

'Provisioning burden could have been eased for banks'

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Much of the capital banks raise will not go towards loan growth, says Brescon Corporate Advisors MD



In the last couple of years, the Reserve Bank of India has come up with a host of remedial measures for speedy resolution of stressed assets. These include facilitating creation of Joint Lenders' Forum, allowing banks to stretch repayment for performing loans to infrastructure and core sectors, permitting banks to convert loans into equity in case a project gets stressed again, and introducing a scheme for sustainable structuring of stressed assets. However, financial turnaround and debt resolution specialist Nirmal Gangwal feels that Indian medicine (solution) needs to be administered for Indian disease (bad loans). Foreign medicines (prescription) will not work. In an interview to *BusinessLine*, Gangwal, MD and Founder of Brescon Corporate Advisors, observed that banks, especially in the public sector, may not be in a position to support loan growth as the capital they raise in the next year or so will go towards provisioning as part of the RBI mandated balance sheet clean-up exercise. He said allowing them to spread the loan loss provisions over a longer period (as against four quarters prescribed by the RBI) would have eased this burden and helped support loan growth. Excerpts:

The RBI has come up with many prescriptions for speedy resolution of stressed assets. Will they really work?

When you keep coming up with circular after circular, changes after changes (to deal with stressed assets) so frequently, it means you really are not able to see the problem in a proper perspective from the beginning. And every time you react to the symptoms and the root cause, the reality, is kept aside.

For example, in the case of mid-sized corporates, the (manufacturing) capacities are fragmented.

The businesses have been set up based on the rules and regulations and demand and supply projections formulated (by the erstwhile Planning Commission) at a given point in time. There is limited risk capital.

Our bankers have lent rightly and our borrowers have also borrowed rightly. But there are inherent risks in projects (such as steel, power, infrastructure, etc).

The hiccups arise either due to internal or external disruption. For example, in the power sector, the Power Purchase Agreement is not adhered to.

Even if you buy the coal, produce power, the Discoms (power distribution companies) don't have the money to pay.

Now, this UDAY (Ujwal Discom Assurance Yojana) — a debt restructuring package for Discoms, whereby the stress is shifted from financial institutions to the State governments — took five-six years. If it had come in 2011, we would have avoided this stress. It came after five years. But by then damage had been done to the power sector.

Same is the case with the steel sector, which has very small capacity.

It was not built on a forward integrated basis. If suddenly iron ore mining is banned and the commodity cycle got affected, the steel sector also got impacted.

So, it is a situation which is beyond both these parties (banks and borrowers). Now, the government as the owner of the (public sector) banks, and the (banking) regulator could have come out with a different version of the solution.

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When the global financial crisis (2007-09) happened, the RBI came out with a one-time relaxation — a one-time restructuring dispensation.

At that time Indian corporates did not need the dispensation because they were sitting on a huge pile of cash from 2003 to 2008.

But the UPA II (government) saw emergence of judicial activism (court intervention), telecom and coal (scams), resulting in cumulative suffering for five-six years.

So, we needed a one-time dispensation in 2013-14. The impact of five years of (policy) non-action during UPA II led to corporate debt increasing by 100 per cent.

Suppose my debt was ₹ 100 and I have been accumulating interest on this debt for five years, then this debt becomes ₹ 200, but I did not have any earnings because neither the power plant nor the steel plant was working. Even if they were working, they were bleeding money.

Now, your asset is capable of servicing only ₹ 100 of debt and it has become ₹ 200, with the economic condition remaining the same.

Now, okay, the regulator says it wants banks to recognise the stress. But, after the recognition, the sustainable debt should not be less than 50 per cent of current funded liabilities in the affected projects.

So, the rest 50 per cent is nothing but unearned income. So, on the unearned income suppose the bank has to make a provision. They could have come out with a prescription that this needs to be provided over a five-year period so that banks could have adjusted the losses.

So, every year you amortise 10 per cent. This is affordable. They could have allowed this. But they wanted banks to provide (for loan losses) upfront. This is the problem.

Do you think the provisioning requirement was harsh on the banks?

The provisions could have been amortised over five years. First of all, the added load of the debt, which has happened over the last five years, needs to be corrected. Without that you can't make the business viable.

Now with that correction, suppose the bank has to make a provision, you have to give them time to amortise over a five-year period.

What is the big deal that it (provisioning) has to be of international standard? We are Indian. It (bad loans) is an Indian disease, give me Indian medicine. Don't give me foreign medicine for my Indian disease.

This is what is required to be done. Or, if you (RBI) don't want to do this, then sit with the government of India, which is the owner of these banks, and tell them that your banks have ₹ 10-lakh crore of stressed assets and 50 per cent needs to be provided for. I'm not giving you time. And if you want to remain owner, either provide ₹ 5-lakh crore or don't be owner.

With the provisioning burden, will banks be in a position to support loan growth?

Banks require, say, ₹ 2-lakh crore not to grow business but to make provisioning. But the government is constrained on this (capital) front. Now, when you are talking of a GDP growth of 8-10 per cent, the only source of funding to business and industry is through banks.

So, we may be facing a situation where banks are burdened with the past (stressed assets) and they will take another couple of years to handle that.

Then where is the question of growth. Who will fund our businesses? You think foreign banks or some multilateral institution will fund our businesses. This is a very serious issue one needs to really consider.

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