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India's banking sector is gasping for air after a spate of scandals

No signs of recovery in the already struggling sector

Credit rating agency Brickwork Ratings announced last month that six Indian banks have received downgraded ratings due to drastic reductions in non-interest incomes. The news comes at a time of turmoil for the Indian banking sector, which has been the subject of several scandals over the past few months, including the evergrowing issue of Non-Performing Assets (NPAs) and bad loans.

Downgraded banking sector

The six banks downgraded by the agency are Bank of India, Union Bank of India, Allahabad Bank, Central Bank of India, Corporation Bank and United Bank of India. According to the agency, the reduction in non-interest income is due to lower treasury income and the increasing stress on assets quality. Brickworks further added, that there has been an increase in the percentage of NPAs and they expect no sigh of relief for the last quarter of the financial year.

"Both the bank management and auditors are expected to be conservative regarding asset classification," the rating firm added.

In January this year, as a result of the Government's recapitalisation plans, the agency had placed state-owned banks under credit watch with positive implications. However, after poor performance in the third quarter of the financial year 2018, fall in treasury income and the increase in requirements for large corporate loans resulted in this change in outlook.

Additionally, apart from these six banks, Brickwork has also decreased the outlook of Andhra Bank, Indian Overseas Bank, Oriental Bank of Commerce, Punjab & Sind Bank and UCO bank to negative.

The case of NPAs

According to the Financial Stability Report of the Reserve Bank of India the country's gross NPA is set to hit 11.1% by September of this year. This percentage includes all stressed assets held by India's leading co-operative and small banks, along with public and private sector banks. India is not only ranked fifth on the list of economies with the highest NPAs, but is also the highest amongst all BRICS nations.

As per a statement by Finance Minister Arun Jaitley in Lok Sabha last year, the gross NPAs of India's public sector banks has increased by 311.22% in last five years. Jaitley added the gross NPAs have risen from Rs 1,55,890 crore in 2013, to Rs 6,41,057 crores in 2017. On the other hand, the gross NPAs of private sector banks rose by 269.47% during the same period, marking an increase from Rs 19,986 crores in 2013 to Rs 73,842 crores in 2017.

It is important to note that the higher ratio of stressed assets, the higher the impact on the economy. As per the data compiled by the Ministry of Statistics and Programme Implementation, and the World Bank, the gross NPA ratio of Indian banks has spurred from 5.884% in 2015 to 9.6% percent in 2017. While for the same period economic growth deteriorated.

What has the government done?

The RBI has taken several steps to reduce bad loans and NPAs, including the banking recapitalisation plan, the Financial Resolution and Deposit Insurance (FRDI) plan, Insolvency and Bankruptcy code have all been designed to prevent banks from incurring losses by lending money to corporates.

However, it appears to be that these are time-consuming plans which seem to have had no impact in improving the condition of the economy. For instance, the cases which are being referred to the National Company Law Tribunal (NCLT) under the Insolvency and Bankruptcy Code command huge processing time, and some of the high profile cases attract multiple legislations, delaying the resolution process further.

What's next?

The Indian Government has also taken few more steps such as the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act, and the Recovery of Debts due to Banks and Financial Institutions (RDDBFI) Act. Additionally, to speed by proceedings, a Debt Recovery Tribunals (DBT) has been instituted to aid the banks.

It is clear that the Indian banking system is currently skating on very thin ice, and while public sector banks are struggling to deal with internal issues of bad loans and stressed assets, the financial scams are adding pressure on them. The already struggling sector is also facing the added pressure of meeting requirements of the Basel-III norms by March 2019. It seems that the only option the government has is to continue keeping tight regulations over banks while monitoring their activities, with hopes that the sector shows signs of recovery soon.