

Impact Of Frauds On Npas And Profitability Of Banks In India

Pawan^{1*}, Swati Singh²

¹Assistant Professor, Hierank Business School, Noida Sector - 62

²Dean Administration, Hierank Business School, Noida Sector -62

*Corresponding Author:- Pawan

^{*}Assistant Professor, Hierank Business School, Noida Sector - 62

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Abstract

Banks serve as engines that guide the money market, financial sector, and economic growth processes. The Indian banking sector has grown at a rapid rate, particularly as we approach the fourth industrial revolution. This, however, has not been without its share of difficulties. Frauds in Indian banks have been on the rise in tandem with the rapidly increasing banking business, and there is an urgent need to restructure the banking sector in India, considering recent scams involving billions of rupees. The purpose of this study is to assess and analyse the current trend of banking frauds and their role in the on-going rise of non-performing assets in India. The study also aims to shed insight on the impact of escalating bank frauds on the banking sector's profitability in India. The report states that the number of frauds affecting the Indian banking sector has been steadily increasing in recent years, resulting to an increase in nonperforming assets (NPAs) and negatively harming the banking sector's profitability. The only way to restore the trust of Indian banks and give the banking sector a facelift is for authorities to take tough action and find new ways to prevent and reduce fraud.

Keywords: Frauds, Non-Performing Assets, Net profit, Schedule Banks

1. INTRODUCTION

The financial system of a country has a significant impact on the economy's stability. The financial institution in a financial system is one of its most important components. Any financial system deception will shake an economy's basis. Banking fraud has a long history, dating back to the founding of the bank. Traceable proof may be found in Indian banking history literature. Few banking books mention the various types of frauds that existed in the 18th century, such as loan disbursement fraud, accounting and clerical frauds, and corruption. The Presidency Bank of Bombay's fall in 1890 is an example of a bank failure caused by mismanagement and credit fraud. Table 1 shows the current scenario of frauds which is rising every year from 2016-20 with a small decline in number of frauds in 2020-21.

Table: 1 Fraud in Indian Banking Industry

Year	No. of Frauds	Fraud amount
16-17	5067	23930
17-18	5916	41168
18-19	6799	71543
19-20	8707	185644
20-21	7363	138422

Source: RBI

Figure 1: Number of Frauds and Amount involved (Crores)

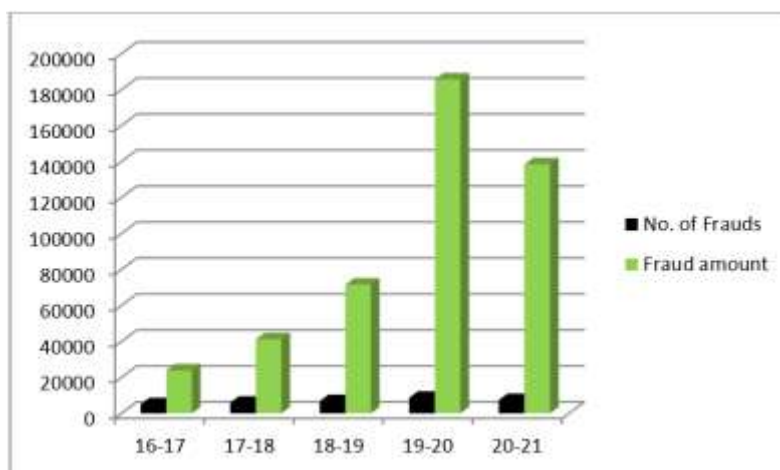


Figure 1 Represent that number of fraud cases increase year on year from 2016 till 2020. But there is small decline in number of frauds cases as well as amount involved in 2021 which shows that banks are trying to control the frauds in banking sector because the maximum cases can be seen in 2019-20 which is an alarming situation for banking sector which needs to be controlled and efforts can be seen in 2020 -21.

2. LITERATURE REVIEW

Rodney D'Silva, (2019) studied the effects of fraud in the Indian banking sector. Secondary data was used in this paper. The goal of this study was to assess and analyse the current fraud trend in India's banking sector and to look into the role of fraud in the rising number of nonperforming assets in the Indian banking system. The goal of the study was to determine the impact of escalating bank frauds on the banking sector's profitability in India.

