

NON PERFORMING ASSETS (NPAS) : A STUDY OF PUNJAB NATIONAL BANK

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ABSTRACT

Manuscript Type : Empirical Study

Research Issue: *The NPAs are considered as a vital parameter to judge the execution and budgetary soundness of banks. The level of NPAs is one of the drivers of money related security and development of the saving money division. The Financial organizations and establishments are these days confronting a noteworthy issue of dealing with the Non-Performing Assets (NPAs) as these advantages are demonstrating to end up a noteworthy misfortune for the development of the economy.*

The aim of study is to evaluate the performance of the Punjab National Bank with reference to the problem of Non-Performing Assets (NPA). The objectives of this study are :

- *To analyze the sources and deployment of funds of PNB.*
- *To examine the trend of NPA in PNB.*
- *To investigate the impact of NPAs on profitability of PNB.*
- *To know the reasons and impact of NPA.*

Research Findings:

- *The fund blocked in as Gross NPA is huge amount of 55818 crore during the year 2015-16. But there is no time frame and follow up to recover the blocked amount.*
- *The Gross NPA level during the study period is quite alarming; it is negative sign to note that Gross NPA ratio increasing from 2.93 percent in 2011-12 to 12.90 percent in 2015-16.*
- *Net NPA ratio shows a marked rising trend during study period. It increases from 1.52 percent in 2011-12 to 8.61 percent in 2015-16. Clearly, this is an undesirable and disturbing aspect.*
- *There is a high negative correlation between Net NPA and Net Profit. It leads to adverse effect on profitability of bank.*

Research Suggestions:

- *Bank management may possess specialized credit rating agencies to finalize the borrowing capacity of the potential borrowers before offering credit to the needy people.*
- *Bank should exercise proper pre sanction scrutiny and post sanction supervision and control.*
- *Bank should conduct loan recovery camp in certain time period.*
- *Bank should provide training and awareness programs regarding the replacement of loans and effective use of funds.*

Keywords: *Gross NPA, Net NPA, Net Profit.*

I. INTRODUCTION

The non-performing assets are considered as an important parameter to judge the performance and financial health of banks. The level of NPA is one of the drivers of financial stability and growth of the banking sector. The financial companies and institutions are now a day facing a major problem of managing the non-performing assets (NPAs) as these assets are proving to become a major setback for the growth of the economy. A non-performing assets is defined as a credit facility in respect of which the interest and / or installment of bond finance principal has remained 'past due' for a specified period of time. NPA is used by financial institutions that refer to loan that are in jeopardy of default.

Non-performing asset is one of the most severe plaguing the Indian Banking sector posing questions over the stability of Indian Banking System. Raghuram Rajan the ex-Governor of RBI has identified the NPA problem as a major challenge facing the Indian Banking sector. The problem which was largely hidden earlier as banks used to do window dressing of their account statement has now come to the forefront after Rajan exhorted the banks to clean up their asset books by March 2017. Resultantly this led to 29 public sector banks writing off Rs. 1.14 Lakh Crore of bad debts between 2013-15, much more than what they had done in the preceding 9 years.

In percentage terms, the average gross non-performing assets (NPAs) of 39 listed Indian Banks rose from 4.41 percent of loans in 2015 to 7.91 percent in 2016. Net non-performing assets in the past one year rose up from 2.45 percent to 4.63 percent.

II. REASONS OF NPA

Some of the reasons for emergence of the NPA typical to Indian Banks include-faulty institutional environment reflected in its economic, political, legal and social environment. Other reasons include use of bank as an instrument of public policy, incompatibility of banks interest with certain policy instruments as well as change in the economic system.

