

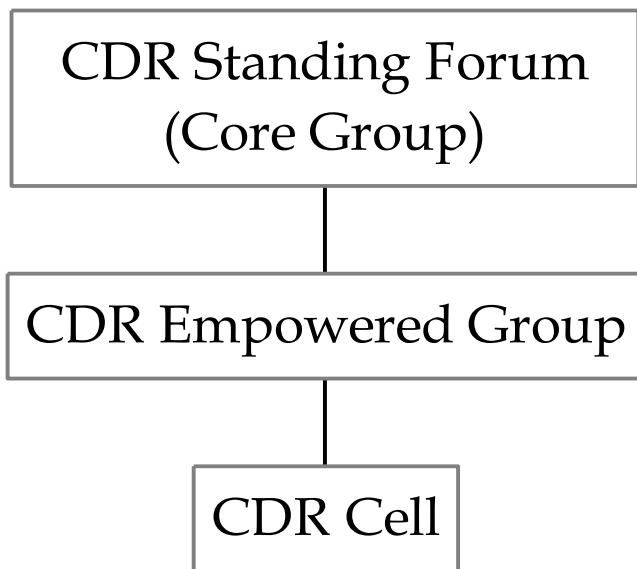
Issues and Solutions in CDR process

IGIDR Roundtable on Recovery & Resolution Mechanisms for Corporate Debt
28th August 2014

Key principles and components of an effective resolution mechanism

- Level playing field for “risk adjusted” process, i.e., no arbitrage
- All stakeholders have skin the game, i.e. incentive for resolution
- Resolution process leads to a “fair” valuation of the stressed asset; legal and regulatory structures are aligned with this price discovery
- Resolution entities are well capitalised

CDR was designed to operate outside of BIFR, DRT and other legal proceedings



- Originated in 2002 since BIFR was not working, one particular FI kept stalling BIFR referrals. 75% of lenders now concurring means ability of a single lender to block is lower
- SARFAESI resulted in a massive rush into restructuring

- CSF: Policy making body
- CEG: EDs of IDBI, SBI, ICICI as Standing Members, EDs of other banks with exposures
- C-Cell is the Secretariat, which received proposals and does workouts

Trends in restructuring across bank groups

Particulars	2009-10		2010-11		2011-12	
	Gross Advances	Restructured Standard Advances	Gross Advances	Restructured Standard Advances	Gross Advances	Restructured Standard Advances (*)
All Banks	17.21	81.17	23.41	0.86	16.88	58.48 (42.54)
Public Sector Banks	19.81	96.59	22.98	3.86	16.02	58.33 (47.86)
Private Sector Banks	12.80	5.60	26.60	(-)28.48	20.65	67.35 (8.12)
Foreign Banks	(-)1.38	(-)25.06	19.06	(-)27.56	16.35	(-)23.76 (-)25.48)

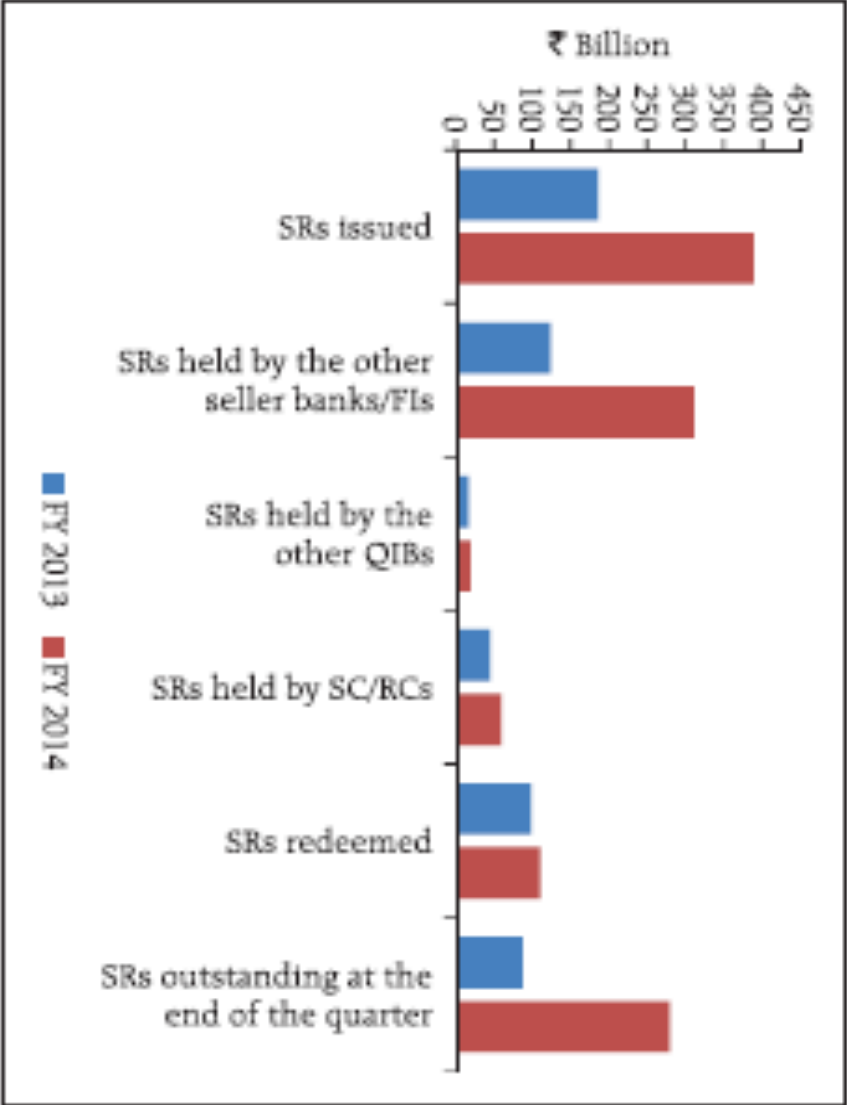
(*) Figures in brackets are the compound annual growth rates between 2009 and 2012

