

Efficiency of Recovery Channels in NPA Management: A Study of Banking Sector

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Abstract- *The Indian banking industry is the backbone of the nation's financial system and is essential to the efficient running of the economy. Even with the efforts to improve the banking industry's performance, Non-Performing Assets (NPA) continue to be a major obstacle. In response, the government has put in place a number of initiatives to reduce the stress caused by non-performing assets (NPAs), with a particular emphasis on NPA recovery channels. These channels—Lok Adalat, SARFAESI Act, Debt Recovery Tribunals (DRTs), and Insolvency and Bankruptcy Code (IBC)—are essential parts of the structure for recovery. In order to determine the relationship between NPAs and recovery methods in terms of the amounts collected compared to those involved in the schemes, the current study will analyse the amounts collected from each channel in an effort to clarify the effectiveness of these recovery channels. The study covers thirteen years, from 2009 to 2023, using secondary data that was obtained from multiple repositories. In addition to offering insightful perspectives to the continuing efforts to address NPA difficulties in the banking industry, this thorough analysis aims to shed light on the dynamics of NPA recovery channels.*

Indexed Terms- *Non-Performing Asset (NPA), Lok Adalat, DRT, SARFAESI ACT, IBC.*

I. INTRODUCTION

The banking sector holds a pivotal role in Indian financial system, plays an important role in smooth operation of countries economy. The primary source of income axis is from credit creation, where loans were disbursed to borrowers, through which banks earns interest on the loan with principal. These funds are again recycled to raise additional resources. Lending activities occur through direct or indirect means in financial markets, significantly contributing

to the maintenance of financial stability. But these lending operations of the Indian banks are subject to regulation of banking and other relevant acts (Moazzam & Singh, 2022). Despite concerted efforts to enhance performance, numerous banks in India continue to grapple with the challenge of Non-Performing Assets (NPAs). NPAs function as a financial indicator, reflecting the health of the banking sector.

According to the Reserve Bank of India's November 2018 report, the total value of poor-quality loans exceeded Rs 9 lakh crores, underscoring the substantial impact on banks' lending practices and liquidity positions. Addressing the NPA issue is imperative for banks to enhance their financial health, fortify their lending capabilities, and reinforce the stability of the overall banking system.

So, the aim of the present study is to know the monetary NPA involvement by the schedule Commercial Banks and whether there is any improvement in amount involved versus amount recovered by various recovery channels. Study is divided in to three sections. *Section A* provides the overview about NPA and various recovery channels. *Section B* describes the Literature study, Methodology and objective formulation followed by Hypothesis. *Section C* involves data analysis and interpretation with findings and suggestion.

II. WHAT IS NON-PERFORMING ASSET?

A Non-Performing Asset (NPA) denotes a loan or advance extended by a bank or financial institution that has ceased to generate interest or principal repayments for a specified period, typically when a

borrower fails to make scheduled payments for at least 90 days. The presence of NPAs on a bank's balance sheet reflects potential losses for the lender, posing a risk to the financial health and stability of the institution.

Key points regarding NPAs include:

- **Recording on Balance Sheet:** NPAs are recorded on a bank's balance sheet after a prolonged period of non-payment by the borrower.
- **Financial Burden:** NPAs impose a financial burden on the lender, and a substantial number of NPAs over time may signal to regulators that the bank's financial fitness is in jeopardy.
- **Classification:** NPAs can be classified based on the length of time overdue and the probability of repayment, with categories such as substandard asset, doubtful asset, or loss asset.
- **Recovery Options:** Lenders have various options to recover their losses, including taking possession of collateral or selling the loan at a significant discount to a collection agency.

Recovery Mechanisms

A. *Lok Adalats:*

Lok Adalat, established by the government under the Legal Services Authorities Act of 1987, serves as a forum for the resolution of disputes, including those related to Non-Performing Assets (NPAs). Operating outside the traditional court system, Lok Adalat handles both pending and pre-litigation cases. With the authority to settle NPA cases involving amounts up to 20 Lakhs, this alternative dispute resolution mechanism promotes quicker resolution and reduces litigation costs.

