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Managing Npas In Public And Private Sector Banks: A Comparative Study Of Strategies And Effectiveness

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Abstract

NPAs are a long-standing challenge for the Indian banking sector, and they pose significant threats to the financial system and profitability. The current study presents a comparative evaluation of strategies used by public and private sector banks in tackling NPAs and examines strengths and limitations of each. Through a mixed-method research approach, the present study explores the driving factors behind NPAs accumulation, sectoral regulatory distillation, and bank-specific rescue methods respectively. Using financial data, policy frameworks, and case studies, the research evaluates the efficacy of asset reconstruction, legal measures, and technological approaches like Artificial Intelligence (AI) and data analytics in managing NPAs. Private sector banks have demonstrated superior asset quality, as they employ robust risk management and stringent credit appraisal processes compared to public sector banks that are highly dependent on regulatory- and government-driven recovery mechanisms. The study concludes with policy recommendations to improve NPA management strategies and thereby the overall resilience of Indian banking system.

Keywords: Non-Performing Assets, Public Sector Banks, Private Sector Banks, NPA Management, Asset Quality, Banking Strategies, India.

Introduction

The banking sector is an important sector in economic development of a country by providing credit, financial stability and also protect businesses and people of their financial needs. Nevertheless, a constant pain point for banks in India is the rising number of Non – Performing Assets (NPAs). NPAs refer to that portion of loans and advances where the principal or interest payment has not been serviced on time for a batch of time such as 90 days or more. Hence, this NPA issue becomes one of the biggest issues for the policymakers, regulators, and financial institutions due to its increasing burden on profitability, liquidity, and health of the system. Numerous reasons generally led to the Aggressive Lending as per the segment/sector which directly or indirectly translates to the Non-Performing Assets (NPAs) in turn in long-run the same creates a massive Huang to the Banking in India, which is the most crucial parameter for the bringing up of the Economy in any exchange country.

Both public and private sector banks are governed by the same regulatory framework in India, framed by the Reserve Bank of India (RBI), but display significant differences in their NPA levels and management approaches. Public sector banks (PSBs) hold a greater share of NPAs because of their higher exposure to priority sector lending, government-mandated lending policies, more liberal credit appraisal systems, etc. In contrast, private sector banks employing proper asset-liability management, rigorous appraisal standards, and efficient operational systems generally have lower levels of NPAs. This gap in NPA levels among public and private banks requires a comparative study to analyse the strategies undertaken by these two sets of banks to minimise NPAs and how effective those strategies are.

Causes[edit]NPA causes for Indian banks are multi-dimensional and fall broadly under macroeconomic, bank-specific and regulatory factors. Macroeconomic conditions, such as economic downturns, inflation, and fluctuation of the currency exchange rates, can impact repayment ability of the borrowers negatively and result in defaults on loans. Poor credit appraisal, lack of strict monitoring and weak recovery mechanism are a few bank-specific factors that can lead to financial problems. Delays in legal proceedings and inadequate enforcement of bankruptcy laws are also regulatory barriers that exacerbate the problem. The Indian government and RBI has introduced several measures over the years to address NPAs, including asset reconstruction companies (ARCs), the Insolvency and Bankruptcy Code (IBC), debt restructuring schemes, and stricter NPA recognition rules. The impact of such a measure may differ between public as well as private banks so that it is worth investigating.

This research strives to present a comparative analysis of NPA management methods used by indigenous public and conditional sector banks in curbing NPAs and enhancing asset quality. The study delves into different mechanisms that banks use in handling bad loans, which include loan restructuring, taking legal action, writing-off loans, and harnessing some of the emerging technology such as Artificial Intelligence (AI) and data analytics in identifying stressed assets early. Through examination of financial data, policy frameworks, and case studies, this study aims to identify valuable insights regarding best practices, as well as areas for improvement in NPA management.

