Chart III.9: Credit, Investments and Deposits of Scheduled Commercial Banks

(Annual Accretion)

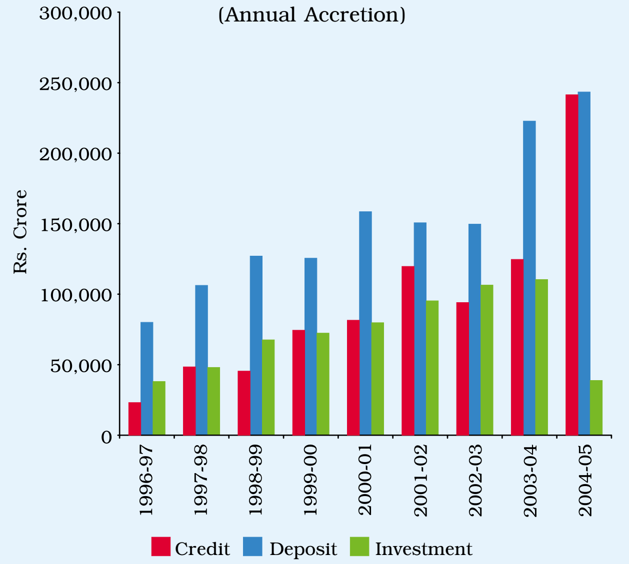
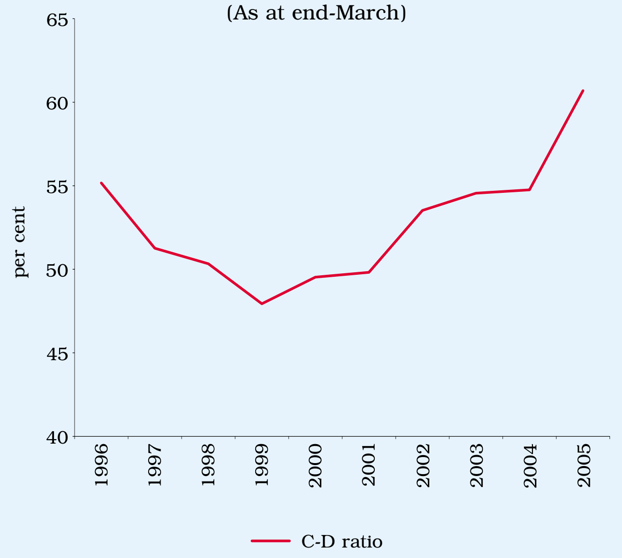


Chart III.11: Credit-Deposit Ratio of Scheduled Commercial Banks

(As at end-March)



a high of over 130 per cent on two occasions (Chart III.10).

3.43 The C-D ratio (in terms of outstandings) of SCBs which declined from 55 per cent in 1995-96 to 48 per cent by 1998-99, increased sharply to touch a high level of 60 per cent at end-March 2005 due to sharp increase in credit during the year (Chart III.11).

3.44 Among bank-groups, the new private sector banks had the highest C-D ratio, followed by foreign banks, old private sector and public sector banks (Chart III.12).

3.45 The C-D ratio, which implies greater credit orientation of banks, is used as a credit efficiency indicator for analysing the role of banks in promoting productive sectors and contributing to economic growth. In a bank-based financial system, the C-D ratio is regarded as an aggregative measure for gauging the effectiveness of credit delivery system. Although the deployment of credit and the time path of C-D ratio, in general, are influenced by the structural transformation of the economy, the role of credit culture and banks' lending policy have an inherent impact on the size of the ratio.

Chart III.10: Credit-Deposit and Investment-Deposit Ratios of Scheduled Commercial Banks

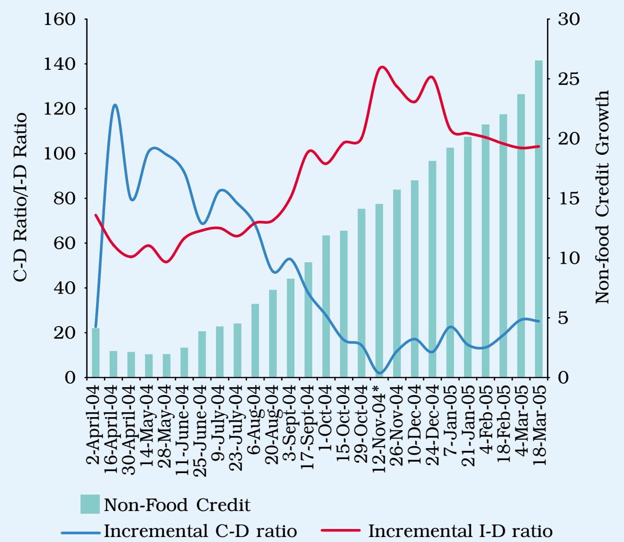


Chart III.12: Credit-Deposit Ratio – Bank Group-wise

(As at end-March)

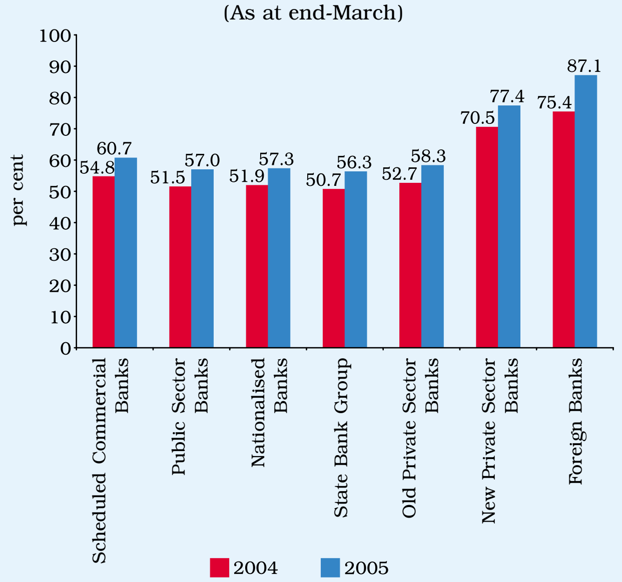


Table III.17: Bank Group-wise Maturity Profile of Select Liabilities/Assets
(As at end-March)

(Per cent)

Assets/Liabilities	Public Sector Banks		Old Private Sector Banks		New Private Sector Banks		Foreign Banks	
	2004	2005	2004	2005	2004	2005	2004	2005
1	2	3	4	5	6	7	8	9
I. Deposits								
a) Up to 1 year	34.4	36.3	51.2	53.3	50.7	54.3	46.2	54.1
b) Over 1 year and up to 3 years	37.8	35.1	37.1	37.6	42.9	42.4	45.6	39.3
c) Over 3 years and up to 5 years	11.7	12.0	4.4	3.4	4.0	2.3	0.7	0.9
d) Over 5 years	16.1	16.6	7.3	5.7	2.4	0.9	7.5	5.7
II. Borrowings								
a) Up to 1 year	82.4	83.2	89.7	80.7	46.4	50.4	85.3	84.5
b) Over 1 year and up to 3 years	14.0	9.6	5.3	4.1	36.4	27.9	11.9	12.3
c) Over 3 years and up to 5 years	2.6	5.3	2.8	7.1	8.3	13.3	2.5	3.3
d) Over 5 years	1.0	2.0	2.2	8.2	8.9	8.4	0.3	–
III. Loans and Advances								
a) Up to 1 year	40.0	37.3	40.5	42.3	35.4	40.2	57.3	55.9
b) Over 1 year and up to 3 years	33.0	35.3	36.1	33.7	31.0	31.4	16.3	18.0
c) Over 3 years and up to 5 years	12.1	11.8	10.3	9.0	12.5	9.5	7.7	6.5
d) Over 5 years	14.9	15.5	13.1	15.0	21.1	18.9	18.7	19.7
IV. Investment								
a) Up to 1 year	10.4	13.2	18.0	21.9	45.0	47.4	45.8	53.2
b) Over 1 year and up to 3 years	11.8	12.5	10.2	11.1	27.3	27.3	30.7	27.1
c) Over 3 years and up to 5 years	14.5	17.2	10.4	12.6	6.6	6.8	8.5	6.1
d) Over 5 years	63.3	57.1	61.4	54.4	21.1	18.6	15.0	13.6

– : Nil/Negligible.
Source : Balance sheets of respective banks.

Maturity Profile of Assets and Liabilities of Banks

3.46 The maturity structure of commercial banks' assets and liabilities reflects various concerns of banks pertaining to business expansion, liquidity management, cost of funds, return on assets, asset quality and also risk appetite during an industrial upturn. In general, major components of balance sheet, including deposits, borrowings, loans and advances and investments, for all bank groups encompassed a non-linear portfolio structure across the spectrum of maturity during 2004-05. Furthermore, for all banks groups, the maturity structure of loans and advances depicted a synchronous behaviour with that of deposits. The maturity structure of deposits and that of investments differed across bank groups. PSBs and old private banks held a larger share of their investment in higher maturity bucket, particularly more than five-year maturity bucket, while private sector and foreign banks held more than 50 per cent of their investments in up to one-year maturity bucket (Table III.17).