B. *Debt Recovery Tribunals (DRTs):*

Debt Recovery Tribunals (DRTs) were instituted under the Recovery of Debts Due to Banks and Financial Institutions Act, 1993. These specialized tribunals aim to facilitate the swift recovery of loans, particularly in cases of NPAs where the debt exceeds ₹20 lakhs. DRTs provide a legal platform for banks to initiate recovery proceedings, with a focus on timely resolution and the collection of outstanding dues.

C. *SARFAESI Act:*

The Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act, 2002, was introduced by the Government of India to expedite the recovery of defaulted loans, thereby alleviating the burden of NPAs on banks. Applicable in cases where the security interest is valued at more than ₹1 lakh and the amount due exceeds 20% of the principal amount, the SARFAESI Act empowers banks to take possession of and sell secured assets without court intervention, facilitating the timely recovery of outstanding dues.

D. *Insolvency and Bankruptcy Code (IBC):*

IBC Enacted in 2016, the Insolvency and Bankruptcy Code (IBC) addresses insolvency and bankruptcy cases in India. The IBC mandates the resolution of cases within 180 days from registration. Individuals or partnership firms can file for insolvency if their default loan amount is a minimum of ₹1,000, while for corporates, the minimum threshold is ₹10,000,000. Providing a structured framework for the resolution of insolvency, the IBC aims to streamline the process and ensure the timely resolution of financial distress.

III. LITERATURE REVIEW

Several studies have examined the effectiveness of different channels for Non-Performing Asset (NPA) recovery in the banking sector. A study by (*Sumathy & S Das, 2021*) recovery channels showed no positive correlation with Non-Performing Assets (NPAs), with the recovery not meeting banks' initial expectations. As defended by (*Sharanraj. 2020*) major reason for increase in Bank NPA and decrease in profitability is the increase in financial fraud due to unauthorized advances. However, (*Moazzam & Singh 2022*) found that despite fluctuations in cases referred to Debt Recovery Tribunals (DRTs), the recovery percentage improved to 24% in 2016-17. Lok Adalats, though experiencing a decline in cases, remain effective for resolving large NPA cases. (*Kumar Sahoo & Majhi 2020*) found significant differences in the number of cases referred and the percentage of amount recovered among three recovery mechanisms, indicating an overall poor recovery mechanism in the banking industry. (*Vivek R. Singh 2016*) highlighted that NPAs significantly reduce bank profitability and credibility, with SARFESI and DRTs being successful in

recuperating amounts. Tinu Anand and Mashu Goel's study showed that while SARFAESI Act initially had positive trends, its resilience declined post-2011 due to more reliance on DRTs, suggesting a need to expand SARFAESI Act for quicker recovery. Lastly, (Srinivas K. T. & Karanth, S. 2021) noted that Lok Adalats have the highest number of cases but low recovery amounts, while SARFAESI Act shows the highest proportion of amount recovery. IBC achieved a 40% recovery in just three years, indicating its effectiveness. These studies collectively suggest a need for improving recovery channel efficiency, possibly through granting more autonomy to these channels, as recommended by the Government of India and RBI.

Objectives

- Examine the Different Recovery Channels of Non-Performing Assets (NPAs):
- Identify the Monetary Involvement in NPA Recovery Channels by Scheduled Commercial Banks:
- Determine Discrepancies in Recovery Amounts Compared to the Initial Involvement in Various NPA Recovery Channels:

Research Methodology

The data used for the study is secondary in nature. Data has been collected from various sources like RBI

and IBBI websites, journals, articles, newspaper and some reputed books. For the analysis, last fourteen years data has been gathered, from 2009-2023. In addition to this data has been analyzed by using an Independent Sample T-test to know the difference between amount recovered against the amount involved in various NPA recovery channels.

Hypothesis

- H₀. There is no statistically significant difference A: between the amount involved and the amount recovered under Lok Adalat.
- H₀. There is no statistically significant difference B: between the amount involved and the amount recovered under Debt Recovery Tribunals (DRT).
- H₀. There is no statistically significant difference c: between the amount involved and the amount recovered under the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act.
- H₀. There is no statistically significant difference D: between the amount involved and the amount recovered under IBC

IV. DATA ANALYSIS

Table- 1.1 Recovery of NPA through various channels
(Amount: In Crores)

