

Analysis on

Framework for One-Time Restructuring and Financial Parameters based on Expert Committee Report

RBI Circulars dated August 06, 2020 and September 07, 2020

September 2020

Economic Crisis and Financial Packages

<p>Covid-19 led Financial Crisis</p>	<ul style="list-style-type: none"> ▪ Covid-19 pandemic and the resultant economic strain has changed the way businesses are being run ▪ Restriction on mobility led to overall demand destruction and financial crisis worldwide
<p>Proactive Government Response to the Crisis</p>	<ul style="list-style-type: none"> ▪ Government of India along with Reserve Bank of India announced ₹ 20 trillion Financial Stimulus Package to enable the businesses to revive and re-start post the near 4-month hiatus ▪ Reserve Bank of India announced moratorium on the loans till August 31, 2020
<p>Reserve Bank of India Framework on Financial Restructuring</p>	<ul style="list-style-type: none"> ▪ Existing restructuring framework under June 07, 2019 RBI circular entails downgrade of restructured loan asset, except where change in ownership is proposed in the Resolution Plan ▪ RBI on August 06, 2020 issued guidelines for one-time restructuring with the existing promoters with the benefit of account remaining standard
<p>Expert Committee to advice on restructuring framework parameters</p>	<ul style="list-style-type: none"> ▪ The one-time restructuring framework inter alia envisages constitution of an Expert Committee under the Chairmanship of Shri K V Kamath ▪ The Committee to recommend on financial parameters that should be factored into resolution plan finalised by the by the lending institutions covering leverage, liquidity, debt serviceability, etc.

Key Features of Resolution Framework for Covid-19 related Stress

Applicability	Eligibility	Key Dates
<ul style="list-style-type: none"> ▪ Applicable to <ul style="list-style-type: none"> - Commercial banks (including small finance banks, local area banks and regional rural banks) - Primary (Urban) Co-operative Banks / State Co-operative Banks / District Central Co-operative Banks - All-India Financial Institutions - Non-Banking Financial Companies (including Housing Finance Companies) ▪ Not applicable on Exposure to <ul style="list-style-type: none"> - Farm Credit - Financial service providers - Housing Financial Companies where the account was rescheduled after March 01, 2020 - State and Central Governments 	<ul style="list-style-type: none"> ▪ Borrowers with aggregate exposure of up to ₹ 25 Crore as on March 01, 2020¹ ▪ Borrower whose account was standard but not in default for more than 30 days as on March 01, 2020 ▪ Accounts should continue to remain standard till the date of invocation ▪ Date of invocation not later than December 31, 2020 ▪ Implementation is not done within 180 days from the date of invocation ▪ Invocation by 75% in value and 60% in number of lenders 	

¹ Separate guidelines are issued for MSME borrowers whose aggregate exposure to lending institutions collectively, is ₹25 Crore or less as on March 01, 2020.