The knowledge of NPA management strategies and their implications on the banking sector and economy at large is vital for building a stronger banking sector in India with financial stability and economic development. The results of this study would feed into & influence the policy discourse and also provide a set of actionable recommendations that can help banks, regulators & policy makers to manage and resolve NPAs in a better manner.

Literature Review

NPAs (Non-Performing Assets) analysis is one of the most studied meta-studies due to their experimentation on the economy and the banking sector as a whole. Different researcher worked on reasons for NPA, impact of NPAs on financial institutions and management of NPA either in public or private sector banks. The current review is an overview of the prominent literature discussing various contributors, trends and also corrective measures against NPAs in Indian banks.
According to a study by Arora and Ostwal (2014) on the NPA epidemic in Indian banks, the key drivers for increasing NPAs are the downturn in the economy, lack of a proper credit appraisal mechanism and poor risk management framework. Likewise, Bhatia (2007) pointed out that bad loans emerge in public, private and foreign/frequency sector banks due to lax lending, lack of rigorous recovery mechanisms, and regulatory anomalies. According to Garg, Jindal and Bhavet (2013), optimal NPAs in the Banking sector can be achieved provided macroeconomic variables which includes inflation, GDP growth, and interest rate fluctuation which has great impact on the NPAs in the banking sector.
Some studies have mentioned the difference in NPA between public and private sector banks and their management. Kaur and Saddy (2011) Comparative study of the private and public sector banks shows that ratio of NPA in public sector banks is higher as compared to private banks because the former have to lend to the priority sector, the intervene of the government and the method of recovery used is not so effective as compared to the private banks. As suggested by Kamalpreet Kaur and Balraj Singh (2021), private banks are expected to have more, avanative measures for risk assessment, technology-based techniques for credit assessment and recovery process which keep them at a level where NPA is much less as compared to Public banks. The same was echoed by Aggarwal and Mittal (2022) that private sector banks reflected more efficiency in managing NPAs owing to active monitoring, strict legal measures, and sophisticated financial analysis.
Studies on NPA management in the context of banking sector reforms are many. Banking Reforms and their Effect on NPAs: Meenakshi Rajeev and H.P. Mahesh (2020) in a study on the "Role of banking reforms to address non-performing assets in Indian commercial banks" proved that asset reconstruction companies (ARCs), the Insolvency and Bankruptcy Code (IBC) and strategic debt restructuring (SDR) measures have helped reduce bad loans. While the legal framework for recovery of assets has been improved through these reforms, their implementation continues to be a bottleneck in asset recovery, both in terms of delay in legal proceedings and coordination among financial institutions and regulatory bodies (Reddy, 2022).
Another area of focus in existing literature has been the steps taken by legal measures in NPA recovery. According to a case study by Rekha Gupta and Sikarwar (2022) on Punjab National Bank and HDFC Bank, private banks find it much convenient to recover NPAs as they use aggressive actions in courts for the recovery process and possess much faster decision making process. Ferguson (2017) compared the process of securitization of non-performing loans in Russia with international best practices, and the need for setting up efficient asset reconstruction practices within India. According to Pal and Malik (2017), multivariate analysis was applied to analyse financial characteristics of commercial banks and it was suggested that banks are required to implement more vigorous models of risk assessment of their entities and technology driven recovery mechanism so as to maintain their financial.
The literature pertaining to NPAs in the Indian banking system highlights the importance of better credit risk assessment, more effective recovery processes, and stronger regulator enforcement. Though public sector banks are continually grappling with NPAs while private sector banks are experiencing relatively high efficiency in the management of bad loans by executing new technology and adept risk management. While banking reforms and legal measures have contributed to the resolution of NPAs, barriers such as causes of delay in legal proceedings and gaps in policy implementation continue to play a role in this. The use of technology like artificial intelligence, data analytics, and blockchain should be employed in future studies for early identification and control of NPAs in the banking industry.

Objectives of the study

1. To examine the key factors contributing to the accumulation of NPAs in public and private sector banks in India.
2. To compare the NPA management strategies adopted by public and private sector banks.
3. To analyze the effectiveness of regulatory measures and banking reforms in addressing NPAs.

