



International Journal of Management and Commerce

www.managementjournal.in

Online ISSN: 2664-6854; Print ISSN: 2664-6846; Impact Factor: RJIF 5.46

Received: 07-12-2020; Accepted: 22-12-2020; Published: 26-01-2021

Volume 3; Issue 1; 2021; Page No. 07-11

A critical analysis of impact of NPA on state bank of India

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Abstract

SBI and its associates is the largest bank in the country. State Bank of India and its Associates (now merged in SBI) are playing a important role in the Indian economy. All over the world State Bank of India is a bank having Associates has branches. Accept deposit and lending is the main purpose of every bank and with the help of these transactions earns profits. State Bank of India and its Associates are public banks and performing the same functions. Lending is main source of earning of a bank and lending customers can be good and can be bad. Bad customers of a bank turn its assets into non-performing assets.

So in the above scenario a research paper is constructed. In this paper the impact of Non-Performing Assets on the earnings of the State of India and its Associate is studied.

Not only that, impact of NPA on the EPS and the dividend paid to its stockholders also analysed.

Statistical tool like correlation is used to reveal the results. Data of 10 years i.e. March 2011-March 2020 is taken into consideration from the website of Reserve Bank of India.

Keywords: NPA, EPS, PAT, earnings, state bank of India and its associates

Introduction

State Bank of India (SBI) is an Indian multinational, public sector banking and financial services statutory body headquartered in Mumbai, Maharashtra. SBI is the 43rd largest bank in the world and ranked 236th in the Fortune Global 500 list of the world's biggest corporations of 2019.[8] A nationalised bank, it is the largest in India with a 23% market share by assets and a 25% share of the total loan and deposits market.

The roots of State Bank of India lie in the first decade of the 19th century when the Bank of Calcutta later renamed the Bank of Bengal, was established on 2 June 1806. The Bank of Bengal was one of three Presidency banks, the other two being the Bank of Bombay (incorporated on 15 April 1840) and the Bank of Madras (incorporated on 1 July 1843). All three Presidency banks were incorporated as joint stock companies and were the result of royal charters. These three banks received the exclusive right to issue paper currency till 1861 when, with the Paper Currency Act, the right was taken over by the Government of India. The Presidency banks amalgamated on 27 January 1921, and the re-organised banking entity took as its name Imperial Bank of India. The Imperial Bank of India remained a joint-stock company but without Government participation.

Pursuant to the provisions of the State Bank of India Act of 1955, the Reserve Bank of India, which is India's central bank, acquired a controlling interest in the Imperial Bank of India. On 1 July 1955, the Imperial Bank of India became the State Bank of India. In 2008, the Government of India acquired the Reserve Bank of India's stake in SBI so as to remove any conflict of interest because the RBI is the country's banking regulatory authority.

In 1959, the government passed the State Bank of India (Subsidiary Banks) Act. This made eight banks that had belonged to princely states into subsidiaries of SBI. This was at the time of the First Five Year Plan, which prioritised the development of

rural India. The government integrated these banks into the State Bank of India system to expand its rural outreach. In 1963 SBI merged State Bank of Jaipur (est. 1943) and State Bank of Bikaner (est.1944).

SBI has acquired local banks in rescues. The first was the Bank of Bihar (est. 1911), which SBI acquired in 1969, together with its 28 branches. The next year SBI acquired National Bank of Lahore (est. 1942), which had 24 branches. Five years later, in 1975, SBI acquired Krishnaram Baldeo Bank, which had been established in 1916 in Gwalior State, under the patronage of Maharaja Madho Rao Scindia. The bank had been the Dukan Pichadi, a small moneylender, owned by the Maharaja. The new bank's first manager was Jall N. Broacha, a Parsi. In 1985, SBI acquired the Bank of Cochin in Kerala, which had 120 branches. SBI was the acquirer as its affiliate, the State Bank of Travancore, already had an extensive network in Kerala.

There was, even before it actually happened, a proposal to merge all the associate banks into SBI to create a single very large bank and streamline operations.

