Opinion

TUESDAY, APRIL 2, 2019

REDUCED EL-NINO IMPACT

Sanjay Kaul, NCML managing director and CEO

"Despite lower production, prices of agri-commodities may not be affected due to large buffer stocks with the government"

SBI does well to challenge the NCLAT in Essar case

CoC is empowered to decide & the law is clear that secured creditors get priority; why ask it to reconsider its decision?

STATE BANK OF India has done well to approach the Supreme Court to challenge the National Company Law Appellate Tribunal (NCLAT) asking the Committee of Creditors (CoC) to reconsider its decision in the Essar Steel matter so as to ensure that operational creditors—like Standard Chartered—get a higher amount than what the CoC has agreed to. The NCLAT, in turn, is asking the CoC to go by the order of the Ahmedabad bench of the National Company Law Tribunal (NCLT) which advised that 85% of the ₹42,000 crore bid by Arcelor Mittal for Essar Steel be kept for the financial creditors and 15% be kept for the operational creditors as well as other stakeholders.

The NCLT, or the NCLAT, can't be faulted for wanting the operational creditors to get more than what they are getting now, in the same way they may want the financial creditors to get more; but these wishes have to be in keeping with the Insolvency and Bankruptcy Code (IBC) law. And the law is very clear in that the CoC takes the final call on the matter and that, after the costs of the bankruptcy process and the workers' dues for the last two years are met, it is the financial creditors that get the first priority. The courts should admit a challenge to the CoC's decision only if *mala fide* is alleged and looks, *prima facie*, a possibility. The courts should not be petitioned to get a better deal for one group or the other; but that is precisely what is happening right now.

Indeed, by giving directions to the CoC, the NCLT/NCLAT are, in a sense, playing into the hands of Essar Steel's promoters, the Ruias, who tried to upset the resolution process by coming in with an offer of ₹54,389 crore after the CoC had approved the Arcelor Mittal proposal for Essar Steel. The Ruia challenge, it is true, was set aside by the NCLT when it approved Arcelor's bid, but if the CoC's decision is to be questioned, the entire IBC law—and its functioning and the hierarchy of repayments—is under threat. While the IBC lays down a 180-day timeline for resolution, the average time taken so far is around 313 days, and, in the case of Essar Steel, this is over 550 days already. The fact that such challenges to the IBC are taking place at a time when a new government is being elected only adds to the uncertainty over the fate of the law.

Sadly, this is not the first time the NCLAT is overstepping. In the case of IL&FS, when the central bank wanted banks to declare its loans to the group as NPAs and to start making provisions for it, the NCLAT said that RBI couldn't ask banks to declare IL&FS loans as NPAs until this was cleared by it. As this newspaper has pointed out before, RBI is the regulator for the banking sector, and if it is to keep the sector solvent, it has to ensure that banks are honest about declaring NPAs and then provisioning for them out of profits. If it so happens that the NPA turns viable later, the banks can write back the provisioning into their books and declare a higher profit; if the NPA doesn't get ok, the banking system will not suffer a sudden shock since the banks would already have provided for it. In this case, it is not just the NCLAT—it said RBI was making classification of IL&FS loans as NPAs a 'prestige issue'—but even the Supreme Court is examining the validity of the RBI's February 12 circular; the judgment is expected later today. If the SC decides to set aside the circular, or parts of it, it will set the NPA-resolution process back in a big way; it doesn't help that the IBC process is also fighting its own challenge.

Need to boost FDI flows

Low FDI levels have led to BoP deficit for 3 straight quarters now

ONE OF THE key takeaways from the Balance of Payments (BoP) data for Q3FY19 is that capital flows, foreign direct investments (FDI) in particular, are slowing. Else, with the current account deficit (CAD) at just 2.5% of GDP, the BoP should not have been in a deficit of $4.3 billion. Indeed, the BoP has now been in deficit for the third-straight quarter primarily because fresh equity flows appear to have plateaued; in the nine months to December, they were $33.5 billion, down 7% y-o-y. The combined FDI inflows in FY16 and FY17 were a hefty $83.5 billion but in FY18, they were at about $45 billion. As a share of GDP, FDI flows have slipped from 2.54% in FY09 to 1.24% in the April-December 2018 period; the lowest in six years.

For a number of reasons—weakening global trade, fickle portfolio flows—India must attract FDI in bigger chunks if the external sector is not to be off kilter. While the NDA government has eased the investment rules across several sectors—defence, for instance—there hasn't been much of an impact. Global defence manufacturers clearly want to have a controlling interest whether or not they're bringing in state-of-the-art technology; they're not content with 49%. Of course, FDI would flow in faster into defence if the quantum of defence orders placed by India was to see a big jump but, unfortunately, that hasn't happened either. Indeed, while the Make in India programme has been a non-starter, the data reveals, manufacturing hasn't been pulling in much FDI for several years now and it is services, telecommunications and e-commerce that have seen the chunky inflows.