3.47 The residual maturity classification of consolidated international claims reveals that banks continued to prefer to invest in/lend for short-term purposes, particularly 'up to 6 months' period whose share in total claims increased by 3.4 percentage points to 73.6 per cent during 2004-05 (Table III.18).

Table III.18: Maturity (Residual) Classification of Consolidated International Claims of Banks

(Amount in Rs. crore)

Residual Maturity	Amount outstanding as at end-March		
	2003	2004	2005
1	2	3	4
Up to 6 months	59,831 (65.7)	54,879 (70.2)	54,665 (73.6)
Over 6 months and up to 1 year	6,412 (7.0)	3,798 (4.9)	6,448 (8.7)
Over 1 year and up to 2 years	4,247 (4.7)	2,872 (3.7)	3,165 (4.3)
Over 2 years	18,861 (20.7)	14,948 (19.1)	8,785 (11.8)
Unallocated	1,710 (1.9)	1,627 (2.1)	1,174 (1.6)
Total	**91,061**	**78,124**	**74,238**

Note : 1. Unallocated residual maturity comprises maturity not applicable (e.g., for equity) and maturity information not available from reporting bank/-branches.
2. Figures in brackets are percentages to total.
3. Based on CBS (Consolidated Banking Statistics)-immediate country risk basis.

3. Off-Balance Sheet Operations of Scheduled Commercial Banks

3.48 Off-balance sheet (OBS) operations of SCBs rose sharply by 60.2 per cent in 2004-05 over and above the increase of 55.3 per cent in 2003-04 and 41.3 per cent in 2002-03. Accordingly, the share of off-balance sheet liabilities in total liabilities increased to 119.7 per cent in 2004-05 from 90.8 per cent in 2003-04. Banks' off-balance sheet exposures have been growing on account of several factors (Box III.4).

Box III.4: Off-Balance Sheet Exposures of Banks

Banks enter into OBS transactions for extending non-fund based facilities to their clients, balance sheet risk management and generating profits through leveraged positions. OBS exposures of banks have witnessed a phenomenal spurt in recent years, reflecting the impact of deregulation, need for risk management, need for diversified income base due to pressure on margin on conventional on-balance sheet items and new opportunities thrown up by technological progress.

OBS exposures essentially take the form of contingent liabilities and derivatives. Contingent liabilities are traditional off-balance sheet exposures, while derivatives, except for traditional forward exchange contracts, have gained prominence in recent years. Like any on-balance sheet exposure, an OBS exposure also exposes a bank to several risks such as credit risk, liquidity risk, market risk and operational risk. Thus, the nature of risks faced by banks in OBS activities is not different from on-balance sheet items. Contingent liabilities such as guarantees and commitments essentially carry credit risk, besides liquidity and operational risk. On the other hand, derivatives transactions expose banks to market risk, liquidity risk and operational risk, although credit risk cannot be entirely ignored.

Schedule 12 of bank's balance sheet on contingent liabilities, designed in1991, does not cover data on new instruments such as derivatives, and needs to be revised in light of the growing use of such OBS exposures. The off-site returns submitted by scheduled commercial banks to the Reserve Bank provide a better picture of the OBS exposures of banks. An analysis of OBS exposures of the banks based on these returns was carried out by the Reserve Bank in December 2004. The main points emerging from the analysis are detailed below:

- Total OBS exposures of the banking system witnessed a significant growth in recent years. Total notional principal amount of OBS exposures of the banking system more than doubled from Rs.8,41,884 crore at end-March 2002 to Rs.18,48,341 crore at end-March 2004 and further to Rs.29,07,457 crore at end-December 2004.

- Letters of credits (LCs) along with guarantees accounted for 80 per cent of total contingent liabilities. The share of LCs in total contingent liabilities steadily increased from around 27 per cent at end-March 2002 to 36 per cent at end-December 2004, while that of guarantees declined from around 58 per cent to 44 per cent during the same period. Banks are exposed to lower risk in LCs which are backed by documents, compared with guarantees. As such, the increasing importance of LCs in total contingent liability portfolio of banks reflects lower contingent risk.

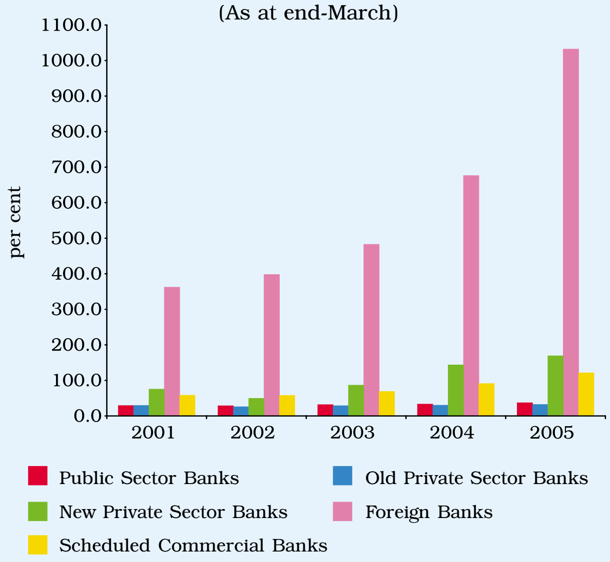
- The spurt in OBS exposures has been fuelled mainly by the sharp increase in the derivatives segment. The share of derivatives in total OBS exposures of the banking system increased from 82.5 per cent in March 2002 to 90.7 per cent in December 2004. In relation to total assets, total OBS exposures of the banking system more than doubled from 57.1 per cent in March 2002 to 137.2 per cent in December 2004.

- The composition of derivatives portfolio of the banking system has undergone a significant transformation since March 2003. Forward foreign exchange contracts, which accounted for 79.6 per cent of total derivatives in March 2002, declined steadily to 49.3 per cent in December 2004. During the same period, the share of single currency interest rate swaps increased from 14.6 per cent to 46.6 per cent. The shift in the composition of contracts and derivatives from the traditional forward foreign exchange contracts to interest rate related contracts has affected the maturity profile of derivatives in recent years. Total contracts and derivatives maturing within one-year horizon, which constituted 84.6 per cent in March 2002, declined sharply to 51.3 per cent in December 2004. The corresponding increase in maturity occurred in '2 to 3 years' segment essentially due to concentration of single currency interest rate swaps in that time band. Recent spurt in derivatives in longer maturity horizon has exposed banks to greater market risk.

- As at end-December 2004, public sector banks accounted for the largest share (64.3 per cent) in total contingent liabilities at the system level, followed by new private banks (19.9 per cent) and foreign banks (12 per cent). The OBS exposures of the banking system are mostly concentrated among 15 banks consisting mainly of foreign banks. The combined share of these 15 banks constituted 78 per cent of total OBS exposures of the banking system. Foreign banks accounted for the largest share (63.7 per cent) in the derivative segment, followed distantly by new private banks (18.1 per cent) and public sector banks (16.3 per cent), respectively.

The risks arising on account of OBS activities of banks are sought to be controlled through a combination of both banks' internal control policies and risk mitigation mechanism imposed by the regulator. The board approved internal control policies covering various aspects of management of risks arising both on- and off-balance sheet exposures is the first line of defence. Holding of minimum defined regulatory capital for all OBS exposures, collection of periodic supervisory data and adequate disclosures in bank balance sheet are some of the major regulatory initiatives undertaken to control and monitor OBS exposures of the banking system.

Chart III.13: Off-Balance Sheet Exposures to Total Liabilities of SCBs
(As at end-March)



3.49 Among bank groups, foreign banks had the highest off-balance sheet exposures, followed by new private sector banks. Public sector banks had a relatively small amount of off-balance sheet exposure (Chart III.13 and Appendix Table III.12).

4. Financial Performance of Scheduled Commercial Banks

3.50 The overall financial performance of the banking sector during 2004-05 remained satisfactory, when viewed in the context of upturn in the interest rate cycle. Banks' continued to earn substantial operating and net profits, *albeit,* lower than the preceding year. However, reduced profits reflected mainly the lower treasury profits due mainly to hardening of sovereign yields. A sharp increase in net interest income driven by increased credit volumes mitigated to a considerable extent the impact of a sharp decline in non-interest income. On the whole, banks were able to weather the impact of rise in interest rates.

Interest Rate Scenario

3.51 Banks' balance sheets comprise largely interest-bearing liabilities and assets and consequently net interest income is the most important driver of profitability of banks. Behaviour of interest rate, therefore, has a direct impact on banks' profitability.

