

**PERFORMANCE OF RECOVERY CHANNELS IN MANAGING NPAS**

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## **ABSTRACT**

Banks are always called as the back bone of every economy. Being the basic function, the prime duty of a bank or banker is to lend money to the public with the condition that the money will be re-paid in due course of time with interest and other charges. The major chunk of banks income is derived from the interest income from advances. Hence, loans and advances play the vital role for the profitability and sustainability of each bank. At the same time, the major challenge banks are often faced from the loans and advances point of view is the regular repayment of the loans. Any irregularity in the repayment schedule of the loans will badly affect the balance sheet of the banks. The analysis revealed that lok adalat is the appropriate method to recover the unsecured loan and SARFAESI is considered to be the effective method for the recovery of secured loans. The cases filed in the DRT are high but the recovery is not as effective as planned by this mechanism.

**Key words:** Asset quality, NPA, RBI, Recovery channels, Recovery rate.

## **INTRODUCTION**

The NPA in banks is creating huge troubles in the Indian economy and to its banks. The definition of a standard asset is that it is being serviced on a periodic basis generating income to the lending institution and it is turned to non performing asset when it failed to generate any income to the lending organisation. As per the regulation of RBI, an asset is classified as NPA when either the principal or interest is overdue for a period of 90 days from the due date. When the asset if failed to generate income, it will affect the performance of banks in multiple ways. The banks need to find provision to the bad debt causing struggles to the future development of the bank. The NPA will erode the valuable capital structure of the bank, affecting the morale of the employees who involved in the lending process. Ultimately the borrowing cost will increase and hence the overall face of the bank will looks horrible to the public in terms of advance health and recovery. Due to such issues for the lending organisation, granting quality advances and getting timely repayment of the loans is the crucial function of any financial organisation. The accumulated and enormous level of NPA in post-

liberalization period forced policy makers to reform banking sector. A Committee on Banking Sector Reforms known as Narasimham Committee was set up by the RBI to analyse the issues faced by Indian Banking Industry and to suggest solutions to the issues. The committee identified NPA as a major threat and recommended prudential measures for income recognition, asset classification and provisioning requirements. These measures embarked on transformation of the Indian banking sector into a viable, competitive and vibrant sector. The committee recommended measures to improve “operational flexibility” and “functional autonomy” so as to enhance “efficiency, productivity and profitability”

## **NEED OF RECOVERY CHANNELS**

Assuring the financial health of the loan portfolio is the vital function of the bank, being the major contributor of income for any financial organisation. The asset that failed to generate the income will make the banks to land in more tension. The RBI and Indian government introduced many measures to recover the dues from the borrowers and formed many rules and regulation to be followed while doing the recovery of the NPA. Hence, the recovery mechanism is the process of developing proper planning and implementation of various recommendations for ensuring the financial strength of bank in the case of failure of the borrower to pay the dues in time.

In India the following are the major tools used to the recovery of bad debt

1. Lok Adalat
2. Debt Recovery Tribunals (RDB Act 1993)
3. SARFAESI Act 2002
4. Insolvency and Bankruptcy Code 2016

### **1. LOK ADALAT**

Lok Adalat means, ‘People's Court’. "Lok" stands for "people" and the term "Adalat" means court. Lok Adalat is a system of alternative dispute resolution developed in India. “Lok Adalat” is defined as a “forum where voluntary effort aimed at bringing about settlement of disputes between the parties is made through conciliatory and pervasive efforts”.

The Indian Bank Association issued many instructions to its member banks on how to use the lok Adalat and settle the issues with them. There are multiple uses of Lok Adalat. There is no court fee to be paid while filing the cases through the lok Adalat. Also all the existing cases can be settle by this mechanism. If no settlement has arrived at the discussions, then the parties can move to next level for redressal of the NPA. All the small cases upto Rs 5 lakhs has been settled in Lok Adalat. The loan which involves small tickets like vehicle loan, small personal loans etc can be settled in this mechanism. They have statutory status under the Legal Services Authorities Act, 1987 and have

powers similar to those vested in a civil court. All awards are binding on all parties and cannot be appealed. According to the RBI guidelines, banks can use lok Adalat to recover loans up to Rs 20 lakh.

