



NPA Recovery Mechanism in India: A Critical Assessment

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Abstract : Banks play an important role in the development of a nation. A well-functioning financial system is fundamental to any economy and a strong banking system contributes for a stronger economy. Banks are the primary suppliers of credits and lends money to different sectors of the economy out of the deposits. The problem arises when banks are not able to recover the amount lent along with the interest resulting in NPA. Mounting NPAs are of great concern even today as it affects the operational efficiency of the banks and as well impede the economic activities. Therefore, the need for addressing the NPA issues is of a great priority for all the researchers. There is numerous research work which concentrated on identifying the causes and its impact of NPAs on banks performance and very few on ways of reducing and recovery of bad loans. This study aims to measure the efficiency of NPA recovery channels in India and also to compare their efficiency of recovery channels by using statistical tools in order to identify the significant difference between the performance by the important players in recovery of non-performing asset loans viz., Lok Adalaths, DRT's, SATFAESI Act and IBC. Secondary data on recovery of non-performing asset loans through major recovery channels during 2016-2020 is analyzed using One Way ANOVA and Tukey-Kramer test for testing the hypothesis. The study finds that there is a significant difference in the performance of recovery channels and recommends for a single window agency for recovery of bad loans which can reduce the losses due to NPAs to certain extent.

Key Words: Banks, Hypothesis, NPA, Recovery Channels

Introduction

The banks have been lending to all kinds borrowers since inception and all such lending is generally secured by collateral securities including personal guarantees. In spite of bank's care in lending to different sectors, Indian banks are confronting with huge stock of stressed assets and that has piled in the system over the years resulting in huge NPA's. The percentage of NPA on gross advances stood at 2.2 percent (Scheduled Commercial Banks), 2 percent (Public Sector Banks), 3, percent (Private Sector

Banks), 3.8 percent (Foreign Banks) during 2008-09 and the NPAs of Scheduled Commercial Banks, Public Sector Banks, Private Banks and Foreign Banks has grown up to 8.2, 10.3, 5.5 and 2.3 percent respectively during 2019-2020. The statistics shows the NPA level is increasing over the years and high level of NPA indicates high credit defaults resulting in banks losing out on investment in long run. If bank continues to remain saddled with huge NPA, it would impede the economic activities in general and operational efficiency of



banks in particular. To reduce the mounting NPA levels and to recover the NPAs, series of measures are initiated by Reserve Bank of India.

Review of Literature

D.J. Singh n.d. (2013) in his research study titled “Recovery of NPAs in Indian Commercial Banks” aims to analyze the causes and impact of high NPA on banking sector. Using secondary data, the author finds that one of the causes for high NPA is unsatisfactory the performance of various recovery channels of NPA in Indian banking system and suggests for the need for and improved NPA recovery mechanism in India.

Garg (2016), in his research study titled “A Study on Management of NPAs in Context of Indian Banking System” aims to identify the causes of NPA along with understanding the preventive mechanism for NPA. Based on the secondary data, the study identifies that ineffective recovery of NPA as one of the factors for raise in NPA.

V. R. Singh (2016) aims to study the status and impact of NPAs on banks and also to know the recovery of NPAs through various channels in his study titled “A Study on Non-Performing Assets of Commercial Banks and its Recovery in India. Based on secondary data relating to years 2000to 2014 finds that ineffective recovery, willful defaults and defective lending process are important factors responsible for risk of NPAs in Indian Banks. The author is of the opinion that there is more dependency on SARFAESI Act for recovery than any other NPA recovery channels and suggests banks for one-time settlement.

Monica & Supreeth (2016), analyses the NPA data pertaining to the period between 2009-10 to 2013-14 in order to study the trends and position of NPA of Public Sector Banks and also to identify

the reasons for occurrence of NPA and to examine the steps taken by RBI for recovery of NPA. One of the recommendations based on analysis is to develop appropriate recovery programmes by banks.