Framework and Permitted Features of Resolution Plan

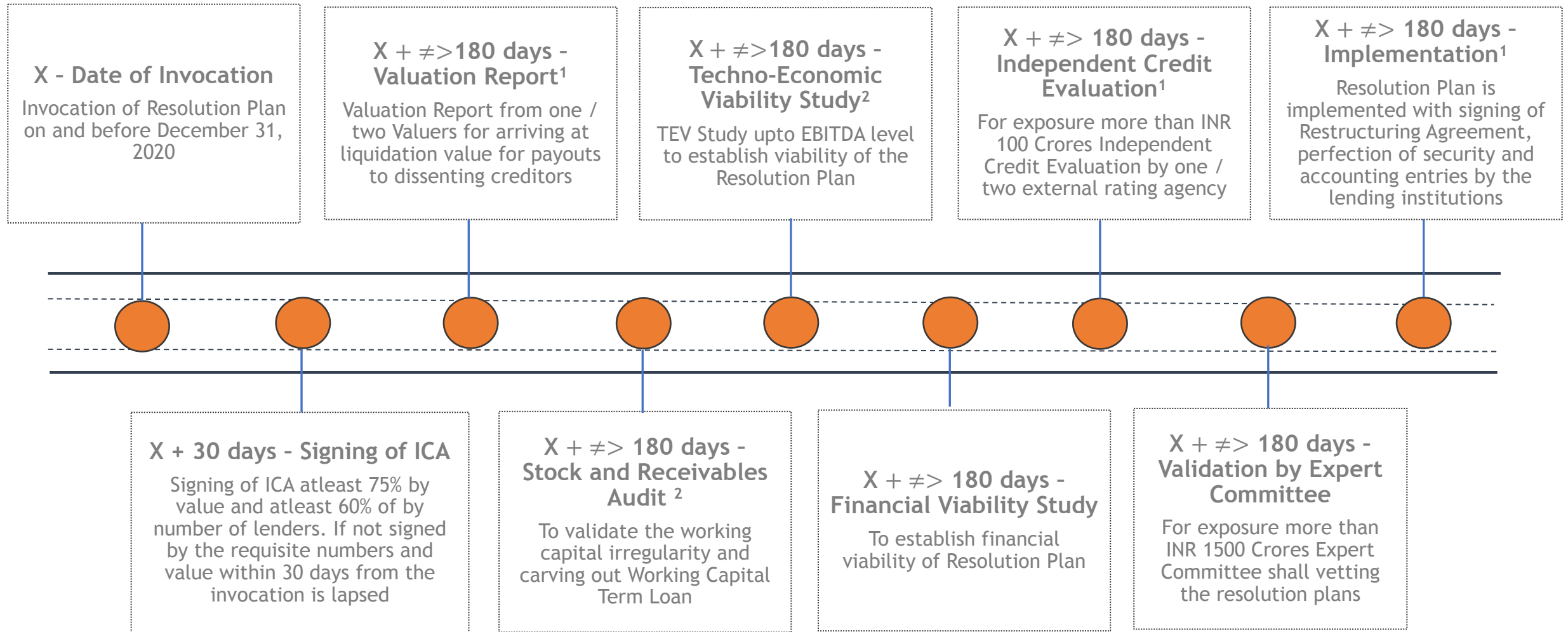
Framework on One Time Restructuring Mechanism

- Enables Lenders to implement a Resolution Plan without change in ownership, while classifying such accounts as Standard
- The resolution under this Framework is extended only to borrowers having stress on account of Covid-19
- Lending institutions are required to sign an inter-creditor agreement ahead of the restructuring
- If 60% of the lenders by number and 75% by value do not sign the ICA, then the invocation would be considered as lapsed. The one-time restructuring scheme cannot be invoked again for such cases
- In cases where aggregate exposure of the lending institutions is more than INR 1,500 Crore, then the Expert Committee shall have the responsibility of vetting the resolution plans to be implemented

Permitted features of Resolution Plan

- Resolution Plan may include sanctioning of additional credit facilities to address the financial stress on account of Covid-19, even if there is no renegotiations of the existing debt
- Extension of the residual tenor of the loan, with or without moratorium, by a period not more than two years
- Resolution Plan may provide for conversion of debt into equity or other marketable non-convertible debt securities provided amortization and coupon are similar to terms of debt
- Equity to be valued as per lower of breakup value or DCF value (for unlisted companies) and market price (for listed companies). Any other instrument to be valued at INR 1
- In cases where aggregate exposure is more than INR 100 Crore, then an Independent Credit Evaluation (ICE) by any on Credit Rating Agency

Resolution Process and Timeline



¹ As per RBI's August 06, 2020 Circular, all the norms applicable to implementation of a Resolution Plan, including mandatory requirements of ICA and specific implementation conditions, as laid out in June 07, 2019, circular are applicable to all lending institutions for the RP implemented under August 06, 2020 circular

² Policy of respective lending institutions

@ Forensic audit is mandated for all NPA accounts by RBI vide July 01, 2016 and June 07, 2019 circular with aggregate exposure of INR 50 Crore and above. It needs to be outlined that as the accounts, under RBI's August 06, 2020 Circular are standard on date of identification for restructuring, no forensic audit will be required if the account happens to slip during the implementation period of 180 days.