3.52 During 2004-05, while interest rates on term deposits offered by public sector banks for maturities up to one year declined slightly, interest rate on deposits exceeding one year maturity after declining marginally up to December 2004, increased in the last quarter of the year. As a result, the spread between typical deposit rates of 15-29 days and over 3-year tenor offered by public sector banks widened to 200 basis points in March 2005 from 175 basis points a year ago (Table III.19).

3.53 The benchmark prime lending rates (BPLRs) of public sector banks and foreign banks softened somewhat during the year. The spread between the

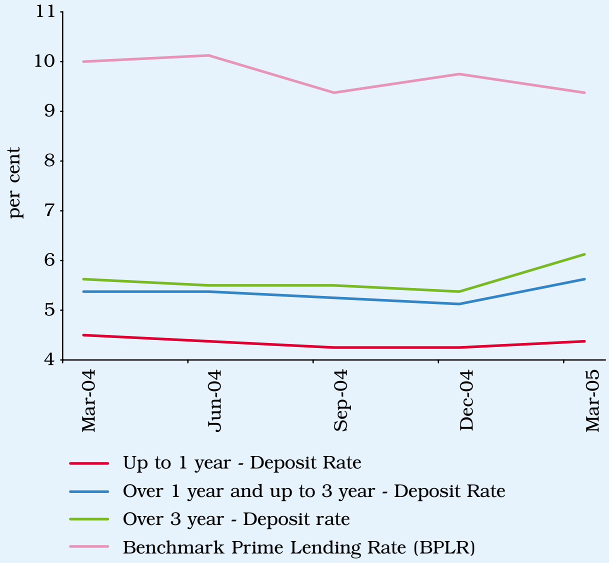
Table III.19: Movements in Deposits and Lending Rates

(Per cent)

Item	March 2003	March 2004	March 2005	September 2005
1	2	3	4	5
I. Domestic Deposit Rates				
Public Sector Banks				
a) Up to 1 year	4.00 - 6.00	3.75 - 5.25	2.75 - 6.00	2.00 - 6.00
b) Over 1 year and up to 3 years	5.25 - 6.75	5.00 - 5.75	4.75 - 6.50	5.25 - 6.25
c) Over 3 years	5.50 - 7.00	5.25 - 6.00	5.25 - 7.00	5.50 - 6.50
Private Sector Banks				
a) Up to 1 year	3.50 - 7.50	3.00 - 6.00	3.00 - 6.25	3.00 - 6.25
b) Over 1 year and up to 3 years	6.00 - 8.00	5.00 - 6.50	5.25 - 7.25	5.00 - 7.00
c) Over 3 years	6.00 - 8.00	5.25 - 7.00	5.75 - 7.00	5.75 - 7.25
Foreign Banks				
a) Up to 1 year	3.00 - 7.75	2.75 - 7.75	3.00 - 6.25	3.00 - 5.75
b) Over 1 year and up to 3 years	4.15 - 8.00	2.25 - 8.00	3.50 - 6.50	3.50 - 6.50
c) Over 3 years	5.00 - 9.00	3.25 - 8.00	3.50 - 7.00	4.00 - 7.00
II. Prime Lending Rates				
Public Sector Banks	9.00 - 12.25	10.25 - 11.50	10.25 - 11.25	10.25 - 11.25
Private Sector Banks	7.00 - 15.50	10.50 - 13.00	11.00 - 13.50	11.00 - 13.50
Foreign Banks	6.75 - 17.50	11.00 - 14.85	10.00 - 14.50	10.00 - 14.50

deposits and the lending rate of PSBs narrowed down slightly, especially in the last quarter of the year, while that of private sector banks firmed up slightly (Chart III.14). However, given the competitive conditions, most of the banks resorted to sub-PLR lending, whose share in total lending of commercial banks, excluding export credit, increased from about 50 per cent in March 2004 to over 60 per cent by March 2005. As at end-March 2005, public sector banks' median (representative) lending rate for the demand and term loans (at which maximum business is contracted) in the range of 9.00-12.50 per cent and 8.35-12.00 per cent, respectively, showed moderation as compared with their corresponding levels of 11.00-12.75 per cent each, in March 2004. The movement in lending rates was in the desired direction keeping in view the concern expressed about downward rigidity in the movement of lending rates in the Mid-term Review of the Monetary and Credit Policy for 2003-04 (Box III.5).

Chart III.14: Spread between Deposit and Lending Rates of Public Sector Banks



Box III.5: Asymmetry in Lending Rate Movement

It is generally believed that banks adjust their lending rates more slowly when interest rates are falling than when they are rising. In other words, banks are apparently sluggish in adjusting the prime lending rate (PLR) to declining market rates. Despite the widespread belief that the PLR adjusts more slowly when interest rates are falling, evidence of asymmetry in the PLR has been mixed. In the case of United States, Arak, Englander and Tang (1984) and Levine and Loeb (1983) find evidence of asymmetric price-setting behavior, while Goldberger (1984) and Forbes and Mayne (1989) find no such evidence. The premise that changes in the discount rate may be important in explaining the behavior of the prime rate is supported by Hendry (1992), who found changes in the Bank of Canada's Bank Rate to be the most important variable in explaining changes in the Canadian prime rate.

With the initiation of financial sector reforms, the lending rates of commercial banks have been gradually deregulated. Keeping in view the international practice on lending rates as also for providing further operational flexibility to commercial banks in deciding their lending rates, a system of benchmark PLR has been adopted by Indian banks since 2004 wherein banks enjoy the flexibility in pricing loans and advances based on market benchmarks. All other lending rates can be determined with reference to the BPLR based on (i) actual cost of funds; (ii) operating expenses; and (iii) a minimum margin to cover regulatory requirement of provisioning/capital charge and profit margin. BPLR continues to be the ceiling rate for credit limit up to Rs.2 lakh.

While the deposit rates of banks have declined from 13 per cent in 1995-96 to about 5 per cent in 2004-05, the average lending rates declined from about 17 per cent to about 10 per cent during the same period. As a result, the spread between the deposit and lending rates has widened by almost one percentage point. The fall in the nominal interest rates have also not kept pace with the declining inflation rate with the result that the real effective lending rates have not declined commensurately. Downward inflexibility of PLR emerged in the recent past as a significant policy issue for the Reserve Bank, especially in respect of credit delivery to small and medium sized borrowers at a reasonable cost. While the introduction of benchmark prime lending rates has, to an extent, addressed the problem of downward rigidity of lending rates, the introduction of sub-PLR lending has resulted in a widening of the spread between the maximum and the minimum lending rates. Widening of interest spread suggests that further efforts are needed to tackle the problem of downward rigidity of lending rates. The continuing reduction in the non-performing asset levels and interest expenditure should enable banks to set the lending rates on a more realistic basis.

Asymmetry of the prime rate is often viewed as an indicator of the market power of banks. At times, this is also explained in terms of financial hierarchy, where firms turn to external finance only after adjusting their internal funds. If bank lending rates rise rapidly when market interest rates are rising, but decline sluggishly when market interest rates are falling, firms may prefer internal finance because the opportunity cost of internal funds moves in tandem with market rates.

Asymmetry in the prime rate might also have implications for the efficacy of monetary policy. In particular, it could help explain why easy monetary policy is less expansionary than restrictive monetary policy is contractionary [Cover (1992) and Rotemberg (1993)]. During periods of falling interest rates, downwardly sluggish bank lending rates would dampen the stimulus that monetary policy could provide to investment spending, whereas in periods of rising interest rates, bank lending rates would generally increase in tandem with market rates.

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3.54 The yield on Government securities with 5-year and 10-year residual maturity hardened by 158 basis points and 150 basis points, respectively, between end-March 2004 and end-March 2005 (Table III.20). Similarly, the yield on securities with 20-year residual maturity increased by 114 basis points from 5.85 per cent to 6.99 per cent during the same period. As the longer-term yields exhibited sharper movements, the tenor spread in the Government securities revealed intra-year variations. The spread between securities with residual maturities of 1-year and 10-year widened from 61 basis points in March 2004 to 114 basis points in March 2005. Similarly, the spread between Government securities with residual maturities of 1-year and 20-year widened from 131 basis points in March 2004 to 148 basis points in March 2005.

3.55 Interest rates in various segment of money market firmed up marginally. At the shorter end of the market, the weighted average call money rate increased by 63 basis points from 4.37 per cent in March 2004 to 5.00 per cent by March 2005. The weighted average discount rate on commercial paper (CP) of 61-90 days maturity increased by 70 basis points from 5.19 per cent to 5.89 per cent.