While the FDI rules need to be eased further and areas such as multi-brand retail should be thrown open to foreign players, the government must simultaneously work to ensure global companies are able to operate in a good business environment. There has been way too much tax terrorism—despite promises to the contrary—and the regulatory environment is far from friendly. A good example is the telecom industry where the rules have been skewed in favour of one player, nearly destroying the businesses of others. India should have seen many more drug majors setting up research labs and manufacturing units given the large pool of scientists and science graduates. But this sector pulled in less than $1 billion in each of the years FY16 and FY17, smaller than the $1.5 billion in FY15. Again, despite commanding one of the biggest markets globally for cars and an abundance of labour, FDI in automobiles fell to $1.6 billion in FY17 from $2.6 billion in the previous year. The government must desist from interfering in the e-commerce sector else flows into this space, too, will dry up.

BirthComplications

The rising incidence of caesarean births highlights the inequity in access to appropriate obstetric healthcare

A STUDY PUBLISHED in the *Journal of the American Medical Association* (JAMA) points to the rising number of caesarean births in India. The proportion of births through the procedure was 17.2% from 2010 to 2016, as per the study, as the researchers analysed NFHS-4 data. This is a rate higher than that noticed in the NFHS-3 data (10.6%) and in developed countries such as the Netherlands or Finland. A large proportion—40.9%—of babies in private hospitals are born through C-sec as compared to just 11.9% of those born in government hospitals. There is also considerable disparity across regions in the C-sec birth numbers—87.1% of deliveries in private hospitals of urban Tripura (against 36.4% in government ones) are caesarean while, in urban Haryana, just 25.3% of private hospital births (10.7% in government ones) are through C-Sec.

C-secs save lives but, last year, WHO released a document underscoring its concern about rising C-section rates. They highlighted that the procedure comes with a sizeable chunk of future health risks to the mother and the child. A study conducted by the Indian Institute of Management, Ahmedabad, last year found that these births not only entailed "large out-of-pocket" expenditure but also "delayed breastfeeding, lower birth-weight, respiratory morbidities" amongst other troubles for the newborn. WHO, in 2015, stated that the ideal C-section birth rate of a population is 10-15%, and although India has crossed this mark, there remains a section of women who are are not able to access it despite needing it—caesarean rates of less than 10% were noticed for Rajasthan, Jharkhand and Bihar while Telangana, the state with the highest caesarean births, reported 57.7%. The study therefore points to significant disparities, with caesarean deliveries less common amongst underprivileged groups vis-a-vis need and almost 2 million excess caesarean births every year amongst the more privileged sections of the population. Effective interventions and policies targeted at women and healthcare professionals to reduce unnecessary caesarean deliveries will be required to avoid growing inequalities in access to safe caesarean delivery procedures and deny unnecessary ones.

POLITICAL FAILURE

CONSIDERING THE POOR RECORD OF FISCAL CONSOLIDATION AND THE TENDENCY OF POLITICAL PARTIES TO MAKE UNVIABLE PROMISES, THE TIME IS OPPORTUNE FOR CREATING THE FISCAL COUNCIL

Need for additional fiscal checks and balances

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The views are personal

ONE OF THE major issues faced in democratic countries is the electoral budget cycle. The issue is of much more concern in developing countries where the single most important task of every political party is to win elections. Their myopic view encourages them to promise various subsidies and transfers to bestow short-term gains to different sections of the electorate on the eve of the elections. The electorate fall prey to this as the lack of transparency and fiscal illusion obscures the true budget constraints and understandings of the long-term implications of deficits.

Election season is the time when the flavour is about fighting poverty. It is during this season that most political parties think about the poor and initiate various schemes and show their concern to garner votes. In fact, in other times, we do not hear much about the poor. Also, hardly any political party comes out with schemes to build skills and generate productive employment so that the poor are adequately endowed with human capital. In a country where the children in the age group of 0-14 years constitute 37% of the population, there is hardly any expression of the concern about their future. Often one is left wondering what they would do if absolute poverty is eliminated. Long live poverty!

The Nyuntam Aay Yojana, or NYAY, is the minimum income scheme announced by the Congress Party. It proposes to give ₹72,000 per year to 20% of the poorest, or 5 crore, families. This is expected to cost ₹3.6 lakh crore to the exchequer. The proposal is to customise the PM-KISAN scheme that aims to provide farm support and was announced by the current government in the interim budget. It seeks to provide ₹6,000 per year to 12 crore farmers with less than 2 hectares of landholdings and the total cost is estimated at ₹75,000 crore in 2019-20.

