rs. 3623.11 in the year 2000-01. The problem of NPAs remained the same during the period of the study. The main reason was that bank had very poor receiving ratio. It had a higher percentage of NPAs in its total advances. The capital adequacy ratio was 14.11% in the year 1998-99 which increase to 18.25% in the year 2000-01. It means the bank making efforts to improve the capital adequacy ratio. At last they concluded that Avadh Gramin Bank, Lucknow had to make efforts to minimize its Nonperforming Assets. For this purpose, the bank regularly analyses, case by case, its sticky advances and makes efforts to recover

loans. The bank had power to issue recovery certificates also and to realize its debts from farmers as arrears of land revenue.

Seema Mahlawat and Sumanjeet (2010) in their study outlined that the enactment securitization Act 2002, Indian banks and financial institutions had been scrutinizing some of their distressed assets. The mechanism thus far had been selling banks to trade in their assets for Security Receipts (SRs) issued by SPV set up for holding these assets. The recovery and workout process was managed by Assets Reconstruction Company (ARC) set up under the SARFAESI Act 2002. The Act had paved the way of several out-of-court settlements. The act confers power on secured creditors to take possession and sell assets kept as security if a default is committed by the borrower in repaying secured debt. The 2002 Act aims to regulate securitization, reconstruct financial assets and enforce security interests. Prior to 2002 there was no provision for facilitating securitization of financial assets and the power to take possession of securitized assets and selling them off. The study was based on secondary data. Data collected from Global Financial Stability Report 2006,

Revealed that public sector banks have settled about 30% of their NPAs cases for which they issued notices under the securitization Act 2002. Data also shows that after the introduction of Securitization Act 2002, Indian public sector banks are able to manage the problem of NPA. Study shows that 1, 18980 notices to recover amounts outstanding to the tune of rs35, 650 crore are estimated to have been issued till March 31, 2006 under the SARFAESI Act. Lastly, concluded that SARFAESI Act 2002 has been positive and has helped the Indian banking sector reduce, to an extent, the problem of NPA assets.

J. Rama Devi and Dr. B. Ramachandra Reddy (2014) found that N.PAs is a major problem for banking sector in indianite does not generate income for the banks. Today public sector banks give loans to different sectors, So that the most critical area in the improvement of the profitability of banks continues to be the reduction of non-performance assets (NPAs). The specific objectives of the study were to analyze the classification of loan assets in Public Sector Banks and to examine the causes and remedial measures to arrest. The study concentrated on PSBs only and study based on the secondary data. The data are collected from annual report of RBI publications

including Trend and Progress of Banking in India, Statistical Tables relating to Banks in India, Articles and Papers relating to NPAs published in different journal and magazines were studied. The amount of standard assets showed an increasing trend during the stated period. In the initial year 2004 the ratio of standard assets to total advances stood at 92.2 percent. It increased to 96.4 percent in 2013. Total advances of Public Sector Banks is increased from Rs.6, 61,976 crore in 2004 to Rs.39,428 crore in 2012. The Net NPAs to per cent of Net Asset ratios it was 1.3 per cent in 2004 and increased to 2.0 per cent in 2013. At last concluded that a large number of compromise proposals are being approved by banks with a view to reducing the NPAs and recycling the funds instead of resorting to expensive recovery proceedings spread over a long period.

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 level of Net NPAs of Indian public sector banks before and after the enactment of SARFAESI Act 2002.
2. To analyze the trends in the level of Gross NPAs of Indian public sector banks before and after the enactment of SARFAESI Act 2002.

Hypothesis of the study

H₀: (There is no significant difference between the level of net and gross NPAs of public sector banks before and after the enactment of SARFAESI Act 2002.)