Cost of Deposits and Return on Advances

3.56 Cost of deposits declined significantly during 2004-05, reflecting largely the impact of significant decline in deposit rates in the last year. In the recent period, the decline in cost of funds has emerged as a notable feature of operations of the banking sector, a trend which continued during 2004-05. Significantly, the cost of borrowings was much lower than the cost of deposits across all bank groups, barring foreign banks. The cost of funds across bank groups declined in the range of 60-70 basis points in 2004-05. The decline in cost of funds was accompanied by a larger decline in return on advances, reflecting mainly the increased lending at sub-PLR rates on account of competitive pressures. As a result, interest spread came under pressure, suggesting that the benefits of low interest rates have begun to percolate to banks' borrowers (Table III.21).

Table III.20: Structure of Interest Rates

(Per cent)

Item	March 2003	March 2004	March 2005	September 2005
1	2	3	4	5
I. Debt market				
1. Government Securities Market				
5 –Year	5.92	4.78	6.36	6.71
10–Year	6.13	5.15	6.65	7.11
II. Money Markets				
2. Call Borrowings (Average)	5.86	4.37	5.00	5.05
3. Commercial papers				
WADR 61 - 90 days	6.53	5.19	5.89	5.89 *
WADR 91-180 days	6.45	4.73	5.87	5.97 *
Range	6.00-7.75	4.70-6.50	5.45-6.51	5.69-7.50
4. Certificates of Deposit				
Range	5.00-7.10	3.87 - 5.16	4.21-6.34	4.66-7.00 @
Typical Rate				
3 Months	–	4.96	5.90	5.90 @
12 Months	5.25	5.16	6.26	5.97 @
6. Treasury Bills				
91 days	5.89	4.37	5.32	5.49
182 days	–	–	–	5.40
364 days	5.89	4.44	5.66	5.79

– : Nil/Negligible.
WADR- Weighted Average Discount Rate.
* : Data pertain to period-ended October 1-15, 2005.
@ : Data pertain to period-ended September 15, 2005.

Table III.21: Cost of Funds and Returns on Funds – Bank Group-wise

(Per cent)

Variable/ Bank Group	Public Sector Banks			Old Private Sector Banks		New Private Sector Banks		Foreign Banks		Scheduled Commercial Banks		
	2003-04	2004-05	2004-05#	2003-04	2004-05	2003-04	2004-05	2003-04	2004-05	2003-04	2004-05	2004-05#
1	2	3	4	5	6	7	8	9	10	11	12	13
1. Cost of Deposits	5.1	4.4	4.4	5.4	4.6	4.2	3.4	3.6	3.1	4.9	4.2	4.2
2. Cost of Borrowings	2.3	2.6	1.3	2.8	2.7	1.5	1.4	4.3	3.5	2.5	2.4	1.7
3. Cost of Funds	5.0	4.3	5.7	5.3	4.6	3.7	3.0	3.8	3.2	4.8	4.1	5.2
4. Return on Advances	7.9	7.0	7.2	8.8	8.0	8.8	7.3	8.3	7.3	8.1	7.2	7.3
5. Return on Investments	8.5	8.2	8.0	8.1	7.7	6.2	5.2	8.5	6.9	8.2	7.8	7.6
6. Return on Funds	8.2	7.6	7.5	8.5	7.9	7.7	6.5	8.4	7.2	8.2	7.4	7.4
7. Spread (6-3)	3.2	3.2	1.8	3.1	3.3	4.0	3.5	4.6	4.0	3.4	3.3	2.2

: Includes the impact of conversion of a non-banking entity into a banking entity.

Note : 1. Cost of Deposits = Interest Paid on Deposits/Deposits.
2. Cost of Borrowings = Interest Paid on Borrowings/Borrowings.
3. Cost of Funds = (Interest Paid on Deposits+Interest Paid on borrowings)/(Deposits+Borrowings).
4. Return on Advances = Interest Earned on Advances / Advances.
5. Return on Investments = Interest Earned on Investments / Investments.
6. Return on Funds = (Return on Advances+Return on Investments)/(Advances+Investments).

Income

3.57 In a rising interest rate scenario, two key financial performance parameters, *viz.*, interest income and non-interest or 'other' income respond differently. As interest rates rise, interest income goes up. However, since banks normally hold a large portfolio of fixed income investments, rise in interest rates depresses bond prices, resulting in decline in banks' trading profits, a major component of 'other income'. Interest income, which is the major source of income, rose sharply by 6.1 per cent (excluding the conversion impact) during 2004-05 as against 2.6 per cent last year mainly due to increased volumes (Table III.22).

3.58 With the diversification of banks' portfolio, 'other income', comprising trading income and fee-based income has evolved as an important source of income for banks over the last few years (Appendix Table III.13). However, during 2004-05, 'other' income, declined sharply by 15.1 per cent (excluding the conversion impact) as against an increase of 25.1 per cent last year mainly due to decline in trading income and marked-to-market (MTM) losses (Table III.23).

Table III.22: Important Financial Indicators of Scheduled Commercial Banks

(Amount in Rs. crore)

Item	2002-03		2003-04		2004-05		2004-05 #	
	Amount	Per cent to Assets	Amount	Per cent to Assets	Amount	Per cent to Assets	Amount	Per cent to Assets
1	2	3	4	5	6	7	8	9
1. Income	1,72,345	10.1	1,83,872	9.3	1,86,703	8.2	1,93,269	8.2
a) Interest Income	1,40,742	8.3	1,44,347	7.3	1,53,127	6.7	1,58,438	6.7
b) Other Income	31,603	1.9	39,525	2.0	33,576	1.5	34,831	1.5
2. Expenditure	1,55,268	9.1	1,61,601	8.2	1,65,998	7.3	1,71,949	7.3
a) Interest Expended	93,596	5.5	87,563	4.4	86,601	3.8	91,537	3.9
b) Operating Expenses	38,067	2.2	43,709	2.2	49,140	2.2	50,048	2.1
of which:								
wage bill	23,610	1.4	26,360	1.3	28,734	1.3	29,032	1.2
c) Provisions and Contingencies	23,605	1.4	30,329	1.5	30,256	1.3	30,364	1.3
3. Operating Profit	40,682	2.4	52,600	2.7	50,962	2.2	51,684	2.2
4. Net Profit	17,077	1.0	22,271	1.1	20,706	0.9	21,320	0.9
5. Net Interest Income/Margin (1a-2a)	47,146	2.8	56,784	2.9	66,526	2.9	66,901	2.8

Note : The number of scheduled commercial banks in 2002-03, 2003-04 and 2004-05 were 93, 90 and 88, respectively.
: Including the impact of conversion of a non-banking entity into a banking entity.

Table III.23: Changes in Income-Expenditure Profile of Scheduled Commercial Banks

(Amount in Rs. crore)

Indicator	2003-04	Per cent	2004-05	Per cent	2004-05 #	Per cent
1	2	3	4	5	6	7
1. Income (a+b)	**11,527**	**6.7**	**2,831**	**1.5**	**9,397**	**5.1**
a) Interest Income	3,604	2.6	8,780	6.1	14,091	9.8
b) Other Income	7,923	25.1	-5,949	-15.1	-4,695	-11.9
2. Expenses (a+b+c)	**6,333**	**4.1**	**4,396**	**2.7**	**10,348**	**6.4**
a) Interest Expenses	-6,034	-6.4	-961	-1.1	3,974	4.5
b) Other Expenses	5,642	14.8	5,431	12.4	6,339	14.5
c) Provisioning	6,725	28.5	-73	-0.2	35	0.1
3. Operating Profits	**11,918**	**29.3**	**-1,638**	**-3.1**	**-916**	**-1.7**
4. Net Profits	**5,194**	**30.4**	**-1,565**	**-7.0**	**-951**	**-4.3**

: Including the impact of conversion of a non-banking entity into a banking entity.

3.59 The composition of 'other income' of SCBs underwent a significant change during 2004-05 due to decline in the share of trading income on investments and increase in the share of fee income and income from foreign exchange operations and miscellaneous income (Chart III.15).

3.60 The share of non-interest income in banks' total income, after showing a continuous increase from 10.7 per cent in 1993 to 21.5 per cent in 2003-04, declined sharply to 18.0 per cent in 2004-05 (Chart III.16).

3.61 Banks' overall income grew by 1.5 per cent in 2004-05 (excluding the conversion impact) as compared with 6.7 per cent in the previous year. On an incremental basis, the contribution of interest income to total income during 2004-05 was 310.0 per cent compared with 31.3 per cent in 2003-04; contribution of 'other income' was negative (Chart III.17).

3.62 Among bank groups, income of PSBs grew at the highest rate, followed by new private sector banks (Appendix Table III.14). Income of foreign banks grew at a nominal rate, while that of old private sector banks declined on account of a small rise in interest income, which was more than offset by a sharp fall in 'other' income. The income of certain PSBs also improved as the Reserve Bank allowed banks to recognise income on an accrual basis in respect of some categories of projects under implementation with time overruns [Appendix Table III.15(A) to (I)].