## **2. DEBT RECOVERY TRIBUNALS - RDB Act 1993**

Debt Recovery Tribunals (DRTs) in India are the specialized tribunals introduced to facilitate the expeditious adjudication and recovery of bad debts by banks and financial institutions. DRTs can take bad debts from banks for disputed loans above Rs 20 Lakhs. In 1993, the Recovery of Debts Due to Banks and Financial Institutions (RDDBFI) Act was passed leading to establishment of Debt Recovery Tribunals (DRT) to initiate debt recovery including banks and other financial institutions.

## **3. SARFAESI ACT 2002**

The Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act, 2002 is an Indian law that empowers banks and financial institutions to recover their non-performing assets without the intervention of the court. Hence this act is applicable to loans which are secured by the assets.

ARCs are formed under this act so that the banks can transfer and re contracts the assets to these companies. This allows banks to sell the collaterals as bonds, Pass Through certificates and collateralized debt obligations. The banks can directly seize the properties of the borrowers excluding he agricultural lands. The act also formed the central registry to avoid the fraud of multiple loans under same property. With recent amendment the NBFC are also comes under the act and can utilize the facilities under SARFAESI Act 2002

The SARFAESI Act applies to loans above Rs. 1 lakh that are classified as NPAs. It excludes loans where more than 80% has been repaid and certain types of assets like agricultural land. The Act has significantly improved the recovery process for banks and financial institutions, reducing the time and cost involved in loan recovery.

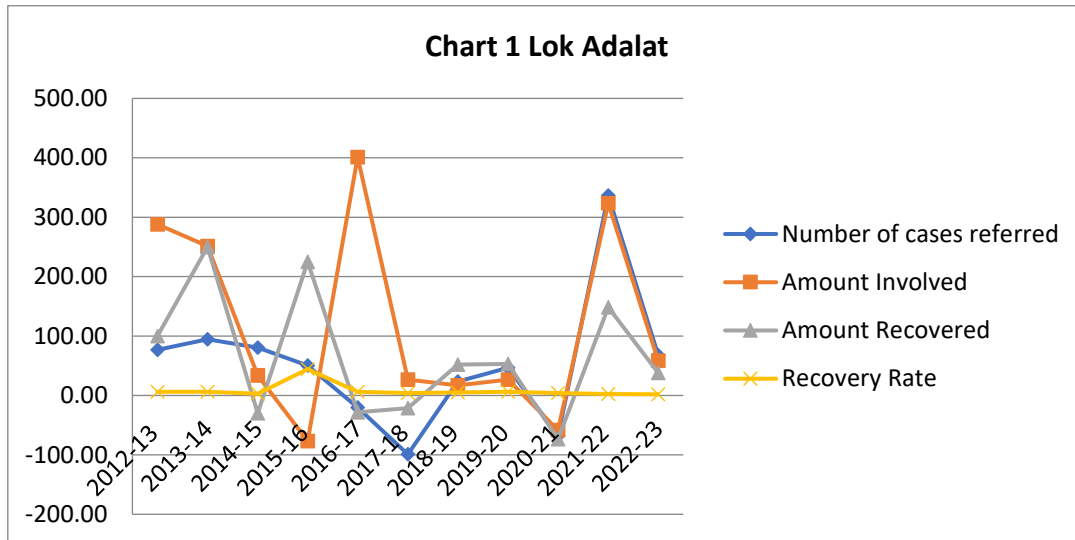
## **4. INSOLVENCY AND BANKRUPTCY CODE, 2016**

The Insolvency and Bankruptcy Code (IBC) was introduced in 2016 to address the issue of non-performing assets (NPAs) in India. It aimed to expedite the resolution process for insolvent companies and improve the recovery of bad loans. Resolution of stressed assets (NPAs and restructured assets) requires coordinated approach of the government, the Central Bank (RBI), and the lending bank itself. In 2016, with this objective, the Insolvency Bankruptcy Code (hereinafter “the code”) was enacted which seeks to achieve resolution of distressed corporate debtors (CDs). It also facilitates liquidation in time bound manner under the supervision of National Company Law Tribunal (NCLT) if there is no resolution.

