Yes Bank in Moratorium: How it Collapsed and What Next?

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Summary

The private sector Yes Bank Limited, which was granted banking licence in 2004, had been showing steady signs of decline in its asset quality. There were also issues of questionable corporate governance, weak regulatory compliance and its inability to raise adequate capital to cover potential non-performing accounts. In the face of such decline in the bank's financial health, the government has imposed a moratorium on the bank and capped withdrawals. The Reserve Bank of India has also proposed a restructuring plan for the bank.

Career bankers Rana Kapoor and Ashok Kapur launched Yes Bank Limited in 2004. They were related as their wives were sisters. The latter was unfortunately killed in the terrorist attack in Mumbai in 2008. That enabled Rana to take total control of the bank. He did not allow the daughter of the deceased promoter to join the Board, which led to a corporate litigation.

It was initially believed that Yes Bank would be built and sold to a foreign bank in three to four years. However, with regulatory restrictions on foreign ownership being introduced and the Lehman Brothers crisis overtaking the financial markets, the sale did not take place. Yes Bank commenced lending very aggressively and, by 2014, its loan book had grown to about US$10 billion (S$13.8 billion). By 2018, it had grown to US$40 billion (S$55.1 billion). Just about all the growth was through corporate lending. Borrower experience in India had it that, if financial institutions were hesitant to lend to a borrower perceived in the market to be risky, Yes Bank would come forward to lend despite the risk element. What seemed incredibly 'good performance' was that, in spite of such fast growth in the loan book, the bank managed to keep its non-performing assets (NPA) below 0.5 per cent. In an environment wherein other banks were running into very high non-performing loans, such a low figure prompted the Reserve Bank of India (RBI) to monitor Yes Bank's books closely. It was revealed that the bank was indulging in clever ever greening, lending to subsidiary companies and, in fact, even misrepresenting facts on its books. Close scrutiny revealed that the actual NPA surged about 87 per cent in the last quarter of 2016. The bank was found to have heavy exposure to lower-rated corporates. Corporate governance lapses were perceived with divergences in the reporting of stressed accounts.

A recent report by Jefferies Financial Group on stress exposure across major accounts revealed that among high risk borrowers, while the exposure of other private sector banks such as ICICI Bank and HDFC Bank was US$500 million (S$689 million) and US$250 million (S$344.5 million) respectively, Yes Bank's exposure was US$2 billion (S$2.76 billion). While regulatory compliance requires that exposure to group companies be restricted, Yes Bank's lending to Reliance ADAG's finance businesses stands at US$2.6 billion (S$3.6 billion), with Axis Bank (its peer), having the largest exposure at US$100 million (S$138 million), with ICICI Bank and HDFC Bank together at US$95 million (S$131 million). The total exposure of Yes Bank to Reliance ADAG across its businesses is a stupefying US$200 million (S$276 million). Yes Bank's exposure to Cox & Kings, again a high-risk borrower in Jefferies' report, is US$20 million (S$27.6 million). The State Bank of India (SBI) from the state-owned segment has an exposure of US$10 million (S$13.8 million) to this entity. This is illustrative of the rather 'risky' lending by Yes Bank, leading to the stress on its books and the erosion of its capital.

The scrutiny by the RBI revealed that Yes Bank was showing signs of poor compliance, wrong asset classification and risky credit decisions as well as questionable corporate governance. In September 2018, the RBI decided not to renew the term of Rana as its Chief Executive Officer and a new head took over at the start of 2019.

The bank has a good branch network of 1,200 branches and a retail book of about US$600 million (S$827 million).

Yes Bank's scrip fell from ₹280 (S$5.19) in April 2019 to around ₹40 (S$0.74) in January 2020. The bank was displaying all the ingredients of questionable corporate governance, erosion of confidence among depositors, investors and indeed the regulator too. There was a steady decline in its financial position due to its inability to raise adequate capital to make provision for likely NPA's arising. This led to downgrades by credit rating agencies. As its attempts to have a market-led revival and over regulatory restructuring did not appear to be succeeding, on the advice of the RBI, the government imposed a moratorium on Yes Bank on 5 March 2020 for a period of 30 days. Subsequently, the RBI superseded the bank's board and appointed an administrator. Under the moratorium, deposit withdrawals have been capped at ₹50,000 (S$925). The RBI has proposed a reconstruction scheme under which the SBI could take a maximum 49 per cent stake in the restructured capital of the bank. This plan, inter alia, proposes that the depositor's funds would be protected. The SBI will seek new investors who will be issued new shares in the future and the SBI will not be permitted to reduce its stake below 26 per cent in the first three years. The RBI has proposed a write-down of additional Tier-I bond holders.

Considering the conditions prevailing in the market and the need to restore client and investor confidence, the route followed by the regulator and government appears to be the most suitable. There will not be any value erosion to SBI stakeholders and depositors have been assured that their money is safe. A write-off of bonds will unnerve bond holders. However, it is reported that the RBI's proposal is in sync with Basel III guidelines. Hopefully, within the month, the reconstruction plan will be implemented and Yes Bank will be able to function normally. It is hoped that, barring some initial depositor inconvenience and digital payment platforms having to re-route their operations, there may not be any other deleterious effect.

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