There is nothing wrong in assuring a minimum basic income, particularly in a country where there is no social security. In fact, assuring a minimum basic income is more desirable than having many subsidies and transfer schemes. Therefore, any proposal to substitute the multitude of subsidies and transfers with the minimum income support plan is welcome as it does not distort relative prices. The important question, however, is which of the prevailing subsidies are going to be subsumed in the new scheme? At present, there are explicit subsidies on food, fertiliser and petroleum products budgeted at ₹2.96 lakh core for 2019-20 and, in addition, there are many transfers such as MGNREGA (₹60,000 crore), housing subsidy (₹25,853 crore), interest subsidy for short-term credit to farmers (₹18,000 crore) and a crop insurance scheme (₹14,000 crore). If the proposed scheme is additional and not a substitute to the above schemes, it will be a fiscal disaster. One shudders to think of the fiscal outcome if NYAY becomes an additional fiscal liability.

> What do we do when the political parties fail the people? It is here that the importance of institutions of checks and balances becomes relevant

Equally important is the problem of targeting in the wake of the poor information system. Many who should really qualify will be left out and many who will be given are not necessarily those who deserve to be supported. Big data analysis can help only if there is accurate and basic information. Like many other schemes where targeting has been poor, this will be another costly ill-targeted programme. But who cares?

There are two additional issues which must be noted. The first is that the introduction of the scheme is likely to reduce the numbers of the employed, particularly women. There will be resistance to earn and cross ₹12,000, the threshold of being considered the poorest. More importantly, people would prefer to undertake unorganised sector employment unless the wage differentials are very high. Secondly, what about the people earning in the next 20% category? They will find themselves to be having less take-home income than those who earn less than ₹12,000.

The fiscal cost of this proposal will be horrendous. Unless other sources of revenue are found, this would cost an additional 1.8% of GDP to the fiscal deficit and the entire consolidation path will go astray. If the experience is any guide, raising additional resources to meet the new commitment may not be easy. There is hardly any scope for reducing spending on social sector or physical infrastructure. This implies that the process of fiscal consolidation is at serious risk. We have had similar experiences in the 2008-09 budget when three important decisions (farm loan waivers, extension of rural employment guarantees from 200 districts to the entire country and implementation of the sixth pay commission recommendations) created a serious fiscal problem. Strangely, empowering the future generation (the children in the age group of 0-14) is not in the agenda of any political party. Instead, schemes like NYAY will only subject them to the burden of servicing and repaying loans.

When the markets fail, we seek government intervention. What do we do when the political parties fail the people? It is here that the importance of institutions of checks and balances becomes relevant. A growing number of countries have been appointing independent fiscal institutions (IFI) or fiscal councils to enhance their effectiveness in calibrating fiscal policies. These are called by various names such as the Congressional Budget Office in the United States, Parliamentary Budget Office in Australia and Canada, Office for Budget Responsibility in the United Kingdom, Public Finance Council in Portugal, Fiscal Advisory Council in Ireland and Fiscal Councils in most other countries. This is a part of the rule-based fiscal policy in these countries.

The objective of all these fiscal councils is to (i) assist the Parliament in monitoring and evaluating the fiscal adjustment process and (ii) impart greater transparency by objectively estimating the costs of various policies and programmes and enhancing accountability to the Parliament. In addition, these institutions could be mandated to undertake objective and independent evaluations of budget forecasts to impart greater realism to budget formulation. An independent bipartisan institution can assist the Parliament and its committees by helping the parliamentarians understand complex issues and providing them information to facilitate informed debate on fiscal matters.

There was a recommendation to have a Fiscal Council by the 13th Finance Commission and the same was again made by the FRBM Review Committee. The only problem was that they recommended that the finance ministry should appoint such a Council and the latter should be sending reports to the finance ministry. On the other hand, the Fourteenth Finance Commission recommended that the FRBM Act should be amended so as to enable the Parliament to appoint the Fiscal Council that then should be sending reports to the Parliament. Considering our poor record of the fiscal consolidation process and the tendency of political parties to make unviable promises that bind future generations in indebtedness, the time is opportune for creating the Council in order to ensure additional checks and balances.