**PERFORMANCE OF DEBT RECOVERY CHANNELS IN INDIA**  
**RECOVERY OF NPAS THROUGH LOK ADALAT**

The number of cases referred, amount involved and amount recovered through Lok Adalat is given in the chart 1 and table 1

**Chart 1 Performance of Lok Adalat during 2011-12 to 2022-23**



**Table 1 Performance of Lok Adalat during 2011-12 to 2022-23**

	Mean	Max	Min	Std. Dev	CAGR
<b>Number of Cases Referred</b>	119211025	445663400	1949249	159116420	-9.56%
<b>Amount Involved</b>	50701	188527	1700	54016	48.05%
<b>Amount Recovered</b>	2082	4211	200	1309	27.90%
<b>Recovery Rate %</b>	8	44	2	12	-13.87%

**Source:** Reports on Trend and Progress of Banking in India, RBI, Various Issues.

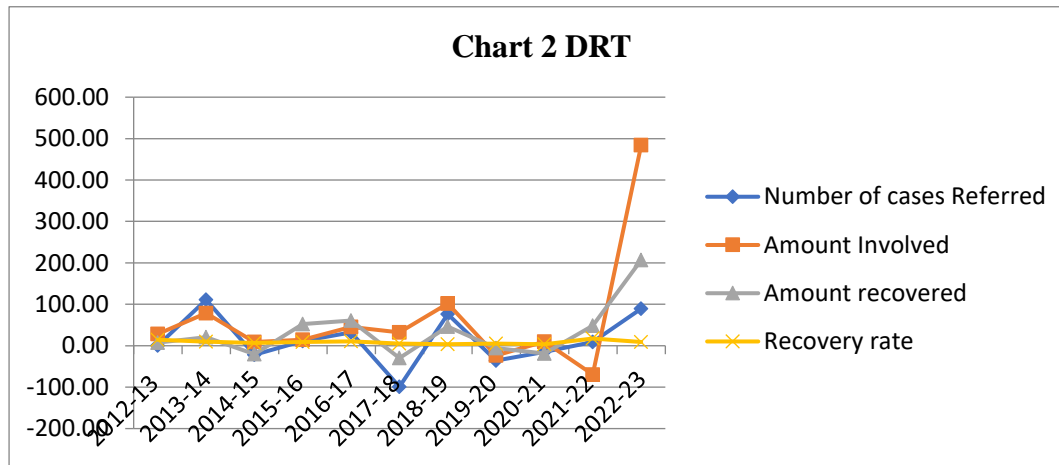
Chart 1 and Table 1 depicts the NPAs of Scheduled Commercial Banks recovered through Lok Adalat during 2011-12 to 2022-23. The descriptive statistics of number of cases referred, amount involved, amount recovered and recovery rate of Lok Adalat is given in table 1 and its growth rate is given in chart 1. The highest number of cases, 445,663,400, was recorded in 2015–16, this was followed by a sharp fall to 3,317,897 cases in 2017–18 (a decrease of more than 99 percent). A notable recovery occurred in 2021–2022, with a growth rate of 336.41 percent. The amount involved represents the monetary stakes in these cases. The maximum amount involved was 188,527 in 2022-23, while the minimum was a mere 1700 in 2011-12. The recovery rate ranged from a minimum of 2.03% in 2020-21 to a maximum of 44.44% in 2011-12, indicating fluctuations in the effectiveness of recovery efforts

over the years. The recovery process is influenced by various factors, including case complexity and cooperation from parties. The number of cases referred recorded a negative CAGR of -9.56% signifies an overall decline. However, positive CAGRs for amounts involved with 48.05% and amount recovered with 27.90% indicate a significant growth in the recovery of NPAs through Lok Adalat.

