

THE NEEDLE'S EYE Will the NPA black hole suck in the country's entire banking universe?

# A Crisis of Extreme Gravity



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With barely nine months to go before the Lok Sabha election, how serious is the crisis in our banking system? Put simply, it is not going to be resolved any time soon, although GoI is scrambling to force more medicine into the patient on life support.

RBI's latest financial stability report tries to sound optimistic. It says credit picked up in 2017-18 despite sluggish deposit growth. But it sees banks' gross non-performing advances (GNPA) ratio worsening from 11.6% in March 2018 to 12.2% in March 2019. A Credit Suisse (CS) report says banks' GNPA climbed to ₹10.09 trillion at end-March from ₹8.82 trillion at end-December.

Last year, RBI placed 11 of 21 public sector banks (PSBs) on its prompt corrective action (PCA) list — in other words, under constant watch in the ICU. Over the last three years, GoI has injected ₹1.4 trillion of capital into PSBs. The sickest banks have received nearly two-thirds, or ₹810 billion — almost matching those 11 banks' losses in the three years. GoI has budgeted ₹650 billion of fresh capital infusion in 2018-19, but this will not suffice.

The PCA banks' pallor is turning greyer. RBI says their GNPA ratio may worsen from 21% at end-March to 22.3% by March next year. Nine of them will see severe capital shortfalls. At the same time, PCA banks' loan

books are shrinking.

Two of the 21 PSBs reported modest profits in fiscal 2017-18. But losses at the other 19 widened to ₹873.5 billion. IDBI Bank, which has GNPA of 28% and is pitifully called the 'Industrial Dust Bin of India', will now be controlled 51% by the Life Insurance Corporation (LIC). This could be a temporary vitamin boost, because there are reports that GoI plans to merge IDBI with three other ailing PSBs.

Most of our PSBs continue to be bloated, inefficient and mismanaged. CS analysis shows that operating expenses, which include salaries and pensions, now exceed 90% of PSBs' net interest income, which means the banks have almost no headroom to resume lending.

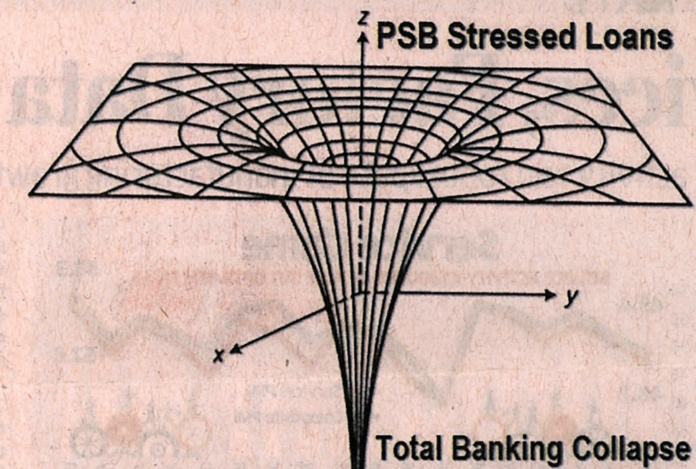
## Detox for the Banks

Banks' total stressed loans, which stood at ₹12.47 trillion at end-March, or 14.3% of their total loans, were down slightly from ₹13.29 trillion, or 15.8%, at end-December.

To put the NPA problem in perspective, our banks' stressed assets now stand at 9.6% of our GDP, or about half of Budget 2018. Looked at another way, our banks' stressed assets equal 46 times the Budget of the ministry of health and family welfare, and 28 times our education Budget.

GoI is struggling to break the logjam. The bankers' committee it set up has ruled out a 'bad bank' that would take over all toxic assets. Instead, it recommended a combination of a bank-led asset management company, alternate investment funds, and a platform to auction bad assets. It set a 90-day limit for resolution of bad loans to small and medium enterprises (SMEs). And it proposed inter-creditor agreements to speed up resolution under the Insolvency and Bankruptcy Code (IBC), which came into force

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in December 2016.

The urgency is growing because the IBC pipeline is already dangerously clogged. CS noted that as of March, the National Company Law Tribunals (NCLTs) were hearing about 700 cases, of which only 37% had been referred by financial creditors, and another 2,200 cases were waiting to be admitted. Only 180 cases had been closed, and a tiny 13% of those had been resolved. Nearly half ended in liquidation, and more than 40% have been disputed.

There just aren't enough resources to tackle the mountain of bad debt and bankrupt companies. Ten NCLTs were set up two years ago. An 11th in Jaipur has just been announced. There is also a 'principal' bench in New Delhi, and an Appellate Tribunal (NCLAT). Disputed cases go to the Supreme Court. I counted a total of 2,667 'insolvency professionals' who have to be certified by the Insolvency and Bankruptcy Board of India, the regulatory body. You need to possess just a BCom degree to be an insolvency professional, which is like asking a paramedic to perform brain surgery.

One of the seven NCLT judges in Delhi told me each of the four benches in the capital was hearing an aver-

age of 20 cases a day, and the workload was impossible. NCLTs also handle non-bankruptcy cases like mergers, and disputes between directors and shareholders. There is a 14-day deadline for admission of IBC cases, but it is observed more in the breach. Resolutions have a 180-day deadline, extendable by 90 days. But only two of the original 12 'dirty dozen' big IBC cases referred by RBI have so far been resolved.

## Expensive Haircut

The good news is that in 12 insolvency cases resolved in the January-March quarter, creditors recovered about 70% of the debt. The average time for resolution was 267 days. CS says NPA levels have probably peaked and should start declining as the IBC process continues. CS estimates an average 45% haircut, or loss, for creditors on the RBI-referred 12 cases. But the central bank has named 28 more large NPA cases, and the NCLTs have admitted only 14.

With RBI tightening the NPA screws in February, CS expects another 70 big cases to be referred to the NCLTs in the July-September quarter, including 40 comatose power projects. The worst is yet to come.