Issue of NPA and its resolution

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What is NPA?

- A non-performing asset (NPA) is a loan or advance for which the principal or interest payment remained overdue for a specified period of time.

Types of NPAs?

- **How serious is the problem?**

- More than Rs. 7 lakh crore worth loans are classified as Non-Performing Loans in India. This is a huge amount.
- The figure roughly translates to near 10% of all loans given.
- This means that about 10% of loans are never paid back, resulting in a substantial loss of money to the banks.
- When restructured and unrecognized assets are added the total stress would be 15-20% of total loans.

Reasons for NPA?

- **Economic Slowdown:** Economic growth slowing down & rate of interest going up sharply, corporates have been finding it difficult to repay loans, and it adds up to rising NPA.
- **Wait and watch approach:** Banks allow deteriorating asset class to go from bad to worse in the hope of a revival and often offer restructuring options to corporate.
- Fear of 3Cs-Courts, CBI and CAG

- **The poor credit assessment process**
    - Operational factors: Ordinary people often complain about the difficulty in getting loans, while some large borrowers just get loans on a platter.
    - The project not completed in time
    - Failure of business
    - Willful defaulters
    - Natural calamities
    - Diversion of funds
- The origins of India's NPA problem lie not in the events of the past few years, but much further back in time, in decisions taken during the mid-2000s.
- During that period, economies all over the world were booming with India's GDP growth surging to 9-10 per cent per annum. For the first time in the country's history, everything was going right: corporate profitability was amongst the highest in the world, encouraging firms to hire labour aggressively, which in turn sent wages soaring. Firms made plans accordingly.
- They launched new projects worth lakhs of crores, particularly in infrastructure-related areas such as power generation, steel, and telecoms, setting off the biggest investment boom in the country's history.
- This investment was financed by an astonishing credit boom which was the largest in the nation's history.But just as companies were taking on more risk, things started to go wrong. **Cost of the firms** soared far above their budgeted levels, as **securing land** and **environmental clearances** proved much more difficult and time-consuming than expected (in the last three years of UPA-II, a lot of project clearances and land acquisition were blocked).
- At the same time, forecast revenues of the firm collapsed after the **Global Financial Crisis**; projects that had been built around the assumption that growth would continue at double-digit levels were suddenly

- confronted with growth rates half that level.
- As if these problems were not enough, borrowing costs increased sharply. Firms that borrowed domestically suffered when **RBI increased interest rates to tackle double-digit inflation.**

Sashakt Plan

Sunil Mehta Panel Recommendations

The panel under the chairmanship of PNB non-executive chairman Sunil Mehta has recommended a five-pronged

approach in Project "Sashakt" consisting of the following:

- **SME resolution** approach for dealing with bad loans up to Rs 50 crore, involving the creation of a steering committee by banks for formulating and validating the schemes, with a provision for additional funds.
- **Inter-creditor agreement:** Bank-led resolution approach for loans between ₹50 crore and Rs. 500 crore, with the resolution being achieved in 180 days.
- **Asset Management Company (AMC)/Alternative Investment Fund** (AIF) led resolution approach to deal with NPA cases of more than Rs 500 crore. Alternative Investment Fund will raise resources from banks and institutional investors so that it can bid for the insolvent assets under insolvency and bankruptcy.
- **National Company Law Tribunal (NCLT)/IBC approach** for assets larger than Rs 500 crore already before the NCLT and any other assets whose resolution is still pending.
- **Asset-trading platform** for both performing and non-performing assets.

Inter Creditor Agreement:

- The inter-credit agreement is aimed at the resolution of loan accounts with a size of ₹50 crores and above that are under the control of a group of lenders.
- It is part of the "Sashakt " plan approved by the government to address the problem of resolving bad loans.
- Over the last few years, Indian banks have been forced by the Reserve Bank of India to recognise troubled assets in their books, but their resolution has remained a challenge.
- According to banker Sunil Mehta, who headed a panel that recommended the plan, disagreement between joint lenders is the biggest problem in resolving stressed assets.
- The government hopes that the holdout problem, where the objections of a few lenders prevent a settlement between the majority lenders, will be solved through the intercreditor agreement.
- As per the terms of the agreement, if 66% of the lenders agree to a resolution plan it would be binding on all lenders. A dissenting creditor could sell its loan at a discount of 15% of the liquidation value to other lenders or buy the entire loan at 125% of the resolution plan agreed to by other lenders. Another option with a dissenting creditor is to sell their loans to any person at a price mutually arrived between the dissenting lender and the buyer. In case there is no resolution in 180 days, the stressed asset will be referred to the National Company Law Tribunal (through IBC).