**RECOVERIES OF NPAS THROUGH DEBT RECOVERY TRIBUNAL (DRT)**

The performance of DRT during 2011-12 to 2022-23 is given in the chart 2 and table 2

**Chart 2 Performance of DRT during 2011-12 to 2022-23**



**Table 2 Performance of DRT during 2011-12 to 2022-23**

	Mean	Max	Min	Std. Dev	CAGR
<b>Number of Cases Referred</b>	1135842	3241800	28182	1260191	-23.00%
<b>Amount Involved</b>	137030	402636	24100	115733	26.45%
<b>Amount Recovered</b>	9963	36924	4100	8921	20.10%
<b>Recovery Rate %</b>	9	14	4	5	-15.6%

**Source:** Reports on Trend and Progress of Banking in India, RBI, Various Issues.

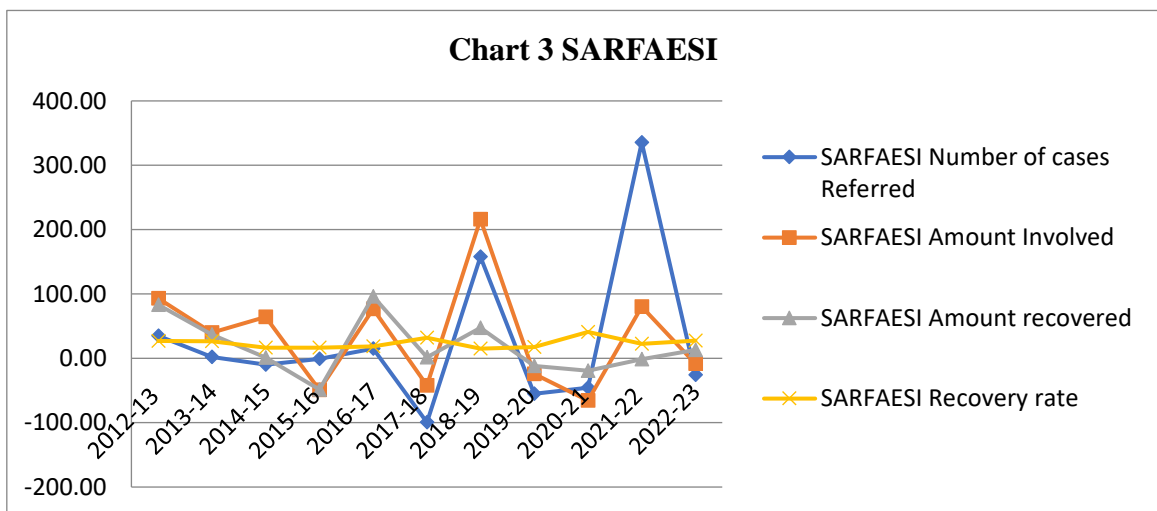
Chart 2 and Table 2 depict the DRT’s recovery performance during 2011-12 to 2022-23. The number of cases referred through the DRTs has varied significantly with some years showing significant growth or decline. Notably, there was a sharp decline of 99.094% in 2017-18, followed by a subsequent improvement in recovery. The CAGR stands at -23% suggest a decline in the number of cases handled annually. The amount involved has fluctuated, peaking in 2022-23 at ₹402,636 crore. The recovery amounts have also seen substantial variations, reaching ₹36,924 crore in the same year. The CAGR for amount involved and recovered are positive, indicating significant growth. Despite the fluctuations, the recovery rate remains relatively low, averaging around 9%, this suggests challenges in effective debt recovery within the DRT framework. The minimum case referrals was 28,182 occurred in 2020-

21, and the maximum case referrals was 3,241,800 recorded in 2016-17. The wide standard deviation indicates substantial dispersion in the data points. The volatility in the case referrals and recovery amounts contributes to this variability. The positive CAGR for amounts involved and recovered underscores gradual progress. However, the recovery rate's CAGR remains modest.