Financial Parameters Threshold for Resolution Process

Parameters	Definition	Timeline to achieve financial threshold
Total Outside Liability / Adjusted Tangible Net Worth (TOL / Adjusted TNW)	Addition of long-term debt, short term debt, current liabilities and provisions along with deferred tax liability divided by the tangible net worth net of the investments and loans in the group and outside entities	Ensure compliance to TOL / ATNW agreed as per the resolution plan at the time of implementation. Should be met for each year as per the resolution plan starting from FY 2022
Total Debt / EBIDTA	Addition of short term and long-term debt divided by addition of profit before tax, interest and finance charges along with depreciation and amortisation.	Should be met for each year as per the resolution plan starting from FY 2022
Current Ratio	Current assets divided by current liabilities	Should be met for each year as per the resolution plan starting from FY 2022
Debt Service Coverage Ratio (DSCR)	For the relevant year, addition of net cash accruals along with interest and finance charges divided by addition of current portion of long-term debt with interest and finance charges	Should be met for each year as per the resolution plan starting from FY 2022
Average Debt Service Coverage Ratio (ADSCR)	Over the period of the loan, addition of net cash accruals along with interest and finance charges divided by addition of current portion of long-term debt with interest and finance charges	Should be met for each year as per the resolution plan starting from FY 2022

Sector-wise Financial Parameters prescribed by Expert Committee

Industry	TOL / ATNW	Total Debt/ EBITDA	Current Ratio	Average DSCR	DSCR
Auto Components	<= 4.50	<= 4.50	>= 1.00	>= 1.20	>= 1.00
Auto Dealership	<= 4.00	<= 5.00	>= 1.00	>= 1.20	>= 1.00
Automobile Manufacturing	<= 4.00	<= 4.00	NA	>= 1.20	>= 1.00
Aviation	<= 6.00	<= 5.50	>= 0.40	NA	NA
Building Materials - Tiles	<= 4.00	<= 4.00	>= 1.00	>= 1.20	>= 1.00
Cement	<= 3.00	<= 4.00	>= 1.00	>= 1.20	>= 1.00
Chemicals	<= 3.00	<= 4.00	>= 1.00	>= 1.20	>= 1.00
Construction	<= 4.00	<= 4.75	>= 1.00	>= 1.20	>= 1.00
Consumer Durables / FMCG	<= 3.00	<= 4.00	>= 1.00	>= 1.20	>= 1.00
Corporate Retails Outlets	<= 4.50	<= 5.00	>= 1.00	>= 1.20	>= 1.00
Gems & Jewellery	<= 3.50	<= 5.00	>= 1.00	>= 1.20	>= 1.00
Hotel, Restaurants, Tourism	<= 4.00	<= 5.00	>= 1.00	>= 1.20	>= 1.00
Iron & Steel Manufacturing	<= 3.00	<= 5.50	>= 1.00	>= 1.20	>= 1.00
Logistics	<= 3.00	<= 5.00	>= 1.00	>= 1.20	>= 1.00
Mining	<= 3.00	<= 4.50	>= 1.00	>= 1.20	>= 1.00
Non-Ferrous Metals	<= 3.00	<= 4.50	>= 1.00	>= 1.20	>= 1.00
Pharmaceuticals Manufacturing	<= 3.50	<= 4.00	>= 1.00	>= 1.20	>= 1.00
Plastic Products Manufacturing	<= 3.00	<= 4.00	>= 1.00	>= 1.20	>= 1.00
Port & Port Services	<= 3.00	<= 5.00	>= 1.00	>= 1.20	>= 1.00
Power					
- Generation	<= 4.00	<= 6.00	>= 1.00	>= 1.20	>= 1.00
- Transmission	<= 4.00	<= 6.00	>= 1.00	>= 1.20	>= 1.00
- Distribution	<= 3.00	<= 6.00	>= 1.00	>= 1.20	>= 1.00
Real Estate					
- Residential	<= 7.00	<= 9.00	>= 1.00	>= 1.20	>= 1.00
- Commercial	<= 10.00	<= 12.00	>= 1.00	>= 1.20	>= 1.00
Roads	NA	NA	NA	>= 1.10	>= 1.00
Shipping	<= 3.00	<= 5.50	>= 1.00	>= 1.20	>= 1.00
Sugar	<= 3.75	<= 4.50	>= 1.00	>= 1.20	>= 1.00
Textiles	<= 3.50	<= 5.50	>= 1.00	>= 1.20	>= 1.00
Trading - Wholesale @	<= 4.00	<= 6.00	>= 1.00	Interest Coverage Ratio	>= 1.70
Others not Specified Above		To be decided by the lenders		>= 1.20	>= 1.00