- **Defaulter Friendly Legal System:** The legal system of our does not favor early recovery of dues. According to the report, the Indian Legal system is supposed to be sympathetic towards borrowers to the extent of working against banks interest, specifically their tendency to write off small advances if their recovery was not possible. Accordingly, banks also believe that writing off such loans would help them clean up the Balance-sheet and bring about greater transparency.
- **Intentional Misuse of Settlement Policy of RBI:** A policy of settlement of loans with the borrowers initiated by the RBI involves an element of concession granted to the defaulters. This resulted in even the smaller and less influential borrowers refusing to pay off their loan and the tendency to misuse the settlement policy of RBI has increased over the years.
- **Absence of Structured Monitoring Mechanisms:** Ineffective, inadequate and incompetent supervision owing to shortage of qualified manpower as well as absence of structured monitoring mechanisms. Subsequently the concept of centralized as well as specialized loan advancing hub came into being leading to marginal improvement.
- **Lack of Entrepreneurship:** Lack of entrepreneurship and knowledge on the part of the borrowers about proper use of funds coupled with absence of proper guidance by the lending institution.

- **Improper Discharge of Responsibilities:** Occasional connivance between the borrower and loan granting authority further supplemented by improper discharge of responsibilities by lawyer in respect of security of title of properties , values in respect of proper valuation of the mortgaged assets and even auditors by being very casual and mechanical in their approach.
- **Delay in Disbursements:** Delay in disbursements of loan of various phases in project implementation throwing the same off track, thereby increasing project implementation cost.
- **Lack of Proper Payment Culture:** Lack of proper payment culture mainly in priority sector advances where there are numerous instances of loan waiver by the political establishment of the day. The borrowers expect their loan to be waived off and the bank also do not feel the necessity to follow a particular segment of advances vigorously with the hope that one day or other they would have the advances reimbursed by the government.
- **Improper Networking:** Lack of improper networking among the banks where one particular bank is not aware of the default history of a particular borrower with other banks.

III. EARLY SYMPTOMS OF NPA

Early symptoms by which one can recognize a performing assets turning to Non-performing assets . Four categories are there-

1. Financial :

- Nonpayment of the very first installment in case of term loan.
- Bouncing of cheque due to insufficient balance in the account.
- Irregularity in installment.
- Irregularity of operations in the accounts.
- Unpaid overdue bills
- Declining Current Ratio
- Payment which does not cover the interest and principal amount of that installment.
- While monitoring the accounts it is found that partial amount is diverted to sister concern or parent company.

2. Operational and Physical:

- If information is received that the borrower has either initiated the process of winding up or are not doing the business.
- Overdue receivables
- Stock statement not submitted on time.
- External non-controllable factor like natural calamities in the city where borrower conduct his business.
- Frequent changes in plan
- Nonpayment of wages

3. Additional Changes:

- Use of personal comfort, stocks and shares by borrower.
- Avoidance of contact with bank
- Problem between partners

4. Others:

- Changes in Government policies
- Death of borrowers
- Competition in the market

IV. IMPACT OF NPA

- **Profitability:**

NPA means booking of money in terms of bad assets, which occurred due to wrong choice of client. Because of the money getting blocked the prodigality of bank decrease not only by the amount NPA but also NPA lead to opportunity cost as that much of profit invested in some return earning project/assets. So NPA does not affect current profit but also future stream of profit, which may lead to loss of some long term beneficial opportunity. Another impact of reduction in profitability is low ROI (Return on Investment), which adversely affect current earnings of bank.

- **Liquidity:**

Money is getting blocked, decreased profit lead to lack of enough cash at hand which lead to borrowing money for short period of time which lead to additional cost to the company. Difficulty in operating the functions of bank is another cause of NPA due to lack of money, routine payments and dues.

- **Involvement of Management:**

Time and efforts of management is another indirect cost which bank has to bear due to NPA. Time and efforts of management in handling and managing NPA would have diverted to some fruitful activities, which would have given good returns. Now day's bank have special employees to deal and handle NPAs, which is additional cost to the bank.

- **Credit Loss:**

Bank is facing problem of NPA then it adversely affect the value of bank in terms of market credit. It will lose its goodwill and brand image and credit which have negative impact to the people who are pulling their money in the bank.