Brexit: A minor miracle is required

No proposal may again command majority. Then the UK falls out without a deal and without a transition period on April 12. If so, the economic consequences are the least of the problems

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THE PREAMBLE TO the Indian Constitution begins with the words 'We, the people...'. Indian democracy is also a Republic. The people are sovereign as we and all politicians will soon realise when they have voted. United Kingdom, India's model for its democracy, does not have people as sovereign. It is not a Republic but a constitutional monarchy. Sovereignty lies with the 'Crown in Parliament'. Parliament has one chamber popularly elected and its executive is held by the Party that gets a majority. People are indirectly sovereign via their MPs.

Even so, it is the executive—the PM and her Cabinet—which controls the business of Parliament. Most of the legislation is proposed by the executive. Backbench MPs can introduce Private Members' Bills but very few get to the statute book. It is the PM who represents the Crown for all parliamentary purposes. Indeed, the PM can sign treaties with other governments and even take the country to war as a result of the Royal Prerogative. The US president has no such prerogative. He has to go to the Congress for permission to wage war.

Brexit has stretched the system to its limits. The referendum implicitly makes the people the deciding party. Technically, the referendum result has to be validated by the Parliament. After the referendum of June 2016, Parliament did endorse the popular result. Then, the executive declared the date of leaving the European Union as March 29, 2019. As we all know, the Parliament has twice rejected the deal put to it by the PM. Time was running out and the EU has allowed a short extension.

Even so, the executive was running out of ideas. So there was a radical innovation introduced last week. An influential Backbench MP Sir Oliver Letwin, a former Cabinet Minister, proposed that Parliament take control of the proceedings away from the executive. For the first time ever on Wednesday, it was MPs who controlled the timetable and the business. They arranged an 'indicative vote' on a series of alternative policies for Brexit including no Brexit, a second referendum, softer versions of Brexit, etc.

The change was so radical that many began referring to Oliver Letwin as the prime minister. He was *Ek Din ka Sultan*. In a way, the British people came closer to exercising sovereignty via their MPs independently of the executive. It was made possible by overriding all conventions and protocols to vote without treating them as draft bills. Even so, all that was achieved was what everyone suspected. There is no majority for any alternative to the deal Theresa May offered. But then, in a dramatic turn, May offered to resign if her deal would have been accepted by Parliament. Since there was no alternative that commanded a majority, Parliament had to vote once more on the deal.

> May could resign but there is no one else immediately available. Formally, there is no PM nor a deputy leader of the Conservative Party

Had it been accepted, then, UK would have left by May 22. But the deal was rejected for a third time on Friday afternoon. In effect, the PM has lost all authority. But as she had said, "I will go if you accept my deal". They have not and she has not gone. But the situation is anomalous. Thirty-four of her own party MPs voted against her deal. Had they voted for it, she would have had her deal. She could resign but there is no one else immediately available. Formally, there is no PM nor a deputy leader of the Conservative Party. To elect a new leader, the procedure provided would take four months, at least. Firstly, there has to be a contest among the MPs until only two are left. Then they go to the 'country', i.e., Conservative Party members across the UK. When the party members would have voted, the leader is chosen. Theresa May was lucky that in her case, with only two left, her rival Andrea Leadsom made a political blunder and dropped out. So no hustings were required.

It would need a miracle for the House of Commons to come to a decision before April 12, which will persuade the EU to give UK more time. On Monday (April 1), the Letwin process was repeated. Of the many which were rejected last week, some were quite close, including one which is almost no Brexit and another called Common Market 2.0. If any gains a majority then, in a more formal setting, that proposal could be pitted against Theresa May's deal once more. The winner will be the UK's Brexit.

So much more remains to be negotiated. There is a transition period for twenty-one months to work out future arrangements. Of course, no proposal may again command majority. Then the UK falls out without a deal and without a transition period on April 12. If so, the economic consequences are the least of the problems. The UK itself may splinter with Scotland going independent, Northern Ireland caught with a border problem and a constitution in tatters.

LETTERS TO THE EDITOR

Corrigendum

In the article, *RPG's Seniority to launch private label products by next year'* published on March 22, 2019, the company plans to launch them this year, according to Seniority co-founder Ayush Agrawal, and not as reported. The error is regretted

Stymied to no end

In the UK, every conceivable negative of a two-party democratic dispensation, considered the most ideal, has been attempted and, worse, achieved. The lay citizen was dragged through a vortex of disinformation if only to serve the personal ambitions of leaders across the aisle. Both Labour and Tory were mauled by severe internal rifts and the nation left directionless. The first referendum 'for staying' in the EU came in 1975 and 67% voted in support. This ended up in a split of the Labour party. The second one in 2016 was now for 'leaving EU' and was voted 51.9% in favour. What an enigma. A simple choice between a square and a circle in two muddled years stands transformed into a paradox worse than the famed one of "squaring the circle". It challenges the Parliament and threatens to segregate regional components of the kingdom itself. In this state of flux, even a third referendum, however far fetched, could evolve. The short extension now on the table over Brexit is a chance for meaningful repair. But each voting only makes the mire run deeper and the issues even more so. The onus could well shift to EU nations to stitch together a lasting compromise formula for progressive co-existence. A failure invites lasting damage to the very essence of the two-party governance system that has endured in all progressive democracies