**NPAS RECOVERED THROUGH SARFAESI**

Chart 3 and Table 3 provide the number of cases referred, amount involved, amount recovered and recovery rate through SARFAESI.

**Chart 3 Performance of SARFAESI during 2011-12 to 2022-23**



**Table 3 Performance of SARFAESI during 2011-12 to 2022-23**

	Mean	Max	Min	Std. Dev	CAGR
<b>Number of Cases Referred</b>	9031422	19935200	57331	9383376	-30.30%
<b>Amount Involved</b>	117926	258642	35300	62663	10.08%
<b>Amount Recovered</b>	25339	38905	10100	8157	9.76%
<b>Recovery Rate %</b>	24	41	15	8	-0.29%

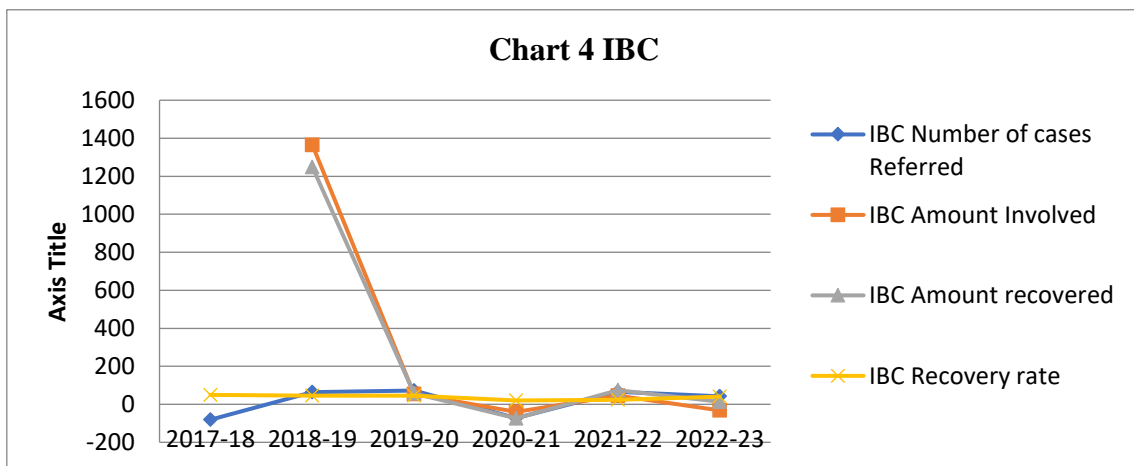
Source: Reports on Trend and Progress of Banking in India, RBI, Various Issues.

Chart 3 and Table 3 pertain to the recovery of NPA through SARFAESI during 2011-12 to 2022-23. The number of cases referred to SARFAESI has fluctuated significantly over the years. The growth rate includes both extreme with a drastic decline of 99.54% in 2017-18, followed by a remarkable rebound in 2021-22 with 335.45% increase. These fluctuations suggest changing trends in loan defaults and enforcement actions. The negative CAGRs for cases referred suggest a decline in the number of cases handled annually at -30.30%. The amount of money involved in SARFAESI cases also varies significantly each year, ranging from a minimum of 35,300 units in 2011-12 to a maximum of 258,642 units in 2018-19. The amount recovered by SARFAESI also varies annually, ranging from a minimum of 10,100 units in 2011-12 to a maximum of 38,905 units in 2018-19. This reflects the success of SARFAESI in recovering defaulted loans or assets. The CAGR for both amount involved and recovered are positive, indicating overall growth. The recovery rates, calculated as the ratio of amount recovered to amount involved, vary from a minimum of 15% to a maximum of 41%. Higher recovery rates suggest more successful enforcement of security interests and recovery of defaulted amounts. Surprisingly, the highest recovery rate occurred in 2020-21, despite a decrease in case referrals and the amount involved. The minimum case referrals (57,331) occurred in 2020-21, and the maximum referrals (19,935,200) were recorded in 2016-17, the wide standard deviation indicates substantial dispersion in the data points.

