



# NPA's Impact on Financial Performance of Public Sector Banks

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**Abstract:** *The banking system in India is significantly different from that of other Asian nations because of the country's unique geographical, social, and economic character. India has a large population and land size, a diverse culture, and extreme disparities in income, which are marked among its region. The study is based upon secondary data retrieved from Report on Trend and Progress of banking in India, Websites, Journals and Articles. The scope of the study is limited to analysis of nonperforming assets of public sector banks covering the period of 2009-2013. For analyzing the data statistical tool such as t-test, and mean are used. The study observed reduction in NPA is necessary to improve profitability of banks.*

**Keywords:** *Non performing asset, Public sector banks,*

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## I. INTRODUCTION

Banking sector in Indian financial system occupies a predominant position. A big challenge facing Indian banks is how, under the current ownership structure, to attain operational efficiency suitable for modern financial intermediation. On the other hand, it has been relatively easy for the PSB's to recapitalize, given the increase in non-performing assets (NPA's) as the government dominant ownership structure has reduced the conflicts of interest that private banks would face. In 1991, a former governor of RBI, Mr. Narasimhan was appointed to review the present banking system and to suggest the ways to overcome the existing crisis. The main objective of Narasimhan committee was "Great emphasis on banking efficiency and better customer services". Since the nationalization of banks till first banking sector reforms (1991) the main thrust of the banks was on social banking where profitability was not considered as an important factor of their performance.

## II. REVIEW OF LITERATURE

**Review: 1 Ray R. and Patil D.Y. (2013)**, as per their research paper entitled on "Management of NPA in Banks: A comparative study of commercial & cooperative Banks with reference to selected Banks in Pune". Their research study based on the objective of comparative analysis of non-performing assets and its effect on profitability position of the bank and productivity of the bank. The findings of the study was presented in the form of thesis which comprises various chapters like: introduction, guidelines of NPA, present scenario of NPA, effect of NPA, reasons of NPA, management of NPA and conclusion and suggestions. They tested hypothesis that the occurrence of NPA affects the profitability and financial health of a Bank adversely.

**Review: 2 Ghosh.S and Ghosh.D (2011)** presented research paper on "Management of Non-Performing Assets in Public Sector Banks: Evidence from India" This study emphasizes on management of non-performing assets in the perspective of the public sector banks in India under strict asset classification norms, use of latest technological platform based on Core Banking Solution, recovery procedures and other bank specific indicators in the context of stringent regulatory framework of the Reserve Bank of India. As per researchers reduction of non-performing asset is necessary to improve profitability of banks and comply with the capital adequacy norms as per the Basel Accord.

**Review: 3 Paul.P, Bose.S.K, Rizwan.S.D (2011)** in their research paper entitled "Efficiency measurement of Indian Public Sector Banks: non-Performing Assets as Negative Output" attempt to measure the relationship of Indian PSU banks on overall financial performance. Here, NPA is a negative financial indicator.

**Review: 4** As per research paper "Empirical study of Non-Performing Assets Management of Indian Public Sectors Banks" by **Kanika Goyal (2010)** study is analytical in nature, and it is based on the secondary data retrieved from Report on Trend and Progress of Banking in India, Report on Currency and Finance etc. The scope of the study is limited to the analysis of NPAs of the public sector banks for the period 2002-03 to 2008-09. She examined trend of NPAs; quality of assets; health of several loan



assets; sector wise NPAs etc. Her study observed increase in gross as well as net NPAs in absolute terms and improved asset quality of banks.

**Review: 5 Uppal.R.K(2009)**” given paper on “Priority sector advances: Trends, issues and strategies” attempted to study the priority sector advances by the public, private and foreign bank groups. His study is based on the parameters like lending to priority sector by public, private sector and foreign bank groups, targets achieved by public, private sector and foreign bank group, NPAs (Non-performing assets) while lending to priority sector.

