



Impact of NPA'S on the earnings of SBI and its associates

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Abstract

Indian banking system has undergone a tremendous change since liberalization in the year 1991. State Bank of India and its Associates (now merged in SBI) are playing a very significant role in the Indian economy. State Bank of India is a bank having Associates and branches all over the world before merger. The main function of every bank is to accept deposits for the purpose of lending and earn profits with the help of this transaction. State Bank of India and its Associates are public banks and performing the same functions. Lending is main source of earning and lending constitutes customers which can be good and can be bad. Bad customers of a bank turn its assets into non performing assets. So in present research paper we will study the impact of Non Performing Assets on the earnings of the State of India and its Associate. We will use statistical tool like correlation in order to reveal the results. Data of 12 years i.e. March 2004-March 2015 is taken into consideration from the website of Reserve Bank of India. And results reveal that there is positive correlation between the two said factors.

Keywords: correlation, earnings, non performing assets, state bank of India and its associates

Introduction

State Bank of India and its Associates (now merged in SBI) are working at a very fast pace in the development of Indian economy having branches all over the world and SBI is acting as an agent of Reserve Bank of India. Accepting deposits and lending advances are the main function of the banks. State Bank of India is the conversion of Imperial Bank of India in 1955. And there after its associates are come into existence. These associates are State Bank of Patiala, State Bank of Bikaner and Jaipur, State Bank of Travancore, State Bank of Mysore, State Bank of Saurashtra, State Bank of Hyderabad and State Bank of Indore. Like another banks State Bank of India and its Associates are having huge amount of NPAs. And these NPAs are affecting the profitability of these banks. In this paper we will discuss the impact of NPAs on the earnings of State Bank of India and its Associates.

Litrature review

Narula, Sonia, Singla, Monika (2014) ^[1] has conducted the study on Punjab National Bank's Earnings and NPAs and concluded that there is positive relationship between the two factors having correlation 0.31. They concluded their results by saying that this can be possible because of the mismanagement of funds and wrong choice of clients by PNB. They concluded their research by saying that there are two categories of customers viz. good customers and bad customers. Good customers are those who pay interest on time and bad are those who convert bank's assets into bad debt. So banks should manage their funds properly and continuously monitor their cutomers.

Siraj. K. K & Dr. P. Sudarsanan Pillai (2013) ^[3] says that NPA is a virus affecting banking sector. It affects liquidity, profitability and solvency of the banks. The study concluded that NPA still remains a major threat and the incremental

component explained through additions to NPA poses a great question mark on efficiency of credit risk management of banks in India.

Srinivas, K.T. (2013) ^[4] concluded that the banks should not sanctioning loans to the non creditworthy borrowers by adopting certain measures. Banker should constantly monitor the borrowers in order to ensure that the amount sanctioned is utilized properly for the purpose to which it has been sanctioned. The banker should get both the formal and informal reports about the goodwill of the customer. If he had already proven as a defaulter then there is no question of sanctioning loan to him. It is the duty of the banker to educate the borrowers regarding the effects and consequences of defaulting. By considering all the above factors the banker can reduce the non-performing assets in a bank. The use of technology like Core Banking Solutions in Apex bank should make more reachable to all borrowers.

Pathak (2009) ^[2] explained that NPA is a serious danger to the Indian Economy, estimated around 9.8% of GDP at constant prices in 2005. His study detailed the list of banks whose NPA is more than their net worth which posed a significant question on the efficiency of credit risk management.

Objectives of the study

1. To study 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. 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 12 years i.e. March 2004-March 2015 will be covered in this study. Two factors namely, Non Performing Assets (NPAs) and Earnings will be covered where NPA will be independent factor and Earnings will be dependent factor. One thing is to be noted over here that we have two types of NPAs, 1) Gross NPAs & 2) Net NPAs. And here we will take into consideration the amount of Net NPAs. Thereafter we will see that whether changes in NPA will affect the earnings of the bank, if yes, then to what extent. 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.

Selected Factors	Symbols
Non Performing Assets	X
Earnings	Y

Analysis and discussion on results

To analyze the results, we will first check the Non Performing Assets of the State Bank of India and its Associates for the period March 2004-March 2015. Following table will show the figures related to NPAs.

(Amount in Billions)

Table 1: Showing Combined Statement of Net Non Performing Assets of State Bank of India and its Associates.