Year	Recovery Channels	No. of Cases Registered	Amount Involved	Amount Recovered
2022-23	Lok Adalats	1,42,49,462	1,88,527	3,831
	DRTs	58,073	4,02,636	36,924
	SARFAESI Act	1,85,397	1,11,805	30,864
	IBC	1,261	1,33,930	53,968
	Total	1,44,94,193	8,36,898	1,25,587
2021-22	Lok Adalats	85,06,741	1,19,006	2,778
	DRTs	30,651	68,956	12,035
	SARFAESI Act	2,49,645	1,21,718	27,349
	IBC	891	1,97,959	47,409
	Total	87,87,928	5,07,639	89,571
2020-21	Lok Adalats	19,49,249	28,084	1,119
	DRTs	28,182	2,25,361	8,113

	SARFAESI Act	57,331	67,510	27,686
	IBC	536	1,35,319	27,311
	Total	20,35,298	4,56,274	64,229
2019-20	Lok Adalats	59,86,790	67,801	4,211
	DRTs	33,139	2,05,032	9,986
	SARFAESI Act	1,05,523	1,96,582	34,283
	IBC	1,986	2,24,935	1,04,117
	Total	61,27,438	6,94,350	1,52,597
2018-19	Lok Adalats	40,87,555	53,484	2,750
	DRTs	51,679	2,68,413	10,552
	SARFAESI Act	2,35,437	2,58,642	38,905
	IBC	1,152	1,45,457	66,440
	Total	43,75,823	7,25,996	1,18,647
2017-18	Lok Adalats	33,17,897	45728	1,811
	DRTs	29,345	1,33,095	7,235
	SARFAESI Act	91,330	81,879	26,380
	IBC	704	9929	4,926
	Total	34,39,276	2,70,631	40,352
2016-17	Lok Adalats	35,55,678	36,100	2,300
	DRTs	32,418	1,00,800	10,300
	SARFAESI Act	1,99,352	1,41,400	25,900
	IBC	37	-	-
	Total	37,87,485	2,78,300	38,500
2015-16	Lok Adalats	44,56,634	72,000	3,200
	DRTs	24,537	69,300	6,400
	SARFAESI Act	1,73,582	80,100	13,200
	Total	46,54,753	221400	22,800
2014-15	Lok Adalats	29,58,313	30,979	984
	DRTs	22,004	60,371	4,208
	SARFAESI Act	1,75,355	1,56,778	25,600
	Total	31,55,672	2,48,128	30,792
2013-14	Lok Adalats	16,36,957	23,200	1,400
	DRTs	28,258	55,300	5,300
	SARFAESI Act	1,94,707	94,602	24,402
	Total	18,59,922	1,73,102	31,102
2012-13	Lok Adalats	8,40,691	6,600	400
	DRTs	13,408	31,000	4,400
	SARFAESI Act	1,90,537	68,100	18,500
	Total	10,44,636	1,05,800	23,200
2011-12	Lok Adalats	4,76,073	1,700	200
	DRTs	13,365	24,100	4,100
	SARFAESI Act	1,40,991	35,300	10,100
	Total	6,30,429	61,100	14,400
2010-11	Lok Adalats	6,16,018	5,254	151
	DRTs	12,872	14,092	3,930
	SARFAESI Act	1,18,642	30,604	11,561
	Total	7,47,532	49,950	15,642

2009-10	Lok Adalats	7,78,833	7,235	112
	DRTs	6,019	9,797	3,133
	SARFAESI Act	78,366	14,249	4,269
	Total	8,63,218	31,281	7,514

Source: www.rbi.org

Table 1.1 presents data on the number of cases registered across various recovery channels and the corresponding amounts recovered relative to the total involved in each Non-Performing Assets (NPA) recovery channel. The analysis encompasses four recovery channels: Lok Adalats, Debt Recovery Tribunals, SARFAESI Act, and Insolvency and Bankruptcy Code (IBC). Lok Adalats, known as people's courts, exhibit the highest number of registered NPA cases. However, despite the large number of cases, the amounts involved and recovered are comparatively lower among the four recovery channels. SARFAESI Act follows with the second-highest number of cases, and it stands out with the highest recovery amount during the period 2018-19 and 2019-20, signifying a notable performance. Debt Recovery Tribunal shows consistent fluctuations throughout the observed period. In contrast, the Insolvency and Bankruptcy Code, introduced by the government in 2016, demonstrates substantial growth since its inception. In the year 2022-23, it reaches a peak by collecting ₹53,968 against a total amount involved of ₹1,33,930.