Swain et al., (2017) in their research titled” NPA of Scheduled Commercial Banks in India and its Regulatory framework” aims study the effectiveness of regulatory framework for recovering debts of scheduled commercial banks using secondary sources of data relating to 2008 to 2016. The study finds that the basic factors responsible for increasing NPAs are ineffective recovery, willful defaults and defective lending process. One of the recommendations by the author is the need for strengthening the recovery mechanism.

Surojit (2018), analyses the various recovery channels and comment on the effectiveness of the recovery process. The research study uses secondary data relating to 2003-04 to 2016-17. The study analyses and finds the loan recovery by SARFAESI is much lower than the expectation, DRT consumes more time and it has a lengthy recovery process and Lok Adalaths cannot recover NPA’s more than ten lakhs. Analysis of data is made using ANOVA through SPSS 20 package. Author suggests for strengthening of credit risk management.

Kumar, B. R. (2018), in their research titled “Genesis for Increase in NPAs in Indian Banks-An Empirical Analysis” aims to identify the causes for increase of NPAs and ranks the causes for NPA to enable the banks to have effective control on NPAs. Primary and secondary data relating to May to June 2018 were analyzed in excel using Garrett ranking and finds that the ineffective recovery channel stands first followed by industrial sickness, poor credit appraisal system,



willful defaults, defective lending process etc.,

Varuna & Nidhi (2019), in their study on “A critical Review of Non-Performing Assets in the Indian Banking Industry” aims to determine the mean growth rate of NPAs for different groups of banks and individual banks and also to assess the growth pattern of gross NPA’s using secondary data pertaining to the period 2010 to 2017. The analysis of data using geometric mean, the study finds that the problem of NPA is not only with small banks but also with the big banks and suggests for stringent norms for control of non-performing assets.

Alamelumangai & Sudha (2019), in their study titled “Recovery of NPAs through debt recovery channels in Indian Banks- An Analysis” aims to study the recovery of NPAs through various channels and to examine the effectiveness of existing channels for recovery of bank loans. Secondary data is analyzed using percentage analysis, trend analysis, one-way ANOVA and Tukeys HSD Post Hoc Test. The study finds that the annual rate of recovery out of the amount involved in the existing channels are not satisfactory and suggests for need for strengthening of existing channels.

Allda & Jnaneshwar (2021), in their research aims to estimate the extent of NPA held by commercial banks and to measure the financial effects of NPA using secondary data. Data pertaining to NPA for the period 2017 to 2020 were analyzed using descriptive statistics and finds that there a steady increase in NPA and recommends for use of NPA recovery tools like Lok Adalaths, Debt Recovery Tribunals and SARFAESI Act an improve recovery mechanism.

Statement of the Problem

Non-performing assets was evaluated systematically only after the

implementation of the recommendations of the committee on Financial System (Narashiman Committee 1991). NPA issue has received considerable attention in the post reform period as accumulated NPAs has direct impact on the efficiency and profitability of banks. In this backdrop, there are many research work carried on to identify the trend, reasons and impact of NPA on performance of banks and as well to suggest policy measures to reduce NPAs. In spite of various measures by Reserve bank of India, there is an increase in the level of NPA over the years. Therefore, the need for reduction and recovery of NPAs and to assess the efficiency of recovery channels to safeguard the interest of the banks is of high priority even today.

Research Questions

- What is the existing recovery mechanism in India?
- What is the percentage of NPA recovery by existing recovery channels?
- Are existing recovery channels effective in recovery of NPA?
- Are there any differences in the recovery performance between the existing recovery channels?
- Is there a need for establishment of Bad bank in India?
- Is there a need to continue with the existing recovery channels even after the introduction of Bad bank?

