

Default jitters calm for India lenders on \$12bn fund boost

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The Reserve Bank of India in Mumbai. The RBI's capital relaxation has reduced the pressure on lenders to raise equity and additional Tier 1 capital, but this doesn't totally eliminate their capital requirements, said an official at CARE Ratings.



Bloomberg/Mumbai

Default risk for Indian banks is dropping after the government promised a fund infusion for state-owned lenders to clear soured loans and the central bank relaxed rules on their capital buffers.

The average of credit default swaps of five Indian lenders has fallen 20 basis points to 199 since February 29, when Finance

Minister Arun Jaitley said the government will infuse at least Rs250bn (\$3.7bn) of capital into state-owned lenders. It fell to a two-month low of 192 basis points on March 11, according to data compiled by Bloomberg.

The Reserve Bank of India said on March 1 it would allow banks to treat some items on their books as common Tier 1 equity, which according to CLSA Ltd could free up as much as \$8bn in capital for state-run lenders. Brokerages and rating companies said more support may still be needed to revive credit growth that fell to an average of 10% over the last year, compared with a five-year rate of 14.7%.

"Investors are getting more comfort from the measures and so CDS spreads for Indian banks are easing as the market perceives government support for public sector banks," said Rajesh Mokashi, deputy managing director at CARE Ratings Ltd. "To some extent, the RBI's capital relaxation has reduced the pressure on lenders to raise equity and additional Tier 1 capital, but this doesn't totally eliminate their capital requirements."

The government plans to infuse the funds in the financial year starting April 1 to boost capital buffers of banks and help them deal with stressed debt.

Moody's Investors Service said last month it expects 11 state-owned lenders to need Rs1.45tn of "external capital" until the fiscal year through March 2019. The estimate "factors in the full extent of the asset quality issues that the banks are facing," Moody's said.

RBI is "relaxing the capital norms for lenders as some of them are facing difficulties meeting the minimum capital requirements under Basel III," Nicholas Yap, a credit analyst at Mitsubishi UFJ Securities in Hong Kong said in an interview March 15. "Poor, and in some cases negative, profitability on the back of higher loan impairments is eroding the capital position of lenders."

The Basel Committee unveiled rules in December 2010 aimed at bolstering the capital of lenders and improving their ability to absorb losses. The changes came after the global financial crisis exposed inadequate buffers to balance sheets.

Problem loans, which include bad debt, restructured loans and written-off assets, rose to 14.1% of total loans as of September 30, the highest in at least 15 years, data compiled by RBI show. Another 4% might sour, bringing total non-performing loans to 18%, when the audit driven by RBI finishes on March 31, Credit Suisse Group AG forecasts. Finance Minister Jaitley said in August India's public sector banks will require Rs1.8tn of infusions in equity to comply with international standards under the Basel III accord.

"The worst seems to be behind us," according to Saswata Guha, director for financial institutions at Fitch Ratings. "When banks get done with provisioning for existing stressed assets, things should start looking better."