V. REVIEW OF LITERATURE

NPA is a burning topic for the banking sector and many authors tried to study the reasons of NPA, the problems created by NPA and the impact of NPA on the banking sector, and moreover came to a solution or remedies of the growing problem of NPA. A number of papers have been written and gone through, and this part of this paper is attempting to present a review of all those available in the same area of non-performing assets of the public sector banks, private sector banks and other banks. This survey has conducted a study on the existing papers, articles, journals, and reports provided by different authors, groups and committees from time to time.

Kavitha, N. (Jan 2012) emphasized on the assessment of nonperforming assets on profitability its magnitude and impact. The study observed that there is an increase in advances over the period of the study. However, the decline in ratio of Non-performing Assets indicates improvement in the assets quality of SBI groups, Nationalized Banks and Private Sector Banks.

Ray, R. (2013) observed various reasons leading to Non- Performing Assets (NPA) and ways of managing NPA in different types of Banks. Since NPA has been growing menace in banking, the study may help understanding this concept better and banks may adopt remedial measures so as to maintain NPA at the minimum level. He concluded that the occurrence of NPA affects the profitability and financial health of a Bank adversely.

Chandraappa, P. (June 2014) suggested that to improve the efficiency and profitability of banks the NPA need to be reduced and controlled. NPAs have been fighting cyclical movement or dieses on week patient and it is an underdevelopment feature like chronic poverty. It reflects the performance of banks. Reduced NPAs generally gives the impression that banks have strengthened their credit appraisal processes over the years and growth in NPAs involves the necessity of provisions, which bring down the overall profitability of banks.

Rao, M. and Patel, A. (March 2015) considered the aggregate data of public sector, private sector and foreign banks and attempts to compare analyze and interpret the NPA management from the year 2009 -2013. The findings reveals that the percentage of Gross NPA to Gross advances is increasing for public banks, ratio of Loss Advances to Gross Advances are higher in foreign banks, the Estimated Gross NPA for 2014 is also more in public banks as compared to private and foreign banks and from the ANOVA test, it is concluded Ratio of Gross NPA to Gross Advances for public sector, private Sector and foreign Banks does not have significant difference between 2009-2013.

Tiwari Chandan (2015) analyzed the causes of NPA in selected co-operative banks in Pune. It studies the causes of NPA at the micro level for co-operative banks and brings out the major causes responsible for assets turning into non-performing. He concluded that identifying the causes of loans turning bad during several stages of disbursement of credit facilities are therefore significant for a banker. Sound appraisal and due diligence must be taken by the branch managers before sanctioning the loans to clients. Effective post disbursal monitoring and control will also enhance the creditability and soundness of the banking sector.

Kumar, S. and Singh, R. (Feb 2016) analyzed the non performing assets in public division banks and a similar study is done between priority sector lending and non-priority sector lending. The study broke down patterns in Gross NPAs and Net NPAs of public sector banks, to examine whether there is critical effect of priority sector bank loaning on the total NPA of open segment banks and to discover the effect of recovery on NPAs of the PSBs amid from 2003-04 to 2013-14. The outcome appeared there is a declining pattern in percentage of Gross and Net NPAs of open part banks till 2009-10 and expanded in the later years and declining pattern in pattern rate of gross and net NPAs of open division banks till 2008-09 and expanded in the later years over the time of the study, the noteworthy effect of Priority segment propels on aggregate NPAs of public area banks. Likewise the outcome demonstrated the critical effect of recovery of NPAs on aggregate NPAs of public area banks.

Singh, V. and Bahadur, R. (Mar 2016) discussed the status and trend of NPAs in Indian Scheduled commercial banks, the factors contributing to NPAs, reasons for high impact of NPAs on Scheduled commercial banks in India and recovery of NPAs through various channels during the period of 14 years i.e. from 2000 to 2014. The result shows that extent of NPA is comparatively very high in public sectors banks. Although various steps have been taken by government to reduce the NPAs but still a lot needs to be done to curb this problem. The NPAs level of Schedule commercial banks is still high as compared to the foreign banks.

