



ICRA

A MOODY'S INVESTORS
SERVICE COMPANY

INSOLVENCY AND BANKRUPTCY CODE JUNE 2020



Realisations for financial creditors through IBC to take a hit in FY2021 and FY2022

Pandemic and suspension of fresh proceedings pose new challenges

Abhishek Dafria
+91 22 6169 3344
abhishek.dafria@icraindia.com

Sankha Subhra Banerjee
+91 22 6114 3420
sankha.banerjee@icraindia.com

Suspension of fresh insolvency cases to provide relief to corporate sector; however, cases being referred could spike later if Covid-19 impact remains prolonged

The recent announcement regarding the Insolvency and Bankruptcy Code (IBC) by the country's Finance Minister, suspending any fresh insolvency cases against any entity for a one-year period, provides relief to stressed companies impacted by the Covid-19 pandemic as creditors cannot initiate bankruptcy proceedings under the IBC during this period. The amendment follows an earlier notification by the Ministry of Corporate Affairs (MCA) on March 24, 2020, which had increased the minimum amount of default to Rs. 1 crore from Rs. 1 lakh for the initiation of insolvency proceedings. The period of lockdown imposed by the Government of India (GoI) due to the Covid-19 pandemic will also not be counted during the corporate insolvency resolution process (CIRP) and the liquidation process.

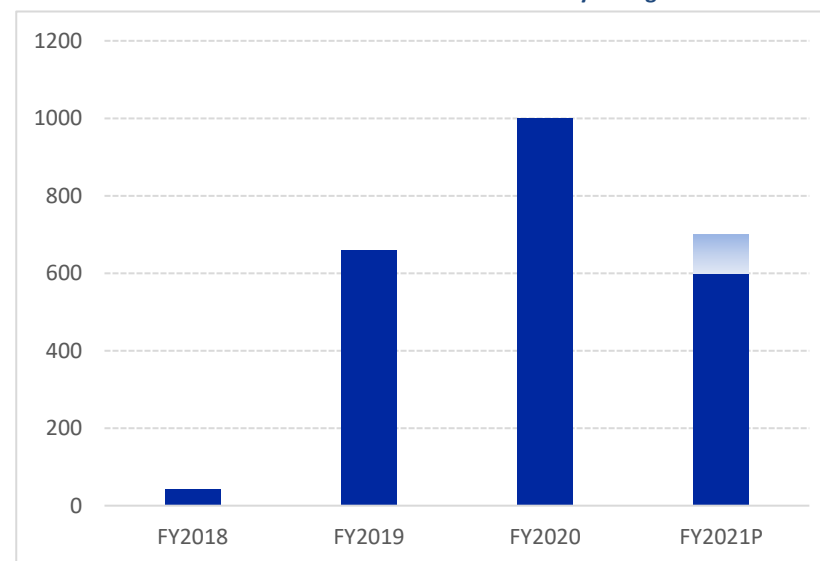
- ICRA believes that the suspension of fresh insolvency proceedings for a period of one year would ensure relief for the companies that are severely impacted by the pandemic and are unable to make payments to their operational and financial creditors in a timely manner. The time frame of one year appears adequate at present for an entity to sort any temporary cash flow mismatches. However, if the severity of the pandemic increases, thereby disturbing normal operation and delaying the economic revival, there could be a sudden surge in the cases being referred under the IBC after the one-year period. This would be detrimental to the resolution process, which is already facing challenges due to overburdened tribunals.
- In the current environment, the ongoing and even future CIRPs are likely to suffer from lower valuations and possibly lower interest from bidders due to the uncertainty across many sectors. This, in turn, may result in creditors having to agree to higher haircuts to successfully conclude the CIRPs. The time required for successfully concluding a CIRP would also increase as, in addition to the lockdown period (which would not be counted under the CIRP timeline), the creditors need to provide additional time to the bidders for due diligence (whose priorities could be to set their own house in order first) and decision-making. In some cases where the response of the bidders is not satisfactory (i.e. a low number of bidders or a low amount of bids), the Committee of Creditors (CoC) may extend the bid timelines or go for further rounds of bidding.
- It might be prudent for the creditors to evaluate the defaulting entities on a case-to-case basis even after the one-year period is over and allow entities that have genuinely suffered due to the economic slowdown following the pandemic to get back on their feet as things improve. Entities that were already under stress prior to the pandemic and which have also received relief following the MCA notification should be dealt with differently. However, as fresh proceedings under the IBC cannot be initiated now for a defined period, the owners' fear of losing control of the company could temporarily dissipate, resulting in usual moral hazards.