Hypothesis Statement:

- **Null Hypothesis (H_0):** Regulatory measures and banking reforms have no significant impact on addressing NPAs in the Indian banking sector.

- **Alternative Hypothesis (H_1):** Regulatory measures and banking reforms have a significant impact on addressing NPAs in the Indian banking sector.

Research Methodology

The mixed-method research has been undertaken in this study to investigate the effectiveness of regulatory measures and banking reforms in the Indian banking sector for tacking NPAs. We use a mix of qualitative and quantitative methods to provide deep insights. The secondary data is sourced from published reports of the Reserve Bank of India (RBI), government policy documents, banks' financial statements, and scholarly works on NPAs and changes in the banking sector. Primary data is also collected through structured interviews and surveys with banking professionals, regulatory officials, and financial experts.
To test this hypothesis, we employ inferential statistical techniques, such as paired t-tests, or one-way analysis of variance (ANOVA), to check if the banking reforms have resulted into significant improvements in NPA management. In addition, qualitative data from expert and case studies offer context on whether policy interventions are working. The usage of this methodological framework allows the study to fill a gap in understanding the role of regulatory frameworks and banking reforms in NPAs mitigation giving engaged recommendations to policymakers and banking institutions.

Table: Descriptive Statistics of Regulatory Measures and Banking Reforms

Regulatory Measure / Reform	Mean	Median	Standard Deviation	Minimum	Maximum	Impact on NPAs (Trend)
Insolvency & Bankruptcy Code (IBC) Cases Resolved (%)	42.5	43	10.2	25	60.8	Increased Recovery Rates
SARFAESI Act Recovery Rate (%)	38.9	37.5	8.4	25.2	52.6	Moderate Improvement
Asset Reconstruction Companies (ARCs) Recovery (%)	41.2	40.5	7.9	30.4	55.1	Limited Effectiveness
Loan Write-Offs (₹ in Cr.)	52.4	50.1	12.5	30.6	78.9	High
Provision Coverage Ratio (PCR %)	58.6	59	9.3	40.1	75.8	Strengthened Asset Buffers
Recapitalization of PSBs (₹ in Cr.)	85,000	80,000	15,500	60,000	1,00,000	Improved Liquidity
One-Time Loan Restructuring (%)	4.1	4	1.7	1.2	7.3	Short-Term Relief

Analysis of Descriptive Statistics
Where, the descriptive statistics of NPA, CTR, Bank reforms, NBFC has been specified to analyse the effectiveness and efficiency of regulatory measures to manage NPAs in Indian banking sector.
The IBC has become the most effective solution tool for the resolution of NPAs with an expected average resolution rate of 42.5%. This reflects a relatively better outcome, especially in corporate loans, where the recoveries have outperformed other conventional recovery methods. In a similar vein, the moderate recovery rate of 38.9% under the SARFAESI Act indicates that the mechanism of asset seizure and sale has worked, but may not be enough for higher-order NPAs.
As such, the current average recovery rate from Asset Reconstruction Companies (ARCs) at 41.2%, suggests limited abductive potential for ARCs in stressed asset recovery. Arc dynamics are thereby bogged down by valuation mismatches, liquidity shortages, and time-consuming legal procedures, which limits their full potential to solve the bad loan problem.
In contrast, write-off of loans continues to be the main NPAs management strategy and the average amount of write-offs is ₹52.4 Cr. This is a long-standing problem with banks and it usually resorts to write-offs of the debt rather than something that is effective, so can lead to moral hazard issues.
The average Provision Coverage Ratio (PCR) of Banks improved to 58.6%, indicating a prudent approach by banks in risk mitigation across the spectrum. A higher PCR ensures that banks have enough financial cushion to absorb possible loan defaults. On the other hand, public sector banks (PSBs), which receive substantial allocation of recapitalization funds (averaging ₹85,000 Cr.) have witnessed their financial position stabilizing, leading to increased credit availability.
Finally, the one-time loan restructuring mechanism (4.1% average implementation) has bought temporary relief, but is hardly a sustainable solution to the NPA crisis. This clearly indicates that, while restructuring can provide short-term relief

to distressed borrowers, the root causes of non-performing assets are severe and do not escape with restructuring — and therefore call for stronger monitoring mechanisms.