Research Gap

There are many research work on non-performing assets aiming to identify the causes and impact of non-performing assets and also to measure the performance of recovery channels. Most of the literature reviewed for this research have concentrated on evaluating the cause for high NPA and recommend for improving recovery mechanism. There



arises a need for evaluating the recovery mechanism in terms of recovery process, effectiveness of recovery channels and trend in recovery of NPAs by recovery channels. Based on the review of literature it was found that the many research work is conducted in the time range from 2000 to 2017 and not much study on evaluating the performance of all recovery channels using statistical tools.

Need for the Study

The announcement of establishment of Bad banks by honorable Finance Minister Dr. Nirmala Sitharaman to address the problems involved in NPA recovery during Budget speech 2021 calls for a need for relooking in to the effectiveness of existing NPA recovery channels to substantiate the need for establishment of Bad banks in India. Review of literature also recommends for the analysis of the performance of existing recovery channels. Therefore, this study aims for evaluating the performance of existing NPA recovery channels.

Research Methodology

The study is based on the secondary data relating to NPA recovery through various existing channels in India viz., Lok Adalaths, DRTs, SARFAESI Act and IBC. The secondary data is collected for the period 2016 to 2020 from the annual reports published by RBI in RBI website and also through review of literature. The present study analyzed the data collected using percentages, trend analysis and averages. One Way ANOVA is used to compare the significant difference in the recovery through various recovery channels and Tukey-Kramer test is used to find the significant differences amongst the NPA recovery channels. Statistical tools for data analyses were decided based on the previous literature and hypothesis is tested using One Way ANOVA and Tukey-Kramer test in Excel.

Objectives of the Study

In order to address the issues raised in the research questions based on the review of literature, the present study aims

1. To understand the existing NPA recovery mechanism.
2. To analyze the trend of recovery by different recovery channels
3. To assess the performance of each of the recovery channel.
4. To compare the recovery performance amongst the existing channels.

Hypothesis

H0= There is no significant difference in NPA recovery through existing recovery channels.

H1= There is a significant difference in NPA recovery through existing recovery channels.

NPA Recovery Mechanism

Recovery mechanism is a process of carrying out the recovery procedures and mechanism to restore the financial assets in the event of failure to repay by the borrower.

Lok Adalat is a forum where cases pending in the court of law or pre-litigation stage are settled/compromised amicably. Lok Adalats have been given statutory status under the Legal Services Authorities Act 1987. Under this Act, the decision made by the Lok Adalats is deemed to be final and binding on all parties and no appeal against such an award. Reserve Bank of India has issued guidelines for compromise settlement pf dues through Lok Adalats to all commercial banks and all India Financial Institutions vide circular LEG.BC.114/09.06.002/2000-01. Coverage of borrowers may include all NPA accounts, both suit filed and non-sit filed accounts, which are in “doubtful” and “loss” category with outstanding balance of rupees ten lakhs at present. The advantage of use of this recovery mechanism is that there are no court fees



involved when fresh disputes are referred to it.

Table 1 showing number of cases referred and the amount involved for NPA recovery through Lok Adalats

(Amount in Crores)

Year	Number of Cases referred	Amount involved	Amount Recovered	Percentage of recovery
2016	2152895	1058	38	3.6
2017	3317897	45728	1811	4
2018	4087555	53484	2750	5.1
2019	5986790	67801	4211	6.2
2020	1949249	28084	1119	4

Source: www.rbi.org.in

Debt Recovery Tribunals (DRT's)

The Recovery of Debts and Bankruptcy Act, 1993 provides for establishment of Debts Recovery Tribunals with original jurisdiction and Debt Recovery Appellate Tribunals with appellate jurisdiction, for expeditious adjudication and recovery of debts due to bank and financial institutions, insolvency resolution and bankruptcy of individuals and partnership firms and connected matters there with.

The Act is applicable to cases where amount of debt due to any bank or financial institution defined under the Act is rupees twenty lakhs or more. One of the major issues associated with the DRT is the success rate of tribunals as it is over burdened with more cases.