- These Parameters are intended as floors or ceilings, as the case may be, but the resolution plans shall take into account the pre-Covid-19 operating and financial performance of the borrower and impact of Covid-19 on its operating and financial performance at the time of finalising the resolution plan, to assess the cashflows in subsequent years, while stipulating appropriate ratios in each case.
- No threshold has been prescribed for Current Ratio for Automobile Manufacturing due to the “just in time inventory” business model for raw materials and parts, and finished goods inventory is funded by channel financing available from the dealers
- DSCR thresholds for Aviation have not been prescribed since most of the airline companies work on refinancing of debt as a financing strategy. Consequently, average DSCR threshold is also not prescribed.
- For the real estate sector, the parameters to be considered at project level rather than at entity level.
- For the roads sector, the financing is cash flow based and at SPV level where the level of debt is decided at the time of initial project appraisal. The working capital cycle in this sector is also negative. Accordingly, ratios like TOL / ATNW, Debt/EBITDA and Current ratio may not be relevant at the time of restructuring in this sector.
- Most of the companies in Trading Wholesale sector do not use long term debt for funding their operations and are unlisted. Hence DSCR and average DSCR may not be relevant for the sector.

Asset Classification by Lending Institutions

	Existing Credit Facilities	Additional Finance
Between Invocation date and Implementation date	Asset Classification based on the IRAC Circular of RBI shall be applicable	May be classified as “Standard” till implementation of the plan regardless of the actual performance of the borrower
If Resolution Plan is implemented within 180 days	Accounts classified as “Standard” may be retained as “Standard” whereas the accounts which may have slipped into NPA between invocation and implementation may be upgraded as “Standard”	May be classified as “Standard”
If Resolution Plan is not implemented	Asset Classification based on the IRAC Circular of RBI shall be applicable	Asset Classification based on the IRAC Circular of RBI shall be applicable

Provisioning Requirement by Lending Institutions

	Lenders who signed the Inter Creditor Agreement within 30 days of invocation	Lenders who did not sign the Inter Creditor Agreement within 30 days of invocation
If Resolution Plan is implemented within 180 days	Provisioning higher of: a) As per IRAC Circular of RBI; or b) 10% of Residual Debt ¹	Provisioning higher of: a) As per IRAC Circular of RBI; or b) 20% of Carrying Debt ²
If Resolution Plan is not implemented	Provision based on the existing IRAC guidelines of RBI shall be applicable	

¹ Residual Debt - Total debt including Debt Securities issued post implementation; ² Carrying Debt - Debt on the lender's books as on expiry of 30 days for signing of ICA

- Any additional provisions maintained by lending institutions in terms as per Prudential Framework, wherever applicable, may be reversed at the time of invocation of the resolution
- For the lenders who signed ICA, half of the provisions made post implementation of resolution plan may be written back upon the borrower paying at least 20% of the residual debt without slipping into NPA and the remaining half may be written back upon the borrower paying another 10 per cent of the residual debt without slipping into NPA subsequently
- In respect of the non-ICA signatories while half of the provisions may be reversed upon repayment of 20 percent of the carrying debt, the other half may be reversed upon repayment of another 10 per cent of the carrying debt, subject to the required IRAC provisions being maintained.

Resolution Framework for MSME Borrowers

Eligibility

- The aggregate exposure, including non-fund based facilities, of banks and NBFCs to the borrower does not exceed ₹25 Crore as on March 01, 2020.
- The borrower's account should be "Standard" as on March 01, 2020
- The borrowing entity is GST-registered on the date of implementation of the restructuring

Implementation Timeline

- The restructuring of the borrower account is implemented by March 31, 2021

Asset Classification

- Borrowers which may have slipped into NPA category between March 02, 2020 and date of implementation may be upgraded as "Standard", as on the date of implementation of the restructuring plan.

Provision Requirement

- Accounts restructured under these guidelines, banks shall maintain additional provision of 5% over and above the provision already held by the lending institutions.

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About Think Capital

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