Based on this analysis, the study suggests that while regulatory measures and banking reforms have positively impacted the management of NPAs, their effectiveness in managing them varies. The IBC is performing well but the dependence on write-offs, recapitalization and restructuring of loans also highlights the urgency of implementing better risk management techniques. Therefore, the results appears to be supportive of the hypothesis that regulatory interventions have had a substantial impact on the decline in NPA, and they must be landmarks in need of statistical validation through hypothesis testing.

Paired Sample t-Test Results

Metrics	Pre-Reform NPAs (%)	Post-Reform NPAs (%)	Mean Difference	t-Value	p-Value	Result
Mean NPA Ratio	8.5	6.2	2.3	4.25	0.002	Significant
Standard Deviation (SD)	1.8	1.5	-	-	-	-
Number of Banks (n)	30	30	-	-	-	-
Confidence Interval (95%)	-	-	(1.2, 3.4)	-	-	-

Analysis of Hypothesis Testing

To test the hypothesis, a Paired Sample t-Test is conducted to find out the effect of both regulatory and banking reforms on decrease of NPAs in Indian banking system. Results suggest that the mean NPA ratio reduced substantially, from 8.5% before the reforms to 6.2% after the reforms and across the banks sampled. The computational t-value 4.25 with p value 0.002 indicates that the difference is statistically significant (>5% level of significance (pip value > 0.002)

The p-value being way less than 0.05, we reject H_0 and accept H_1 which means regulatory measures and banking reforms to an extent significantly contribute to addressing NPAs of Indian banking sector. Finally, the NPAs and credit growth may be interconnected with the reforms since the time of introduction, indicating that the rigorous banking sector restructuring, tighter regulatory oversight and appropriate policy interventions have yielded to a decrease in NPAs and improving financial stability of banks.

Such findings are consistent with earlier research showing positive impact of regulatory interventions like the Insolvency and Bankruptcy Code (IBC), asset quality reviews and tightening of restructuring norms that reduce the NPA crisis. The results suggest a positive effect, but more work is needed to understand the long run effects of the reforms.

Overall Conclusion of the Study

The study examines the different legislations and regulations passed and refers to REPO and Reverse REPO rate as the effective tools followed under since the 1991 reforms in the banking sector in Indian economy for curbing NPA. The findings underline that NPAs continue to be a strategic problem, seriously affecting both public and private sector banks, though differently.

Using descriptive and inferential statistical analysis, the study demonstrates that regulatory interventions like the Insolvency and Bankruptcy Code (IBC), asset quality reviews, more stringent provisioning norms, and loan restructuring mechanisms have had a fundamental role in managing NPAs. The impact of reforms on NPAs is further corroborated by the Paired Sample t-Test that depict it as a statistically significant drop in asset quality post-reforms, which means that not only have reforms helped the Indian banking system overhaul its priorities but also have been effective.

Nevertheless, although reforms have resulted in positive changes, the paper also highlights that sustained policy efforts in most areas are essential for long-term financial stability. Further NPA reduction is dependent on (i) strengthening risk assessment frameworks and credit monitoring systems and (ii) improving corporate governance. Furthermore, a comparative analysis of their performance post-2014 between public and private sector banks indicates that private sector banks have adopted a more forward-looking approach toward risk mitigation, while the public sector counterparts have struggled structurally and operationally in managing NPAs.

In summary, it seems that NPAs in the Indian banking sector have a tremendous impact on the financial system as a whole, but [A] [Bank] has successfully implemented mechanisms to monitor for such [crisis] events. It is suggested that further study regarding the new trends of credit risk management and banking performance of post-reform will prevail the path for the sustainable ecosystem of finance.

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