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Regd. No: DL-21048/03-05. R.N.I. No.26750/74. Printed and Published by R.C. Malhotra on behalf of The Indian Express (P) Limited and printed at The Indian Express (P) Limited Press, A-8, Sector-7, Noida - 201301 and published at The Indian Express (P) Limited, Mezzanine Floor, Express Building, 9 & 10, Bahadur Shah Zafar Marg, New Delhi-110002. Phone: 0120-6651500, Fax: 0120-4367933. (Cover price: Patna: Mon-Fri ₹6, Sat ₹9, Sun ₹11; Raipur: Mon-Fri ₹7, Sat ₹10, Sun ₹10) Chairman of the Board: Viveck Goenka, Managing Editor: Sunil Jain, Deputy Managing Editor: Shobhana Subramanian* (*Responsible for selection of News under the PRB Act) ©Copyright: The Indian Express (P) Limited. All rights reserved. Reproduction in any manner, electronic or otherwise, in whole or in part, without prior written permission is prohibited. The Financial Express®

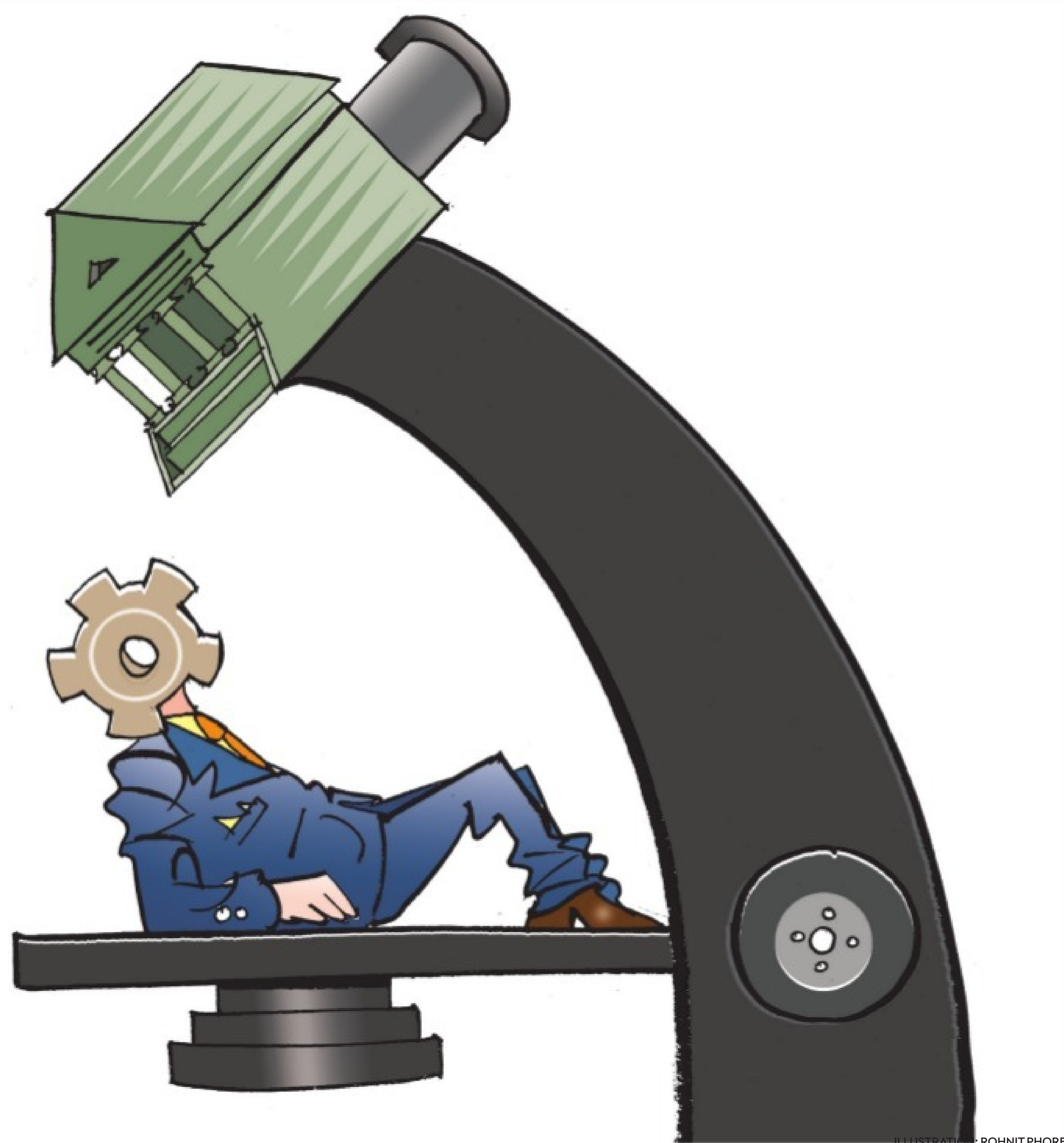

ILLUSTRATION: ROHNIT PHORE

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COMMITTEE OF CREDITORS

An institution of public faith

The Committee of Creditors must build its capacity to distinguish a viable firm from an unviable one, and ensure rescue of only viable firms and closure of only unviable ones, in the interest of the economy

IN ITS LONG TITLE, the Insolvency and Bankruptcy Code, 2016, specifies its objectives. It is reorganisation and insolvency resolution (reorganisation) of certain persons. The purpose of such reorganisation is maximisation of value of assets of the person concerned to promote entrepreneurship and availability of credit and balance the interests of all its stakeholders.

The IBC provides for corporate insolvency resolution process (CIRP) for reorganisation of corporate firms. It separates commercial aspects from judicial aspects, and empowers and facilitates the Committee of Creditors (CoC) to take commercial decisions in a CIRP. The commercial decisions of the CoC are not ordinarily open to any analysis, evaluation or judicial review by the adjudicating authority or the appellate authority, and hence not justiciable.

The IBC envisages a resolution plan for reorganisation of a defaulting firm. The selection and approval of the best resolution plan requires two abilities: namely, the ability to restructure the liabilities and the ability to take commercial decisions. In contrast with operational creditors (OCs) who may pursue immediate realisation of their dues, financial creditors (FCs) generally have the resilience to wait for realisation of their dues post-reorganisation. They have also the ability to determine if a resolution plan will achieve the objectives of the IBC. In view of their abilities, the CoC comprises FCs. The CoC, therefore, has a duty to take commercial decisions that further the objectives of the IBC and do not allow the interests of FCs overshadow the interests of the firm.

