Shobhana's edit

With other measures not working, RBI tries new tack

RBI has been trying for some time now to help banks deal with assets that are stressed and also to identify potential stress in the system. The 5/25 scheme which allows lenders to recast loans in a manner that eases the pressure on the borrower should yield results provided banks don't misuse the provision.The Strategic Debt Restructuring (SDR) scheme, which enables lenders to convert a portion of the debt into equity and bring in a new set of promoters to run the company, however, has been a non-starter.While banks have initiated the process for a dozen companies, a weak economic environment has seen no takers for these assets, many of which are steel companies. Roping in a new management is not easy even in the best of times; so, it is no surprise that lenders haven't been able to sell these assets. The central bank's latest restructuring scheme for sustainable structuring of stressed assets—S4—makes it easier for banks by allowing them to restructure the debt without necessarily bringing in a new promoter. The objective is to let lenders convert the 'unsustainable debt' or what is essentially assessed to be the non-servicable loans into equity as long as this is less than 50% of the total debt. A smaller debt would make it easier for promoters to pay back their dues, although no moratorium or lowering of interest rates is permitted.Meanwhile, banks can enjoy the upside if there is a recovery—the debt can be be converted into either equity, redeemable cumulative optionally convertible preference shares or even optionally convertible debentures.The provisioning requirements—20% of the total exposure or 40% of the amount of loans converted—aren't too stiff either though there will be a hit since the portion converted will need to be marked to market. The central bank is clearly trying to make it easier for banks to try and recover at least some part of their dues—by not insisting on a new promoter being brought in.

At the same time, it wants borrowers to share the pain; if the existing promoters stay on, even as minority owners, they are expected to dilute their stake at least in the same proportion as that of the unsustainable debt to the total debt. Moreover, they will need to furnish a personal guarantee for at least the amount of sustainable debt. While the guidelines are fine, if banks have a very small shareholding, promoters will not cooperate with them. Simply because they have board representatives and voting rights doesn't mean they will have a grip on how the company is being run. If the promoters have a minority stake, they may mismanage affairs to an extent where no other businessman wants to touch the company and the equity becomes worthless. Therefore, banks need to be cautious before they start converting the loans into equity. There are those who will argue that the flipside to a status quo is to watch the exposure turn into a non-performing asset, so it is better that lenders hold some equity which they may be able to sell at some point. It is a difficult decision because the environment is a tough one and borrowers cling to their companies but put off paying their dues for as long as they can. Moreover, waiving off dues—when it is not clear whether the equity will bring returns—is not fair to good borrowers. On balance, banks need to take some calculated bets.