YES Bank's ride ends in forced bailout

DEV CHATTERJEE
Mumbai, 5 March

The YES Bank board has been superseded by the Reserve Bank of India (RBI) and the private lender has become the target of a forced bailout, given the huge bad debt level in its corporate and real estate portfolios. This is in contrast to a few years ago, when it was the fastest-growing bank.

The lender took more risks compared to its peers, say bankers. "Even when other private sector banks would reject loans to corporate clients, it was YES Bank that came to their rescue," said a former executive.

Hence, it was not a surprise that the bank built a portfolio of bad loans to corporations. Companies that failed to repay loans include Dewan Housing Finance, Essel group, CG Power, Anil Ambani group, and Videocon.

Earlier this week, Reliance Infrastructure said it had defaulted on interest and principal payments on a ₹3,600-crore loan to YES Bank.

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Since the founder and former CEO Rana Kapoor *(left)* was forced to exit the bank by the RBI in January last year, new CEO Ravneet Gill — hired from Deutsche Bank — was tasked with reviving the bank. However, Gill failed to bring any respectable investor on board

Bank — was tasked with reviving the bank. However, Gill failed to bring any respectable investor on board, even as several names were linked from Microsoft and Paytm to JC Flowers and Tilden Park Capital. On the contrary, one of the potential investors turned out to be as bizarre as a man who had filed for bankruptcy in Canada.

"None of the investors saw any value even as its management went around soliciting investors," said an analyst.

The crisis in slow motion, however, helped several insiders exit the company's stock. Rana Kapoor had famously tweeted that YES Bank's shares were as good as "diamonds", and that he would never sell and bequeath the "diamonds" to his children. However, Kapoor's shares — a lot of which were pledged — were sold by lenders as share prices tanked.

By November 2019, Kapoor sold his remaining 0.8 per cent stake when the stock was trading at ₹64 a share. On Thursday, the stock closed at ₹37 — up 26 per cent following unconfirmed reports that State Bank of India was taking over the bank. It was at its peak of ₹383 in August 2018.

JPMorgan said that following the "forced" bailout, investors would likely want the bank to be acquired at near-zero value, to account for risks associated with the stress book and likely loss in deposits.

"In sum, we think the bank needs to be recapitalised at nominal equity value, and could test dilution of additional tier-1 (AT1s)," said JPMorgan analysts in a note on Thursday, while cutting the bank's target price to ₹1.

Analysts said YES Bank failed to get any marquee foreign investor given the uncertainties around asset quality, which had been plaguing the bank for at least a year. With a gross non-performing asset ratio of 7.4 per cent, YES Bank's asset quality is the weakest among top private banks.

In its inspection report of 2019, the RBI had found ₹3,277 crore of divergence in non-performing assets, which would keep provisioning costs higher in the ensuing quarters. The lender has still not announced its December quarter (Q3) results, and a board meeting was scheduled for March 14 to consider its Q3 results, before the RBI superseded the bank's board.

In November, Moody's had warned that the bank had close to ₹31,400 crore in additional loans and investments (about 10.4 per cent of YES Bank's total loans and investments), which are rated below-investment grade. About 40 per cent of loans may turn debt, it warned.

The slowdown in commercial real estate further eroded the asset quality as the bank had a sizeable exposure to weaker companies in the sector.

As of September 2019, its exposure to housing finance companies and non-banking financial companies represented 6 per cent of its total exposure to the property sector. At the same time, the lender had 7.2 per cent direct exposure to the commercial and residential real estate sector.

Foreign brokerages attach ₹1 value to YES stock

SUBRATA PANDA
Mumbai, 5 March

JP Morgan cut its target price for YES Bank on Thursday to ₹1 per share, taking into account the potential fall in the lender's net worth due to stressed assets. Macquarie Capital Securities also said if State Bank of India (SBI) decided to buy stake in the bank, they should buy it at ₹1 per share as the net worth is hugely impaired.

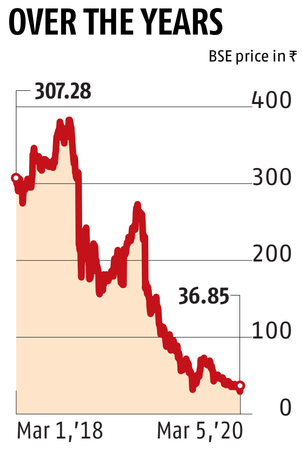
"We believe forced bailout investors will likely want the bank to be acquired at near-zero value to account for risks associated with the stress book and likely loss of deposits. We think the bank will need to be recapitalised at nominal equity value and could test dilution of additional tier 1 (AT1) capital. We remain underweight and cut our target price to ₹1 as we believe net worth is largely impaired," JP Morgan said.