Chart III.15: Composition of Non-Interest Income of Scheduled Commercial Banks

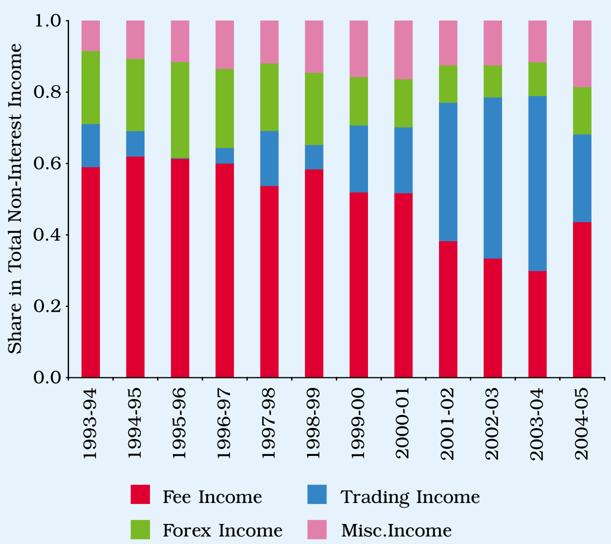


Chart III.16: Interest and Non-Interest Income of Scheduled Commercial Banks

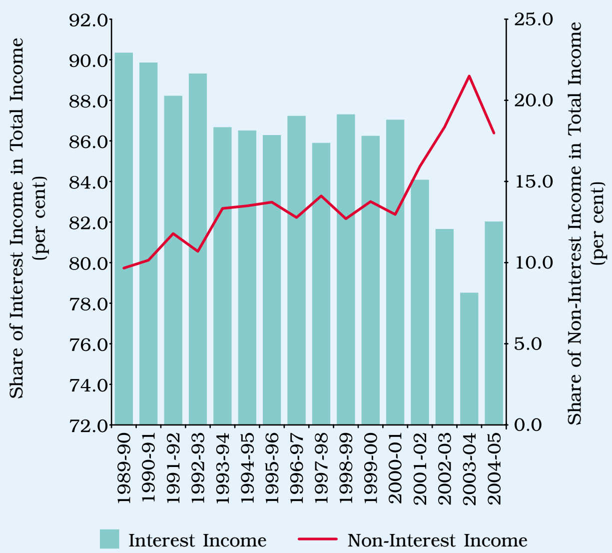
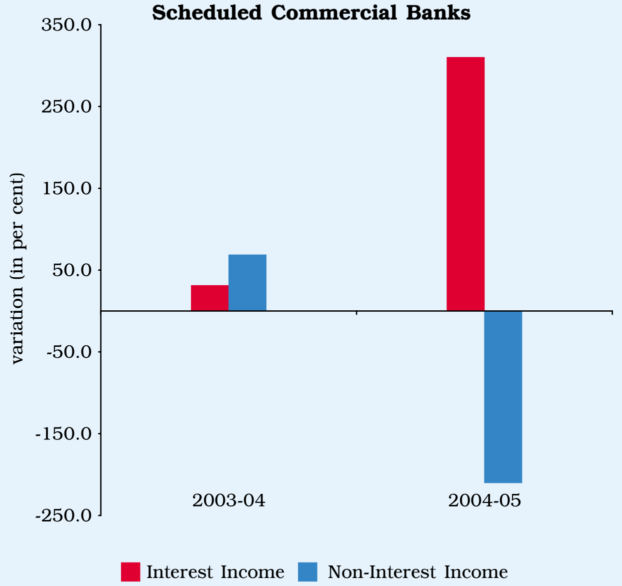


Chart III.17: Sources of Accretion to Income of Scheduled Commercial Banks



Expenditure

3.63 The expenditure of SCBs moved up by 2.7 per cent (excluding the conversion impact) in 2004-05 compared with 4.1 per cent in 2003-04. While interest expended declined by 1.1 per cent (as compared with a decline of 6.4 per cent in the previous year), operating or non-interest expenses increased by 13.7 per cent (as compared with the increase of 12.6 per cent in 2003-04). However, operating expenses as percentage of total assets declined marginally to 2.1 per cent from the previous year's level (2.2 per cent). Banks have been able to contain operating expenditure despite a significant increase in retail loans which, being small, carry higher transaction costs. From the overall profitability viewpoint, operating expenses need to be seen in conjunction with non-interest income. Operating expenditure normally exceeds non-interest income and this has been the case in India as well. However, the gap between the two widened during 2004-05 due to decline in non-interest income (which was entirely due to decline in trading profits). This resulted in sharp increase in what is known as banks' burden (excess of non-interest expenditure over non-interest income) to 0.7 per cent of assets in 2004-05 from 0.2 per cent in 2003-04 and deterioration in the efficiency ratio to 49.2 per cent from 45.4 per cent in the previous year[6].

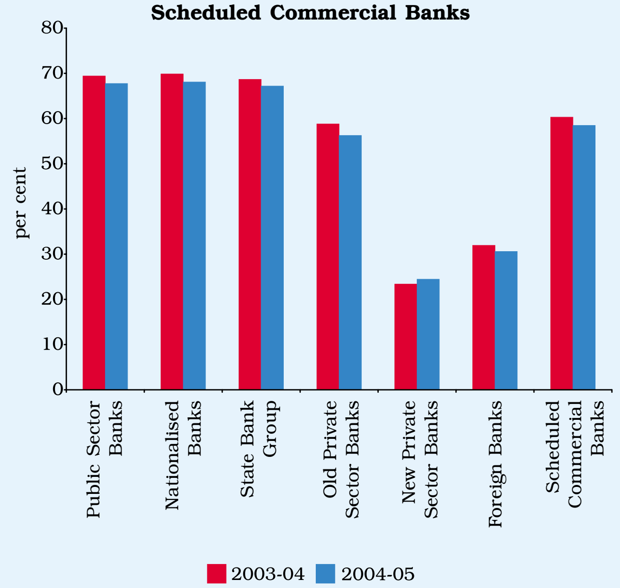
3.64 Wage bill for the banking sector, on the whole, declined as percentage of operating expenses (58.0 per cent in 2004-05 compared with 60.3 per cent in 2003-04). Wage bill as percentage to total assets also declined marginally to 1.2 per cent. Although wage bill of public sector banks declined both in relation to operating expenses and total assets during 2004-05, it continues to be high. The more technology-intensive new private sector and foreign banks had a significantly lower proportion of wage bill in operating expenses as compared with old private sector banks and public sector banks (Chart III.18).

3.65 In the post-VRS period, public sector banks have tended to rationalise staff cost to contain non-interest expenses. However, in recent years, per employee cost of the PSBs has risen due to the changing composition of the staff and increased provisioning towards superannuation liabilities (Box III.6).

Net Interest Income

3.66 Net interest income, defined as the difference between interest income and interest expenses, constitutes an important efficiency indicator of banks. The spread of SCBs remained unchanged at the previous year's level and continues to be high in comparison with international standards. While net interest margin of SBI group, new private sector and

Chart III.18: Wage Bill to Operating Expenses of Scheduled Commercial Banks



[6] Efficiency ratio is defined as operating expenses as percentage of net interest income plus non-interest income.

Box III.6: Post-VRS Trends in Staff Expenses of Public Sector Banks

Wage costs account for a major share in operating cost of the banking industry, especially public sector banks (PSBs). During 2000-01, a voluntary retirement scheme (VRS) for staff was introduced in PSBs with a view to downsizing the staff strength and bringing down the operating cost. The VRS was implemented in 26 out of 27 PSBs and more than one lakh staff members were relieved entailing an expenditure of Rs.11,885 crore. As a special case, banks were allowed to amortise the expenditure over a period of 5 years beginning from the financial year 2000-01. Total VRS related expenses amortised from 2000-01 through 2003-04 amounted to Rs.9,456 crore and the balance amount of Rs.2,429 crore was to be amortised during 2004-05.

