THE PUBLIC UNRAVELLING OF YES BANK

Relevant for: Indian Economy | Topic: Issues relating to Growth & Development - Banking, NPAs and RBI

On Sunday, the Enforcement Directorate (ED) arrested Yes Bank’s swashbuckling co-promoter Rana Kapoor, accusing him and his family of using shell companies to receive kickbacks from the bank’s corporate borrowers.

On March 5, the Reserve Bank of India (RBI) had used its powers to supersede the bank’s board and impose restrictions on its operations. The bank’s depositors cannot withdraw more than 50,000 for the next four weeks at least. Predictably, the State Bank of India (SBI) has emerged as Yes Bank’s knight in shining armour. Surprisingly, though, it is crowd-sourcing the rescue plan.

The manner in which the Yes Bank collapse has unravelled raises several questions. The full extent of its troubles spilled into the public domain two years ago, when, in September 2018, the RBI had declined to extend Mr. Kapoor’s term as managing director and chief executive officer by three years. It directed the bank to end his tenure by January 31, 2019.

The scam on the bank’s balance sheets must have been visible to the RBI as far back as in 2015. The RBI’s asset quality review (AQR) had forced Yes Bank, as it had several other banks, to report transparently their previously unstated non-performing assets (NPAs).

Before the AQR in 2015, bankers avoided recognising bad loans on their books. They did this by restructuring the loans susceptible to defaults or by extending new loans, called evergreening, to keep the stressed borrowers afloat. Thus, while the borrowers were able to avoid defaults on repayments, the lenders managed to show low NPAs.

The RBI found that for the year ended March 2016, Yes Bank had classified loans worth 749 crore as gross NPAs, understating the figure by a whopping 4,176.70 crore. It directed Yes Bank to reclassify more loans as NPAs. Disclosing this to the stock exchanges in May 2017, Yes Bank assured investors that the higher NPAs would not have further ramifications as it had already taken remedial action.

However, just five months later, in October 2017, the bank disclosed, once again, that the RBI had discovered more underreported gross NPAs on its books. For the year ended March 2017, the under reporting was of the tune of 6,355 crore.

Why has the ED then swung into action so late, giving Mr. Kapoor 18 months to cover his tracks and potentially remove all the money he can from the bank in this period? If the RBI’s inspections of the bank’s books left it with no confidence in Mr. Kapoor, surely then that ought to have been a smoking gun to suspect if not investigate his role in Yes Bank’s serial under-reporting of NPAs. Also, Yes Bank was looking for investors for the last few months. The moratorium and the investigation against Mr. Kapoor seem to have been triggered by the failure to find investors. This suggests that had investors been found, Mr. Kapoor may have escaped action. After all the RBI’s discomfort with him was known even back in 2018. Why didn’t the ED take action at that time?

In December 2018, barely two months after Mr. Kapoor’s extension was rejected, former RBI Governor Urjit Patel resigned from the central bank. Did the RBI and other authorities go soft on Yes Bank after that? Its transgressions continued even after the RBI fined the bank and forced changes in its management. For the year ended March 2019, the RBI discovered underreported

NPAs worth 2,299 crore. Incidentally, around the time the moratorium was announced last Thursday, news broke of another resignation at the RBI. This time of its well-regarded Deputy Governor N.S. Vishwanathan, a specialist in regulation, supervision of banks and non-banking finance companies. The exit follows a four-decade career at the RBI and just three months ahead of his retirement in June. Was it prompted by the health issues cited or a protest against the RBI’s stance on policy matters such as handling of Yes Bank?

And what of the bank’s shareholders? Why did they ratify remuneration hikes and a renewal of tenure for Mr. Kapoor despite public information of the serial underreporting of NPAs? The regulators must ensure now that all current equity held by Yes Bank holders should get wiped out since it represents a pure risk capital. If this is not done, any investment by Yes Bank’s saviour, the SBI, will be a subsidy to them. Let us not forget that barely two years ago, the SBI and its associate banks received 8,800 crore in recapitalisation from the Central government. Other public banks received more.

How credible can the rescue be when barely three months ago the SBI had disclosed that the RBI has discovered under-reported NPAs — of 11,932 crore for the year ended March 2019 — on its books?

Most importantly, why are public comments being sought on the restructuring scheme for Yes Bank? This is unfair to the SBI. The restructuring scheme is no one’s business other than the SBI’s. After this precedent, next time a bank, say a Kotak Mahindra Bank or HDFC Bank, is to get an investment from a new investor, will that scheme also be put up for public comments?

If this were a commercial decision taken by the SBI, and not capitulation before the government of the day, it would have put greater financial might and a well-crafted plan behind the rescue.

Finally, what other options were considered by the RBI? Did they include a market-based solution? DBS Bank has just turned into a wholly-owned subsidiary of its Singaporean parent. Could Yes Bank’s network of branches been of interest to it? Ideally, the moratorium ought to have been announced, together with the scheme for restructuring, over a weekend. That would have made it less disruptive, the limit of 50,000 on withdrawals by depositors would not have been needed, and the RBI’s credibility would not have suffered as much.

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To reassure Indian Muslims, the PM needs to state that the govt. will not conduct an exercise like NRC

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