

## Plotting a fantasy: 3 reasons why DHFL's rescue plan is entirely fictional

The only reason the rescue is even being attempted is to delay - as long as possible - the collapse of the large shadow lender Dewan Housing Finance

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Suspend your disbelief, and like the protagonist of the popular Bollywood movie “3 idiots,” keep muttering: “All is well, all is well.”

If it isn't yet, it will be.

That seems to be the whole approach behind the ongoing efforts to restructure an Indian financier, Dewan Housing Finance Corp., which some months back started defaulting on its outstanding debt of \$12 billion.

Trouble is, the rescue is entirely fictional. The only reason it's even being attempted is to delay — as long as possible — the collapse of this large shadow lender. Such an event, as S&P Global said in a rare show of plainspeak by a credit appraiser, could be powerful enough to deliver a “solvency shock” to India's troubled banks. Neither the lenders, nor the Indian government, wants to contemplate this grim prospect. Hence, the make-believe restructuring.

On a spreadsheet, resolution for Dewan appears simple enough. As of March, it had assets of \$14 billion, spread over mortgages, loans against property and other credit to small businesses, as well as advances to builders. Sell the shaky wholesale book to Oaktree Capital Group LLC as planned, and let banks, mutual funds and other creditors try to recover what they can from the well-performing retail loans. A 30 per cent to 40 per cent haircut may be as happy an ending as the lenders could have ever hoped.

That's where the plot thickens.

**Twist #1:** The Bombay High Court is scratching its head and wondering if Dewan securitised — that is, sold to a separate entity — assets that it had pledged to another set of investors to obtain loans. Now, the court wants the beleaguered firm to produce, under oath, a list of assets it repackaged and sold within the last year. This imbroglio has the potential to bring India's securitization market to a standstill.

**Twist #2:** A special review of Dewan by KPMG is still in a draft form. But the parts leaked to the media Wednesday raise damaging questions. The auditor says that \$2 billion was lent to 25 borrowers with little real business or assets, and that “such entities may be working closely” with Dewan without qualifying as related parties. No state-run bank, answerable to anti-corruption authorities, is going to knowingly risk a loss on taxpayers' money before it gets satisfactory answers to KPMG's concerns.

**Twist #3:** The above obstacles are already enough to sink Dewan's debt recast. However, a decent Bollywood potboiler needs a dash of the Mumbai underworld. Sleuths at India's enforcement directorate, an agency tasked to fight economic crime, are probing a loan from Dewan to a late Dubai-based gangster's real-estate firm, according to local Indian media reports. This makes an out-of-court rescue nearly impossible.

S&P analysts are right. The Dewan defaults haven't bred the kind of panic that Indian credit markets witnessed last September after IL&FS Group, a large infrastructure financier, went belly up unexpectedly. What seemed like a liquidity shortage at first was later revealed to be a gaping hole in the balance sheet.

But then, probably because of the example set back then, the market can guess the end game of the Dewan saga. India has no law to deal with a large financial bankruptcy. When defaults accelerate, New Delhi will have to step in and stop the farce of private restructuring negotiations. That's what happened with IL&FS, where a government-appointed new board arranged for blanket protection from creditors, and then began a never-ending wait for buyers of assets. In Dewan, a search for the funds KPMG's audit couldn't find will also get under way. After a while, people will get bored by the mind-numbing minutiae of a story going nowhere, and attention will shift to a new scandal.

All will be well.