

Banks may tighten loan approval process after Syndicate Bank case

Banks in India are wary of a potential regulatory clampdown, leading to stricter checks that may slow credit approvals



Federal investigators apprehended the chief of state-run Syndicate Bank this month, accusing him of accepting bribes in exchange for providing “financial advantages” to companies. Photo: Bloomberg

Mumbai: The arrest of an Indian banker amid probes into lending violations looks set to prompt tighter loan approvals that may deepen the worst credit slowdown since 2009.

Federal investigators apprehended the chief of state-run **Syndicate Bank Ltd** this month, accusing him of accepting bribes in exchange for providing “financial advantages” to companies. They didn’t elaborate. In a separate case, they started an inquiry against **Kingfisher Airlines Ltd** after it defaulted on debt payments, according to an 12 August exchange filing by **IDBI Bank Ltd**, part of a consortium of creditors to the bankrupt carrier.

Banks in India are wary of a potential regulatory clampdown, according to SBICAP Securities Ltd, leading to stricter checks that may slow credit approvals. Loan growth slumped to 11.6% this month, the least since December 2009, after lenders stepped up efforts to lower bad debt from an eight-year high reached in 2013.

“There has been a perceptible rise in apprehension among public sector bankers on possible scrutiny by investigative agencies on past loan sanctions,” Ravikant Bhat, a banking analyst in Mumbai at

SBICAP Securities, a unit of the nation’s largest lender, said in an e-mail on Tuesday. “It is unlikely the PSBs shall refuse to consider new proposals, especially in a system dominated by them, but significantly higher caution is likely to be observed.”

‘Continuous vigilance’

The finance ministry suspended **S.K. Jain** as chairman and managing director of Syndicate Bank, financial services secretary G.S. Sandhu said in New Delhi on 4 August. Jain, who was arrested a day earlier, was found negotiating for illegal gratification directly as well as through middlemen in exchange for financial favours, the Central Bureau of Investigation (CBI) said in a statement on 2 August.

Three calls to Jain’s mobile phone, who’s still in the custody of federal investigators, went unanswered on Tuesday.

“Continuous vigilance and continuous intelligence gathering are the two things we are focusing on,” Reserve Bank of India (RBI) deputy governor R. Gandhi said in an interview on Tuesday. “A forensic audit may be done when there is a fraud to find the modus operandi.”

The probes into lending irregularities comes at a time when policy makers are pushing to rein in bad debt and strengthen the financial system. RBI governor **Raghuram Rajan**, who highlighted curbing soured credit as among his priorities when he took charge last year, has spurred banks to improve loan recoveries.

Bad loans

The efforts have had some early success. Non-performing debt as a proportion of total advances fell to 4% as of 31 March from 4.2% in September, which was the highest since 2005-2006, according to the latest RBI figures. Loan recoveries at State Bank of India, the biggest lender, more than doubled in the April-June quarter and tripled at Bank of Baroda, ranked second by assets.

“The increased legal scrutiny is part of broader efforts to improve the asset quality at the banks,” Asutosh Kumar Mishra, Mumbai-based banking analyst at Karvy Stock Broking Ltd, said in a phone interview on Tuesday. “While these sort of investigations will weigh on the morale of bankers, investors are keenly waiting to see how these measures will address structural issues at the lenders.”

As lenders focus on improving asset quality, the pace of credit expansion has almost halved from an average 22.3% in the decade through 2013.

Modi's challenge

That is heightening the challenge faced by Prime Minister **Narendra Modi**, who needs to unlock \$255 billion of stalled projects to spur investments and revive the economy. Gross domestic product (GDP) increased 4.7% in the year through March, a pace that's just above the decade-low 4.5% in the previous period.

Lending has also slowed as the highest interest rates among Asia's biggest economies damped demand for credit. RBI governor Rajan raised the repurchase rate three times since he took charge a year ago to tame price pressures. He left the benchmark unchanged at 8% at 5 August review.

The yield on five-year AAA corporate notes rose 16 basis points this quarter to 9.35%, while that on 10-year government debt dropped 19 basis points to 8.56%. The rupee declined 0.4% to 60.4350 per dollar.

Bond risk for Indian banks has rebounded from a three-year low in June. The average cost of credit-default swaps insuring the bonds of five lenders has climbed to 194 basis points from a low of 185 on 10 June, according to data provider CMA.

'Being circumspect'

While the federal probes may prompt banks to tighten credit assessment methods, they probably won't have an impact on the pace of lending, according to CARE Ratings Ltd. Instead, loan growth will be influenced more by the performance of the economy, according to the ratings company.

"The recent developments will definitely lead to banks being more circumspect when lending," D.R. Dogra, managing director in Mumbai at CARE Ratings, said in a telephone interview on 25 August. "This is good for the system considering that non-performing assets have been increasing and banks need to hone their credit appraisal techniques. To my mind, this will not have a significant bearing on the growth in credit which is dependent on the overall state of the economy." **Bloomberg**