**RECOVERIES OF NPAs THROUGH IBC**

The total number of cases referred, amount involved and amount recovered through IBC is given in the chart 4 and table 4

**Chart 4 Performance of IBC during 2017-18 to 2022-23**



**Table 4 Performance of IBC channels during 2017-18 to 2022-23**

	Mean	Max	Min	Std. Dev	CAGR
<b>Number of Cases Referred</b>	1461.43	3700	536	1094	-14.25%

<b>Amount Involved</b>	141254.8	224935	9929	74257.3	45.02%
<b>Amount Recovered</b>	50695.2	104117	4926	33955.7	40.77%
<b>Recovery Rate %</b>	38	50	20	12.5	-3.14%

**Source:** Reports on Trend and Progress of Banking in India, RBI, Various Issues.

The performance of Insolvency and Bankruptcy Code during 2017-18 to 2022-23 is given in the chart 4 and table 4. The analysis revealed a significant decline of 536 in the number of cases referred in 2017-18, indicating a potential initial impact after the implementation of the IBC. However, there was a positive trend with increases in the number of cases referred in the following years, peaking at 72.4% in 2019-20 and 41.53% in 2022-23. The increase in the number of cases referred over time suggests growing awareness and utilization of the IBC by stakeholders. The CAGR for case referrals is negative (-14.25%) due to decline in the number of cases handled in 2022-23. The increase in the number of cases referred over time suggests growing awareness and utilization of the IBC by stakeholders. The amount involved showed fluctuations over the years, with a notable decrease of 73.01% in 2020-21 followed by a recovery to positive values in 2021-22 and 2022-23. The maximum amount involved for recovery experienced substantial fluctuations, reaching a peak of ₹224,935 crore in 2019-20. The Recovery amounts also varied, with a maximum of ₹104,117 crore in the same year. The CAGR for both amount involved and recovery are positive, indicating overall growth. Fluctuations in the amount involved and recovered indicate variations in the complexity and outcomes of insolvency cases. Despite the fluctuations, the recovery rate remained relatively stable, ranging from 20% to 50%. The highest recovery rate occurred in 2018-19, and minimum case referrals (536) occurred in 2020-21. The maximum referrals (3,700) were recorded in 2016-17, The wide standard deviation indicates substantial dispersion in the IBC activities due to fluctuation in case referrals and recovery. The negative CAGR for case referrals suggests a declining trend. However, positive CAGRs for amounts involved and recovered highlight progress. The amount recovered shows a similar trend to the number of cases referred, with a dip in recovery in 2017-18 followed by improvements in subsequent years. Notably, there was a substantial increase in the amount recovered from 2017-18 to 2018-19, suggesting a positive impact of the IBC on debt recovery during the period under review. The recovery rate, calculated as the ratio of amount recovered to amount involved, fluctuates between 20% and 49.6% across the years. The recovery rate reflects the efficiency of the resolution process, with fluctuations possibly influenced by factors such as legal reforms, economic conditions, and institutional capacity.

## **RESULTS AND DISCUSSION**

The true effects of Lok Adalat need contribution from both creditors and borrowers as it involves settlement outside the court. The cases filed in Lok Adalat are at its peak in the year 2015-16 but the recovery is not happened as planned. A notable recovery is recorded in the year 2021-22. The delay in



settling the cases under lok adalat causes banks to lose its precious capital and time for development, because, the banks need to provide provision for the NPAs from the day first of its classification as SMA. Hence bank's need to sideline a major part of their valuable capital towards the NPA provision. Until the NPA is settled in any way, the provision needs to be accounted. But being recovery of unsecured assets, lok Adalat is the most effective way to recover the dues. The concerned authorities need to finalise the cases on time bound manner so that both the debtor and creditor are benefited from the lok adalat. Also it is the cheapest way to settle the cases. Most of the people who approach for settlement under lok adalat might be people who are economically down and low income categories. Education loans, small tickets size personal loans, small vendors' loans etc., are the type of loans which come under this type of settlement normally. Hence Lok Adalat is the most effective method to recover the dues from the unsecured category of bank credit.