Table 2 showing number of cases referred and the amount involved for NPA recovery through Debts Recovery Tribunals

(Amount in Crores)

Year	Number of Cases referred	Amount involved	Amount Recovered	Percentage of recovery
2016	28902	671	164	24.4
2017	29345	133095	7235	5.4
2018	51679	268413	10552	3.9
2019	33139	205032	9986	4.9
2020	28182	225361	8113	3.6

Source: www.rbi.org.in

The Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002

SARFAESI Act empowers banks and financial institutions to recover their non-performing asset loan dues without the intervention of the court. The provisions of this Act is applicable only for non-performing loans with outstanding above

one lakh rupees. Further, non-performing loan accounts where the amount is less than 20% of the principal and interest are not eligible to be dealt under this Act. Asset Reconstruction Companies were set up to recover secured loans by enforcing the security interest and auctioning borrower's property. ARC's is another institutional alternative of NPA resolution in India.



Table 3 showing number of cases referred and the amount involved for NPA recovery through SARFAESI Act

(Amount in Crores)

Year	Number of Cases referred	Amount involved	Amount Recovered	Percentage of recovery
2016	80076	1131	78	6.9
2017	3317897	45728	1181	32.2
2018	235437	258642	38905	15
2019	105523	196582	34283	17.4
2020	57331	67510	27686	41

Source: www.rbi.org.in

The Insolvency and Bankruptcy Code

The Insolvency Bankruptcy Code was enacted in 2016 to achieve resolution of distressed corporate debtors. It also facilitates liquidation in time bound

manner under the supervision of National Company Law Tribunal. The code has set up a robust ecosystem where debtors and creditors are initiating resolution process under the provisions of this code.

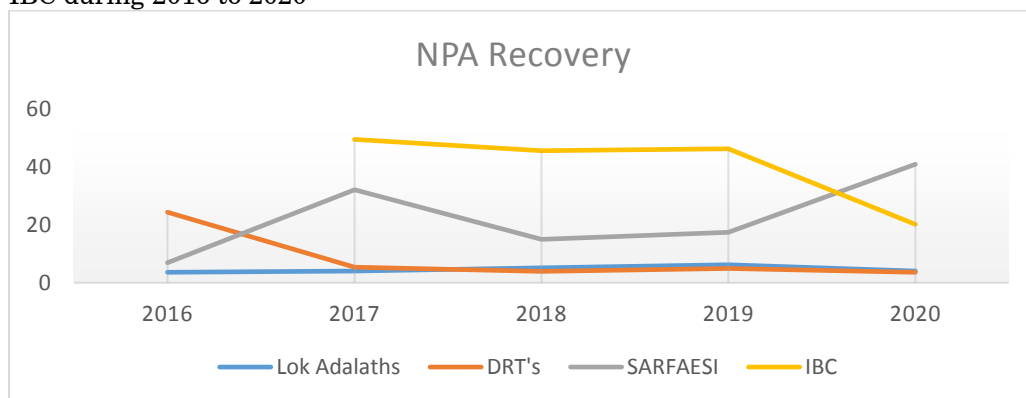
Table 4 showing number of cases referred and the amount involved for NPA recovery through IBC

(Amount in Crores)

Year	Number of Cases referred	Amount involved	Amount Recovered	Percentage of recovery
2016				
2017	704	9929	4926	49.6
2018	1152	145457	66440	45.7
2019	1986	224935	104117	46.3
2020	537	135139	27311	20.2

Source: www.rbi.org.in

Graph 1 showing non-performing asset loans by Lok Adalaths, DTR's, SARFAESI and IBC during 2016 to 2020



Source: Data Tables



The above table and graph indicates the NPA recovery percentage by four major NPA recovery channels during 2016-2020. NPA recovery performance by Lok Adalaths and DRT's is low and consistent, more variance is found in recovery under

SARFAESI Act and the percentage of recovery by IBC is very high when compared to other stated channels of recovery though there is a decline during 2020.

