

Managing Assets Quality by Indian Commercial Banks in the Post Financial Crisis Period of 2008

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Abstract – Financial sector plays an important role for the development of any economy. They channelize the idle cash into a productive use. Credits are made available to the borrowers on the basis of some basic principles i.e. credibility, capacity and collateral securities. When bank ignores these principles and offered loan without credit risk rating, it is the case of sub-prime lending. Excessive use of innovative financial product with the greed to earn more profit lead to the economic crisis in 2008. Financial crisis works as a speed breaker in the process of economic growth. Due to subprime lending in 2008, NPAs started shooting up, leading to stacking of poor quality assets on bank's balance sheet. Stacking up of poor quality assets, due to subprime lending (NPAs) is the threat to banks survival. As, the financial stability of any bank depends upon assets quality on balance sheet. If NPA is less, bank would be in a sound financial position and vice-versa. However, Indian banking system is considered to be sound, well regulated, diversified and shock absorbing, even though due to globalization, Indian financial system was not immune to the financial crisis of 2008. As significant rise in NPAs could be observed on balance sheets of Indian banks. The NPA should be controlled and lessened, to enhance the profitability and efficiency of banks.

Key Words: Commercial Banks, Subprime Lending, NPA

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INTRODUCTION

Bank act as a catalyst in the development of the economy. It create its assets pout of liabilities i.e. demend deposits and term deposits. Bank channelizes fund from unproductive to productive uses. While channelizing or granting funds (loans) banks have to consider some basic principles of credit management credibility, capacity and collateral. If bank ignores these principles, NPAs will strt piling up. Bank's financial stability and NPAs are inverse in nature. Strong and viable banking system is essential for sustainable growth of economy. Thus it is essential that banks should not indulge in lending recklessly simply to achieve business volume. Quality of asset is much more important to the quantity of assets, particularly for banking business. Sub-prime crisis of 2008 is one of the latest example which proves that how holding of sub-prime assets by bank leading to financial crisis.

The turmoil in the financial market adversely affects the economic development. Sub-prime crisis originally taken place in U.S. but it affect all the nations adversely due to the globalization. Banks recklessly granted loans to the customers with the hope to earn more profit without keeping securities.

Which later turned into NPAs? Though Indian banking system is supposed to be strong and regulated, it was also not immune from such crisis.

OBJECTIVES:

In this backdrop the present paper aims to

- I. Analyze the asset quality of Indian commercial banks after the sub-prime crisis
- II. Impact of such crisis on assets quality and
- III. Conduct of comparative study between private and public sector banks in terms of assets quality during the period of study

LITERATURE REVIEW:

Anand (2009) applied ratios (Capital adequacy ratio, Net NPAs as a percentage of Net Advances, Return on assets) to evaluate the performance of all Scheduled Commercial Banks during the period 2005-06 to 2007-08. The study concluded that the

Indian Banking Industry is stable but growing at a slow pace.

Badola and Verma (2006) recognized high and low illustrative power indicators for public sector banks regarding profitability like NII, Provisions and Contingencies, In high indicators, net profit were there ,whereas NPAs, Business per employee, CD Ratio were there as the low explanatory power indicators. Most of the studies measuring efficiency concentrated mainly on cost, profit, and income or revenue efficiency. Most of the studies emphasise basically on income or revenue efficiency, cost and profit. Bhattacharya et al in 1997analyse the productive efficiency of Indian comer ub banks by using DEA technique and resulted that Indian public sector banks were among the best performing banks.

The matter is of utmost concern after the global financial crisis and the breakdown of few big institutions, According to empirical research, the asset quality is the most important factor of credit, in the Indian context along with time deposits and lending interest rate. (RBI, RCF, 2006-08). Immediately after the crisis the asset quality of developed economies was impaired, the same of Indian banks was highly maintained (RBI, AR, 2011-12).

In the period immediately following the global financial crisis, when asset quality of banks in most advanced and emerging economies was impaired, the asset quality of Indian banks was largely maintained (RBI, AR, 2011-12).