Particulars	March 2009	March 2010	March 2011	March 2012
All Banks	2.73	4.23	3.45	4.68
Public Sector Banks	3.03	4.97	4.20	5.73
Private Sector Banks	2.19	2.05	1.16	1.61
Foreign Banks	0.73	0.55	0.34	0.22

Concerns in CDR process arise from mis-alignment of incentives and arbitrage opportunities for stakeholders

- Arbitrage opportunity for banks to take a P&L hit today vs. pushing it forward
- CDR a good way for banks to protect balance sheet
- Good for borrowers: Little skin in the Game
- Banks willing to go to CDR, but reluctant to lend additional funds for Working Capital; borrowers need to tap additional resources
- CDR vs ARCs: ARCs thinly capitalised, do not have the capital to provide WC

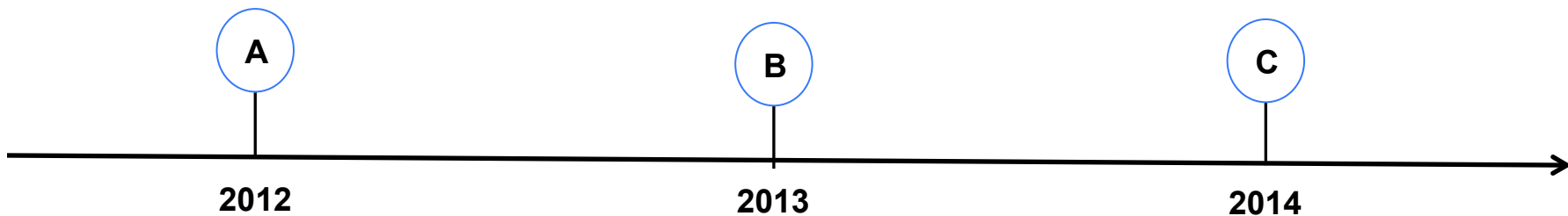
Regulatory pressure led to rise in asset transfers to ARCs



- Increasing provisioning requirements and moral suasion
- But restructuring norms still had potential of arbitrage
- 5 / 95 norm and transfer protocol sufficiently weak to enforce market discipline

Remedial measures to close arbitrage gaps and increase commitment

- Arbitrage window is closing; with requirement for **same** provisioning for new restructured assets beginning April 2015
- Requirement for restructuring borrowers to bring in more “skin in the game”, bring 20% of restructured amount upfront
- Restructuring borrowers need to give a personal, not corporate guarantee
- Remedial measures to identify and respond to potential NPAs with SMA accounting for early detection and Joint Liability Forums for speedier action



Remedial measures timeline

■ Provisioning of restructured standard assets incrementally raised from 2% to 2,75% then to 3.5 % and finally to 5%

2012

■ All incremental restructured assets to be treated like NPAs from April 2015

2013

■ 5 / 95 norm for transfer to ARCs changed to 15 / 85

2014



... but market discipline is the best means of effective resolution

- Intermediate step is to get banks to Mark to Market Security Receipts and / or calibrate valuation for illiquid assets
- Ultimately, need to get banks to sell assets, discover true market price and provision for this

Thank you