SBI provides a range of banking products through its network of branches in India and overseas, including products aimed at non-resident Indians (NRIs). SBI has 16 regional hubs and 57 zonal offices that are located at important cities throughout India.

A non-performing asset (NPA) is a classification used by financial institutions for loans and advances on which the principal is past due and on which no interest payments have been made for a period of time. In general, loans become NPAs when they are outstanding for 90 days or more, though some lenders use a shorter window in considering a loan or advance past due.

A loan is classified as a non-performing asset when it is not being repaid by the borrower. It results in the asset no longer generating

income for the lender or bank because the interest is not being paid by the borrower. In such a case, the loan is considered "in arrears."

Classifications for Non-Performing Assets (NPAs)

Lenders usually provide a grace period before classifying an asset as non-performing. Afterward, the lender or bank will categorize the NPA into one of the following sub-categories:

Standard Assets

They are NPAs that have been past due for anywhere from 90 days to 12 months, with a normal risk level.

Sub-Standard Assets

They are NPAs that have been past due for more than 12 months. They have a significantly higher risk level, combined with a borrower that has less than ideal credit. Banks usually assign a haircut (reduction in market value) to such NPAs because they are less certain that the borrower will eventually repay the full amount.

Doubtful Debts

Non-performing assets in the doubtful debts category have been past due for at least 18 months. Banks generally have serious doubts that the borrower will ever repay the full loan. This class of NPA seriously affects the bank's own risk profile.

Loss Assets

These are non-performing assets with an extended period of non-payment. With this class, banks are forced to accept that the loan will never be repaid, and must record a loss on their balance sheet. The entire amount of the loan must be written off completely. In present scenario NPAs are at the core of financial problem of the banks. Concrete efforts have to be made to improve recovery performance. The main reasons of increasing NPAs are the target-oriented approach, which deteriorates the qualitative

Effects of High NPA's for Banks

Higher NPA impact the revenue strength of the banks and also lose the confidence level of consumers and depositors, banks are back boon to the financial economy of every country. Here are some effects in details:

- Changes in Interest Rates
- Levies of charges for every operation

Looking at the above scenario, the bank is recovering their losses by levies charges on those operations which were free of cost like

- Withdrawal limit from ATM
- Withdrawal number of times
- Cash deposits in other branches
- Internet transaction charges
- Increase in Current account deficit

NPA plays an important role in every economic condition and also the main cause of the increase in the current account deficit. Interest rates, Loan, Housing Loans, CRR, SLR all are directly affected by the system.

- The Corporates also affect the impact of higher NPA.
- Confidence in Share Holders

Higher NPA's in banking system losing the confidence of shareholders, and the depositors, they are switching the segments and losing the trust in the system.

- Effect on the serious borrower

Increase in NPA not only affect the public but also affecting the serious honest borrower with good credentials and credit ranking. They have to suffer and on the other hand, the economy is losing hope of improvement.

Literature Review

In 2014 Narula, Sonia Singla, and Monica made a study on PNB earnings and NPA. In the study it is concluded that correlation factor between earning and NPA is 0.31. So there is a positive relationship between the factors, earnings and NPA of the bank. They said that such possibility can be possible because of management of funds and wrong choice of clients by PNB. In the research it is said that there are two categories of customers. One is called good customers and the other is bad customers. Those, who pay interest on time are good customers and those, who convert Bank's asset into bad debt are bad customer. So bank have to manage their funds properly and continuously by monitoring the customers.

In 2013, K.K. Siraj and Dr P. Sudarshan makes a study on NPA and their effectson banking sector. In the study it is revealed that NPA is like a virus, and this virus affecting the banking sector. Banking sector's liquidity, profitability and solvency is affected by the NPA. In their study they are concluded that NPA is a major threat and incremental component which poses a great question mark on efficiency of credit risk management of banks on India. In 2013 K.T. Shrinivas made a study and concluded that the banks should not sanctioned loans to the browsers who are non credit worthy. Bank should be constantly monitor the borrowers to ensure that the sanction amount is properly utilised and it should be utilised for the purpose to which it has been sanctioned. Formal and informal reports about the Goodwill of the customers should be considered by the banker. No question of sanctioning loan to a defaulter. Borrowers should be educated by the banker about the effects and consequences of defaulting. And such education is a duty of a banker. Non-performing assets in a bank can be reduced by considering all the other factors.