Mamta Shah, (2019), A Case Study on the Rise in Banking Frauds in India was researched. Their goal was to figure out what was causing various forms of banking frauds. And to figure out multiple ways to stop these frauds so that different interests are protected. He came to the conclusion that there are numerous grounds for fraud, including a weak regulatory structure, carelessness on the part of employees, a lack of effective top-level supervision, wrong use of technology, a lack of consumer and employee awareness, and bad coordination.

Sharma et al., (2017), did an empirical study on banking frauds in India, with a focus on the impact of employee awareness in banking frauds. Primary data was used in this paper. The goals were as follows: The goal of the study is to determine the level of internal execution. It aims to distinguish between procedural frauds and other causes of bank frauds, and the study looks to learn about bank employees' attitudes toward.

Kaur . J,(2016), The association between ethical environment and organisational commitment is discovered in his paper Exploring Relationships Among Ethical Climate Types and Organizational Commitment: A Case of Indian Banking Sector. The Indian banking industry is facing significant challenges, including an increase in bank fraud and a high rate of employee turnover.

3. OBJECTIVE OF STUDY

- i To investigate the growing trend of fraud in the Indian banking sector.
- ii To investigate the role of fraud in the rising number of nonperforming assets (NPAs) in the Indian banking system.
- iii To investigate the impact of fraud on the Indian banking sector's profitability.

4. RESEARCH METHODOLOGY

The current research is entirely based on secondary data. For this study, data was gathered from the RBI website, yearly reports, government publications, academic journals, archival RBI speeches, and newspapers. The history and current state of the banking industry in India, as well as the different challenges that plague this sector, have been studied using RBI Financial Stability Reports.

5. HYPOTHESIS

H1: Frauds do not have a significant impact on Non-Performing Assets in the Indian banking sector.

H2: there is no significant impact of frauds on profitability of Indian banking sector.

6. DATA ANALYSIS

Table2. Number of Frauds and amount involved of all Scheduled Commercial Banks

FRAUDS IN SCHEDULE COMMERCIAL BANKS										
Years	2016-2017		2017-2018		2018-2019		2019-2020		2020-2021	
Banks	No. of Fraud	Amt	No. of Fraud	Amt	No. of Fraud	Amt	No. of Fraud	Amt	No. of Fraud	Amt
Public Sector Banks	2709	19530	2885	382608	3568	63283	4413	148400	2903	81,901
Private Sector Banks	1625	3983	1975	24782	2286	6742	3066	34211	3710	46335
Foreign Banks	725	80	974	2561	762	955	1026	972	521	3315
Financial Institution	6	335	12	1647	28	553	15	2048	25	6839
Small Finance Banks	0	0	65	62	115	8	147	11	114	30
Payments Banks	2	2	3	9	39	2	38	2	88	2
Local Area Banks	0	0	2	0.04	1	0.02	2	0.43	2	0
Total	5067	23930	5916	411670	6799	71543	8707	185644	7363	138422

Table2: Shows the fraud in all the schedule commercial banks which comprise of public sector banks, private sector banks, foreign banks, payment banks and local area banks. The total number of frauds was more in public sector banks as compared to private and other sector banks. Similarly the amount involved in fraud was highest 2017. If we look the trend of frauds in private sector banks it is also rising year on year and was highest in 2021.

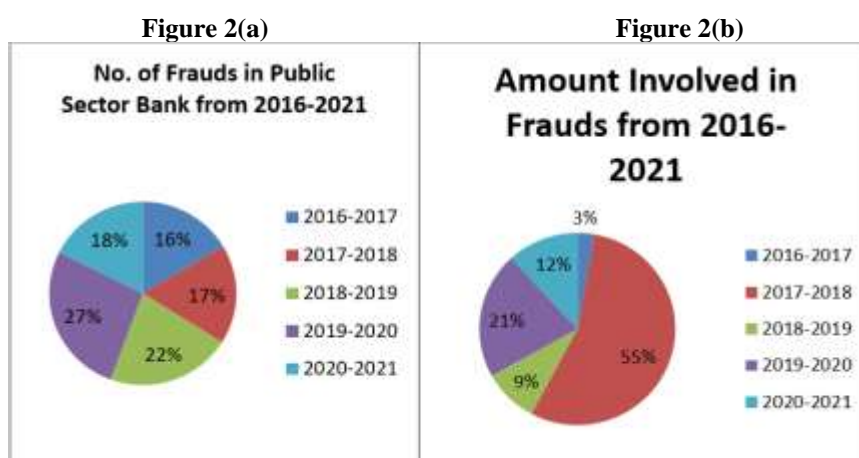


Figure 2 (a) Number of fraud in public sector banks from 2016-2021. It shows that maximum no. of frauds in Public sector bank was in 2019 comprising of 27% of total fraud. While in figure 2(b) represents amount involved in fraud and it was highest 55% in 2017-2018.