A CIRP entails a large variety of commercial decisions by OCs, FCs, insolvency professionals (IPs), the CoC and resolution applicants. This article, however, enumerates four key commercial decisions that a CoC is required to take in a CIRP, to reorganise the firm as a going concern to maximise the value of its assets.

1. A firm in a market economy fails to deliver on account of two broad reasons. First, it carries on a business that is no more viable for exogenous reasons such as innovation. Most such firms have economic distress and are unviable. However, a few of them may have resources to change the business line and become viable. Second, the firm is not doing well for endogenous reasons such as its inability to compete in the market place, while other firms in the same business are doing well. Most such firms have financial distress and are viable. However, a few of them may have significantly depleted their resources and become unviable. The CoC must correctly identify if the firm under a CIRP is viable or not and must rescue a failing, viable firm, and close a failing, unviable one.

2. If the firm is viable, the CoC must visualise the resolution plan required for the reorganisation of the firm. The resolution plan may entail a change of management, technology or product portfolio; acquisition or disposal of assets, businesses or undertakings; restructuring of ownership, balance sheet or organisation, etc. Much in the same way a promoter invites subscription for shares in an IPO, the CoC must create visibility of the underlying value of the firm and invite and encourage appropriate resolution plans for the reorganisation of the firm. It must express its mind as to what kind of resolution applicant can reorganise the firm, keeping in view its complexity and scale of business; what can possibly address the failure by a firm; what are the parameters to assess the viability and feasibility of resolution plans, etc, to enable prospective resolution applicants design and submit competing resolution plans for the reorganisation of the firm.

3. The CoC must ensure that the firm continues as a going concern and its value does not deteriorate during a CIRP. For this purpose, it must appoint a competent IP who can run the business of the firm as a going concern at its optimum potential, provide complete, correct and timely information about the firm to resolution applicants for the design of resolution plans, and safeguard the assets of the firm. It must facilitate interim finance, and cooperate in detection of avoidance transactions, wherever required. It must expedite various tasks for the closure of the CIRP at the earliest.

