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India eyes cleanup of bad debt mountain as wary state banks hesitate

By Reuters | Updated: May 05, 2016, 05.39 AM IST

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NEW DELHI: India is considering setting up an independent panel to help state-owned banks negotiate settlements with big businesses on bad loans, in order to shield bankers from a populist backlash they say is hobbling efforts to clean up their balance sheets.

India's \$121 billion troubled debt pile, over \$100 billion of which is on the books of state-owned banks, has come under close scrutiny from prosecutors, the media and politicians. Some have blamed banks for going too easy on corporate tycoons, and do not want taxpayers propping up the struggling banking sector.

The proposal, being examined by the government and in its early stages, would give the panel power to define the "haircut" a bank should face on a loan gone sour, protecting bankers from critics who want failed Indian firms to pay back in full, two finance ministry and two central bank officials said.

Bad debt has hampered banks' ability to lend, threatening to throttle a nascent economic recovery.

Prime Minister Narendra Modi has made repairing bank balance sheets his administration's "top-most priority," a senior government official said.

"Banks have been very reluctant to take a haircut where they face newspaper criticism," said a second senior official, who is familiar with discussions on the panel. He declined to be named because he was not authorised to speak to the media.

The second official added that the proposal had run into hurdles already, however, amid questions over how it would fit into India's existing legal framework.

A finance ministry spokesman declined to comment. The Reserve Bank of India (RBI) did not immediately respond to requests for comment on the proposal.

Fear of bad headlines was one reason why state-run banks declined to consider embattled tycoon Vijay Mallya's offer to pay up to \$900 million in tranches to settle about \$1.4 billion his defunct Kingfisher Airlines owed, two banking sources said.

Mallya now also faces a money laundering investigation.

Mallya told the Financial Times late last month that he wanted a "reasonable" settlement that he could afford and banks could justify. He has denied any wrongdoing.

Bad loans have piled up as subdued consumer demand hits corporate earnings, making it harder for big businesses to repay loans.

GAPING CAPITAL HOLE RBI Governor Raghuram Rajan has set a deadline of March 2017 for banks to clean up their books, and the government said it would inject \$11 billion in state banks by March 2019 to help them repair their balance sheets.

India Ratings and Research, a local affiliate of Fitch, has said the government would have to cough up as much as \$45 billion if the lenders failed to raise funds from markets to address expected future capital shortfalls.

Negotiated settlements, in which a bank takes a writedown on a loan gone bad, can help speed up the process. They would allow banks to more quickly establish how much money they would need to bolster their balance sheets.

All state lenders including State Bank of India (SBI), the largest, are trading at a steep discount to their book values. Healthier institutions would be able to raise money from the market, reducing the burden on taxpayers.

Several finance ministry officials said stake sales were more likely once valuations of state-run banks improved.

Mahesh Patil, co-chief investment officer at Birla Sun Life Asset Management Co, said an independent panel for deciding haircuts on non-performing assets would accelerate decision making and help banks focus on their core lending business.

"As long as these issues are there, a lot of attention goes in terms of addressing the NPAs," Patil said. "The decision-making will be much better under an independent panel."

PANEL PROPOSAL The proposal envisages setting up a panel comprising leading bankers and government and central bank officials, to review some larger outstanding loans and try to arrive at a settlement, finance ministry and central bank officials said.

There is also a suggestion to include judges, they added.

The idea was first floated in 2014 after Modi took office, but did not gain much traction then, one of the finance ministry officials said.

It resurfaced at a two-day bankers' retreat in March where lenders saw it as a way of giving them some kind of insurance while breaking the logjam on bad loans, one of the central bank officials said.

Banks are trying other means to reduce non-performing loans.

In March, for example, SBI asked industrialist Naveen Jindal's Jindal Steel and Power to speed up a deal to sell a power plant to JSW Energy, run by his elder brother Sajjan, to pare debt, several sources familiar with the matter said.

The deal was announced on Wednesday.

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