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Banks vulnerable to profit decline amid rising bad loans: IMF

By: PTI | Washington | Updated: October 6, 2016 2:04 PM

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Gross NPAs of public sector banks have surged from 5.43 per cent (Rs 2.67 lakh crore) of advances in 2014-15 to 9.32 per cent (Rs 4.76 lakh crore) in 2015-16. (Source: Reuters)

Indian banks are vulnerable to further decline in profits as they face slow credit growth and elevated non-performing assets, IMF has said, calling for “additional and more timely action” to deal with the problem of bad loans.

“Banking systems are vulnerable to further declines in growth or profits, particularly in countries at later stages of the credit cycle (such as India), where slowing credit growth and risks from elevated levels of non-performing loans are most acute,” said the International Monetary Fund’s Global Financial Stability report.

IMF said bank loan-loss reserves have fallen short of the expected loss on non-performing loans under the current debt- at-risk in India

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It said the potential losses arising from adverse deleveraging would require additional provisions for many banking systems and the pressure is more acute in India where loan-loss reserves are low relative to potential losses.

IMF called for swift and transparent recognition of non- performing assets to ensure good health of banking system.

“Some, such as India, are taking steps to reduce non- performing loans, but additional and more timely action is needed,” it said.

The Indian banking sector, particularly public sector banks, have seen a sharp rise in their NPAs in the last couple of years.

The Reserve Bank has already nudged lenders to set aside more funds for stressed loans and clean up their balance sheet by March 2017.

To deal with the bad loan problem, IMF has suggested that corporatae insolvency frameworks should be upgraded, including by facilitating out-of-court settlement and debt-for-equity swaps, with well-defined and transparent rules. Also contingency plans to manage corporate distress should be put in place.

“This should include a timely, market-based restructuring framework that minimises moral hazard while providing for limited state support if necessary,” IMF said.

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Where available, banks should draw on their capital reserves to cushion losses.

“But where these reserves are insufficient, policymakers will have to balance necessary prudential tightening against the risk of being excessively procyclical,” IMF said.

corporate strains will erode banks' asset quality.

“Policymakers should proactively monitor and address corporate vulnerabilities, particularly those arising from excess leverage,” it said.

The IMF report further said reforms to macroprudential and supervisory frameworks should be accelerated to ensure timely and effective responses to these challenges.

“Enhanced supervision of banks will be needed, requiring better coordination among institutions and central banks in some countries,” it said.

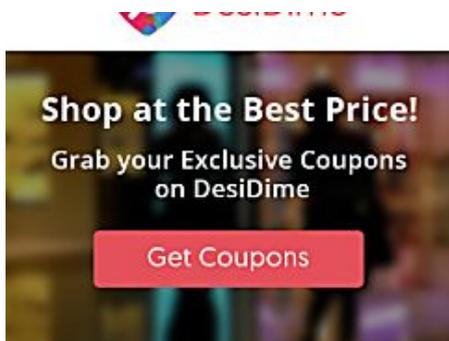
IMF also said that while India continues to benefit from a stable political environment.

Many lenders including Bank of India, Dena Bank and Central Bank of India have reported losses for the quarter ended June 30, due to a sharp jump in provisions for NPAs on account of an asset quality review mandated by the **RBI** in December.

In a bid to shore up cash-strapped public sector banks, the government in August announced infusion of Rs 22,915 crore capital in 13 lenders including SBI and Indian Overseas Bank to revive loan growth that has hit a two-decade low.

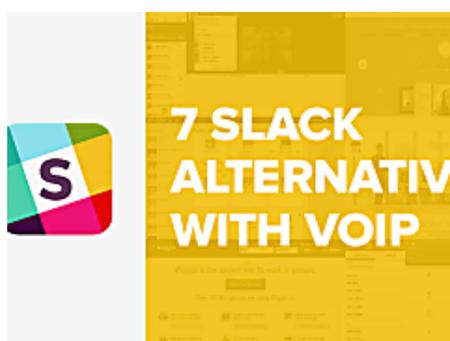
This is the first tranche of capital infusion for the current fiscal and more funds would be provided in future depending on the performance of PSBs.

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