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Smaller banks hit most by RBI's revised note on NPAs

BY JOEL REBELLO & MAULIK VYAS, ET BUREAU | JUN 10, 2019, 07.11 AM IST

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MUMBAI: The central bank's revised circular on stressed assets promises to speed up resolutions of bad assets, but smaller banks in specific deals may now have to follow the larger lenders that have more at stake in a consortium of creditors.

The rule that 75% of creditors' vote is enough to pass a resolution plan and that dissenting lenders must sell at liquidation value would lower the bargaining power of smaller banks that have less exposure in specific deals. On the flipside, that would mean quicker resolutions as banks with less exposure can't stall deals any longer.

"Small lenders would always try to get the full value of the loan even if their exposure was just a few crores. This was not always possible and would delay the process," said Prashant Kumar, CFO at [State Bank of India \(SBI\)](#), the country's biggest lender. "Now, things will be easier: If 75% of lenders by value of the loans or 60% by number agree, the plan can be taken forward."

Mint Road framed a new set of rules on Friday for banks after its previous circular failed to pass legal scrutiny. Power sector companies had approached India's highest court against the regulator's 2018 order that had ordered banks to treat a single-day's payment delay as default and required lenders to initiate insolvency proceedings. The new circular does not expect banks to start restructuring within one day of default but gives them a 'review period' of one month, replacing the earlier guideline that had said lenders 'shall initiate steps to cure the default.' However, after agreeing to a resolution plan, lenders have to sign a so-called inter creditor agreement (ICA) mandatorily, which could become a deterrent in the process. "The catch is that banks may not sign the ICA if not satisfied with the proposed resolution professional (RP) by the borrower, or can even arm-twist the borrowers. Small lenders may not sign the ICA and may lead to all lenders making additional provisioning," said BoB Capital Markets in a note on Saturday. Some others believe that there is no clarity on the realisable, or liquidation, value of an asset, and lack of clarity on as fundamental a point as this will lead to delays.

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RBI framed a new set of rules for banks after its previous circular failed to pass legal scrutiny

Now, 75% of creditors' vote is enough to pass a resolution plan

Dissenting lenders must sell at liquidation value and will lower the bargaining power of smaller banks

It gives banks a review period of one month to start restructuring the default

Some experts believe that there is no clarity on liquidation

"If the liquidation value becomes negative, how much will the small lenders get? When can such an assessment be done is also a question," said Harish Chander, an independent consultant. "Valuation of companies is no longer done on a desktop. It takes three to six months, which means there could be delays." Unlike the previous circular that gave a blanket approval for the IBC process, this time the

central bank has chosen to incentivise the insolvency mechanism instead, disfavoured customised restructuring plans.

Banks have to make an additional 15% provision within one year of the commencement of the review process. This will be in addition to the 20% provision required at the end of the 180-day period, which means a 35% provision if a plan is not put in motion after a year.

"More importantly, RBI has done away with the 50% provision required for IBC cases, which means banks need only a 15% provision if they want to directly take a case to IBC. Or banks risk a higher 35% provision if a plan is not agreed," Kumar said.

Lawyers say the removal of a stringent timeline is welcome.

"The new circular is a relief for lenders who, under the earlier circular, were compelled to initiate the insolvency process within a stringent timeline even where they believed that resolution of a particular stressed asset was possible without approaching the NCLT," said Ayush Agarwala, partner of law firm K Law.

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