NPA Ordinance

What is the issue?

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- Banking Regulation (Amendment) Ordinance has been promulgated. It is aimed at resolving the non-performing assets (NPA) crisis in the banking sector.
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- It creates an illusion of state action, and does little by way of addressing the real concerns.
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What are the problems with the ordinance?

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- Capital allocated for the banking sector in the 2017-18 Union budget, or as part of the mid-term capital infusion plan, falls short of what the banks collectively need.
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- In **absence of additional capital,** the RBI's directions to the banks under the ordinance may impede the resolution process.
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- The RBI may have no option but to direct the banks to extend lifelines to unviable companies to defer the problem to a future date.
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- For the banks, resolving these cases requires the most capital.
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- Given the lack of capital, banks could be given the regulatory cover under the ordinance to refinance these large corporate debtors.
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What are the hurdles for RBI in handling NPA's?

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- **The tools available to RBI are limited.** If the RBI intervenes on a case-by-case basis, questions about conflict of interest, regulatory capacity and capability will arise.
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- If RBI intervenes through general rules and conditions, this will be no different from the corporate debt restructuring (CDR) mechanism, the strategic debt restructuring (SDR) scheme, and the scheme for sustainable structuring of stressed assets (S4A) that have failed in the past to resolve the problem.
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- Either way, the ordinance puts RBI's credibility and reputation as a micro-prudential regulator at stake.
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- If the RBI is to now get directly involved in these loan restructuring decisions, or indirectly through committees reporting to it, this would put it in a difficult spot.
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What is the way forward?

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- Resolving a bank's NPAs requires resolving the entity to which money has been lent.
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- By empowering the RBI to act, the government has taken away any incentive of the banks to act on their own.
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- The ordinance was presumably brought about because banks on their own could not trigger IBC proceedings against the stressed companies for fear of investigation and prosecution, or due to lack of capital or because of challenges in negotiating with politically connected promoters.
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- The ordinance gives banks the regulatory cover to take resolution-related decisions but it is not clear whether it also gives the required political cover.
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Source: Live Mint

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