Banking Capital

For Growth and Stressed Asset Resolution

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Current Issues

Main Issues:

- Capital constraints and stressed assets at PSBs are posing structural constraints for GDP growth
- Tier 1 Capital Requirement for PSBs till March 2019 : Rs. 1 – 1.2 trillion
- Stressed Assets takeover (through GoI owned ARC) may need an additional Rs. 600 billion
- Fiscal Constraints don't allow for such large equity infusion over next two years

Additional Issues:

- Moral Hazard Issue of 'Govt money being used for Funding Losses'
- No visibility on some PSBs turning around
- Too many PSBs – Consolidation is the need of the hour
- PSBs with phenomenal franchise are available at the fraction of the valuation of Private Sector because of profitability and growth concerns
- Resolution of bad loans: Process is slow and haircuts seem large
- CVC / CBI and tough agreements in the past make resolution process slow

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Group the PSBs to determine Capital Requirement

Group	Approach	Indicative List
Group 1 (8 PSBs, market share ~70%) (Net NPAs in relation to Operating Profits <2.5)	• Banks to focus on providing credit to support growth • No need to merge / Consolidate • Govt to provide Capital to Support Growth	Indicative List: SBI, PNB, BoB, BoI, Canara, Union, Indian & Vijaya
Group 2 (7 PSBs, market share ~15%) (Net NPAs in relation to Operating Profits 2.5-4.5)	• Need to reorient / Merge • Restricted Capital to help them reorient	Indicative List: Allahabad, Andhra, Corp, OBC, P&SB, Synd & United
Group 3 (6 PSBs, market share ~15%) (Net NPAs in relation to Operating Profits >4.5)	• No visibility on Profits • Get Capital through asset sale, Govt support only for deposit holders	Indicative List: BoM, CBI, Dena, IDBI, IOB & UCO

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Capitalize, Growth Capital for Economic Activity, Consolidate and Conserve

Group 1 (Net NPAs in relation to Operating Profits <2.5)	Rs. 640 billion **Growth Capital**	Target market share Gain, ROE 12%-15%, Growth in excess of 10%, Net NPA to net worth of less than 10%
Group 2 (Net NPAs in relation to Operating Profits 2.5-4.5)	Rs. 220 billion **Consolidate**	Target Consolidation with ROE 8-9%, Growth 5%, Net NPA to Networth 25-35%
Group 3 (Net NPAs in relation to Operating Profits >4.5)	Rs. 360 billion **Conserve**	Minimise equity infusion through sale of assets, Branches, or the majority stake

Size the Capital for Stressed Asset Resolution

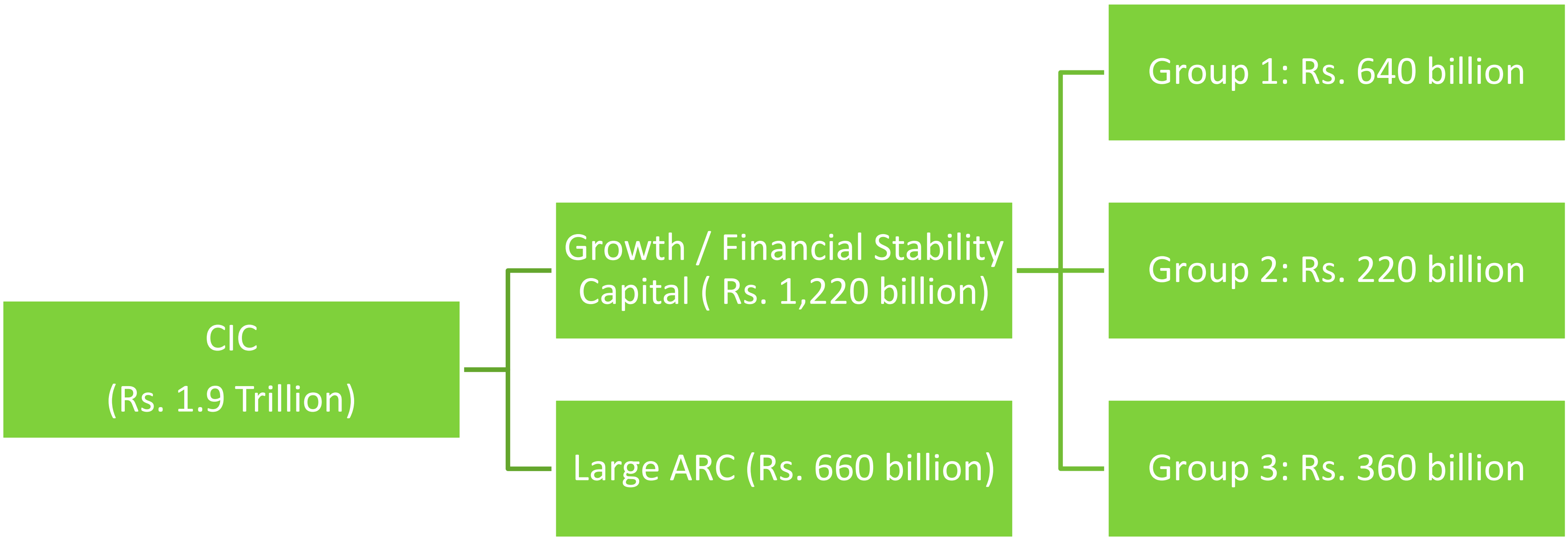
Rs. 7,330 Billion Gross NPAs

Rs. 4,400 Billion

- ARC takes over 60%

Rs. 660 Billion Equity Required

Overall Capital Map



Proposed Structure

- Transfer Equity worth Rs. 1 trillion to the holding company
  - Fiscal Deficit neutral
- CIC gets Capitalized to the extent of Rs. 1 trillion
- CIC can be leveraged to the extent of Rs. 2.3 Trillion
- Borrow to the extent of Rs. 2 trillion
  - Issue 15 year Tax free bonds to the extent of Rs. 0.5 – 0.6 trillion
  - Issue bonds worth Rs. 1.4-1.6 trillion, bonds to be backed by future GOI infusion, bonds subordinated to tax free bonds
    - Subscribers: Multilaterals / FPIs/ NRIs
- Commit annual budgetary allocation of Rs. 250 billion for next ten years
- Contract can be cancelled with a notice period of 11 years

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Projected Scenario

Issue	Addressed
•Capital constraints and stressed assets at PSBs are posing structural constraints for GDP growth	Addressed through Group 1
Impact on Fiscal Deficit	Nil
•Capital Gaps of Rs. 2 Trillion	Addressed
•Moral Hazard Issue of ‘Govt money being used for Funding Losses’	Addressed through ‘Limited Support to ‘Group 3 banks’
•No visibility on some PSBs turning around	
•Too many PSBs – Consolidation is the need of the hour	Group 2 Banks

Projected Scenario

Issue	Addressed
•PSBs with phenomenal franchise are available at the fraction of the valuation of Private Sector because of profitability and growth concerns	Different trajectory for Group 1, Group 2 and Group 3
•Resolution of bad loans: Process is slow and haircuts seem large	Addressed through Govt. owned ARC
•CVC / CBI and tough agreements in the past make resolution process slow	
Likely position of CIC at the end of 10 years	Net worth of over Rs. 2 trillion Liabilities of Rs. 0.2 – 0.3 trillion

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Thank you!

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