A Detailed Study of Non-Performing Assets & Its Impact on Financial Performance of Commercial Banks

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Abstract— The primary activity of commercial banks is to accept deposits and to provide loans. The motive of Commercial banks is to earn profits by lending loans to the public and charging interest on the same. It makes profit on the spread i.e. the difference between the borrowing rate and lending rate. However when the borrower makes a default in the payment of the interest and the principal amount of the loan provided banks have to suffer. Such non-payment of interest and principal are treated as Non-performing assets. They adversely affect the financial performance of commercial banks. The aim of this research study is to evaluate the impact of NPA on financial performance of selected commercial banks. The data is collected from secondary data sources. The data sources include research articles, papers, journals and various websites. The collected data is analyzed utilizing different statistical tools and techniques.

Key words: Commercial Banks, Non-Performing Asset, Financial Performance

I. INTRODUCTION

The primary activity of commercial banks is to accept deposits and to provide loans. The motive of Commercial banks is to earn profits by lending loans to the public and charging interest on the same. The commercial banks earnings are determined by the spread between the interest it pays on deposits and the interest it earns on loans. This spread is called as net interest income. It makes profit on the spread i.e. the difference between the borrowing rate and lending rate. However when the borrower makes a default in the payment of the interest and the principal amount of the loan provided banks have to suffer. Such nonpayment of interest and principal are treated as Non-performing assets. An asset, including a leased asset, ceases to generate income for the bank, it becomes non-performing asset. These non-performing assets adversely affect the financial performance of commercial banks.

II. RELATED WORK

Kaur K. and Singh B. (2011) in study on "Non-performing assets of public and private sector banks' (a comparative study) It has been studied that the NPAs are considered an important parameter for judging the performance and financial health of the banks. The level of NPA is one of the drivers of financial stability and growth of the banking sector.

Rai (2012) in study on 'Study on performance of NPAs of Indian commercial banks' concluded that Corporate borrowers, even after continuous non-compliance, have never been afraid that the bank would take steps to recover their commissions. This is because there was no legal framework to safeguard the banks' real interest.

Chatterjee C., Mukherjee J. and Das (2012) in study on 'Management of non- performing assets a current scenario' has found out that Banks must find out the original purposes of the loan requested by the borrower. The bank must verify the correct identification of the guarantor, including the control of its activities.

III. OBJECTIVES

1) To evaluate NPA in relation to Loan Advances Ratio and its impact on financial performance of selected commercial banks
2) To evaluate the impact of NPA on the capital adequacy ratio of selected commercial banks

IV. ANALYSIS

Following are the selected commercial banks for the purpose of research study:

1) Bank of India
2) Andhra Bank
3) Citi Union Bank
4) Axis Bank

V. EXPERIMENTAL RESULTS

Calculation of Ratios for selected commercial banks:

A. *Bank of India*

	2017-18	2016-17	2015-16	2014-15	2013-14	2012-13	2011-12	2010-11	2009-10	2008-09
Capital Adequacy Ratio	12.94	12.14	12.01	10.73	9.97	11.02	11.95	12.17	12.94	13.01
Return on Assets	-0.24	0.94	0.27	0.51	0.65	0.72	0.82	0.7	1.49	1.25
Return on Equity	-5.04	-19.5	5.57	10.14	12.25	14	15.79	12.56	24.97	24.38
Net Profit Margin	-15.87	-3.96	-14.56	3.93	7.19	8.62	9.4	11.44	9.74	18.39
Operating expenses Ratio	19.59	19.27	19.92	16.37	15.33	16.7	17.34	23.3	20.52	18.92
NPA to Loan Advances Ratio	6.9	7.79	3.36	2	2.06	1.47	0.91	1.31	0.44	0.52
Credit to deposit ratio	66.72	67.86	70.02	75.58	77.73	75.78	78.2	71.3	73.33	75.33

Table 1:

B. Andhra Bank

	2017-18	2016-17	2015-16	2014-15	2013-14	2012-13	2011-12	2010-11	2009-10	2008-09
Capital Adequacy Ratio	11	12.38	11.58	10.63	10.78	11.76	13.18	14.38	13.93	13.22
Return on Assets	-1.36	0.08	0.28	0.38	0.29	0.99	1.19	1.36	1.39	1.09
Return on Equity	-30.77	1.56	5.13	6.79	5.07	16.19	19.25	23.24	25.96	18.94
Net Profit Margin	-18.64	1.03	3.04	3.88	2.97	9.99	11.86	15.28	16.41	12.15
Operating expenses Ratio	15.48	16.23	14.49	14.66	14.2	15.78	15.91	20.56	21.18	20.54
NPA to Loan Advances Ratio	8.48	7.57	4.61	2.93	3.11	2.45	0.91	0.38	0.17	0.18
Credit to deposit ratio	70.86	70.02	75.04	81.25	75.89	79.46	78.62	77.52	72.23	74.32

Table 2:

C. Citi Union Bank

	2017-18	2016-17	2015-16	2014-15	2013-14	2012-13	2011-12	2010-11	2009-10	2008-09
Capital Adequacy Ratio	16.22	15.83	15.58	16.52	15.01	13.98	12.57	12.75	13.46	12.69
Return on Assets	1.48	1.5	1.5	1.49	1.44	1.58	1.71	1.67	1.52	1.5
Return on Equity	14.21	15.18	15.47	16.74	18.94	22.33	24.91	23.47	20.55	19.9
Net Profit Margin	17.39	17.39	15.84	15.1	14.63	14.71	16.52	17.65	15.97	15.18
Operating expenses Ratio	17.85	17.39	15.06	15.21	15.52	17.09	16.49	17.76	17.34	17.35
NPA to Loan Advances Ratio	1.7	1.71	1.53	1.3	1.23	0.63	0.44	0.52	0.58	1.08
Credit to deposit ratio	82.08	79.14	77.53	74.62	73.11	75.09	74.28	71.67	66.44	68.79

Table 3:

D. Axis Bank

	2017-18	2016-17	2015-16	2014-15	2013-14	2012-13	2011-12	2010-11	2009-10	2008-09
Capital Adequacy Ratio	16.57	14.95	15.29	15.09	16.07	17	13.66	12.65	15.8	13.69
Return on Assets	0.03	0.65	1.72	1.83	1.78	1.7	1.68	1.68	1.67	1.44
Return on Equity	0.43	6.76	16.81	17.75	17.43	18.53	20.29	19.34	19.15	19.12
Net Profit Margin	0.6	8.26	20.06	20.73	20.29	19.05	19.29	22.36	21.6	16.75
Operating expenses Ratio	23.65	20.79	19.18	20.07	19.81	25.44	27.31	31.54	31.88	26.38
NPA to Loan Advances Ratio	3.4	2.27	0.74	0.46	0.44	0.36	0.27	0.29	0.4	0.4
Credit to deposit ratio	93.63	90.03	94.64	87.17	81.89	77.97	77.13	75.25	73.84	69.48

Table 4:

VI. Conclusion

The problem of NPAs in the Indian banking system is one of the most important and most formidable problems that have affected the whole banking system. A higher NPA ratio shakes the confidence of investors, depositors, lenders, etc. It also causes poor recycling of funds, which in turn will have a negative effect on the development of credit. The non-recovery of loans affects not only the increased availability of credit, but also the financial soundness of the banks.

From the above analysis it is very certain that the commercial banks financial performance as well as the Capital Adequacy of commercial banks is affected by the NPAs.

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