

How banks can improve recoveries under Insolvency and Bankruptcy Code

Updated: April 9, 2018 1:38 AM

PSU banks have not been able to achieve significant improvement in recoveries even post the enactment of the Insolvency and Bankruptcy Code (IBC). We believe banks need to realign their strategies to taste success under IBC.



PSU banks have not been able to achieve significant improvement in recoveries even post the enactment of the Insolvency and Bankruptcy Code (IBC). We believe banks need to realign their strategies to taste success under IBC.

Preparing for bankruptcy: Under IBC, insolvency proceedings can be triggered by various stakeholders, including unsecured lenders, trade creditors, unpaid employees or the corporate debtor. Banks can prevent surprises by continuously monitoring vulnerable accounts and pre-planning restructuring options, giving due consideration to the size, industry, indebtedness and business model of borrowers.

Adapt decision-making within the time-bound IBC framework: Delays in extracting recovery from a stressed borrower can erode value and make a bad situation worse. It is important for PSU banks to be well-prepared before the bankruptcy process starts to achieve higher recovery.

Areas of preparedness to improve recovery for banks:

Evaluating stressed/distressed accounts, and filing for bankruptcy at the appropriate time to retain/recover maximum value. In most stressed companies, value erosion is rapid and severe, and by filing for bankruptcy at an opportune time, banks can arrest or minimise the value erosion. Waiting for too long may result in loss of value and tilting of negotiating power away from banks.

Evaluating the available options and then prioritising them for ease of implementation and recovery. These may include restructuring of debtor's balance sheet, including converting some of the debt to equity, or changing terms/tenor of the debt for companies that have viable businesses but are suffering from over-leveraged balance sheets. Other options include selling the whole business, or parts of the business, or liquidation. Evaluating recovery-risk options will help banks channel the efforts of insolvency professionals towards the highest recovery option, eliminating surprises and achieving positive outcomes.

Identifying insolvency professionals, investment bankers and interim managers with relevant industry experience to manage the bankruptcy process to execute the chosen strategy. The ability to develop, assess and execute restructuring strategies will be critical for banks to successfully manage bankruptcies. The process requires banks to allocate substantial and skilled resources to achieve recovery in a short time. Banks may need assistance of external advisers/consultants to bolster internal resources, and to fully utilise the IBC process and maximise their recovery.

Effectively analysing information including outstanding dues, securities, legal agreements, guarantees, charges, assets, etc, to get a quick start and minimising value erosion. Similarly, identifying potential buyers for assets/companies, recommending duly experienced investment bankers to insolvency professionals, or preparing for liquidation early in the process is also essential.

Value creation under IBC can be through multiple routes such as debt restructuring, debt sell-out/buy-out, converting part/full debt to equity, or by buying debt of others to gain CoC control, etc. Banks need skills for debt buy-outs/sell-outs, negotiations, corporate/operating/financial restructuring, taking controlling stake in companies, etc, to effectively manoeuvre IBC process. Lenders will have to consider multiple factors including asset-security available to themselves and other lenders, percentage of voting held by members in the CoC, perspective of other CoC members, quality of proposals for restructuring received, industry type, etc, to develop effective strategies. Expecting the best recovery automatically is a risky assumption for banks. A well-planned, coordinated and deliberate plan of action is needed for successful resolution of banks' distressed debts. IBC throws up effective recovery possibilities for banks if they build requisite capabilities and successfully leverage IBC provisions. Banks that act effectively and are willing to deploy adequate resources, including capital and specialised external experts, will benefit from the bankruptcy regime and successfully navigate their way out of NPA problems.