Financial creditors to witness material decline in realisations through IBC in FY2021, which could be even worse in FY2022

ICRA expects the resolution of CIRPs under the IBC to be impacted in FY2021 due to a decline in the number of CIRPs yielding a resolution plan as well as an increase in the haircuts that lenders would have to take. The pandemic has resulted in operational challenges for the various parties involved in a CIRP, which could result in limited cases yielding a resolution plan, especially in Q1 FY2021. As per ICRA's estimates, the financial creditors could realise about Rs. 600-700 billion in FY2021 through successful resolution plans from the IBC compared to about Rs. 1,000 billion realised in FY2020 (refer Exhibit 1). The resolution amount would also be lower in FY2021 as the previous year witnessed the successful completion of the CIRPs for large-sized non-performing assets (NPAs); such as Essar Steel Limited and Bhushan Power & Steel Limited, though the lenders are yet to receive funds for the latter). In FY2021, the successful resolution of Dewan Housing Finance Corporation Limited (DHFL) would be a key determinant of the amount that the financial creditors would realise during the year as more than 50% of the estimated realisation could be from DHFL's resolution plan alone. DHFL is the first and only financial service provider (FSP) admitted for resolution under the Insolvency and Bankruptcy Rules, 2019, notified in November 2019. DHFL's resolution process is also hampered by the lockdown and the resolution plan submission timeline has been extended to July 24, 2020.

ICRA also notes that realisations from the resolution plans could suffer further in FY2022 as no new insolvency proceedings are likely to be initiated in FY2021. The CIRPs at the beginning of FY2022 would include those CIRPs that have been going on for more than a year and are possibly headed for liquidation. New insolvency proceedings initiated in FY2022 are unlikely to get resolved in the same fiscal, given the typical average time period seen for CIRPs to conclude with a resolution plan is quite high.

EXHIBIT 1: Realisation for financial creditors from CIRPs yielding resolution



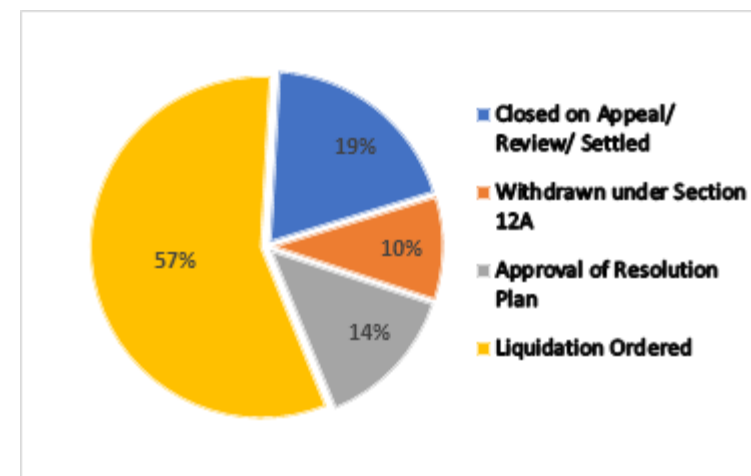
Source: The Insolvency and Bankruptcy Board of India (IBBI), ICRA research

Number of successful resolution plans achieved through IBC remains modest till date compared to number of cases taken to liquidation; realisations by financial creditors through IBC largely driven by resolution of eight large NPAs

The CIRPs under the IBC have been affected over the years by the overburdened National Company Law Tribunal (NCLT), innumerable litigation, defiant promoters and failing sectors. Even with such challenges, the IBC process has shown significant progress. From its commencement in December 2016, 3,774 CIRPs had commenced, of which 1,604 were closed till March 2020. The break-up of the closed cases is given in Exhibit 2.