Apex Bank should be more reachable to all browsers by using the technology like core banking solutions etc. In 2009 Pathak made a study aboutNPA and explained that for Indian economy NPA is very dangerous. He estimated that around 9.8 % of GDP is NPA at constant prices.

Objectives of the stud

1. To analyse the Earnings of State Bank of India and its Associates and check the trend.
2. To study the Non-Performing Assets of State Bank of India and its Associates and check the trend.
3. To compare the Earnings and NPAs of the bank and study their relationship.
4. To compare the EPS and NPAs of the bank and study their relationship.

5. Suggest some measure for improvement if there is any inefficiency.

Research methodology

In order to conduct the empirical research, secondary data from the website of Reserve Bank of India is taken into consideration. State Bank of India and its Associates will be considered. Time period of 10 years i.e. April 2010-March 2020 will be covered in this study. Factors namely, Non-Performing Assets (NPAs), Earnings, EPS and DPS will be covered where NPA will be independent factor and Earnings, EPS, DPS will be dependent factors.

One thing is to be noted over here that we have two types of NPAs,

1. Gross NPAs &
2. Net NPAs.

Here Net NPA’s amount is taken into consideration. Thereafter we will see that whether changes in NPA will affect the earnings

of the bank, if yes, then to what extent.

We also examine whether NPA has any impact on EPS and DPS of the bank.

In order to see the relationship between the two said factors, Karl’s Pearson coefficient of correlation will be used. And then we will see that whether there is positive correlation or negative correlation between the two factors.

Hypothesis Testing

H0: There is no relation between earning and NPA of the state bank of India and its associates.

H1 There is no relation between NPA and PAT of the SBI and its associates.

H2: There is no relation between EPS and NPA of the state bank of India and its associates.

Data Analysis

1. To study the Earnings and NPA of State Bank of India and its Associates we take the data for last 10 years i.e from 2011 to 2020

Table 1

Year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Earning (in bn)	972.19	1208.73	1356.92	154.9	1749.73	1918.44	2109.79	2651	2796.43	3025.45
NPA (in bn)	123.47	158.19	219.56	310.96	275.9	558.07	582.77	1108.55	658.95	518.71

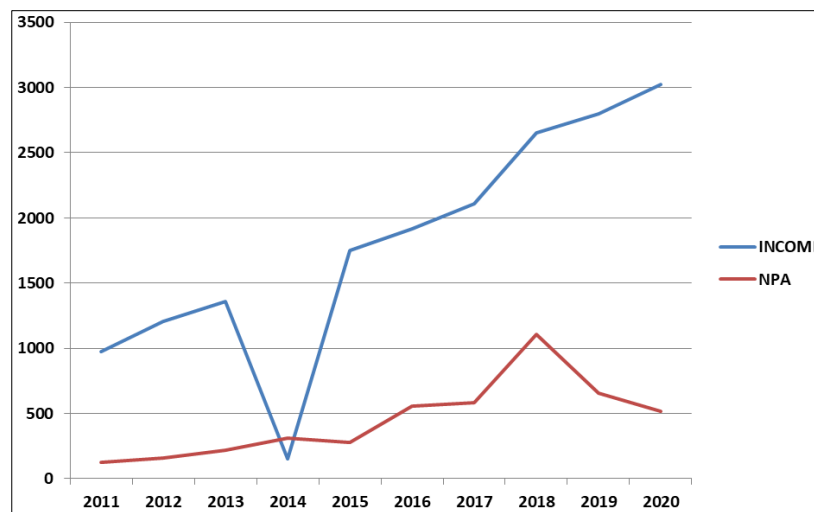


Fig 1

From the above figure it has been cleared that earning of SBI and its associates has been continuously increased since 2011 to 2020 except in the year 2014. In 2014 the earnings of the bank is drastically fall. In last 10 years the earnings of SBI increased from 972.19 billion to 3025.45 billion i.e. almost 211.20%

But NPA of SBI and its associates has been continuously rising. In last 10 years the NPA of SBI increased from 123.47 billion to 518.71 billion i.e almost 320.11%.