VI. RESEARCH METHODOLOGY

- **Objectives of the study:** The major objective of this study is to evaluate the performance of Punjab National Bank with reference to the problem of Non-performing assets.
 - To analyze the sources and deployment of funds of PNB.
 - To examine the trend of NPA in PNB.
 - To investigate the impact of NPAs on profitability of PNB.
 - To know the reasons and impact of NPA.
- **Sample Size:** Though Non-performing assets bind to all types of bank but for this research we select PNB bank which holds third highest capitalization in public sector banks.
- **Sources and Collection data:** This study is based on the basis of secondary data. Data and information collected from annual report of PNB. The present study has been covered a period of five financial year from 2011-12 to 2015-16.
- **Tools and Techniques:** The data has been analyzed by using tables, average, standard deviation, coefficient of variance and coefficient of correlation
- **Hypothesis Development:**
 - H₀₁:** There is no relationship between Net Profit and Net NPA.
 - H₁₁:** There is a relationship between Net Profit and Net NPA.
- **Limitations :**
 - The basis for identification of non-performing assets is taken from the Reserve Bank of India publications.
 - NPAs are changing with the time. The study is done in the present environment without foreseeing future developments.
 - This study is only restricted to Punjab National Bank.
 - The result of the study may not be applicable to any other banks.
 - Since the part of the study is based on their perceptions, the findings may change over the years in keeping with the changes in environment factor.

VII. SOURCES OF WORKING FUNDS

The PNB derives its working fund from Share capitals, Reserves, Deposits from the public and other institutions and Borrowings and refinance. The optimum size of working funds and bank's efficiency in strategically applying the funds has a long term impact on the volume of business. It is extremely desirable for the bank to manage the working funds prudently in such a way as to maintain the cost of total working funds at the optimum level. It is obvious that higher income earned at lower cost ensures profitability.

Table 1 Sources of Working Funds

| Year | Share Capital | | Reserve & Surplus | | Deposit | | Borrowings | | Working Fund | | Trend on Working Fund |
|---------|---------------|------|-------------------|------|-----------|-------|------------|-------|--------------|-----|-----------------------|
| | Rs | % | Rs | % | Rs | % | Rs | % | Rs | % | |
| 2011-12 | 339.18 | 0.07 | 28864.66 | 6.33 | 384408.22 | 84.25 | 42645.42 | 9.35 | 456257.48 | 100 | 100 |
| 2012-13 | 353.47 | 0.07 | 34115.56 | 7.09 | 399000.16 | 83.03 | 47089.98 | 9.79 | 480559.17 | 100 | 105.86 |
| 2013-14 | 362.07 | 0.06 | 37731.15 | 6.76 | 461203.53 | 82.60 | 59033.31 | 10.57 | 558330.06 | 100 | 119.94 |
| 2014-15 | 370.91 | 0.06 | 41668.53 | 6.76 | 515245.43 | 83.57 | 59204.76 | 9.60 | 616489.63 | 100 | 131.24 |
| 2015-16 | 392.72 | 0.05 | 41411.53 | 5.96 | 570382.64 | 82.20 | 81673.74 | 11.77 | 693860.63 | 100 | 144.33 |
| Average | | 0.06 | | 6.58 | | 83.13 | | 10.22 | | | |

Source: Compiled from Annual reports of the PNB from 2011-12 to 2015-16.

Interpretation

The sources of working funds of PNB are shown in Table 1. It shows that the share of share capital to the working funds continues to be increasing. However the actual size of share capital in relation to total working funds declined from 0.07 percent to 0.05 per cent in 2015-16. The reserve and surplus, has gone up from Rs. 28864.66 crores to Rs. 41411.53 crores, its percentage to total working funds shows fluctuations. Reserve and surplus stand at 6.58 percent on an average during study period. Similarly deposits of PNB registered a phenomenal increase from Rs. 384408.22 crores to Rs. 570382.64 crores in 2015-16. However, the percentage share of deposits to working funds shows a small decline during the study period. This is because of high increase in the other components of its working funds. On the whole the average (83 percent) show that deposits is the single major source of working fund. Therefore careful measures to be taken for the deployment of cheap sources of funds secured through deposits channels determines the successful functioning of PNB. The borrowings, has gone up from Rs. 42645.42 crores to Rs. 81673.74 crores. Though it has shown a remarkable two-fold increase, its percentage to total working funds shows fluctuations.