Upon closer examination of the table, it is evident that SARFAESI Act and IBC mechanisms exhibit a positive impression with the recovery of NPAs, reflecting their effectiveness in comparison to other recovery channels.

Amount	Leven e's Test for Equality of Variances		t-test for Equality of Means					
	F	Sig.	t	df	Sig. (2 Dif)	Mean Dif	Std. Err	95% Confidence
Equal variances assumed	14.366	.000	3.42	112	.000	1803.35	515.67	1783.97 to 2422.73
Equal variances not assumed			3.42	111	.000	1803.35	515.67	1783.97 to 2422.73

				- tailed	ference	or Difference	Interval of the Difference	
							Lower	Upper
Equal variances assumed	14.366	.000	3.42	112	.000	1803.35	515.67	1783.97 to 2422.73
Equal variances not assumed			3.42	111	.000	1803.35	515.67	1783.97 to 2422.73

In above table 1.2 An independent sample t-test was employed to compare the amount involved and amount recovered in the Lok Adalat Scheme. The analysis revealed a significant difference in the scores ($t = 3.42, p = 0.005$). Specifically, the mean for the amount involved ($M = ₹48978.43, SD = ₹51567.19$) was found to be significantly higher than the mean for the amount recovered ($M = ₹1803.35, SD = ₹1397.387$). The magnitude of the difference in means, as indicated by the 95% confidence interval (CI) for the mean difference (₹17394.57 to ₹76955.57), further emphasizes the significance of this disparity. Consequently, the null hypothesis is rejected, confirming a substantial and statistically significant difference between the amount involved and the amount recovered under the Lok Adalat Scheme.

Table 1.3- Independent Sample test of DRT

A mo unt	Leve ne's Test for Equal ity of Varia nces		t-test for Equality of Means						
	F	S i g .	t	d f	Si g. (2 - ta il e d)	Me an Dif fer enc e	Std . Err or Dif fer enc e	95% Confiden ce Interval of the Differenc e	
								Lo we r	Up per
Eq ual var ian ces ass um ed	2 3. 2 9	. 0 0 1	3 . 5 5	2 2 6	.0 0 1	11 01 16. 92	31 01 8.8 2	46 35 6.8 1	17 38 77. 03
Eq ual var ian ces not ass um ed			3 .5 5	1 3. 1 4	.0 0 4	11 01 16. 92	31 01 8.8 2	43 17 8.0 0	17 70 55. 85

In above table 1.3 An independent sample t-test was executed to compare the amount involved and the amount recovered through the Debt Recovery Tribunal (DRT) Scheme. The analysis revealed a significant difference in the scores ($t = 3.55$, $p = 0.004$). Specifically, the mean for the amount involved ($M = ₹119160.92$, $SD = ₹115747.69$) was found to be significantly higher than the mean for the amount recovered ($M = ₹9044.00$, $SD = ₹8533.26$). The magnitude of the difference in means, as indicated by

the 95% confidence interval (CI) for the mean difference (₹43178 to ₹177055.85), emphasizes the statistical significance of this disparity. Consequently, the null hypothesis is rejected, confirming a substantial and statistically significant difference between the amount involved and the amount recovered under the DRT Scheme.

Table 1.4- Independent Sample test of SARFAESI ACT

A mo unt	Leve ne's Test for Equal ity of Varia nces		t-test for Equality of Means						
	F	S i g .	t	d f	Si g. (2 - ta il e d)	Me an Dif fer enc e	Std . Err or Dif fer enc e	95% Confiden ce Interval of the Differenc e	
								Lo we r	Up per
Eq ual var ian ces ass um ed	1 5. 7 2	. 0 0 1	4 .2 4 7	2 6	.0 0 1	81 44 7.8 5	18 19 4.6 6	44 04 8.1 8	11 88 47. 52
Eq ual var ian ces not ass um ed			3 .5 5	1 3. 1 4	.0 0 4	81 44 7.8 5	18 19 4.6 6	42 30 5.6 0	12 05 90. 11

In above table 1.4 An independent sample t-test was conducted to compare the amount involved and

amount recovered through the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act Scheme. The analysis revealed a significant difference in the scores ($t = 3.55, p = 0.004$). Specifically, the mean for the amount involved ($M = ₹104233.50, SD = ₹67353.85$) was found to be significantly higher than the mean for the amount recovered ($M = ₹22785.64, SD = ₹9904.57$). The magnitude of the difference in means, as indicated by the 95% confidence interval (CI) for the mean difference ($₹42305.60$ to $₹120590.11$), further emphasizes the statistical significance of this disparity. Consequently, the null hypothesis is rejected, confirming a substantial and statistically significant difference between the amount involved and the amount recovered under the SARFAESI Act Scheme.