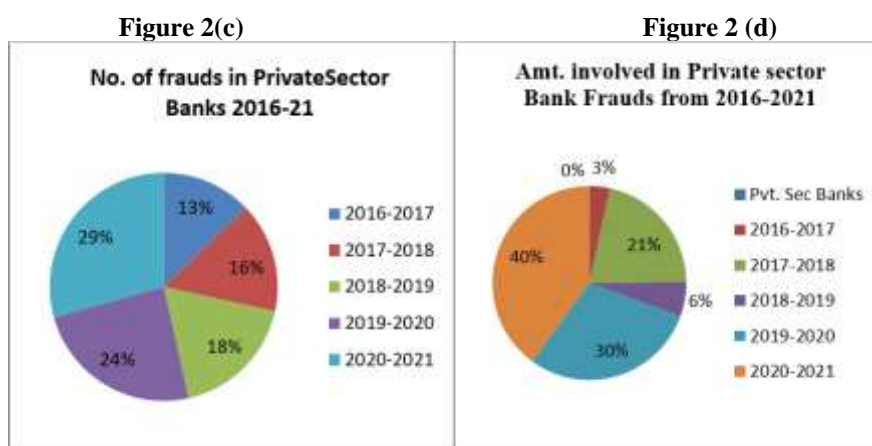


Figure 2(c) shows that in Private sector bank no. of fraud was maximum in 2020-2021 i.e. 29% which was higher than public sector bank. While figure 2(d) shows that maximum amount of fraud involved in private sector was also during 2020-2021 i.e. 40%.

Figure 2(e)

Figure 2(f)

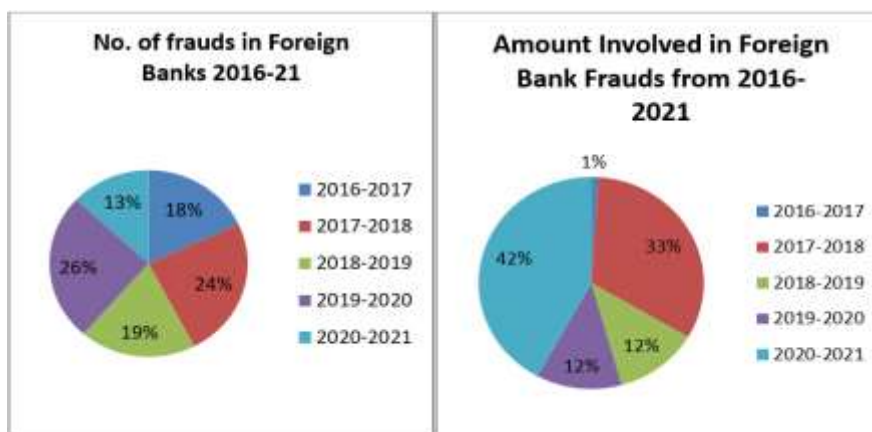


Figure 2(e) shows no. of frauds in foreign banks which was highest in 2019-2020 comprising of 26%. Figure 2(f) shows maximum amt. of fraud in foreign bank was in 2020-2021 i.e. 42%.

Table 3: Gross Non Performing Assets and Gross Advances

YEAR	GROSS NPA	GROSS ADVANCE	Gross NPAs to Gross Advances Ratio (%)
2016-17	790268	8476705.25	9.32
2017-18	1036187.19	9266209.56	11.18
2018-19	933608.86	10287085.25	9.08
2019-20	896082.52	10918917.66	8.21
2020-21	835051.42	11399607.98	7.33

Source: www.rbi.org.in

Table 3 provides a comparative analysis of gross non-performing assets and gross advances. It is clearly seen that gross NPA start declining after 2018 till 2021. Gross NPA was maximum during 2017-2018. While growth in deposit have risen steadily over the years. The ratio between gross NPA and Gross Advances was also declining from 2018 onwards.