4. The IBC envisages the CoC to consider only those resolution plans that (i) have been received from credible and capable resolution applicants; (ii) comply with the applicable laws; (iii) are feasible and viable; (iv) have the potential to address the default; and (v) have the provision for effective implementation of the plan. These considerations ensure that the resolution plan achieves reorganisation of the firm as a going concern, on a sustained basis. Of the plans that meet these requirements, the CoC must approve that resolution plan that maximises the value of the assets of the firm, irrespective of realisation for creditors under the plan.

The CoC also takes a few other decisions along with approval of a resolution plan. It may approve restructuring of realisations for FCs to enhance maximisation of value under the resolution plan. It may also approve sharing the realisations under the plan between FCs and OCs or between classes of FCs or OCs, or exemptions from taxes and duties sought for implementation of the plan, etc. It is doubtful if these are strictly commercial decisions and, therefore, beyond scrutiny. In any case, the IBC does not mandate consideration of these aspects while approving a resolution plan, as these may not have a bearing on the viability and feasibility of the plan. Therefore, the CoC must not discard a resolution plan that maximises the value of the assets of the firm just because it yields realisations in the future for FCs or yields relatively lower realisation for them.

> The CoC must ensure the firm continues as a going concern and its value does not deteriorate during a CIRP. It must appoint a competent IP who can run the business of the firm as a going concern

It is important to note that commercial decisions are not amenable to a precise mathematical formula. It is not that a firm is viable, or a resolution plan is viable and feasible, where the realisations for FCs under the plan exceeds liquidation value of the firm. In fact, it requires considerable commercial dexterity and acumen. The CoC must build its capacity to distinguish a viable firm from an unviable one, and ensure rescue of only viable firms and closure of only unviable ones, in the interest of the economy.

Doing away with physical meetings?

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The (ir)relevance of physical meetings of shareholders in this era of e-voting

THE MERRIAM-WEBSTER dictionary defines a 'meeting' as "an act or process of coming together" or as "an assembly for a common purpose". Corporate law contemplates two types of shareholder meetings—the annual general meeting (AGM) and the extraordinary general meeting—whose purpose is to arrive at decisions after discussions and vote on the proposed resolutions.

The ordinary business, which is the adoption of accounts, declaration of dividend, appointment of auditors and directors, is left out of the purview of postal ballots by the Companies Act, indicating that the legislature intended that these matters need to be voted on at an AGM. However, SEBI and securities laws (often at variance with the Companies Act) have a listing agreement (for 'listed companies') which, *inter alia*, mandates electronic voting for ordinary business. The electronic vote is received by the company prior to the meeting date and the members who attend the meeting may fill in ballot slips at the venue. The aggregate of electronic and ballot votes are the results declared after the meeting.

Take a mid-level listed company with, say, 10,000 members. Usually about 50 members would be physically present at the meeting. The promoter group usually controls 40% and more of voting power. Shareholders are geographically scattered. Electronic voting is used by promoters and all institutional investors. Physical votes at the meeting typically account for less than 1% of the votes received in all.

Ordinary business to be transacted at an AGM includes the declaration of dividend. Shareholders can decrease but not increase the rate of dividend as recommended by directors. It is illogical to even assume that any shareholder will ever demand such a reduction.

Adoption of accounts is another resolution that cannot be commented on by a non-finance background individual. Annual reports today are really technical with new accounting standards, increased corporate governance and consequent reporting. It is difficult for even a finance professional to meaningfully analyse consolidated balance sheets of very large companies that have umpteen subsidiaries and are involved in many business activities.

> There is no value addition to the knowledge of shareholders about the performance of a company in physical meetings

Quarterly results have to be published and all important developments have to be reported to the bourses regularly. Most corporates have regular interaction with analysts. So, the accounts or any technicality therein are never really 'discussed' at an AGM. Appointments of auditors and directors are also not really discussable at a general meeting as individual shareholders are unlikely to have a contrary point of view in these matters. Special business can be conducted by postal ballot or electronic voting. This also does not warrant a physical meeting of shareholders. This article is not meant to show disregard for the capability and understanding of the average individual shareholder, but to address the issue of whether the purpose of a shareholders' meeting is really served under the current legal framework?

Share splitting and lower face values have made it possible for a person to have invested as little as ₹100 in shares and be entitled to attend an AGM. Is it really worth his or her time to spend half a day, besides the expense on transportation, to attend and vote at an AGM? The shareholder 'mafia' in each city comprises of such shareholders who demand various favours at the meeting for their 'silence'. Electronic and postal voting recognise the principle of voting rights being proportional to shareholding rather than 'one person, one vote' as was the old practice in pre-electronic vote era.

