CREDIT MONITORING AND NPA MANAGEMENT

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ABSTRACT

NPA management is a major concern not only to the individual banks but also to the regulators and the supervisors.At 9.9 per cent ratio, India has been ranked fifth on the list of countries with highest Non-Performing Assets (NPAs), and is on top spot among the BRICS (BRICS is the acronym for an association of five major emerging national economies:Brazil, Russia, India, China and South Africa.Nations), a recent report by CARE Ratings revealed. In this paper we have discussed the utility of Credit Monitoring in NPA Management.

INTRODUCTION:

The country is reeling under a huge NPA burden of over Rs 7.33 lakh crore as of June 2017. The main reason of such high level of NPA is mainly huge lapse in credit monitoring.Banking is growing in complexity with passage of time. Especially from last few quarters the asset quality deterioration becomes major concern for all banks which further leads to intolerable stress due to high regulatory provisioning. So relevance of better Credit Monitoring is felt deeply in the current scenario.

Tools of credit monitoring:

1. Due diligence in advance management
2. Data collection and analysis
3. Generation of early warning signals

Due diligence in credit both in pre-sanction and post sanction stages is the major pillar of credit management. Guidelines and best practices at branch level should focus on the following points:

Pre-sanction stage	Post- sanction stage
• Compliance of KYC Norms • Scrutiny of loan application, credit reports, IT returns and other documents submitted by the borrower • Market reports • CIBIL report • Credit report • Search report from ROC • Check with the wilful defaulter list • Legal opinion • Valuation report of the property/assets offered as security - frequency and Periodicity of valuation. • Assessment and bank ability of the proposal	• *Acceptance of terms and conditions of sanctions by the borrower* • *Documentation and legal compliance certificate* • *Vetting of security documents* • *End use offunds* • *Insurance of securities /assets charged to the bank* • *Registration of equitable mortgages* • *Stock audit* • *Regular monitoring of operations in the borrower's account* • *Information system - offsite monitoring* • *Periodical inspection/unit visit report* timely

• Disposal of loan applications within the time framework: • Pre-disbursement audit	• Renewal of cash credit limits and revival of securities. • MIS to the controlling office

Preventive steps:

Preventive steps are the only antibiotics that act against advance being sub-standard and security offered to the bank being physically and legally irrecoverable through a system of early warning signals of deterioration in financial health of the borrowers. All banks should have credit monitoring policy with the following objectives in view:

- Compliance of terms of pre-disbursement conditions
- keeping documents legally enforceable
- end use of funds as per the loan agreement to prevent diversion of bank funds

Data collection and analysis:

The process involves:

- To obtain a certified statement of actual cost of the project from the borrower. The actual cost as per the certified statement submitted by the borrower should be compared with the projected statement of project cost to be incurred at each stage of the project.
- For cost overrun, if noticed, close monitoring is called for to prevent the account from turning into a NPA
- Site inspection of securities report, Any erosion in the value of securities / negligence noticed on the part of the borrower to keep securities in order would be a matter of concern
- The project loans should be disbursed as per the periodical progress reports submitted by the borrower and subsequent site inspection done by the branch.
- obtaining periodical returns and statements from the borrowers:

(i) stock statement and book debt statement,
(ii) monthly select operational data (MSOD) / quarterly information system (QIS),
(iii) half-yearly operating statement,
(iv) credit audit report in eligible cases
(v) concurrent audit report/transaction audit
(vi) long form audit report (LFAR)of the statutory auditor
(vii) RBIinspection report / RBIrisk-based supervision report
(viii) Periodic search report from RaC
(ix) annual review report prepared on a borrowal account at the time of renewal of cash credit limit
(x) SMAsreport,
(xi) list of potential NPAs/ stressed advances
(xii) Others to be analysed:

- Banks should obtain a list of debtors of the borrower to ascertain timely realisation of book debts. Here, we can compare sales realisation with the turnover in the account and enquire reasons for poor turnover. One such reason for poor turnover may be that the borrower has opened a current account with another bank wherein the sales proceeds are deposited.from the statement of debtors, we can confirm whether bills discounted are deducted from the list of debtors

- Similarly, the bank should receive a list of major suppliers of raw-materials to ensure the end use of bank funds..
- Detect those cheques which are drawn in favour of parties not related to the borrower's business under the RTGS environment to prevent diversion of funds.
- Similarly, while calculating drawing power (DP) based on stock statement and stock inspection, we should ensure whether advances received against orders for goods are deducted to arrive at DP.
- Letters of Credit (LCs) should be deducted from the total inventory.
- Ledger account/statement of account of the borrower: Month-wise purchases and sales should reasonably be reflected in the borrower's ledger account/statement of account to prevent diversion of funds. In this regard, banks should insist on the auditor of the borrower firm to certify, among other items, sources of funds, funds brought in and end use of funds.

Generation of early warning signals

A detailed and analytical study would lead us to many critical observations:

- Sale proceeds routed through another account in other bank
  (Low turnover in the account)
- DP inflated to match with credit outstanding
  (Frequent transfer to an account not connected with business)
- Projected level not achieved
  (Non-submission/delayed submission of stock statements/MSOD)
- Poor Management Information System
  (Non-submission of returns)
- Shortage of liquid funds
  (Frequent overdrawing)
- Decline in sales
  (Frequent overdrawing)
- Borrowing from outside
  (Unusual Credit Entries)
- Diversion of fund
  (Unusual Credit Entries)
- DP shortfall
  (Frequent return of cheques)
- Shortage of working capital
- (Frequent return of cheques)

The list of early warning signals listed above is only indicative. Intuition and sound knowledge of credit monitoring may give us many more important signals.

CONCLUSION

Needless to mention, there is no lasting solution to the problem of NPAs. However NPAs reduction can be achieved only with proper credit assessment and risk management mechanisms. Though the banking sector has grown in complexity with passing time and in this situation credit monitoring is getting difficult, an effective Credit monitoring mechanism at branch levelcan save the banks from the potential danger of addition to the stock of NPAs.

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