Impact of fraud on Gross NPA with Regression Analysis

Regression Statistics	
R Square	0.594989416
Coefficient	660411.5683
P-value	0.004760559

Source: Authors Compilation

For the purpose of regression analysis, amount involved in frauds is considered as independent variable and Gross NPAs are considered as dependent variable. R Square is 0.5949 which implies that 59.49% variations in Non-Performing Assets are explained by frauds. It is found that frauds have a significant impact on Non-Performing Assets at 5 % level of significance. Coefficient Value is positive indicating that increase in frauds will lead to a corresponding rise in NPAs. We therefore reject the null hypothesis and conclude that frauds have a significant impact on Non-Performing Assets in the Indian banking sector

Table 4: Profitability of All Scheduled Banks

Financial Years	Net Profit
16-17	43899.49
17-18	-32437.7
18-19	-23397.4
19-20	11244.72
20 -21	122297.65

Source: www.rbi.org.in

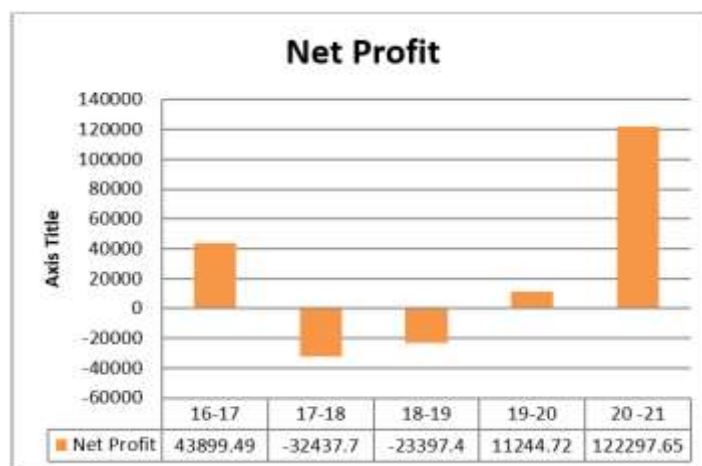


Figure 4: Profitability of All Schedule Banks

Impact of Frauds on Profitability of the Indian Banking Sector with Regression Analysis

<i>Regression Statistics</i>	
R Square	0.292582569
coefficient	-45021.18116
P-value	0.629338563

For the purpose of regression analysis, amount involved in frauds is considered as independent variable and profitability is considered as dependent variable. R Square is 0.2925 which implies that 29.25% variations in profitability are explained by frauds.. Coefficient Value is negative indicating that increase in frauds will lead to a corresponding decrease in profitability. We therefore reject the null hypothesis and conclude that frauds have a significant impact on profitability of the Indian banking sector.

FINDINGS

- Among all the commercial banks public sector banks have the maximum number of frauds.
- Gross NPA was maximum during 2017-2018.
- Gross advances are rising steadily over past 5 years.
- R Square is 0.5949 which implies that 59.49% variations in Non-Performing Assets are due frauds.
- It is found that frauds have a significant impact on Non-Performing Assets at 5 % level of significance.
- R Square is 0.2925 which implies that 29.25% variations in profitability are explained by frauds.

CONCLUSION

It is undeniable that the post-liberalization age has brought new colours of growth to the Indian banking sector, but it has also brought new issues, one of which is the surge in fraud and nonperforming assets (NPAs). This unwelcome trend of increasing fraudulent operations in the financial sector not only results in losses for the banks involved, but also has a negative impact on their credibility. Banks and their consumers face serious financial difficulties because of fraud and fraudulent operations, and the amount of money available for economic development is significantly reduced.

It can be concluded from above study that

- In proportion to the increase in the number of frauds, the money involved has increased dramatically.
- The majority of banking frauds involve advances, which is a source of concern for Indian banks.
- In the Indian banking sector, fraud has a considerable impact on non-performing assets.
- Frauds have a substantial influence on profitability of the Indian banking sector.

SUGGESTIONS

- Before authorising loans, PSBs should establish an internal rating agency to conduct a thorough review of large-scale projects.
- After making a loan, banks should continue to monitor the company's ability and be able to determine whether it is going to go bankrupt. Banks can then sell the assets before the loans become non-performing.
- Strict penalties for bank employees and anyone who collude with fraudsters may be beneficial.

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