### III. RESEARCH METHODOLOGY

#### a. NEED AND OBJECTIVES OF THE STUDY

At the present the Indian banking structure consist of several banks such as commercial banks, co-operative banks etc. Indian banking sector has become more competitive due to the presence of new private sector banks and foreign banks. But in India, the public sector banks still dominate with all 85% market share in the total deposits and advances of the industry. The PSB are successfully meeting the challenges of its customers by providing services but biggest challenge before them is management of NPA. Therefore the object of study is:

- To analyze the financial performance of PSB’s in India.
- To understand the relationship between NPA, net profits and advances.

#### b. HYPOTHESIS

- Gross NPA and gross advance of public sectors banks are not significantly associated.
- Net NPA and net advance of public sectors banks are not significantly associated.

#### c. METHODOLOGY

The study is based on secondary data where a major portion of data is extracted from report on trend and progress of banking in India 2009-2013 and statistical tables relating to the banks in India as published by RBI for various years. Secondary data were also being collected from various books, journals, and websites.

Following five banks have been selected randomly as sample banks for study:

- STATE BANK OF INDIA
- BANK OF BARODA
- ALLAHABAD BANK
- INDIAN BANK
- PUNJAB NATIONAL BANK

### IV. ANALYSIS AND INTERPRETATION

In order to analyze the magnitude of NPA of each bank an attempt has been made to compare the mean value of NPA for universe and mean value for each individual sample bank for the period under study. Since the sample is small “t-test” has been administered with null hypothesis (H<sub>0</sub>) assuming that there is no significant difference between NPAs of each bank and the mean NPA of universe as a whole.

#### a. ANALYSIS OF GROSS AND NET NPA OF SELECTED PSB’S

TABLE-1

Gross Non-Performing Assets as percentage to Total Assets – sample banks

| Years          | 2009 | 2010 | 2011 | 2012 | 2013 | Mean  | df | Table value | ‘t’ value | Ho |
|----------------|------|------|------|------|------|-------|----|-------------|-----------|----|
| SBI            | 1.63 | 1.85 | 2.07 | 2.97 | 3.27 | 2.358 | 4  | 2.776       | 2.06      | A  |
| Bank of Baroda | 0.81 | 0.86 | 0.87 | 1.00 | 1.46 | 1     | 4  | 2.776       | 5.82      | R  |
| Indian bank    | 0.55 | 0.50 | 0.61 | 1.31 | 2.19 | 1.032 | 4  | 2.776       | 2.039     | A  |
| PNB            | 1.02 | 1.08 | 1.16 | 1.90 | 2.81 | 1.594 | 4  | 2.776       | 0.291     | A  |
| Allahabad bank | 0.72 | 1.00 | 1.10 | 1.12 | 2.51 | 1.29  | 4  | 2.776       | 1.178     | A  |
| Universe       | 1.2  | 1.95 | 1.4  | 1.89 | 2.03 | 1.694 | 4  | 2.776       |           |    |

**Source:** Report on trend and Progress of Indian Banks

**OBSERVATION FROM THE TABLE:**

The T values from above table shows that null hypothesis is rejected for Bank of Baroda as the calculated value of the ‘t’ for this bank is more than the table value (5.82>2.776). It means there is a significant difference between the mean value of gross NPAs as the percentage of total asset for this bank and the mean value of gross NPAs to total assets for the universe at 5% level of significance. The null hypothesis is accepted for other four banks viz. State bank of India, Indian Bank, Punjab National Bank and Allahabad Bank as the t-value calculated for them is less than the table value of ‘t’ at 5% level of significance. It means there is no significance difference between the mean value of gross NPAs as the percentage of total asset for these banks and the mean value of gross NPAs to total assets for the universe.