- 469 cases (~29%) were closed on appeal/ review or settled or withdrawn under section 12A. Section 12A permits the corporate debtor to be withdrawn from the IBC proceedings if the CoC agrees to do so (with 90% votes). ICRA believes that the IBC, to some extent, has been successful in instilling the fear of losing control of the company in the mind of the owner. This has resulted in a change in the mindset of the borrowers, who have become more willing to pay their debts or settle with the lenders, just to keep the IBC proceedings at bay.
- 221 cases (~14%) are closed through approval of resolution plan, of which 120 were approved in FY2020. Financial creditors have realised/expect to realise an average 45% of their claims and the realisation value, in comparison to their liquidation value, stands at 183%. However, the realisation figures are primarily dominated by the CIRP of the Reserve Bank of India's (RBI) first list of the 12 largest NPAs (refer Exhibit 6 for details). Till date, the resolution plan has been approved for 8 of these 12 companies while the CIRP is still ongoing for 2 companies and the remaining 2 companies have been referred for liquidation. The break-up of the resolution from the eight large cases compared to other cases through the IBC has been given in Exhibit 3.

EXHIBIT 2: Outcome of closed cases



Source: IBBI, ICRA research

EXHIBIT 3: Realisation by financial creditors under IBC process – Accounts with approved resolution plan

	Financial creditors' claims (Rs. billion)	Claims realised (Rs. billion)	% Realised
Total resolution	3,872	1,742	45%
For specific 8 companies# (part of RBI's first list of 12 defaulting companies)	2,369	1,361	57%
Others (excluding the above 8)	1,503	381	25%

Bhushan Steel, Bhushan Power & Steel, Monnet Ispat, Electrosteel Steels, Essar Steel, Alok Industries, Jaypee Infratech, Jyoti Structures

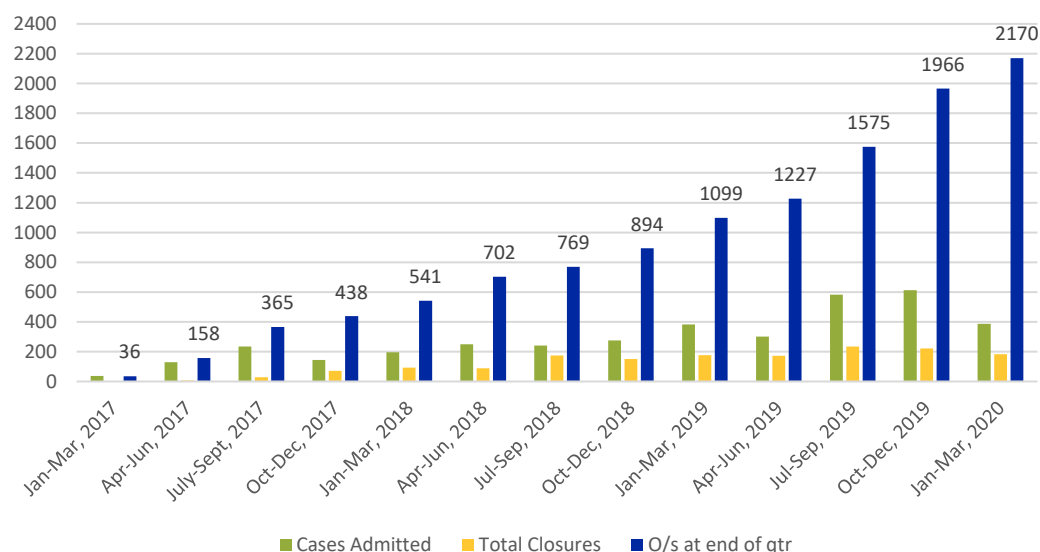
Source: IBBI, ICRA research

- 914 cases (~57%) have been referred to liquidation. The progress on liquidation has been slow as the process is extensively time consuming. So, the final reports for only 69 cases have been submitted with the time taken for the same ranging from 1 to 2 years. The average realisation through liquidation has been a mere ~1% of

the claim amount. The low liquidation value is partly on account of a large portion of the cases being already under the Board of Industrial and Financial Reconstruction (BIFR)/defunct where the value of these entities had already eroded, before admission to the CIRP, to make any meaningful recovery.