H₁: (There is a significant difference between the level of net and gross NPAs of 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 non-performing assets 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 NPAs and trends in the recovery of NPAs 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 - 1.1 Trends in Net NPAs before the SARFAESI Act 2002 (From year 1995-96 to 2001-02)

Year	Net NPAs (Amount in crores)	Net NPAs to total Assets ratio (%)	Net NPAs to total Advances ratio (%)
1995-96	19985	3.6	8.9
1996-97	20285	3.6	9.18
1997-98	21232	3.3	8.15
1998-99	24211	3.1	8.13
1999-00	26187	2.9	7.42
2000-01	27969	2.7	6.74
2001-02	27958	2.4	5.8
Mean Value	23975.29	3.08	7.76
CAGR	0.0491	-0.0563	-0.0593

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

Table-1.2: Trends in Net NPAs after the SARFAESI Act 2002 (From year 2003-04 to 2013-14)

Year	Net NPAs (Amount in Crores)	Net NPAs to total Assets ratio (%)	Net NPAs to total Advances ratio (%)
2003-04	19335	1.28	3.1
2004-05	16904	0.95	2.1
2005-06	14566	0.72	1.3
2006-07	15145	0.62	1.1
2007-08	17836	0.6	1.0
2008-09	21155	0.6	-0.9
2009-10	29375	0.6	1.1
2010-11	36000	0.7	1.2
2011-12	59300	0.7	1.5
2012-13	90000	1.0	2.0
2013-14	130624	1.3	2.6
Mean	40930.909	0.82	1.46
CAGR	0.1897	0.0014	-0.0159

Source: RBI handbook of statistics on the Indian economy

Table - 1.3 Analysis of Net NPAs

	SARFAESI Act 2002	N	Mean	Std. Deviation	t-value	df	Sig. (2-tailed)
Net NPAs to total Assets ratio	Before	7	3.08	.45251			
	After	11	0.82	.26741	13.418*	16	.000
Net NPAs to total Advances ratio	Before	7	7.7571	1.19740			
	After	11	1.4682	1.04045	11.818*	16	.000

Note: * significant at 5 percent.

The Table 1.1 showed that the amount of Net NPAs was Rs.19985 in the year 1995-96 and then in the year 2001-02 increased up to Rs.27958. Net NPAs shows fluctuating trend from the year 2003-04 to 2013-14. The table also revealed that percentage of Net NPAs to total Assets ratio shows reduction from 3.6 % in the year 1995-96 to 1.3% in the year 2013-14 and the percentage of Net NPAs to total Advances ratio shows reduction from 8.9% in the year 1995-96 to 2.6% in the year 2013-14. Throughout Bank showing a reduction in the ratio of Net NPAs to total assets and net advances on YOY basis, which also means that the Bank successful in effecting recovery in NPA account on a regular basis and the Bank's ability to assess the credit risk has enhanced with the help of Securitization Act. In terms of Asset quality table 1.3 showed that the

difference in mean scores of Net NPAs to total Assets Ratio (3.08v/s0.82, t-value 13.418) and Net NPAs to total Advances Ratio (7.7571v/s1.4682, t-value11.818) is significant at 5 percent, thereby concluding that banks Net NPAs has decreased after the enactment of securitization Act 2002. There is an increase in the CAGR of net NPAs with comparative to post act period.

After analyzing the trends in the Net NPAs than trends in the Gross NPAs analyze. Gross NPAs shows the actual burden of the banks. The Securitization Act 2002 also helpful in the problem of Gross NPAs. To know the impact of Act phase wise study carried out. Phase –I covered the period (1995-96 to 2001-02) of 7 years before the enactment of the Act because after the introduction of economic reforms, many changes come in the banking industry

like low interest rate, increase credit in the market so that Gross NPAs start increasing since the year 1995-96. Phase –II covered the

period (2003-04 to 2013-14) of 11 years after the enactment of the Act.

Table 1.4: Trends in Gross NPAs before the SARFAESI Act 2002 (From year 1995-96 to 2001-02)

Year	Gross NPAs (Amount in crores)	Gross NPAs to total Assets ratio (%)	Gross NPAs to total Advances ratio (%)
1995-96	41661	8.2	18
1996-97	43577	7.8	17.8
1997-98	45653	7.0	16.2
1998-99	51710	6.7	15.9
1999-00	53294	6.0	14
2000-01	54774	5.3	12.4
2001-02	56507	4.9	11.1
Mean Value	49596.57	6.5	15.05
CAGR	0.0445	-0.0709	-0.0667

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

Table-1.5: Trends in Gross NPAs after the SARFAESI Act 2002 (From year 2003-04 to 2013-14)

