

Annus horribilis for lenders

K Ram Kumar Updated on December 28, 2018



The 10 Most Legendary Investors Who Have Trendingstock Today

With bank frauds leading to massive losses at PSBs, defaults that had a ripple effect on the banking sector, and a change of guard at the RBI, it was an eventful 2018

The year 2018 proved to be one of the most disastrous for the banking sector in recent memory. The year started with the \$2-billion letter of undertaking (LoU) fraud at Punjab National Bank – alleged perpetrated by diamantaires Nirav Modi and Mehul Choksi – coming to light in January. The year is ending with banks staring at the possibility of having to provide for their ₹50,000-crore exposure to the debt-laden IL&FS Group in the third quarter results.

The LoU scam knocked the bottom out of PNB, India's second-largest public sector bank (PSB). It had to make heavy provisions, resulting in a whopping ₹13,420-crore net loss in the quarter ended March 31, 2018.

During the March quarter, most of the PSBs totted up losses due to the huge loan-loss provisions they had to make. However, things started looking up for some in the September quarter, as the loan-loss provision burden eased.

If banks don't end up making provisions for the IL&FS Group-related exposure, then the December quarter is likely to be better than the preceding three quarters due to possible improvement in asset quality and write-back in provisions due to a decline in bond yields.

The banking sector's overall credit growth, at about 12 per cent (between January 5 and December 7), was better than last year's 8 per cent, mainly on the back of demand for loans from sectors such as retail, services, and highly-rated corporates. Though deposit growth, at 8 per cent, was higher than the 3 per cent growth in the year-ago period, it lagged credit growth.

Farm loan waivers

While loans to the agriculture segment picked up steam only in October, the latest round of loan waivers, announced by States such as Madhya Pradesh, Chhattisgarh, Rajasthan and Assam, may have a ripple impact, leading to non-payment of farm loans on expectation of waivers in the run-up to the general and Assembly elections in 2019. As this will impact the credit culture, banks may turn conservative in lending to the farm sector.

While the retail juggernaut is expected to continue, in the run-up to elections in 2019, India Inc is likely to turn conservative vis-a-vis its investment plans due to uncertainty on the dispensation that could take power at the Centre.

IL&FS has become a bugbear for banks, turning them cautious in lending to the NBFC sector as a whole, following defaults on debt obligations by the beleaguered NBFC and some of its subsidiaries.

Bankers fear that if the RBI does not give them dispensation, then their loans aggregating ₹50,000 crore to the IL&FS Group may turn sour in the December 2018 quarter. If these loans are classified as non-performing, banks will have to make provisions, thereby impacting their bottomline.

IL&FS Group defaults

On account of the massive mismanagement of public funds, allegedly by the erstwhile board of IL&FS Group and on the grounds that the affairs of IL&FS were being conducted in a manner prejudicial to public interest, the MCA sought suspension of the previous board of IL&FS and put in place a new board.

To help PSBs make loan-loss provisions, meet minimum regulatory capital requirements, grow business and help at least four-five of the 11 weak PSBs to come out of the restrictive prompt corrective action framework and step-up lending, the government announced dollops of capital

infusion, running into thousands of crores. About ₹83,000 crore is set to be infused over the next three months.

About a year after SBI took over its five associate banks, the government pressed forward with structural reforms in the public sector banking space. The government is in the process of ceding majority control in IDBI Bank to the Life Insurance Corporation of India, and has initiated the process of merging Vijaya Bank and Dena Bank with Bank of Baroda.

According to credit rating agency ICRA's analysis, public sector banks managed to cut their net loss from ₹62,700 crore in the March quarter to ₹14,700 crore in the September quarter. Their gross non-performing assets (GNPAs) came down to 14.1 per cent of gross advances in the September quarter, against 14.6 per cent in the March quarter. While public sector banks struggled with loan woes and massive dent to their bottomlines, private sector banks – whose net profits improved from ₹7,600 crore in the March quarter to ₹10,700 crore in the September quarter, and GNPAs declined to 4.4 per cent of gross advances in the September quarter, against 4.8 per cent in the March quarter – grabbed the headlines on account of violation of corporate governance and shareholding norms and the RBI wanting to curtail the terms of CEOs.

Chanda Kochhar stepped down as ICICI Bank chief amid allegations of *quid-pro-quo* in certain loans. The private sector bank's board elevated Sandeep Bakhshi, Chief Operating Officer, as Managing Director and Chief Executive Officer. In June, Bakhshi was moved back to

the bank from ICICI Prudential Life Insurance which he was heading.

In mid-September, RBI said Rana Kapoor could continue as the MD and CEO of YES Bank only till January-end. Though the bank's board of directors requested an extension for Kapoor until April 30, 2019, to help finalise the audited financial statements for 2018-19, and then up to September 30, 2019, for the statutory annual general meeting process to be completed, the RBI put its foot down.

In the case of Axis Bank, its board, in December 2017, had decided to re-appoint Shikha Sharma for three years from June 1, 2018, for her fourth term. However, in April 2018, Sharma decided to cut short her fourth term at the helm and step down from her post at the end of the year. The RBI is understood to have raised questions as to why Sharma was being given a fourth term.

Later, the bank appointed Amitabh Chaudhry, Managing Director and CEO of HDFC Life Insurance, as its Managing Director and CEO, for three years with effect from January 1.

In August, Kotak Mahindra Bank claimed that promoter group holding in the bank had come down from 30 per cent to 20 per cent, following issuance of the non-convertible perpetual non-cumulative preference shares on private placement basis. But the RBI said the bank did not meet the requirements for dilution of promoter holding.

On December 17, the Bombay High Court declined Kotak Mahindra Bank's plea for a stay on the Reserve Bank of

India's December 31 deadline to reduce its promoter stakeholding.

The RBI had, in September this year, pulled up Bandhan Bank for its failure to bring down promoter holding to 40 per cent as mandated in the licensing norms for universal bank. It had also withdrawn permission to open new branches, and had put a freeze on the remuneration of CS Ghosh. Bandhan Financial Holdings (BFHL) – the promoting entity of Bandhan Bank – is owned by Bandhan Financial Services (BFSL). The promoter holding in the bank currently stands at 82.28 per cent.

As per the RBI's licensing norms, promoter holding should be brought down to 40 per cent within three years of starting operations. So, Bandhan Bank, which had commenced operations in August 2015, should have ideally brought down the promoter holding by August 2018.

However, the bank, which floated an IPO in March 2018, could not have pared promoter stake due to the SEBI mandate of a one-year lock-in on shares held by the promoter post an issue. In October, however, the bank received an exemption from SEBI to help it comply with the requirements of RBI's Licensing Guidelines.

On December 12, Bandhan Bank received the RBI's permission to open as many as 40 branches by the end of December. The central bank's approval comes nearly three months after it had imposed restrictions on the bank's branch expansion plans.

IBC, a mixed bag

The outcome of the corporate insolvency resolution process initiated by banks against defaulting corporates under the Insolvency and Bankruptcy Code was a mixed bag. While large accounts such as Bhushan Steel, Electrosteel Steel, and Binani Cement have been taken over under the IBC process, other large accounts such as Essar Steel, Videocon Group, Bhushan Power and Steel, and Amtek Auto remain to be resolved.

With authorities pursuing promoters, who took flight to avoid facing legal consequences of their wrongdoings , there is hope that they will be brought back to the country and face legal action. Bankers are keeping their fingers crossed that justice will prevail and that they can recoup some of the monies they lent.

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