In summary, there is no value-add to the knowledge of shareholders about the performance of the company at the forum of physical meetings. The authorities must seriously consider immediately doing away with the concept of mandatory physical meetings for all companies. Electronic voting ensures shareholders' supremacy in the corporate management structures. The time has come to review and revisit the purpose served by physical meeting of shareholders in this era of electronic voting and other issues raised above by all the stakeholders, professionals and authorities.

NBFCs

On a path to diversify liability profile

Volatility in the demand and supply side of financial markets presents a unique opportunity to NBFCs and HFCs to re-engineer their operations for FY20

SANJAY CHAMRIA

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NON-BANKING FINANCIAL companies (NBFCs) in India constitute a key frontier of economic stability by functioning outside the purview of the formal banking system. Since September 2018, capital access constraints have hampered operational competencies of NBFCs and driven the need to inject liquidity into their systems. As NBFCs have been grappling with higher borrowing costs and tighter liquidity positions over the last six months, the race to explore new avenues for raising capital has gained momentum.

Having braved a lull, 2019 is the year of revival for the sector, with some NBFCs initiating the process of raising capital while others already raising capital via retail bonds, dollar bonds and dollar loans. A rise in the number of deals and bilateral assignments apparently dominating securitisation markets in India is bolstering the capacity of NBFCs to lend to the underserved. The competitive edge of shadow banking institutions has been boosted and their capacity for extending credit to the priority sector has been strengthened on the back of guidelines issued last year that facilitate blended lending and co-origination agreements between NBFCs and banks. This is a key development that could open new funding avenues for NBFCs and lay the groundwork for their sustained growth and development.

IL&FS defaults, corporate governance issues concerning a large mortgage player, and a couple of ratings downgrades in the sector have led to a volatile undercurrent in liquidity conditions since September 2018. With the debt market grinding to a halt on account of these developments, lenders which include money market players have undertaken a stock check of their portfolio and re-evaluated the positions of companies. Fresh lending limits and revised pricing strategies have been implemented for companies after ranking them on the basis of their risk profile assessments. The changes have impacted NBFCs and housing finance companies (HFCs) and several small to large A and AAA rated entities in varying degrees.

Liability management has become a key focus area for companies, a factor that remained largely unheeded in the last five years. The net income margins of the sector have been impacted with growth rates witnessing significant reduction on account of asset-liability mismatches (ALM) and interest rate volatilities, leading to the re-rating of the entire sector. These developments have led to the emergence of new avenues for raising debt capital, including retail issuance of NCDs, overseas dollar borrowings and dollar bonds. Given the appetite of retail investors and foreign institutional players to invest in sound financial companies with strong risk management, it presents

a unique opportunity to diversify the liability profile and reduce dependence on banks and debt market players like mutual funds and insurance companies. Sensing a unique business opportunity in the current situation, banks are poised to extract their pound of flesh by hiking rates and seeking higher risk participation from even tiered players.

A significant development in the current context has been the revival of the co-origination model for retail asset classes like vehicles, equipment and tractors. The model was successfully executed by renowned foreign banks in the late 1990s and later replicated by the country's top two private banks in the early 2000s. The application of the co-origination model under the new RBI guidelines can be a game changer and a strong alternative in the liability franchise for NBFCs, given the risk participation and vast business opportunity presented by the informal segment. A doorstep servicing model, strengthening balance sheets of banks and cheaper funds have the potential to greatly enhance the distribution outreach and effective penetration of NBFCs in the retail segment and MSME sector in India.

An in-depth analysis points to the fact that the entire sector has been divided into two parts. At one level, companies having secured lending and good asset quality with tenured presence and retail franchise are being courted by debt market players with a heightened appetite to lend to these companies at comparatively softer rates. At another level, companies specifically in the real estate business having limited tenured presence with wholesale books and increasing underwater lending books are getting increasingly isolated in the debt market. There remains lurking apprehension about the asset quality and ALMs of these companies, adversely impacting their ability to service their liabilities.

Capital infusion by the government, resolution of big-ticket NPAs and improved capital adequacy injecting fresh liquidity in the system have significantly bolstered the banking system in the last six months. The removal of a large number of banks from the PCA framework has increased credit flows in the commercial market and eased liquidity to the SME sector, signalling the revival of economic growth in the country.

Increased flow of liquidity in the economy is likely to uplift consumer demand on the back of an anticipation of normal monsoon, rise in MSP for major crops and fiscal boost to affordable housing in the Budget.

In a nutshell, volatility in the demand and supply side of financial markets presents a unique opportunity to NBFCs and HFCs to re-engineer their operations for FY20 and develop their franchise. The players who are quick to tap market sentiments and curate investor-friendly products will gain customer confidence and build new relationships to emerge triumphant.