Total staff expenses of PSBs increased at a compound annual growth rate (CAGR) of 11.8 per cent during the period from 1996-97 through 1999-00 (pre-VRS period), but only at 2.2 per cent during the next four years from 2000-01 through 2003-04 (post- VRS period), reflecting the positive impact of staff reduction. If VRS expenses amortised are netted out, the CAGR in staff costs during the post-VRS period worked out to 4 per cent. The real positive impact of VRS was discernible during 2001-02 when total staff costs of PSBs declined by 9.4 per cent even without adjusting for VRS expenses. However, during the next two financial years (2002-03 and 2003-04), staff costs, net of VRS expenses amortised, increased by 8 per cent and 12 per cent, respectively. The staff expenses increased even as total staff strength declined from 7,95,092 at end-March 2001 to 7,49,575 at end- March 2004. Consequently, the cost per employee (net of VRS expenses amortised), which dropped down from Rs.2.24 lakh in 2000-01 to Rs.2.18 lakh in 2001-02, increased to Rs.2.37 lakh and further to Rs.2.67 lakh in the next two financial years. A detailed analysis of staff expenses of 13 select PSBs, accounting for 68 per cent of total staff expenses of PSBs, reveals the following:

- The proportion of officers in relation in total staff strength of the PSBs has increased. While total staff strength of the select banks declined from 5,06,241 at end-March 2003 to 5,03,935 at end-March 2004, strength of officers increased from 1,45,793 (28.8 per cent) to 1,53,652 (30.4 per cent) during the same period. With the growing proportion of officers in the overall staff strength, gross emoluments (basic pay along DA and other allowances) also went up across all the banks during the last couple of years.
- Outgo on account of provisions for provident fund and pension liability of the select banks increased significantly in the post-VRS period, especially during the 2002-03 and 2003-04, accounting for the increase in staff expenses. The share of pension and provident fund liabilities increased from 11.5 per cent of total staff expenses of the select banks in March 2002 to 12.3 per cent in March 2003 and further to 14.9 per cent during year ended March 2004. Between 2001-02 and 2003-04, pension and provident fund liabilities accounted for 54.2 per cent of the incremental staff expenses of 12 (out of 13) banks.
- Profitability of the banking sector, including PSBs, improved in recent years. Consequently several PSBs made substantial provisions to cover the shortfall in past years' staff liabilities that also accounted for the rise in total staff expenses in recent years.
- Majority of the banks have in recent years adopted the actuarial method for valuing and providing superannuation liabilities to comply with the relevant Accounting Standard. This might have also led to the spurt in provisions for superannuation liabilities in recent years.

old private sector banks increased, that of nationalised banks and foreign banks declined.

Operating Profits

3.67 Operating profits of SCBs during 2004-05 declined by 3.1 per cent in 2004-05 as against an increase of 29.3 per cent in the previous year, reflecting largely the impact of decline in non-interest income. Among bank groups, operating profits of nationalised banks, old private sector banks and foreign banks declined during 2004-05, while those of SBI group and new private sector banks increased.

Provisions and Contingencies

3.68 The provisions and contingencies of SCBs showed a marginal decline during 2004-05. At the aggregate level, while provisions for loan losses declined sharply by 59 per cent, those for depreciation in value of investments increased by 7.7 per cent during 2004-05 (see also paragraphs 3.77 and 3.83). While provisions and contingencies by PSBs and old private sector banks increased, those by new private sector banks and foreign banks declined. The provisions for loan losses declined across bank groups, barring PSBs. Provisions for depreciation in value of investments increased for all bank groups, except foreign banks.

Net Profit

3.69 Net profits declined by 7.0 per cent (excluding the conversion impact) during 2004-05 as against an increase of 30.4 per cent in the last year. While net profits of nationalised banks, old private sector banks and foreign banks declined, those of SBI group and new private sector banks increased. Sharp increase in the net profits of new private sector banks was on account of a sharp decline in provision and contingencies (Table III.24).

Return on Assets

3.70 Return on assets (RoA) reflects the efficiency with which banks deploy their assets. Net profits to assets ratio of SCBs declined

Table III.24: Operating Profit and Net Profit – Bank Group-wise

(Amount in Rs. crore)

Bank Group	Operating Profit				Net Profit			
	2003-04	Percentage variation	2004-05	Percentage variation	2003-04	Percentage variation	2004-05	Percentage variation
1	2	3	4	5	6	7	8	9
Scheduled Commercial Banks	**52,600**	**29.3**	**50,962**	**-3.1**	**22,271**	**30.4**	**20,706**	**-7.0**
	–	**–**	**(51,684)**	**(-1.7)**	**–**	**–**	**(21,320)**	**(-4.3)**
Public Sector Banks	39,290	32.2	39,413	0.3	16,546	34.6	15,784	-4.6
Nationalised Banks	24,927	34.8	23,431	-6.0	10,928	40.4	9,494	-13.1
State Bank Group	14,364	27.9	15,260	6.2	5,619	24.5	5,676	1.0
Other Public Sector Bank	–	–	722	–	–	–	615	–
Old Private Sector Banks	3,192	13.8	2,239	-29.9	1,446	17.4	436	-69.9
New Private Sector Banks	5,133	15.8	5,435	5.9	2,035	17.9	3,098	52.2
Foreign Banks	4,986	33.7	4,597	-7.8	2,243	23.0	2,002	-10.7

– : Nil/Negligible.
Note : Figures within parentheses include the impact of conversion of a non-banking entity into a banking entity.

marginally in 2004-05. However, except for the new private sector banks, the ratio declined across bank groups, the decline being the highest in case of old private sector banks, followed by foreign banks and public sector banks (Chart III.19).

Return on Equity

3.71 Return on equity (RoE) reflects the efficiency of banking institutions in using capital. It is thus an indicator of banks' conduct of business in the interests of shareholders. Reflecting the combined impact of lower net profits and higher capital base, RoE for scheduled commercial banks, on the whole, declined significantly to 13.8 per cent in 2004-05 from 19.8 per cent in the previous year (Chart III.20).

3.72 Financial parameters of individual banks across bank groups of public sector, private sector and foreign banks are set out in Appendix Tables III.16 to III.24.

Chart III.19: Net Profitability of Bank Groups

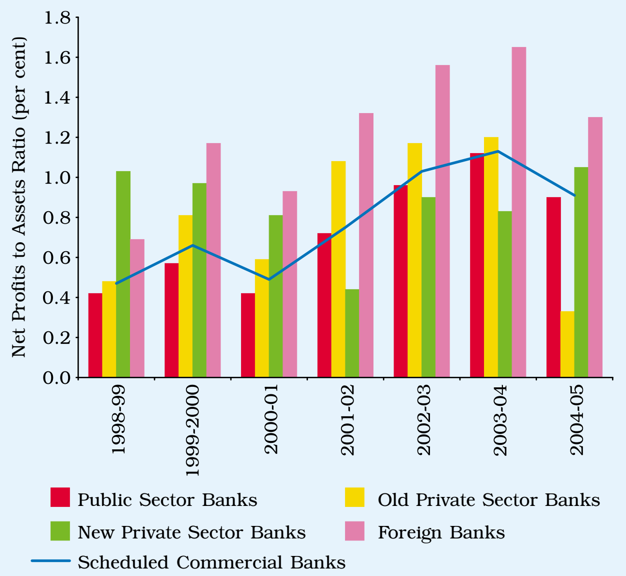


Chart III.20: Return on Equity of Scheduled Commercial Banks

5. Soundness Indicators

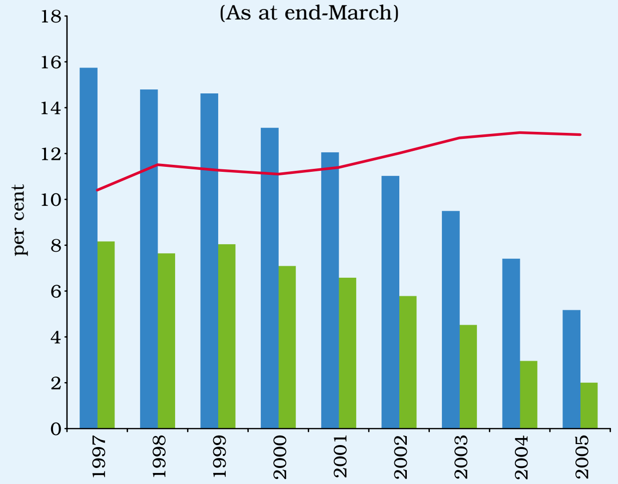
3.73 Capital adequacy and asset quality are two crucial parameters which reflect the soundness of a financial institution. In the Indian context, both these parameters have shown a significant improvement over the years. While the level of non-performing assets (NPAs), both in gross and net terms, has declined, the capital adequacy ratio has improved steadily (Chart III.21). Reflecting the combined impact of increase in the capital position and improvement in asset quality, net NPLs to capital ratio, which is a worst-case scenario measure, declined steadily from a high level of 71.3 per cent at end-March 1999 to 22.8 per cent at end-March 2004 and further to 15.5 per cent by end-March 2005.

Asset Quality

3.74 The sharp rise in credit growth was underpinned by a steady improvement in asset quality. Following the trend of the previous year, reductions in NPAs for SCBs outpaced additions to NPAs during 2004-05 (Table III.25). This trend was observed across all bank groups, barring new private sector banks. Gross NPAs of SCBs (excluding the conversion impact) declined by Rs.6,485 crore between end-March 2004 and end-March 2005.