Year	Gross NPAs (Amount in crores)	Gross NPAs to total Assets (%)	Gross NPAs to total Advances ratio (%)
2003-04	51541	4.2	3.5
2004-05	47796	3.5	2.7
2005-06	42117	2.7	2.1
2006-07	38974	2.1	1.6
2007-08	40598	1.6	2.2
2008-09	45918	1.3	1.97
2009-10	57301	1.2	2.19
2010-11	74616	1.3	2.23
2011-12	117839	1.4	3.3
2012-13	165606	1.9	4.1
2013-14	228074	2.4	4.3
Mean	82761.81	2.14	2.7
CAGR	-0.1448	-0.0496	0.0189

Source: RBI handbook of statistics on the Indian economy 2014-15

Table - 1.6: Analysis of Gross NPAs

	SARFAESI Act 2002	N	Mean	Std. Deviation	t-value	df	Sig. (2-tailed)
Gross NPAs to total Assets ratio	Before	7	6.5571	1.23134			
	After	11	2.1455	.98322	8.426*	16	.000
Gross NPAs to total Advances ratio	Before	7	15.0286	2.63357			
	After	11	2.7445	.91280	14.380*	16	.000

*Note: * significant at 5 percent.*

The Table 1.4 revealed that the amount of Gross NPAs was Rs. 41661 in the year 1995-96 and then in the year 2001-02 increased up to Rs. 56507. Gross NPAs shows fluctuating trend from the year 2003-04 to 2013-14. Amount of Gross NPAs was decreasing from year 2003-04 to 2007-08 after that it started again increasing from year 2008-09 to 2013-14. The table also revealed that percentage of Gross NPAs to total Assets ratio shows reduction from 8.2% in the year 1995-96 to 2.4% in the year 2013-14 and Gross NPAs to total Advances ratio shows reduction from 18% in the year 1995-96 to 4.3% in the year 2013-14. Throughout Bank showing reduction in percentage of Gross NPAs on YOY basis,

which also means that the Bank's ability to assessing and managing its credit risk has enhanced with the help of Securitization Act. In terms of Asset quality table 1.6 exhibited that the difference in mean scores of Gross NPAs to total Assets Ratio (6.5571v/s2. 1455, t-value8. 426) and Gross NPAs to total Advances Ratio (15.0286v/s2. 7445, t-value14. 380) is significant at 5 percent thereby concluding that banks Gross NPAs has decreased after the enactment of securitization Act 2002. There is a marginal decrease in the CAGR of gross NPAs with comparative to post Act period.

Findings of the study:

The result of the study revealed that Net NPAs shows an increasing trend from the year 1995-96 to 2001-02 but after that it shows fluctuating trend from the year 2003-04 to 2013-14. Throughout the study period bank showing a reduction in percentage of Net NPAs to Net Advances on YOY basis, which also means that the Bank's ability to assess the credit risk has enhanced with the help of Securitization Act. The result of the study also highlighted that Gross NPAs shows an increasing trend from the year 1995-96 to 2001-02 after that it shows fluctuating trend from the year 2003-04 to 2013-14. Throughout the study period Bank shows reduction in percentage of Gross NPAs to total Assets ratio on YOY basis, which also means that the recovery of the NPAs has enhanced with the help of Securitization Act.

Conclusion

The review of literature and feedback from experts enabled this research to develop the various dimensions of the NPA in Indian banking sector. This background provides a strong foundation for future research in this subject. The research utilized many statistical techniques which were not dealt in detail in previous researches in order to examine the various

objectives and to test various hypothesis and theories. These new tools can be utilized and may be further developed and hence might help new researches in their research. The analysis indicates that ratio of gross and net NPAs to total assets and advances decreasing during the study period. It means after the introduction of Act the level of NPAs decreased in the public sector banks. The regulatory authorities have introduced significant measures in the post-millennium period that includes SARFAESI Act etc. Even though these measures are significant and to a greater extent helped the banks to reduce their level of NPA, the generation of fresh NPA particularly its increased trend during financial crisis highlights the need for effective credit risk management mechanism. Amount of NPAs recovered through SARFAESI Act 2002 also increased YOY.

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