TABLE-2  
Net Non-Performing Assets as percentage to Total Assets – sample banks

| Years          | 2009 | 2010 | 2011 | 2012 | 2013 | Mean  | df | Table value | ‘t’ value | Ho |
|----------------|------|------|------|------|------|-------|----|-------------|-----------|----|
| SBI            | 1.00 | 1.03 | 1.01 | 1.18 | 1.41 | 1.126 | 4  | 2.776       | 5.427     | R  |
| Bank of Baroda | 0.20 | 0.21 | 0.22 | 0.34 | 0.76 | 0.346 | 4  | 2.776       | 3.34      | R  |
| Indian bank    | 0.11 | 0.14 | 0.33 | 0.84 | 1.46 | 0.576 | 4  | 2.776       | 0.491     | A  |
| PNB            | 0.17 | 0.33 | 0.54 | 0.97 | 1.51 | 0.704 | 4  | 2.776       | 0.01      | A  |
| Allahabad bank | 0.43 | 0.39 | 0.48 | 0.6  | 2.02 | 0.784 | 4  | 2.776       | 0.264     | A  |
| Universe       | 0.6  | 0.6  | 0.6  | 0.8  | 0.91 | 0.702 | 4  | 2.776       |           |    |

Source: Report on trend and Progress of Indian Banks

**OBSERVATION FROM THE TABLE:**

The T values from above table observed that null hypothesis is rejected for SBI and Bank of Baroda as the calculated t-value for these banks are more than table value of ‘t’ at 5% level of significance. For other three banks i.e. PNB, Indian Bank and Allahabad bank null hypothesis is accepted as the calculated value of ‘t’ is less than the table value of ‘t’. It means that there is no significant difference between the mean value of Net NPAs as the percentage of total asset for these three banks and the mean value of Net NPAs to total assets for the universe i.e. Public Sector Banks in India at 5% level of significance.

TABLE-3  
Gross Non-Performing Assets as percentage to Total Advances – sample banks

| Years          | 2009 | 2010 | 2011 | 2012 | 2013 | Mean  | df | Table value | ‘t’ value | Ho |
|----------------|------|------|------|------|------|-------|----|-------------|-----------|----|
| SBI            | 2.84 | 3.05 | 3.28 | 4.44 | 4.75 | 3.672 | 4  | 2.776       | 2.7       | A  |
| Bank of Baroda | 0.87 | 1.27 | 1.36 | 1.53 | 2.40 | 1.486 | 4  | 2.776       | 4.53      | R  |
| Indian bank    | 0.82 | 0.81 | 0.98 | 2.03 | 3.33 | 1.594 | 4  | 2.776       | 2.12      | A  |
| PNB            | 1.60 | 1.71 | 1.79 | 2.93 | 4.27 | 2.46  | 4  | 2.776       | 0.33      | A  |
| Allahabad bank | 1.81 | 1.69 | 1.74 | 1.83 | 3.92 | 2.198 | 4  | 2.776       | 1.01      | A  |
| Universe       | 1.97 | 2.19 | 2.3  | 3.1  | 3.6  | 2.632 | 4  | 2.776       |           |    |

Source: Report on trend and Progress of Indian Banks

**OBSERVATION FROM THE TABLE:**

The T value from above table shows that null hypothesis is accepted for all the banks except Bank of Baroda as the calculated ‘t’ value for the bank is more than the table value of ‘t’ (4.53>2.776). It means there is no significant difference between the mean values of gross NPAs as the percentage of total advances. While null hypothesis can be accepted for all the banks as the calculated ‘t’ value for the banks is less than the table value of ‘t’, it mean there is significance difference between the mean value of gross NPAs as the percentage of total advances for all the sample banks and the mean value of gross NPAs to total advances for the universe i.e. Public Sector Banks in India at 5% level of significance.