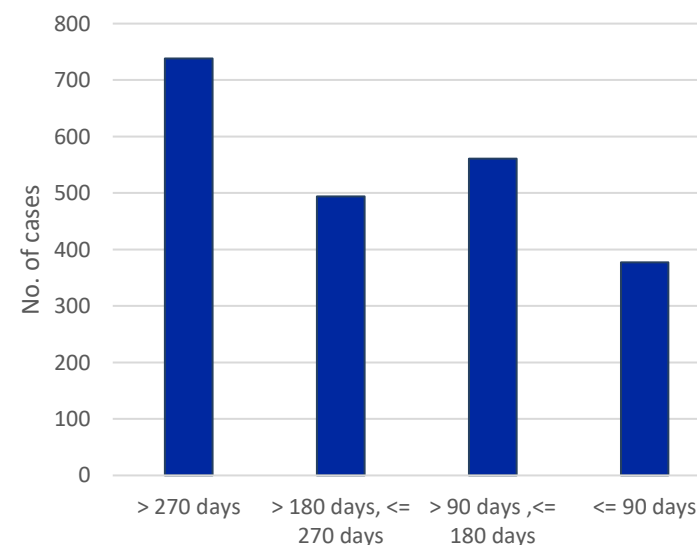
- As on March 31, 2020, 2,170 cases are still undergoing CIRP under the IBC, which has been increasing every quarter since commencement of the IBC. The highest quarterly admissions of 613 cases was reported in Q3 FY2020 (refer Exhibit 4).
- Against the stipulated resolution period of 330 days (increased from maximum period of 270 days in August 2019), the average time taken for the completion of the CIRPs yielding approval of resolution plan has been 415 days so far. Of the total CIRPs as on March 31, 2020, 34% had already crossed 270 days (refer Exhibit 5).
- Many cases have seen delays in the implementation of the resolution plans even after NCLT approval for reasons like substantial litigation in higher courts or enforcement actions (Ex: lenders of Essar Steel had to wait a further nine months after NCLT approval; lenders of Bhushan Power & Steel are still waiting after eight months), refusal of the resolution applicant to abide by the resolution plan (Amtek Auto's CIRP had to recommence even though the first resolution plan was approved in July 2018) or for various other reasons (many large value accounts took more than six months), thus resulting in a decrease in the time value of the lenders' realisation. For cases resulting in an order of liquidation, the average time taken for the CIRP was 309 days. After this, the average time taken for the liquidation process was around 1-2 years, thus substantially eroding the value of recovery as well as the time value of money for the lenders. However, as fresh applications under the IBC process are barred for one year, the burden on the NCLT may reduce to some extent and focus can be on expediting the hearing and judgement of the cases currently under process.

EXHIBIT 4: Number of cases undergoing CIRP



Source: IBBI, ICRA research

EXHIBIT 5: Timelines for ongoing CIRPs as on March 31, 2020



Source: IBBI, ICRA research

ANNEXURE

EXHIBIT 6: Progress of CIRPs for RBI's list of 12 large defaulting companies

Corporate Debtor	Financial creditor Claims (Rs. billion)	Claims realised (Rs. billion)	% haircut	CIRP duration	Status
Bhushan Steel Limited	560.2	355.7	37%	293 days	Completed; acquired by Tata Steel
Essar Steel India Limited	494.7	410.2	17%	583 days	Completed; acquired by ArcelorMittal
Alok Industries Limited	295.2	50.5	83%	598 days	Completed; acquired by JV between Reliance Industries and JM Group
ABG Shipyard Limited	181.3	NA	NA	633 days	Ordered into liquidation
Electrosteel Steels Limited	131.8	53.2	60%	270 days	Completed; acquired by Vedanta
Monnet Ispat & Energy Limited	110.1	28.9	74%	371 days	Completed; acquired by JV between JSW Steel and Aion Investments
Jyoti Structures Limited	73.6	36.9	50%	631 days	Completed; acquired by HNIs
Lanco Infratech Limited	452.6	NA	NA	385 days	Ordered into liquidation
Bhushan Power & Steel Limited	471.6	193.5	59%	771 days*	Supreme Court order pending related to further litigation
Amtek Auto Limited	123.2	Pending	Pending	1,038 days (ongoing)^	Brought back to NCLT as previous resolution applicant did not proceed as per plan
Jaypee Infratech Limited	231.8	232.2	0%	937 days	NCLT approval received in March 2020
Era Infra Engineering Limited	122.1	Pending	Pending	750 days (ongoing)	Ongoing

Source: ICRA research

* Resolution plan approved by NCLT but still under litigation at Supreme Court

^ CIRP was initially completed in 366 days but was subsequently brought back to NCLT

ABOUT ICRA

ICRA Limited (formerly Investment Information and Credit Rating Agency of India Limited) was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange.