Years ending March	Amount of Net Non Performing Assets (X)
2004	59.6678
2005	63.6285
2006	60.7210
2007	63.5930
2008	85.0893
2009	107.4457
2010	125.6219
2011	147.906
2012	202.367
2013	281.009
2014	418.151
2015	372.777

Source: www.rbi.org.in

And now to analyze the results, we will check the Earnings (Profit & Loss) of the State Bank of India and its Associates for the period March 2004-March 2015. In order to calculate the earnings, the following formula is taken into considerations.

$$\text{Profit \& Loss} = \text{Interest Earned} + \text{Other Incomes} - \text{Interest Expended} - \text{Operating Expenses} - \text{Provisions \& Contingencies.}$$

Following table will show the figures related to Earnings. (Amount in Billions)

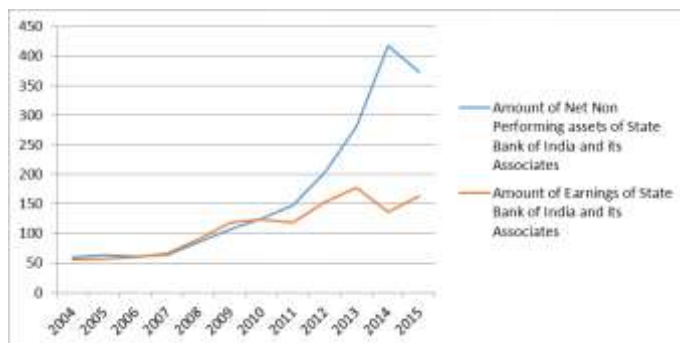
Table 2: Showing Combined Statement of Earnings of State Bank of India and its Associates.

Year s	Interest Earned	Other Incomes	Interest Expended	Operating Expenses	Provisions & Contingencies	Profits & Loss (Y)
2004	409.56	109.20	253.96	121.17	87.45	56.18
2005	440.52	94.80	248.42	134.12	96.03	56.75
2006	491.16	97.94	278.09	157.71	93.73	59.57
2007	534.65	94.19	326.06	159.86	77.20	65.72
2008	704.27	118.17	478.09	169.92	84.38	90.05
2009	891.96	160.72	617.71	200.86	115.15	118.96
2010	979.54	183.94	662.29	252.83	124.03	124.33
2011	1098.28	192.40	670.18	291.46	210.41	118.63
2012	1435.55	178.23	888.61	327.30	244.41	153.33
2013	1637.67	197.44	1065.33	370.94	221.01	177.83
2014	1841.72	227.075	1211.846	452.178	268.088	136.686
2015	2020.86	276.164	1327.700	486.989	319.319	163.018

Source: www.rbi.org.in

Check the trend with the help of diagram

Following diagram is clearly showing the trends of two factors. Amount of NPA is far more than the amount of Earnings. But we can't compare NPA with the Earnings because NPA is the amount of loan and earnings are returns (according to Rate of Interest charged by the banks).



Graph 1: Showing the Trend of Non Performing Assets and Earnings of State Bank of India and its Associates.

Above trend shows that amount of NPAs are continuously increasing except in the year 2006 and the amount of earnings is also continuously increasing except the years 2006, 2011 and 2014. With the help of this diagram we can clearly see the ups and downs of the situation faced by State Bank of India and its Associates.

Overall analysis of two factors of different years with the help of correlation

Table 2

Variables	Correlation Coefficient	Degree	Description
XY	0.7965	High Degree	+ve correlation

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. NPAs are those assets which do not produce earnings for the banks means banks are not getting interest on that loans. In that way earnings should be decreased. But in this study earnings are increased because of the efficiency of the bank in managing the funds. Good customers of the banks are paying interest on time, which compensate the loss of bad customers. Banks should try to minimize the NPAs as early as possible.

Findings

1. Amount of NPAs are continuously increasing except in the year 2006 and 2015. The amount of earnings is also continuously increasing except the years 2011 and 2014.
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 good customers of the banks, who are continuously paying their interest on time. Otherwise relationship between the two factors should be negative.
4. Graph 1 is showing the position and trend of two factors where amount of NPA is too high as compare to Earnings.
5. But comparison between the two factors 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.
6. Continuously increase in the amount of NPA shows the inefficiency of the banks. And because of this inefficiency good customers are suffering.
7. Banks are unable to cut down the rate of interest for good customers who are paying their interest well on time because of NPAs.
8. 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.
9. Increasing amount of NPA have adverse effect on Liquidity, Profitability and Solvency.
10. Banks have a wrong choice of clients which results in NPAs.

Suggestons

1. Banks should give its advances by making proper selection of a client. Financial position of a client should be regularly checked not only before but after sanctioning the loan.
2. Banks should try new and effective methods for managing their funds.
3. Banks should make full use of Asset Reconstruction Fund which takes bad debts of the banks at concessional rates.
4. Banks should encourage its customers by giving them proper discounts to those who continuously pay their interest without any default. This step will motivate the

defaulters.

Limitations of the study

Only secondary data is taken into consideration to reveal the results and out of various banks only State Bank of India and its Associates are selected.

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