Even though the DRT is formed to have a great recovery of bad debt for the bankers, it is often failed to perform well as planned. The major issue faced under DRT is that verdicts of the DRT can be questioned by the parties with DRTC. The time delay in settling and executing the orders or DRT is another issue. The number of DRT courts also not sufficient to cover the total cases pending to be settled. The third parties can also claim on the assets of the borrowers if they had any outside liabilities other than to the bankers. Hence the third parties might file another case against the borrowers outside the DRT which again delays the process. The number of cases filed in the DRTs is high but the recovery is not as effective as planned by this mechanism.

SARFAESI Act 2002 is considered to be one of the most effective methods in recovery of NPA. The major portion of secured assets by banks and the NBFCs are recovered through this method. Using SARFAESI Act the banks can recover the dues without the involvement of court and that help the organization to save the time delay in executing the recovery. The banks can easily sell this asset to ARC and settle the cases. The cases are settled on a time bound manner and hence the precious time and provision on bad debt for the banks. Hence SARFAESI is considered to be the most effective method for the recovery of dues in case of secured loan category.

The IBC is introduced in the year 2016 to improve the relationship between the debtors and creditors. It is very much effective for the insolvent companies. The IBC provides a structured and time-bound framework for resolving insolvency, which helps in maximizing the value of assets and promoting faster resolution of distressed entities.

## **CONCLUSION**

The real economic health of any financial institutions is analysed based on the quality of its assets. The maintenance of assets quality reflects the actual strength of the organisation and its capacity to manage the entire business. Hence the banks need to have a proper control over the assets and its quality without compromising on the compliances part. The quality of assets will definitely reflect in the open

market and the public opinion on the bank. The mounting amount of NPA and its recovery is a hard nut to the Indian Banks over the years. Being NPA a such complicated issue that directly affect the financial health of the Indian economy as a whole, the government and RBI come out with many redressals mechanism to overcome the NPA task.

The quality of the lending officers and the recovery staff play a vital role in executing the recovery techniques in the most productive way. The borrower needs to be educated properly while granting the loan and the proper follow-up of the assets in person is the most effective method to ensure the smooth function of the assets and its repayment. Even if the assets start to shows the sign of SMA, the bank official can initiate the recovery action if there is proper follow-up and personal touch with the borrower both in case of secured and unsecured cases. The recovery process can be initiated when the assets start to shows in signs of SMA, without waiting for the assets to turn to NPA category.

The studies shows that personal contact with the borrower is the most effective methods to recover any dues both in case of secured and unsecured loans. Even in case of one-time settlement and Lok Adalat, the dues can be settled with mutual consent from the borrower and the lender. Such agreement can be arrived only with personal contact with the borrowers. Similarly in case secured assets the NPA can be cleared with settlement clause if there is a personal contact with the borrowers. Otherwise, Banks need to follow the entire process of secured assets recovery which might take time and money. Even though the SARFAESI, DRT and IBC are considered to be effective to claim the entire dues to the banks, the time, provision making and the money spending on the expenses is also to be considered while settling under one time settlement. Being the most effective method, there is wide public opinion against the SARFAESI Act and its implementation. But banks need to recover its dues on time as per the process. Finally, the finding till date shows that proper borrower education and effective implementation of follow-up is the leading way to proper recovery and smooth function of asset quality. Without loans and advances the banks cannot be survived and hence the financial health of every asset matter both for banks and the economy as a whole.

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