

Unravelling firm distress

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- ▶ Policy discourse focused on bank NPAs
- ▶ What about the distress in the underlying firms?

Key questions

- ▶ Who to restructure?

Identifying distress, financial versus economic distress

- ▶ When to restructure?

Early identification critical to minimising losses

- ▶ How to restructure?

Strategies vary, depending on:

- whether bankruptcy proceedings are debtor or creditor controlled;
- whether distress is firm level, industry wide or economy wide;
- whether capital and asset markets support transactions.

Indian context

- ▶ No obvious signals of firm distress. Firm balance sheets provide clues.

Identifying distress

- ▶ In literature, $ICR < 1$ and P-ICR used to assess distress. Claessens, Djankov, and Lang (1998), Chung and Ratnovski (2016)

	$ICR < 0$		$0 < ICR < 1$	
	FY 16	FY 15-16	FY 16	FY 15-16
Number of firms	1,627	1,006	749	340
Borrowing (Rs. trillion)	8.9 (1,502)	5.7 (952)	9.1 (741)	5.0 (340)
Bank Borrowing (Rs. trillion)	3.9 (1,091)	2.4 (719)	4.7 (622)	2.5 (292)
Median D/E	0.95 (976)	0.98 (518)	2.32 (601)	2.83 (260)
$D/E > 2$	326	181	328	155

Financial versus economic distress

- ▶ In literature,

High leverage + Negative operating performance = Economic distress

Hotchkiss (1995), Denis and Rogers (2007)

- ▶ Of the 1,632 firms that have $ICR < 1$ in FY 15 and FY 16, the top 250 by size account for 82% (Rs. 11.2 trillion) of borrowings and 89% of bank borrowing (Rs. 7.3 trillion).
- ▶ The industries from which these firms come:

Steel, Telecom, Electricity generation, Cement, Metal Products, Infrastructure Construction, Electricity Distribution.
- ▶ Let's look at the Steel, Telecom and Electricity Generation in some detail.

Steel

	ICR<1 firms	Industry
No. of firms with P-ICR<1	13	
Median firm size (Rs. bn)	57.3	
Median firm borrowing (Rs. bn)	48.7	
Median firm bank borrowing (Rs. bn)	17.0	
Median EBITDA/TA	0.025	0.075
Firms with negative EBITDA/TA	4	
Median D/E	9.4	1.1
Firms with negative net worth	3	

	ICR<1 firms	Industry
No. of firms with P-ICR<1	14	
Median firm size (Rs. bn)	58.3	
Median firm borrowing (Rs. bn)	55.4	
Median firm bank borrowing (Rs. bn)	30.4	
Median EBITDA/TA	0.039	0.041
Firms with negative EBITDA/TA	4	
Median D/E	5.5	0.15
Firms with negative net worth	7	

Electricity Generation

	ICR<1 firms	Industry
No. of firms with P-ICR<1	15	
Median firm size (Rs. bn)	32.4	
Median firm borrowing (Rs. bn)	43.2	
Median firm bank borrowing (Rs. bn)	29.3	
Median EBITDA/TA	0.065	0.015
Firms with negative EBITDA/TA	2	
Median D/E	4.4	1.4
Firms with negative net worth	2	

What next?

1. The old stock
2. Restructuring/liquidation strategies for the old stock
3. Development of a distress resolution market
4. Future distress
5. Restructuring/liquidation strategies for future distress

Thank you.