Hypothesis Testing

One Way ANOVA is used for testing the hypothesis

	Lok Adalaths	DRT's	SARFAESI Act	IBC
	3.6	24.4	6.9	
	4	5.4	32.2	49.6
	5.1	3.9	15	45.7
	6.2	4.9	17.4	46.3
	4	3.6	41	20.2
Sum	22.9	42.2	112.5	161.8
Mean	4.58	8.44	22.5	32.36
Variance	1.132	80.133	190.49	466.133
Factor Levels	4			
n	20			
s ² _{pooled}	184.472			
n.	5			

SUMMARY

<i>Groups</i>	<i>Count</i>	<i>Sum</i>	<i>Average</i>	<i>Variance</i>
Column 1	5	22.9	4.58	1.132
Column 2	5	42.2	8.44	80.133
Column 3	5	112.5	22.5	190.49
Column 4	5	161.8	32.36	466.133

ANOVA

<i>Source of Variation</i>	<i>SS</i>	<i>df</i>	<i>MS</i>	<i>F</i>	<i>P-value</i>	<i>F crit</i>
Between Groups	2468.53	3	822.8433333	4.460532	0.01852	3.238872
Within Groups	2951.552	16	184.472			
Total	5420.082	19				

Interpretation

Hypothesis of the study is tested by comparing the p value (Significance level

0.05) and by comparing the F value with F critical value.



The analysis indicates that the p-value 0.01852 which is less than the significance level of 0.05 indicating the rejection of the null hypothesis and acceptance of alternate hypothesis.

F statistic is used in analysis to decide the acceptance or rejection the null hypothesis based on the F value and F critical value. If calculated f value is larger than the F

critical value, null hypothesis will be rejected and vice versa. The above analysis shows the output of F value 4.460532 and F critical value 3.238872 indicating the rejection of null hypothesis and acceptance of the alternate hypothesis.

Further, in order to find out the statistical significant differences between the group, Tukey-Kramer test is used.

Q	4.05		
Num df	4	Den df	16

Tukey-Kramer

Comparison	Absolute difference	Critical Range	Results
a-b	3.86	24.60	Not significantly different
a-c	17.92	24.60	Not significantly different
a-d	27.78	24.60	Means significantly different
b-c	14.06	24.60	Not significantly different
b-d	23.92	24.60	Not significantly different
c-d	9.86	24.60	Not significantly different

The above output table indicates that the significant difference between the NPA recovery channels exist between group a (Lok Adalaths) and group d (IBC). Thus, Tukey-Kramer test output statistically proves and supports the rejection of the null hypothesis i.e. there is no significant difference between the performance NPA recovery by Lok Adalaths, DRT’s, SARFAESI Act and IBC and acceptance of the alternate hypothesis i.e. there is a significant difference between the performance NPA recovery by Lok Adalaths, DRT’s, SARFAESI Act and IBC.

Conclusion

The deterioration of asset quality and recovery of these asset loans has been a subject of continued concern since decades. Lok Adalaths, DRT’s, SARFAESI Act and IBC are considered to be the

important players in the NPA recovery in India and each of the channels are in to the recovery process with their legal framework. The structure and the business operations of these channels decides the amount and time for recovery of NPA loans resulting in considerable delay and low percentage of recovery of loans. The reason behind the delay and lesser percentage of recovery by these players may be attributed to over stretched operating capacity as they are not concentrating only on NPA resolutions. Moreover, consistent increase in the deterioration of assets in Indian banks have resulted in mounting NPA’s and the same need to be addressed by these recovery channels along with the other settlement of debts. Though the percentage of recovery through IBC has



been on rise in recent years, stands as a complementary mechanism for asset resolution. The analysis of the data in the study highlights that there is a significant difference in the performance of each of the stated recovery channels and significant difference is found between Lok Adalaths and IBC and there is no significant difference between the performance in relation to recovery of NPA between other recovery channels. With the mounting of non-performing asset loans, need for a single window recovery mechanism is preferable and the same is proposed in the union budget.

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