And if prices of the house are not associated with the fundamentals, they can make threats the economic and financial stability of the country majorly because of the macro-financial linkages, as empirical evidence demonstrates. Mainly financial crises was happened because of collapses in real estate prices, either commercial or residential or both (Reinhart and Rogoff, 2009).

The recent crisis can be mark as an example, wherein drop in the real estate prices led to a radical decline in securitized asset prices in 2007. Moreover, the unsteadiness which keep to impacted balance sheets of various financial institutions as was predicted by Feldstein (2007). The financial crisis then got carried forward to the real sector. The profitability of the operating banks tn the country is effected by the GDP of a country, whereas the asset quality of any bank is measured by the NPA/TA ratio and by OEXP/TA we examine expense management, which affects the bank’s performance adversely , Singh(2010).

GROWTH TREND OF ADVANCES AND NPAs

However public sector bank’s share is high in NPAs, the contribution of new private sector banks and

foreign banks in the total NPAs has increased in the post-crisis period.

Public sector banks on an average contributed nearly more than three fourth share of the total NPA (around 76%) in total gross advances, lined up by new private sector banks (approximately 13%), old private sector banks (approximately 6%) and foreign banks(over 5%).(chart 1) However, the contribution pattern in NPAs is different when viewed separately in the pre and post-crisis period. Public sector bank’s share falloff in total NPAs during the post crisis period (around 73%), in comparison to pre-crisis period (around 79%), likewise the old private sector bank contributed less NPAs during the post crisis period (around 4%) compared to pre-crisis period (around 7%).Though, foreign banks & new private sector bank’s share has risen considerably in the post-crisis period from 4% to 7% and 10% to 15% respectively (chart 2).

CHART 1: BANKS GROUP WISE SHARE IN TOTAL NPAs

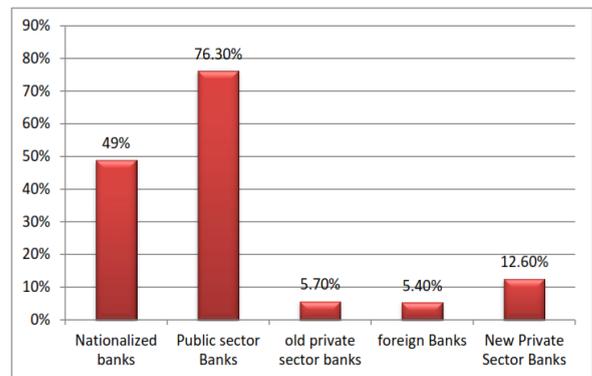
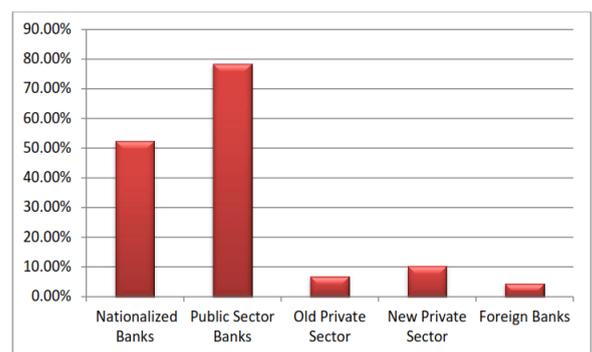
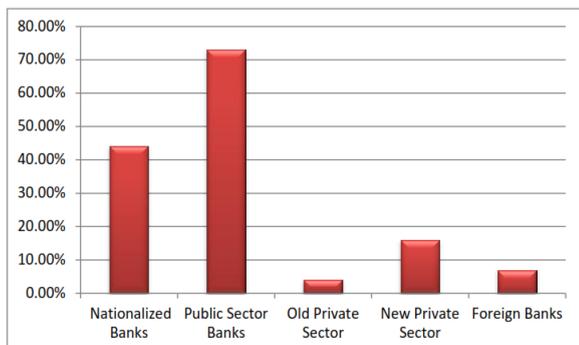


CHART 2: BANK GROUP-WISE SHARE IN TOTAL NPAs



PRE-CRISIS IN PERIOD (2001-2007)



POST CRISIS PERIOD (2008-2012)

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