Explaining its reasons for the meagre price for YES Bank shares, Macquarie said the bank has a net worth of ₹25,000 crore. However, its BB and below rated loan portfolio is approximately ₹30,000 crore and the BBB below book is almost ₹50,000 crore. "If we assume substantial portion of BB and below is wiped off, and say 10-15 per cent of the BBB book is to be written off, it implies the current net worth of the bank is zero (after factoring in 25 per cent of the tax benefits)," it said.

YES Bank's shares soared 26 per cent to ₹36.85 on Thursday after reports said that SBI-led consortium would buy a significant stake in the bank. But the share price may not hold at current levels if these brokerages' projections turn true.

"The quasi-sovereign bailout, we believe, is a bondholder/depositor bailout and not an equity one. Hence, today's rally in the

OVER THE YEARS



stock is unjustified. The new capital will likely come in at a steep discount to current share price," JP Morgan said.

Worse, it would send out wrong signals. Any bail out of a private sector entity by public sector undertakings (PSUs), government, or taxpayers indeed creates a moral hazard. "The fact that the government is considering such a bail out proposal shows the risk inherent in investing in PSU banks/companies who continue to be subjected to the vagaries and compulsions of the government. The bigger casualty is taxpayers as their money is being used to infuse capital in PSU banks time and again. It is the taxpayers who are bailing out YES Bank indirectly," wrote analysts at Macquarie led by Suresh Ganapathy.

The acquisition of a significant stake in YES Bank may not be good for SBI's shareholders either, say analysts. "It will be incrementally negative for its valuations, as it sets a precedent for nationalisation of any future private losses. Part of this is already captured in the sharp discount at which the stock trades versus private peers," JP Morgan said.

There could be other challenges. "One buys a bank for its liabilities franchise and not for its assets. We are unsure of YES Bank's quality of liabilities franchise, which perhaps could have further got affected due to the current solvency issues. Consolidation would have brought about a lot of integration challenges as well as legal challenges, as we believe SBI Act needs to be amended for SBI to acquire a private sector bank. Even in this case, the deal will require blessings of the regulator as well as the government," Macquarie said.

ED grills Goyal, asks him to appear today

SHRIMI CHOUDHARY
New Delhi, 5 March

Jet and Goyal have been under the agency's lens for alleged violation of foreign exchange regulations during the signing of a $150-million deal with strategic partner Etihad Airways in 2014 for a loyalty programme

The Enforcement Directorate (ED) has asked Naresh Goyal, former chairman of now-defunct Jet Airways, to appear before it again on Friday for further questioning in connection with a money laundering probe registered against him on Tuesday.

This will be the third consecutive day of questioning. On Wednesday, he was summoned to ED Mumbai's office, where he was interrogated for four hours and taken to his residence later in the evening. On Thursday, too, he was grilled for a few hours.

Sources in ED said the probe indicated that funds were siphoned off through entities created abroad and the money was diverted to the personal accounts of Goyal and his family.

The agency has also detained Goyal's fund manager as he was allegedly in charge of the former's personal finances.

ED, which had conducted extensive search operations at Goyal's residences on Wednesday, seized several digital documents and records pertaining to alleged fictitious transactions, an official said.

ED's case is based on the first information report filed by the Mumbai police, which is necessary to probe "predicate offence" under Prevention of Money Laundering Act (PMLA).

Sources said that the probe agency could also write to lenders who did not get back their money, like State Bank of India, and nudge them to file a complaint.

Jet and Goyal have been under the agency's lens for alleged violation of foreign exchange regulations during the signing of a $150-million deal with strategic partner Etihad Airways in 2014 for a loyalty programme.

During the FEMA (Foreign Exchange Management Act) probe, the agency had alleged that Goyal's companies executed several "colourable transactions" under the guise of selling and distribution expenses.

"Commission and other fictitious expenses were booked at unrealistically high prices and, therefore, they were projecting huge losses," ED had said last year.

Further, Jet Airways had executed allegedly suspicious aircraft lease transactions with ghost entities located abroad, made payments towards lease rentals, and in exchange diverted the monies to Goyal, ED had said.