VIII. DEPLOYMENT OF WORKING FUNDS

Table 2 Deployment of Working Funds

| Year | Cash balance with RBI | | Investment | | Loan & Advances | | Fixed Assets | | Other Assets | | Total Assets | | Trend on Total Assets |
|---------|-----------------------|------|------------|-------|-----------------|-------|--------------|------|--------------|------|--------------|-----|-----------------------|
| | Rs | % | Rs | % | Rs | % | Rs | % | Rs | % | Rs | % | |
| 2011-12 | 18507.64 | 4.03 | 125746.34 | 27.40 | 301346.34 | 65.67 | 3217.14 | 0.70 | 10015.50 | 2.18 | 458832.96 | 100 | 100 |
| 2012-13 | 17292.51 | 3.56 | 134733.99 | 27.73 | 320218.45 | 65.92 | 3422.36 | 0.70 | 10069.27 | 2.07 | 485736.58 | 100 | 105.86 |
| 2013-14 | 22406.14 | 4.07 | 149224.70 | 27.11 | 366073.21 | 66.51 | 3490.44 | 0.63 | 9166.14 | 1.66 | 550360.63 | 100 | 119.94 |
| 2014-15 | 24435.78 | 4.05 | 156761.66 | 26.03 | 404614.06 | 67.19 | 3655.77 | 0.60 | 12720.46 | 2.11 | 602187.73 | 100 | 131.24 |
| 2015-16 | 26492.19 | 4.00 | 165126.48 | 24.93 | 446083.03 | 67.36 | 5308.12 | 0.80 | 19225.95 | 2.90 | 662235.77 | 100 | 144.33 |
| Average | | 3.94 | | 26.64 | | 66.53 | | 0.69 | | 2.19 | | | |

Source: Compiled from Annual reports of the PNB from 2011-12 to 2015-16.

Interpretation:

The deployment of working funds of PNB is shown in Table No. 2. It shows that share of Cash balance with RBI decrease in 2012-13 than increase continuously. Investment has gone up from 125746.34 crore to 165126.48 crore. The actual size of investment in relation to total assets declined from 27.40 percent to 24.93 percent. Its stand at 26.64 percent on an average during study period. Similarly Loan and advances increase from 301346.34 crore to 446083.03 crore. However, the percentage shares of loan and advances to total assets increasing. On the whole the average 66.53 percent show that loan and advances single major deployment of working fund. Share of fixed assets increase continuously. It stands only 0.69 percent on an average during study period. The percentages of other assets are increasing from 2.18 percent to 2.90 percent. It can be concluded from the analysis of this table that PNB has been managing its working funds very prudently.

IX. ANALYSIS OF GROSS NPA RATIO AND NET NPA RATIO:

Table No. 3 Gross NPA ratio and Net NPA ratio of PNB

(Rs. In Crore)

| Year | Gross NPA | Gross Advances | Gross NPA Ratio | Net NPA | Net Advances | Net NPA Ratio |
|----------------|-----------|----------------|-----------------|---------|--------------|---------------|
| 2011-12 | 8720 | 297610 | 2.93 % | 4454 | 293775 | 1.52 % |
| 2012-13 | 13466 | 315358 | 4.27 % | 7237 | 308796 | 2.35 % |
| 2013-14 | 18880 | 359620 | 5.25 % | 9917 | 349269 | 2.85 % |
| 2014-15 | 25695 | 392290 | 6.55 % | 15397 | 380534 | 4.06 % |
| 2015-16 | 55818 | 432698 | 12.90 % | 35423 | 412326 | 8.61 % |
| Average | | | 6.38 % | | | 3.88 |
| SD | | | 1.55 | | | 2.50 |
| CV | | | 24.29% | | | 64.46% |

Source: Compiled from Annual reports of the PNB from 2011-12 to 2015-16.