TABLE-4  
Net Non-Performing Assets as percentage to Total Advances – sample banks

| Years          | 2009 | 2010 | 2011 | 2012 | 2013 | Mean  | df | Table value | ‘t’ value | Ho |
|----------------|------|------|------|------|------|-------|----|-------------|-----------|----|
| SBI            | 1.79 | 1.72 | 1.63 | 1.82 | 2.10 | 1.812 | 4  | 2.776       | 7.13      | R  |
| Bank of Baroda | 0.31 | 0.34 | 0.35 | 0.54 | 1.28 | 0.564 | 4  | 2.776       | 3.73      | R  |
| Indian bank    | 0.18 | 0.23 | 0.53 | 1.33 | 2.26 | 0.906 | 4  | 2.776       | 0.86      | A  |
| PNB            | 0.17 | 0.53 | 0.85 | 1.52 | 2.35 | 1.084 | 4  | 2.776       | 0.42      | A  |
| Allahabad bank | 0.72 | 0.66 | 0.79 | 0.98 | 3.19 | 1.268 | 4  | 2.776       | 0.02      | A  |
| Universe       | 0.94 | 1.10 | 1.1  | 1.4  | 1.7  | 1.248 | 4  | 2.776       |           |    |

Source: Report on trend and Progress of Indian Banks

**OBSERVATION FROM THE TABLE:**

The above table shows that null hypothesis is accepted for three banks i.e. Indian Bank, PNB and Allahabad Bank as the calculated value of 't' for these banks is less than the table value of 't' (0.86, 0.42, 0.02 and < 2.776). It means there is no significant difference between the mean value of Net NPAs as the percentage of total assets for these banks and the mean value of Net NPAs to total assets for the universe i.e. Public Sector Banks in India at 5% level of significance.

The null hypothesis is rejected for two bank viz. SBI and Bank of Baroda as the value of 't' (7.13 and 3.73 > 2.776) is more than the table value of 't'. It means there is a significant difference between the mean value of Net NPAs as the percentage of total assets for these banks and the mean value of Net NPAs to total assets for the universe.

**V. IMPACT OF NON-PERFORMING ASSETS****a. IMPACT ON ECONOMY AND BUDGET ALLOCATION OF THE GOVERNMENT**

In 1998, Narasimham committee recommended that the capital adequacy ratio of banks should be increased. Public sector banks should be urging to access the market for the capital. It shows the importance of capital adequacy ratio and its burden on budget resources to overcome the problem created by NPAs and bad debts written-off.

**b. IMPACT ON DEPOSITORS**

Depositors are the main liabilities and lending resources of a bank. It has been the history of the past whenever a banks fail, depositors bears the burnt up to the maximum. Therefore depositors are more concerned about NPAs of a bank. Though the deposits of the banks are insured by DIGCI but the insurance cover is partly up to a certain limit.

**c. IMPACT ON SHAREHOLDERS**

In view of non-recognition of interest income and profit sharing on NPAs, earning per share will decline and value per share will fall in the market. So, NPA will result in the impairments of assets thereby resulting in the direct loss to shareholders.

**d. IMPACT ON STANDARD BORROWERS**

Standards borrowers contribute towards the interest income and profits of the bank. NPAs result in low interest income which is partly compensated by charging higher standard rate with standard borrowers.

**e. IMPACT ON BANK IMAGE AND BANKING DEVELOPMENT**

Everyone wants to raise reputation in the market for gaining confidence and faith of the public. For building goodwill bank provide some facilities which bear some extra cost all this is result to increase NPA directly or indirectly. High NPA affect the profitability of bank and its image building.

**VI. CONCLUSION**

Our study shows impact of NPAs upon banks erodes current profit through provisioning requirements which result in reducing the interest income and profit. Above the five banks SBI and Bank of Baroda suffer highly from NPA which adversely affect their accretion of capital and shows that country has a weak payment culture and legal system that often result in low recoveries and delayed settlement of foreclosures. According to the Reserve Bank of India, deterioration in economic activities, net non-performing assets (NPA) of all banks have increased to 1.68 percent of the total loan at the end of 2012-13. Therefore, the government must bring in capital infusion plans for the bank so that they can fulfill the BASEL-3 norms and reduce the current crisis at some extend.

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