Chart III.21: Movements in CRAR and NPAs of Scheduled Commercial Banks

(As at end-March)



* as ratio of advances

Table III.25: Movements in Non-performing Assets – Bank Group-wise

(Amount in Rs. crore)

Particulars	Scheduled Commercial Banks (87)	Scheduled Commercial Banks (88)#	Nationalised Banks (19)	State Bank Group (8)	Public Sector Banks (27)	Public Sector Banks (28)#	Old Private Sector Banks (20)	New Private Sector Banks (9)	Foreign Banks (31)
1	2	3	4	5	6	7	8	9	10
Gross NPAs									
As at end-March 2004*	63,096	64,439	35,549	15,989	51,538	52,880	4,393	4,517	2,649
Addition during the year	20,210	20,396	10,221	5,603	15,824	16,011	1,154	2,199	1,032
Recovered during the year	23,488	23,801	13,247	5,833	19,080	19,394	1,270	2,004	1,134
Written-off during the year	1,519	1,519	814	143	956	956	71	136	356
As on 31st March 2005	58,300	59,516	31,709	15,616	47,325	48,541	4,206	4,576	2,192
Net NPAs									
As at end-March 2004*	24,615	24,615	12,893	5,967	18,859	18,859	2,140	2,717	898
As at end-March 2005	21,441	22,289	10,280	6,363	16,642	17,490	1,859	2,292	648
Memo:									
Gross Advances	11,10,986	11,52,682	5,42,768	2,93,360	8,36,128	8,77,825	70,412	1,27,420	77,026
Net Advances	10,74,044	11,15,663	5,23,253	2,84,040	8,07,293	8,48,912	67,742	1,23,655	75,354
Ratio:									
Gross NPAs/Gross Advances	5.2	5.2	5.8	5.3	5.7	5.5	6.0	3.6	2.8
Net NPAs/Net Advances	2.0	2.0	2.0	2.2	2.1	2.1	2.7	1.9	0.9

: Including the impact of conversion of a non-banking entity into a banking entity.
* : Data do not include NPAs of banks which were closed during the year.
Note : Figures in brackets indicates the number of banks in that group for the year 2004-05.
Sources : 1. Balance sheets of respective banks.
2. Returns submitted by banks.

Table III.26: NPAs Recovered by Scheduled Commercial Banks through Various Channels

(Amount in Rs. crore)

Item	2003-04			2004-05		
	No. of cases referred *	Amount involved	Amount Recovered	No. of cases referred *	Amount involved	Amount Recovered
1	2	3	4	5	6	7
i) One-time settlement/ compromise schemes*	1,39,562	1,510	617	1,32,781	1,332	880
ii) *Lok Adalats*	1,86,100	1,063	149	1,85,395	801	113
iii) DRTs	7,544	12,305	2,117	4,744	14,317	2,688
iv) SARFAESI Act	2,661 #	7,847	1,156	39,288 #	13,224	2,391
v) Asset Reconstruction Companies (ARCs)	–	–	–	368	–	14,506

– : Nil/Negligible.
: Number of notices issued under Section 13(2) of the SARFAESI Act.
* : The scheme was operational up to July 31, 2004 and the last date for processing of application was October 31, 2004.

3.75 In view of several options available to banks for dealing with NPAs, banks have been able to recover a significant amount of NPAs (Table III.26). An improved industrial climate contributed to a better recovery position. The recourse to aggressive restructuring by banks in 2004-05 also helped in reducing the level of NPAs.

3.76 The setting up of the Asset Reconstruction Corporation of India (ARCIL) has provided a major boost to banks' efforts to recover their NPAs. During 2004-05, several banks and certain FIs sold their NPAs to the ARCIL to the extent of Rs.15,343 crore (Table III.27)

Movements in Provisions for Non-performing Assets

3.77 Write-offs and write back of excess provisions by SCBs exceeded the provisions made during the year leading to a decline in the cumulative provisions made for NPAs. The cumulative provisions at end-March 2005 were lower than their respective levels at end-March 2004 in respect of all bank groups, barring old private sector banks. However, in view of decline in gross NPAs, the cumulative provisions made to cushion the NPAs increased to 59.7 per cent at end-March 2005 from 56.6 per cent at end-March 2004. The cushion of provisions against NPAs improved despite the improvement in recovery climate and credit risk environment as reflected in the robust macroeconomic environment. The cumulative provisions as percentage of gross NPAs was the highest for foreign banks at end-March 2005, followed by public sector banks, old private banks and new private banks (Table III.28).

Table III.27: Details of Financial Assets Acquired by ARCIL

(As on March 31, 2005)

(Amount in Rs. crore)

Bank/FIs	No. of cases	Principal debt acquired	Interest and other charges	Total Dues pur-chased
1	2	3	4	5
Public Sector Banks	314	2,584	2,920	5,504
Old Private Sector Banks	11	153	84	237
New Private Sector Banks	132	4,436	4,329	8,765
Financial Institutions	12	386	450	837
Total	**368**	**7,559**	**7,783**	**15,343**

Note : Figures in brackets are percentage variations over the previous year.

3.78 A significant improvement in recovering the NPAs combined with a sharp increase in gross loans and advances for SCBs led to a sharp decline in gross NPAs to gross advances ratio to 5.2 per cent at end-March 2005 from 7.2 per cent at end-March 2004. The decline in gross and net NPAs was evident across all bank groups (Table III.29 and Appendix Tables III.25 and III.26).

3.79 Net NPAs ratio was the highest in respect of old private sector banks at end-March 2005 (2.7 per cent), followed by public sector banks, new private banks and foreign banks. At end-March 2005, 51 banks (as against 38 last year) out of 88 had net NPAs to net advances ratio less than 2 per cent. The number of banks with net NPAs to net advances ratio more than 10 per cent declined to four at end-March 2005 as compared

Table III.28: Movements in Provisions for Non-performing Loans – Bank Group-wise

(Amount in Rs. crore)

Particulars	Scheduled Commercial Banks (87)	Scheduled Commercial Banks (88)#	Nationa-lised Banks (19)	State Bank Group (8)	Public Sector Banks (27)	Public Sector Banks (28)#	Old Private Sector Banks (20)	New Private Sector Banks (9)	Foreign Banks (31)
1	2	3	4	5	6	7	8	9	10
Provision for NPAs									
As at end-March 2004	35,735	36,199	20,619	9,030	29,649	30,113	2,069	2,431	1,585
Add : Provision made during the year	11,498	11,630	5,946	1,977	7,923	8,055	568	2,364	642
Less : Write-off, write back of excess during the year	12,070	12,297	5,380	2,797	8,177	8,404	441	2,601	852
As at end-March 2005	35,162	35,531	21,185	8,210	29,395	29,764	2,197	2,195	1,376
Memo:									
Gross NPAs	58,300	59,516	31,709	15,616	47,325	48,541	4,206	4,576	2,192
Ratio:									
Cumulative Provision to Gross NPAs (per cent)	60.3	59.7	66.8	52.6	62.1	61.3	52.2	48.0	62.8

: Including the impact of conversion of a non-banking entity into a banking entity.
Note : Figures in brackets indicate the number of banks in that group for the year 2004-05.
Source : Balance sheets respective banks.

with nine in the previous year. All four banks belong to the foreign banks group (Table III.30).

3.80 With provisioning for NPAs being somewhat lower during 2004-05, the decline in

Table III.29: Gross and Net NPAs of Scheduled Commercial Banks – Bank Group-wise

(As at end-March)

(Amount in Rs. crore)

Bank Group/Year	Gross Advances	Gross NPAs			Net Advances	Net NPAs		
		Amount	Per cent to Gross Advances	Per cent to total Assets		Amount	Per cent to Net Advances	Per cent to total Assets
1	2	3	4	5	6	7	8	9
Scheduled Commercial Banks								
2002	6,80,958	70,861	10.4	4.6	6,45,859	35,554	5.5	2.3
2003	7,78,043	68,717	8.8	4.0	7,40,473	32,671	4.4	1.9
2004	9,02,026	64,785	7.2	3.3	8,62,643	24,615	2.9	1.2
2005	11,10,986	58,300	5.2	2.6	10,74,044	21,441	2.0	0.9
2005 #	11,52,682	59,516	5.2	2.5	11,15,663	22,289	2.0	0.9
Public Sector Banks								
2002	5,09,368	56,473	11.1	4.9	4,80,681	27,958	5.8	2.4
2003	5,77,813	54,090	9.4	4.2	5,49,351	24,867	4.5	1.9
2004	6,61,975	51,538	7.8	3.5	6,31,383	18,860	3.0	1.3
2005	8,36,128	47,325	5.7	2.8	8,07,293	16,642	2.1	1.0
2005 #	8,77,825	48,541	5.5	2.7	8,48,912	17,490	2.1	1.0
Old Private Sector Banks								
2002	44,057	4,851	11.0	5.2	42,286	3,013	7.1	3.2
2003	51,329	4,550	8.9	4.3	49,436	2,740	5.5	2.6
2004	57,908	4,393	7.6	3.6	55,648	2,140	3.8	1.8
2005	70,412	4,206	6.0	3.2	67,742	1,859	2.7	1.4
New Private Sector Banks								
2002	76,901	6,811	8.9	3.9	74,187	3,663	4.9	2.1
2003	94,718	7,232	7.6	3.8	89,515	4,142	4.6	2.2
2004	1,19,511	5,961	5.0	2.4	1,15,106	2,717	2.4	1.1
2005	1,27,420	4,576	3.6	1.6	1,23,655	2,292	1.9	0.8
Foreign Banks in India								
2002	50,631	2,726	5.4	2.4	48,705	920	1.9	0.8
2003	54,184	2,845	5.3	2.4	52,171	921	1.8	0.8
2004	62,632	2,894	4.6	2.1	60,506	898	1.5	0.7
2005	77,026	2,192	2.8	1.4	75,354	648	0.9	0.4

: Including the impact of conversion of a non-banking entity into a banking entity.
Note : Constituent items may not add up to the totals due to rounding- off.
Sources : 1. Balance sheets of respective banks.
2. Returns submitted by respective banks.