So comparing both the growth rate NPA’s growth rate is more than the Bank’s income growth rate. It may be the alarming sign for the bank. But in last 2 years NPA is decreasing constantly, which indicates a positive sign for the bank. Specially after 2018 NPA has been decreased drastically from 1108.55 bn to 518.71

bn i.e 53% decreased in last 2 years. It is a very great sign for the SBI.

Table 2

	% Change in Earning	% Change in NPA
2011 to 2018	179.68%	798%
2018-2020	14%	(-) 53%

Hypothesis testing

H0: There is no relation between earning and NPA of the state bank of India and its associates. To test the above hypothesis persons correlation coefficient test has been done from the above two set of data. Overall analysis of two factors (earning and NPA) of different years with the help of correlation

Table 3

Variables	Correlation	Coefficient Degree	Description
Earning, NPA	0.70	High Degree	Positive

Above calculation shows that there is high degree positive correlation between the two factors. Means Net Non-Performing Assets has a positive impact on Earnings. Means increase in NPAs leads to increase in Earnings. This positive correlation

shows the efficiency of State Bank of India and its Associates because generally NPA have negative impact on earnings. So we reject the null hypothesis and accept that there is positive relationship between earnings and NPA of the SBI and its associates.

- To study the PAT and NPA of State Bank of India and its Associates we take the data for last 10 years i.e from 2011 to 2020

Table 4

year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
NPA	123.47	158.19	219.56	310.96	275.9	558.07	582.77	1108.55	658.95	518.71
PAT	8.26	117.07	11.05	108.91	131.01	99.5	10.84	-65.47	8.62	144.88

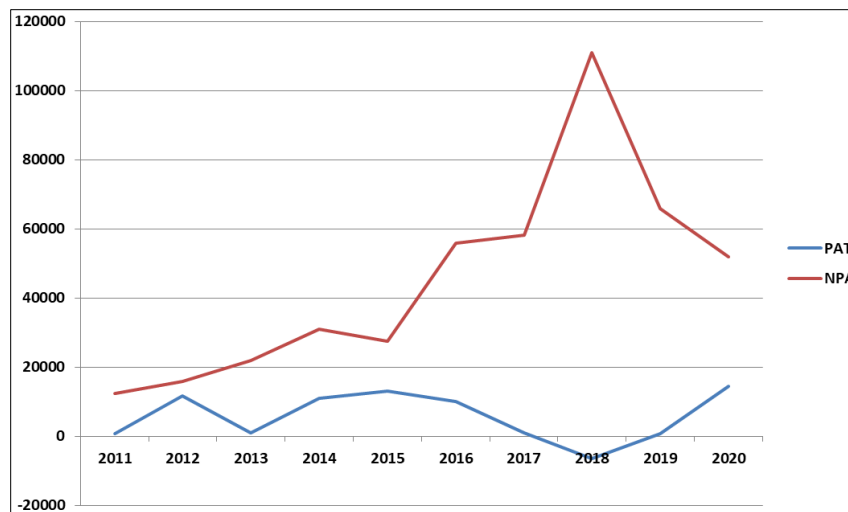


Fig 2

NPA of SBI and its associates has been continuously rising. In last 10 years the NPA of SBI increased from 123.47 billion to 518.71 billion i.e almost 320.11%. But after 2018 Bank has taken some major steps against NPA and as a result in last 2 years NPA is decreasing drastically (i.e almost 53%) which indicates a positive sign for the bank.

PAT has been increased from 8.26 billion to 144.88 billion in last 10 years. i.e almost 1654%. Specially in last 2 years PAT increased 321%.

