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Banks in no hurry to convert NPAs to equity

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KOLKATA: The Securities and Exchange Board of India may have decided to allow banks to turn vulture funds by converting their loans to distressed company into equities, but lenders are unlikely to start acting until they get more clarity on the pricing mechanism, say analysts and bankers.
"We will have to wait and see how exactly the fair price is determined," said DR Dogra, managing director and chief executive of CARE Ratings.

Senior bankers ET spoke to offered similar views. "We are watching the development closely. We may not go for taking majority holding immediately, but this provision would certainly empower us in our dealing with the borrowers," said a bank executive, requesting anonymity.

The new guidelines that Sebi announced on Sunday allow banks to convert debt to equity at a valuation that is mutually agreed upon and based on what the regulator called a "fair-pricing formula". Sebi hasn't explained the formula. Current rules require conversions to be based on market price.

"It is not that banks would immediately jump and start throwing out the management of failing companies because they are not equipped to run businesses, but this enabling provision will empower banks to act appropriately against companies with noncooperative managements," said Shinjini Kumar, PriceWaterhouseCoopers' partner and leader for banking and capital markets.

The Reserve Bank of India has also been trying to correct the power skew in favour of lenders, particularly in view of the burgeoning non-performing assets in the system and the recognition of errant behaviour by promoters.She said Sebi's latest decision was consistent with this approach.

As of September 2014, stressed assets in the banking system totalled 10.7% of loans outstanding. Sebi chairman UK Sinha on Sunday dubbed the new move as a "major development".

If lenders jointly take 51% equi ty, they can control the management or even get a buyer as the majority control is with it. "Once the formula is decided, then banks will be able to ease their NPAs and redeploy capital for other productive assets," CARE's Dogra said.

"With Sebi allowing this conversion, it would mean that certain clauses of Sebi's Issue of Capital and Disclosure Requirements regulations and takeover norms have to change. Both takeover and preferential allotment norms have to be relaxed to make the move effective," Dogra said.As of now, Sebi's stance is that any allotment made outside public transaction is a preferential allotment and preferential allotment guidelines do not fit for negotiated settlement of debts, he explained.