Table III.30: Distribution of Scheduled Commercial Banks by Ratio of Net NPAs to Net Advances

(Number of banks)

Bank Group	As at end-March				
	2001	2002	2003	2004	2005
1	2	3	4	5	6
Public Sector Banks	**27**	**27**	**27**	**27**	**28**
Up to 2 per cent	1	–	4	11	19
Above 2 and up to 5 per cent	5	9	14	13	7
Above 5 and up to 10 per cent	16	15	7	3	2
Above 10 per cent	5	3	2	–	–
Old Private Sector Banks	**23**	**22**	**21**	**20**	**20**
Up to 2 per cent	1	2	2	2	4
Above 2 and up to 5 per cent	4	2	4	9	12
Above 5 and up to 10 per cent	11	13	13	7	4
Above 10 per cent	7	5	2	2	–
New Private Sector Banks	**8**	**8**	**9**	**10**	**9**
Up to 2 per cent	1	1	3	4	5
Above 2 and up to 5 per cent	5	3	2	5	3
Above 5 and up to 10 per cent	2	4	3	–	1
Above 10 per cent	–	–	1	1	–
Foreign Banks	**42**	**40**	**36**	**33**	**31**
Up to 2 per cent	21	21	20	21	23
Above 2 and up to 5 per cent	6	4	2	3	2
Above 5 and up to 10 per cent	4	1	6	3	2
Above 10 per cent	11	14	8	6	4

– : Nil/Negligible.

the NPA ratio was attributable to both increased recovery of NPAs and overall reduction in asset slippages. In absolute terms, non-performing assets in 'doubtful' category increased, while those in sub-standard category declined sharply, reflecting the change in asset classification norm from the year ended March 2005, whereby an asset was treated as doubtful if it remained as NPA for 12 months as against the earlier norm of 18 months. However, NPAs in doubtful category as percentage of net advances declined significantly (Table III.31).

Sector-wise NPAs

3.81 NPAs of public and private sector banks are classified in three broad sectors, *viz*., priority sector, public sector and non-priority sector. The share of NPAs in the priority sector to total NPAs of public sector banks increased marginally to 48.9 per cent at end-March 2005 from 47.5 per cent at end-March 2004. However, the share of NPAs of small scale industries in respect of PSBs declined. While the share of NPAs of non-priority sector increased during 2004-05, the share of NPAs of public sector undertakings declined (Table III.32).

3.82 As regards private sector banks, the share of NPAs on account of all the three components of priority sector, *viz.*, agriculture, small scale industries and other priority sector increased during 2004-05 as compared with 2003-04. The absolute amount of NPAs in each of these sectors, however, registered a decline during the year. The share of non-priority sector NPAs in total NPAs of private sector banks remained steady at 75.0 per cent during 2004-05. Bank-wise details of advances to agriculture and weaker sections and NPAs arising out of weaker sections are furnished in Appendix Tables III.27 (A) and III.27 (B) and Appendix Tables III.28(A) and III.28(B), respectively.

Movements in Provisions for Depreciation on Investments

3.83 The provisions for depreciation on investments increased significantly by 81.4 per cent during 2004-05. Provisions made during the year were much in excess of the write-offs and write back of excess provisions. As a result, cushion of total provisions for investment portfolio 'held for trading' and 'available for sale' categories improved to 1.7 per cent at end-March 2005 from 0.7 per cent at end-March 2004. With higher provisioning for

Table III.31: Classification of Loan Assets – Bank Group-wise
(As at end-March)

(Amount in Rs. crore)

Bank Group/Year	Standard Assets		Sub-standard Assets		Doubtful Assets		Loss Assets		Total NPAs		Total Advances
	Amount	per cent	Amount	per cent	Amount	per cent	Amount	per cent	Amount	per cent	Amount
1	2	3	4	5	6	7	8	9	10	11	12
Scheduled Commercial Banks											
2002	6,09,972	89.6	21,382	3.1	41,201	6.1	8,370	1.2	70,953	10.4	6,80,925
2003	7,09,260	91.2	20,078	2.6	39,731	5.1	8,971	1.2	68,780	8.8	7,78,040
2004	8,37,130	92.8	21,026	2.3	36,247	4.0	7,625	0.8	64,898	7.2	9,02,027
2005	10,93,523	94.9	14,016	1.2	37,763	3.3	7,382	0.6	59,161	5.1	11,52,684
Public Sector Banks											
2002	4,52,862	88.9	15,788	3.1	33,658	6.6	7,061	1.4	56,507	11.1	5,09,369
2003	5,23,724	90.6	14,909	2.6	32,340	5.6	6,840	1.2	54,089	9.4	5,77,813
2004	6,10,435	92.2	16,909	2.6	28,756	4.3	5,876	0.9	51,541	7.8	6,61,975
2005	8,30,029	94.6	11,068	1.3	30,799	3.5	5,929	0.7	47,796	5.4	8,77,825
Old Private Sector Banks											
2002	39,262	89.0	1,834	4.2	2,668	6.0	348	0.8	4,850	11.0	44,112
2003	46,761	91.1	1,474	2.9	2,772	5.4	321	0.6	4,567	8.9	51,328
2004	53,516	92.4	1,161	2.0	2,727	4.7	504	0.9	4,392	7.6	57,908
2005	66,212	94.0	784	1.1	2,868	4.1	549	0.8	4,201	6.0	70,413
New Private Sector Banks											
2002	70,010	91.1	2,904	3.8	3,871	5.0	41	0.1	6,816	8.9	76,826
2003	87,487	92.4	2,700	2.9	3,675	3.9	856	0.9	7,231	7.6	94,718
2004	1,13,560	95.0	1,966	1.6	3,665	3.1	321	0.3	5,952	5.0	1,19,512
2005	1,22,577	96.2	1,449	1.1	3,061	2.4	334	0.3	4,844	3.8	1,27,421
Foreign Banks											
2002	47,838	94.5	856	1.7	1,004	2.0	920	1.8	2,780	5.5	50,618
2003	51,288	94.7	995	1.8	944	1.7	954	1.8	2,893	5.3	54,181
2004	59,619	95.2	990	1.6	1,099	1.8	924	1.5	3,013	4.8	62,632
2005	74,705	97.0	715	0.9	1,035	1.3	570	0.7	2,320	3.0	77,025

Note: Constituent items may not add up to the totals due to rounding off.
Source : DSB Returns(BSA) submitted by respective banks.

depreciation on investment, banks have made significant progress towards appropriate management of risks in their investment portfolio in a rising interest rate scenario. New private sector banks, on the other hand, wrote-back their provisions, reflecting the higher proportion of investments with lower tenor of investments in the 'AFS' category (Table III.33).

Table III.32: Sector-wise NPAs – Bank Group-wise
(As at end-March)

(Amount in Rs. crore)

Country	Public Sector Banks		Old Private Sector Banks		New Private Sector Banks		All SCBs*	
	2004	2005	2004	2005	2004	2005	2004	2005
1	2	3	4	5	6	7	8	9
A. Priority Sector	23,840	23,397	1,802	1,782	681	407	26,323	25,586
i) Agriculture	7,240	7,254	288	304	171	161	7,699	7,719
ii) Small Scale Industries	8,838	7,835	859	792	404	172	10,101	8,799
iii) Others	7,762	8,308	655	686	106	73	8,523	9,067
B. Public Sector	610	450	8	8	66	34	684	493
C. Non-Priority Sector	25,698	23,849	2,591	2,444	5,205	4,125	33,494	30,417
Total (A+B+C)	**50,148**	**47,696**	**4,401**	**4,234**	**5,952**	**4,566**	**60,501**	**56,496**

* : Excluding Foreign Banks.
Source: Based on off-site returns submitted by banks.