Interpretation:

It is observed from the table no.3 the Gross NPA ratio has shown a increasing trend in PNB from 2011-12 to 2015-16. Gross NPA ratio of PNB increased from 2.93 percent to 12.90 percent. Though it has shown a remarkable six-fold increasing trend. The average of gross NPA ratio is 6.38 percent. The standard deviation of gross NPA ratio is 1.55 and coefficient of variance of gross NPA ratio is 24.29 percent. Net NPA ratio has shown a increasing trend in PNB from 2011-12 to 2015-16. Net NPA ratio increased from 1.52 percent to 8.61 percent. The average of net NPA ratio is 3.878. The standard deviation of net NPA ratio is 2.50 and coefficient of variance of net NPA ratio is 64.46 percent. An intensive Assets Quality Review conducted to clean up the stressed by the PNB led to increased provision. As a result, the bank's gross NPA and net NPA rapidly increased.

Table No. 4 NET PROFIT AND NET NPA

(Rs. In Crore)

| Year | Net Profit | Net NPA |
|------------------------|--------------|---------|
| 2011-12 | 4884 | 4454 |
| 2012-13 | 4748 | 7237 |
| 2013-14 | 3343 | 9917 |
| 2014-15 | 3062 | 15397 |
| 2015-16 | -3974 | 35423 |
| Correlation (r) | -0.81 | |

Interpretations:

It is observed from the above table no. 4 that the correlation is equal to -0.81. It means that there is a high degree of negative correlation between net profit and net NPA. Thus null hypothesis is rejected. It means that

while NPA is increasing, the net profit is decreasing. It shows weak position of bank. As we already know that there are two types of customers such as good and bad. Good customers leads to increase in profit by paying interest and principal amount timely while the bad customers leads to increase in NPA by not paying interest and installment amount timely. Thus if there is good management in the bank then the amount of NPA will decrease and net profit will increase. The main reason of increasing NPA is the mismanagement of bank. Maximum amount of NPA is due to the loan given to the priority sector especially to agriculture sector and SSI. There is high degree of negative correlation between net NPA and net profit. Net profit of PNB starts decreasing from 2012-13. The main reason of this decreasing is the large amount of NPA during this time period. It leads to adverse effect on profitability of bank and the bank is unable to give loans to the new customers.

X. RESEARCH FINDINGS

- The fund blocked in as Gross NPA is huge amount of 55818 crore during the year 2015-16. But there is no time frame and follow up to recover the blocked amount.
- The Gross NPA level during the study period is quite alarming; it is negative sign to note that Gross NPA ratio increasing from 2.93 percent in 2011-12 to 12.90 percent in 2015-16.
- Net NPA ratio shows a marked rising trend during study period. It increases from 1.52 percent in 2011-12 to 8.61 percent in 2015-16. Clearly, this is an undesirable and disturbing aspect.
- There is a high negative correlation between Net NPA and Net Profit. It leads to adverse effect on profitability of bank.

XI. RESEARCH SUGGESTIONS

- Bank management may possess specialized credit rating agencies to finalize the borrowing capacity of the potential borrowers before offering credit to the needy people.
- Bank should exercise proper pre sanction scrutiny and post sanction supervision and control.
- Bank should conduct loan recovery camp in certain time period.
- Bank should provide training and awareness programs regarding the replacement of loans and effective use of funds.

XII. CONCLUSION

The problems of Non-performing assets (NPAs) are a serious issue and danger to Public banks, because it destroys the sound financial position of them. The customers and the public would not keep trust on the banks any more if the banks have higher rates of NPAs. So the problem of NPAs must be handled in such a manner that would not ruin the financial positions and affect the image of the banks. Results of study through light on the level of non-performing assets of Punjab National Bank. It finds that level of NPAs both gross and net is increasing trend. It also finds that there is a negative relationship between Net profits and NPA of PNB. This is because of mismanagement and wrong choice of client. To improve the efficiency and profitability, the NPA has to be reduced further.

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