RBI makes debt recast norms more stringent

The Reserve Bank of India (RBI) on Thursday said all loans recast after April 1, 2015, should be classified as non-performing asset (NPA). Also, from June 1, 2013, the provisioning requirement for fresh standard restructured advances would be increased to five per cent from 2.75 per cent, for the interim period.

For the existing stock of restructured assets, provisioning would be increased to five per cent in a phased manner over three years.

At present, banks are allowed to recast debt without classifying it as NPA but they have to make higher provisions. Standard restructured advances attract a provision of 2.75 per cent, as against 0.4 per cent in standard advances.

According to banking analysts, for fresh restructuring, where the provision is increased to five per cent, banks' profit before tax would be impacted by one-three per cent in FY14.

Ratings agency Icra's quick estimates suggest banks might have to keep an additional Rs 1,500-2,500 crore as provisions in 2013-14 for their existing recast loan book. RBI has prescribed a raise in provisioning requirement for this stock for FY14 from 2.75 per cent to 3.5 per cent. The total provision burden on banks till 2015 is estimated to be Rs 2,500-5,000 crore.

RBI has also said short-term loans, (except working capital), if rolled over more than twice, would amount to restructuring.

These steps had been suggested by the Mahapatra committee on loan restructuring. The central bank has now accepted and implemented the panel's report, despite banks' reservations on the ground that the economy is going through difficult times and bad loans in the banking sector have increased.

The move has come at a time when the debt-restructuring exercise has risen significantly over the past two years. Under the corporate debt restructuring (CDR) cell, there were 106 cases of restructured loans, of Rs 76,470 crore, in 2012-13. This was a rise from 50 cases (exposure of around Rs 39,600 crore) the previous year. In addition to the CDR platform, lenders had also gone for substantial recast at the bilateral level during the period.

According to a finance ministry estimate, if all restructured loans are classified as NPAs from on Thursday, the gross NPA level of public-sector banks would shoot up to 11.59 per cent of gross advances, from 4.18 per cent at the end of December. The estimate suggests, restructured standard advances formed 7.41 per cent of advances for public-sector banks.

RBI has also decided that promoters of firms would have to shell out more to get their exposure restructured. Promoters would now have to bring in 20 per cent of the erosion

of the net present value, compared with 15 per cent earlier. RBI has suggested, for large exposure, such as those referred to the CDR cell, banks should ask for more promoter contribution.

To ensure promoters' commitment to the recast process, their personal guarantee has been made mandatory and it has been made clear that corporate guarantee cannot replace personal guarantee, except in cases where the promoters of a company are not individuals but other corporate bodies, or where the individual promoters cannot be clearly identified.

India Inc is clearly not happy with the new norms. "In the current circumstances, if promoters are asked to bring in more money, it will put further strain on companies. A firm seeks restructuring only when its ability to pay is affected due to various reasons. Given the current slowdown, it would only add fuel to the fire. Tightening norms at this point is a negative," says JSW Steel CFO Seshagiri Rao.

GVK Group CFO Isaac George adds: "Asking promoters to chip in now will be very difficult. This is the time to support corporate India because the current situation is not entirely our doing. We currently have power plants that can run at 100 per cent capacity but there is no gas available to these plants." GVK Power and Infrastructure has seen its losses rising to Rs 171 crore in the fourth quarter.

In the short run, however, there will be a slight relief for banks; RBI's prescription of 3.5 per cent provisioning for existing recast loans for 2013-14 is less than the 3.75 per cent proposed by the Mahapatra committee.

According to a senior State Bank of India executive, the relief for SBI in FY14 due to lower provisioning requirement would be of Rs 80 crore. "RBI has given one more year (2015-16) for making provisions for the existing stock. This will help spread the burden," the executive said.

Besides, it has been decided that the benefit of asset classification would continue for infra projects, commercial real estate (CRE) and non-infra projects where delay is due to legal and other extraneous reasons like delayed government approvals.

The infra project loans that were restructured within two years of the date of commencement of commercial operation (six months for non-infra loans) would not be considered as restructuring, RBI said.

It has also been decided that mere extension of the date of commencement of commercial operation even in the case of CRE projects would not be considered restructuring if the revised date is within a year and there is no change in other terms and conditions, except possible shift of the repayment schedule.

In another relief for CRE projects, RBI has said reworking of CRE loans due to change in date of commencement of commercial operation will not be treated as loan recast. At

present, any restructured CRE loan is immediately treated as NPA. Banks will be more flexible in taking exposure to CRE, improving chances for revival.

For an upgrade from the NPA category, RBI said, such reclassification could only be done after a year from the commencement of the first payment of interest or principal, whichever is later, on the credit facility with the longest period of moratorium under the terms of restructuring package.

Putting debt recast in order

- Provision for existing stock of recast debt to be raised from 2.75% to 5% in a phased manner over three years
- If principal converted into debt or equity, it will be held under the available-for-sale category
- Banks not to artificially reduce the net present value of cash flows by resorting to any sort of financial engineering
- Banks to ensure infrastructure units achieve viability in 8 years and other cases in 5 years
- Promoters' contribution should be a minimum 20% of banks' sacrifice or 2% of restructured debt, whichever is higher
- Banks to insist on higher sacrifice from promoter if exposure is large
- Conversion of debt into preference shares the last resort, with a cap of 10% of restructured debt
- Only listed companies' debt could be converted into equity
- Promoters' personal guarantee must, corporate guarantee not a substitute for personal guarantee

(Business Standard)