Alliance with Moody's Investors Service

The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder. The participation of Moody's is supported by a Technical Services Agreement, which entails Moody's providing certain high-value technical services to ICRA. Specifically, the agreement is aimed at benefiting ICRA's in-house research capabilities, and providing it with access to Moody's global research base. The agreement also envisages Moody's conducting regular training and business seminars for ICRA analysts on various subjects to help them better understand and manage concepts and issues relating to the development of the capital markets in India. Besides this formal training programme, the agreement provides for Moody's advising ICRA on Rating-products strategy, and the Ratings business in general.

The ICRA Factor

Our services are designed to

- Provide information and guidance to institutional and individual investors/creditors;
- Enhance the ability of borrowers/issuers to access the money market and the capital market for tapping a larger volume of resources from a wider range of the investing public;
- Assist the regulators in promoting transparency in the financial markets;
- Provide intermediaries with a tool to improve efficiency in the funds raising process.



Business Contacts

Mr. L. Shivakumar
E-mail: shivakumar@icraindia.com
Tel: +91 22 6114 3406 / +91 98210 86490

Mr. Jayanta Chatterjee
E-mail: jayantac@icraindia.com
Tel: +91 80 4332 6401/ +91 98450 22459

Media and Public Relations

Ms. Naznin Prodhani
E-mail: communications@icraindia.com
Tel: +91 124 4545 860

Registered Office:

1105, Kailash Building, 11th Floor,
26, Kasturba Gandhi Marg,
New Delhi - 110 001
Tel: + 91 11 2335 7940-45

Corporate Office:

Building No.8, 2nd Floor,
Tower A, DLF Cyber City Phase II,
Gurgaon- 122 002
Tel: +91 124 4545300

Ahmedabad

1809-1811, Shapath V,
Opposite Karnavati Club
S.G. Highway, Ahmedabad - 380015
Tel: +91 79 4027 1500/01

Bengaluru 1

'The Millenia', Tower- B, Unit No. 1004,
10th Floor, 1 & 2 Murphy Road,
Bengaluru - 560 008
Tel: +91 80 4332 6400

Bengaluru 2

2nd Floor, Vayudooth Chamber,
15-16, Trinity Circle, M.G. Road,
Bengaluru - 560 001
Tel: +91 80 4922 5500

Chennai

5th Floor, Karumuttu Centre,
634, Anna Salai, Nandanam
Chennai - 600 035
Tel: +91 44 4596 4300

Hyderabad 1

No. 7-1-58, 301, 3rd Floor, 'CONCOURSE',
Above SBI-HPS Branch, Ameerpet,
Hyderabad - 500 016
Tel: +91 40 4920 0200

Hyderabad 2

4A, 4th Floor, SHOBHAN,
6-3-927, A&B Somajiguda,
Raj Bhavan Road,
Hyderabad - 500082
Tel: +91 40 40676500

Kolkata

A-10 & 11, 3rd Floor,
FMC Fortuna 234/3A,
A.J.C. Bose Road,
Kolkata - 700 020
Tel: +91 33 7150 1100/01

Mumbai

3rd Floor, Electric Mansion
Appasaheb Marathe Marg,
Prabhadevi,
Mumbai - 400 025
Tel: +91 22 6169 3300

Pune

5A, 5th Floor, Symphony,
S. No. 210 CTS 3202 Range Hills Road,
Shivajinagar, Pune - 411 020
Tel: +91 20 2556 0194, 020 6606 9999

Email: info@icraindia.com

Helpdesk: 9354738909

Website: www.icra.in/ www.icraresearch.in