

PARA (Public Sector Asset Rehabilitation Agency)

Why in News?

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The Economic Survey 2016-17 called for a need to set up a government-owned asset reconstruction company, PARA.

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What is TBS?

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- The Economic Survey of 2015-16 recognised a key issue called 'the twin balance sheet' problem.

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- The balance sheets of both public sector banks (PSBs) and some corporate houses private entities are in bad condition i.e overleveraged and distressed private companies and the rising NPAs in Public Sector Bank balance sheets.

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- India has been fighting with its twin balance sheet (TBS) problem since global financial crisis.

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- It is important because it is discouraging private investment in the country and hence growth in all sectors.

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What is the current situation?

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- TBS was considered a minor problem, which would be resolved as economic recovers. But the problem has only worsened.

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- Earnings of the stressed companies have deteriorated, forcing them to borrow more to sustain their operations.

- Since 2007-08, the debts of the top 10 stressed corporate groups have multiplied five times.
- Around 12% of the gross advances of public sector banks turned non-performing.
- Hence the private corporate sector has been forced to curb its investments, while banks have been reducing credit in real terms.
- To sustain growth, these trends should to be reversed and the only way to do so is by fixing the underlying balance sheet problems.

What is the need for centralised approach?

- **Size** - So far, the strategy has been to solve the TBS through a decentralised approach. The banks have been put in charge of the restructuring decisions.
- But it has become less effective because the banks have simply been overwhelmed by the size of the problem.

- **Companies** - It's not just about banks, but it is also a lot about companies. So far, public discussion of the bad loan problem has focused on bank capital. But securing funding is actually the easiest part than finding a way to resolve the bad debts.
- **Not just a moral problem** - Though crony capitalism and diversion of funds is also important reasons, a bulk of the problem has been caused by unexpected changes in the economic environment. Therefore it
- Stressed debt is heavily concentrated in large companies.
- Many of these companies are unviable at current levels of debt, requiring debt write-downs.

- Banks are finding it difficult to resolve these cases, despite a proliferation of schemes to help them.
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- Other mechanisms like Private Asset Reconstruction Companies (ARCs) haven't proved any more successful than banks in resolving bad debts and are too small to handle the large cases.
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- Delay is costly - Since banks can't resolve the big cases, they have simply refinanced the debtors. But this is costly for the government, because it means the bad debts keep rising, increasing the ultimate recapitalisation bill.
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- Therefore a centralized approach could eliminate most of the obstacles currently plaguing loan resolution.
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How would a PARA actually work?

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- It could solve the coordination problem since debts would be centralised in one agency.
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- It could be set up with proper incentives by giving it an explicit mandate to maximise recoveries within a defined time.
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- It would separate the loan resolution process from concerns about bank capital.
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- It would purchase specified loans from banks and then work them out, depending on professional assessments of the value-maximising strategy.
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- Once the loans are off the books of the public sector banks, the government would recapitalise them, thereby restoring them to financial health.
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- Similarly, once the financial viability of the over-indebted enterprises is restored, they will be able to focus on their operations, rather than their finances.

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Source: The Indian Express

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