Table 1.4- Independent Sample test of IBC

Amount	Levene's Test for Equality of Variances		t-test for Equality of Means						
	F	Sig.	t	df	Sig. (2-tailed)	Mean Difference	Std. Error Difference	95% Confidence Interval of the Difference	
								Lower	Upper
Equal variances assumed	.719	.395	2.74	157	.007	86.046	31.326	16.259	155.837

Equal variances assumed	2.74	7.31	.027	86.046	31.326	12.59	155.84
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In above table 1.4 An independent sample t-test was conducted to compare the amount involved and amount recovered through IBC. The analysis revealed a significant difference in the scores ($t = 2.74, p = 0.027$). Specifically, the mean for the amount involved ($M = ₹136739.66, SD = ₹68793.68$) was found to be significantly higher than the mean for the amount recovered ($M = ₹50692.83, SD = ₹33962.45$). The magnitude of the difference in means, as indicated by the 95% confidence interval (CI) for the mean difference ($₹12598.22$ to $₹159495.43$), further emphasizes the statistical significance of this disparity. Consequently, the null hypothesis is rejected, confirming a substantial and statistically significant difference between the amount involved and the amount recovered under the IBC Scheme.

Findings

- Effectiveness of Recovery Channels: Lok Adalats, acting as people's courts, have the highest NPA case registrations, but with relatively lower amounts involved and recovered, indicating challenges in achieving substantial recoveries. In contrast, the SARFAESI Act performs exceptionally well, displaying the second-highest case numbers and the highest recovery amount during 2018-19 and 2019-20. The Debt Recovery Tribunal exhibits fluctuations, while the Insolvency and Bankruptcy Code, introduced in 2016, shows significant growth and peak effectiveness in 2022-23.
- Positive impression of SARFAESI Act and IBC Mechanisms: Upon meticulous examination, a positive impact of SARFAESI Act and Insolvency and Bankruptcy Code (IBC) mechanisms becomes evident. These mechanisms showcase heightened effectiveness compared to other recovery channels

(Karanth, S. & Prabu, R. 2024), indicating their robust contribution to NPA recovery.

- Significant Discrepancy in Lok Adalat Scheme: The independent sample t-test conducted for the Lok Adalat Scheme reveals a significant difference between mean value of amount involved and the amount recovered. Despite being known as people's courts and having the highest number of registered NPA cases, the amounts involved and recovered in Lok Adalats are comparatively lower. The rejection of the null hypothesis underscores the substantial and statistically significant difference between the two parameters.
- Lok Adalat Scheme and DRT Scheme Discrepancies: Independent sample t-tests for Lok Adalat and Debt Recovery Tribunal (DRT) Schemes show significant differences between mean value of amounts involved and recovered. In both cases, means for amounts involved are markedly higher than amounts recovered, suggesting challenges or inefficiencies in achieving full recoveries. These findings emphasize the importance of scrutinizing operational dynamics and effectiveness in addressing NPAs.

CONCLUSION

Even if the banking industry's overall performance has improved, Non-Performing Assets (NPA) continue to be a major concern. NPAs are an important financial metric that show how the banking sector is doing. The study shows that there is a significant discrepancy between the quantities implicated and recovered, indicating that the recovery of NPA amounts through various channels is insufficient. The glaring disparity highlights how ineffective the current recovery methods are at bolstering the total value of non-performing assets. Therefore, it is essential that the Reserve Bank of India and the Indian government take proactive steps to lower NPAs. Additionally, selective interventions must to be used to improve the effectiveness of the current channels of healing. These actions are essential to addressing the NPA issue, strengthening the banking industry, and maintaining long-term stability and health of the financial system.

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