Hypothesis testing

H1: There is no relation between PAT and NPA of the state bank of India and its associates.

To test the above hypothesis persons correlation coefficient test has been done from the above two set of data. Overall analysis of two factors (PAT and NPA) of different years with the help of correlation

Table 5

Variables	Correlation	Coefficient Degree	Description
PAT, NPA	(-) 0.51	Moderate	Negative

Above calculation shows that there is negative correlation between the two factors. Means Net Non-Performing Assets has a negative impact on PAT. Means increase in NPAs leads to

decrease in PAT and decrease in NPA leads to increase in PAT. It is a logical conclusion because profitability of a bank depends upon the recovery of loans and existence of bad loan will jeopardize it.

So we reject the null hypothesis and accept that there is a relationship between earnings and NPA of the SBI and its associates. The relationship is negative relationship.

- To study the EPS and NPA of State Bank of India and its Associates we take the data for last 10 years i.e from 2011 to 2020

Table 6

year	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
NPA	123.47	158.19	219.56	310.96	275.9	558.07	582.77	1108.55	658.95	518.71
EPS	130.16	184.31	210.06	15.68	17.55	12.98	13.3	-7.67	0.97	16.23

NPA of SBI and its associates has been continuously rising. But EPS is very high upto 2013. In 2013 it is Rs 210. After 2013 EPS decreases to only 15.68 and after that there is no such change in EPS. In last 6 years i.e from 2014 to 2020 EPS increase only 3.5%. However from 2014 to 2020 PAT increases almost 33.03%.

Hypothesis testing

H1: There is no relation between EPS and NPA of the state bank of India and its associates.

To test the above hypothesis persons correlation coefficient test has been done from the above two set of data. Overall analysis of two factors (EPS and NPA) of different years with the help of correlation

Table 7

Variables	Correlation	Coefficient Degree	Description
EPS, NPA	(-) 0.58	Moderate	Negetive

Above calculation shows that there is negetive correlation between the two factors. Means Net Non-Performing Assets has a negetive impact on EPS. Means increase in NPAs leads to decrease in EPS and decrease in NPA leads to increase in EPS.. So we reject the null hypothesis and accept that there is a relationship between earnings and NPA of the SBI and its associates. The relationship is negative relationship.

Findings

1. Amount of NPAs are continuously increasing from 2011 to 2020. The amount of earnings is also continuously increasing for the above said period.
2. Net Non-Performing Assets and Earnings of the banks have high degree positive correlation which shows the efficiency of the SBI & its Associates.
3. It is possible because of goodwill of the bank and a large number of customers of the banks, and who are continuously paying their interest on time. Otherwise relationship between the two factors should be negative.
4. PAT continuously increased except 2018 and 2019. In 2018 there is a negative return and in 2019 PAT is only 862 billion.
5. In 2018 as well as there is a negative PAT and NPA was highest on that year. So it is cleared that NPA has a negative impact on PAT of SBI.
6. The coefficient of correlation for SBI was found to be -0.51 that is moderate negative correlation between net profit and net NPA of the bank. This means that as NPA is increasing, the net profit will decrease.
7. The same picture is reflected on EPS also. In 2018 there is a negative EPS.
8. There is a negative relationship between NPA and EPS.

Conclusion

1. Actually comparison between the earning and NPA is not possible on the basis of trend or amount because NPA is the amount of loan and Earnings are the return received by the banks on the loans. In short NPA is a bad debt on which no return is received by the banks.
2. Continuously increase in the amount of NPA shows the inefficiency of the banks. And because of this inefficiency good customers are suffering.
3. Banks are unable to cut down the rate of interest for good customers who are paying their interest well on time because of NPAs.
4. Because of NPAs huge funds of banks are blocked due to which banks are unable to give further loans to new as well as to existing customers.
5. Increasing amount of NPA have adverse effect on Liquidity, Profitability and Solvency.
6. Banks have a wrong choice of clients which results in NPAs.

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