TALK TO EXPERTS - 17

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Among many reasons for unduly lingering Highways projects in the country such as issues associated with land acquisition, departmental clearances, utility shifting, unexpected natural calamites, another most important reason is difficulty in getting additional debt for the stalled projects since the account in many cases would have been already classifed as NPA, that is, Non-Performing Assets.

We will look into this popular nightmare of the banks, the lenders.

What is NPA?

It simply means that the bank has not received the stipulated interest for the loan given for 90 days. The payment is overdue for more than 90 days. It clearly suggests that the principal also is likely not to be returned in time.

From the bank's point of view, the NPAs are classified under three categories: for administrative convenience: Substandard Assets, Doubtful Assets and Loss Assets.

An asset that has not fetched interest, that is, it has not performed, for a period less than or equal to 12 months is called Substandard Asset. If the asset has remained as NPA in the substandard category for a period of 12 months, it is called Doubtful Asserts. If the asset is considered uncollectible, it becomes Loss asset.

All these details of all the three kinds of NPAs are to be found in the books of the financial institutions, that is, the lending banks, here.

Why do banks shy away from the NPAs?

The presence of NPAs on the balance sheet of the banks has three distint negative impacts on the banks. First and foremost, an NPA cuts the cash flow of the bank, thereby reducing its earnings. As a consequence, the budget provision for subsequent loans becomes diminished; less lending of loans means less of revenue generation. And most devastating effect is it cuts into the very earnings of the bank in the sense that the loss from defaulted loans is written off against earnings. It means in effect, the bank takes the load of the interest payment and the capital. The hard work of the bank is denied its due recognition.

The bank, on its part, does not take the failure of payment of interest lying down; it takes efforts to recover loan within structured frame work. The first step it takes is it tries to restructure the loan to maintain cash flow so that the asset is not immediately classified as an NPA. Next, the defaulted loans are collateralized by assets of the borrowers; the bank can take possession of the collateralized assets and sell them off to cover losses, as much as possible, to the market value. It exercises due diligence when it thus collateralizes the borrower's assets.

A restructured asset or a loan generally gets an extended repayment schedule with some reduced intererst rate; the bank can also convert a part of the loan into equity, thus providing additional financing. In effect, a new loan is a bad loan in a new form and it is actually an NPA.

It must be pointed out here that the bank based on its experience with the recurring NPAs makes a bad loan provision in the budget. If the bank has been lending for years, it is estimable how much it can lend loan; say, for example, the bank has been lending for years annually a sum of Rs. 1000 crores; then, it sets aside as a bad debt provion about 10% of the total loan it used to provide, that is, 100 crores. This provision for bad debt comes useful when it is calculating the Net NPAs for the bank. The Net NPA is the total bad assets minus the bad debt provision.

When all is said and done, the government cannot allow the projects to linger endlessly. Of course, it cannot ask banks to keep lending on their own without any sanction from the Reserve Bank of India's regulation. Banks are governed by the RBI. Let us see in the next session how do the governments meet the crisis.