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.
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2. The **SARFAESI Act** was setup to enable banks a to enforce their security interest and recover dues even without approaching the DRTs.
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3. Yet the recovery was only 13% of the amount at stake and only 25% of these cases were disposed off during a year.
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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.
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5. **Joint Lenders' forum** was created to decide on an approach for resolution, while giving the opportunity to exit for unconvinced borrowers.
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6. 5/25 scheme was created to establish reliability on projects that have long dated future cash flows.
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7. Strategic Debt Restructuring (SDR) scheme to enable banks to displace weak promoters by converting debt to equity.
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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.
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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.
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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

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2. Lethargy of promoters before Bankruptcy Code was enacted, hoping to regain control though 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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