

ET EXCLUSIVE INTERVIEW**UDAY KOTAK**

MANAGING DIRECTOR, KOTAK MAHINDRA BANK

Rules for Indian Financial Sector Need to be Reviewed

Kotak Bank MD says local banks losing out to global rivals without leeway to build scale

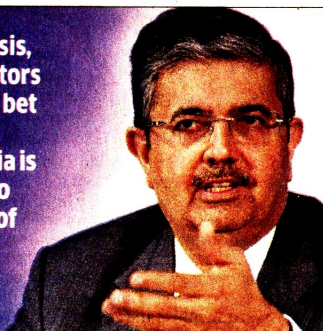
MC Govardhana Rangan, Saloni Shukla & Bodhisatva Ganguli

Mumbai: Rules governing the Indian financial sector need to be rewritten to realise the economy's growth potential, said Kotak Mahindra Bank managing director Uday Kotak. Domestic banks are losing out to global rivals without the leeway to build scale and the inability to underwrite riskier credit due to poor recoveries from bankrupt companies, he said in an interview.

India is well placed to upstage China on the global platform with the banking industry at a "Cinderella" moment that provides scope for expanding loans to leveraged corporates, he said.

"Indian banks are losing big time to international banks," Kotak said. "As a banker, with adequate mar-

On a tactical basis, portfolio investors may want to take a bet on China. But, on a strategic basis, India is better positioned to get a bigger piece (of allocations) in the global pie



FULL INTERVIEW
➤ 5

and ACC shares," he said, referring to Adani's buyout of the companies from Holcim.

"But in this case, foreign banks have lent the money. It had to be an off-shore transaction because no bidder in India could get money from Indian banks."

Reserve Bank of India (RBI) rules restrict Indian banks from lending to companies for takeovers. The In-

dian central bank always viewed lending against shares as a risky activity because a sudden collapse in stock prices could leave banks holding worthless paper. They can lend only up to ₹20 lakh, a rule that was set after the so-called Harshad Mehta scam of 1992.

Kotak, who was tasked with the

recovery of money from the nation's biggest bankruptcy in 2018 — the blow-up of Infrastructure Leasing & Financial Services — said the insolvency code is fine in principle.

But signs of meagre recoveries from the insolvencies of conglomerates and non-banking finance companies (NBFCs) such as Reliance Capital and Srei call for a review, apart from a public interest board for large defaults.

"I am not saying we need to junk the IBC (Insolvency and Bankruptcy Code) option," said Kotak. "There has to be a policy think on this. We have to figure out that for large national assets, we must think about the public interest route. The objective of the public interest board is to optimise value for stakeholders, which we have demonstrated in IL&FS. And IBC may not be the only route. It needs to be relooked at even for NBFC resolutions."

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Corporate India Should Really Get the Animal Spirits Back ... The Time is Good

India may be the only game in town for international investors, but the country needs to tweak laws that will help the banking sector build scale to fund economic aspirations, said Uday Kotak, managing director of Kotak Mahindra Bank. In an interview with **MC Govardhana Rangan, Saloni Shukla & Bodhisatva Ganguli**, he said China poses a short-term challenge to India in terms of equity flows and that his bank will ensure a succession plan that ensures all interests are protected. Edited excerpts.

India appears to be on top investors' minds when it comes to growth. The numbers show consumption has picked up, but investments are yet to do so.

India has differentiated itself. And I like to call India a cleaner white shirt in a dirty shirt world. I would like to see the investment cycle come back. We are seeing people still cautious on the investment cycle. And we are still too much driven by consumption as the core of our economy. I think the time has come for getting investments back. We did a survey with some of our corporate and SME customers. We found two-thirds of them having capacity utilisation now about 80% but only 15% of the total wanted to do capex.

If capacity utilisation is so high and companies are making good profits and deleveraged, why aren't investments happening?

If you dig deeper, it is post-Covid shocks, Russia-Ukraine war. International factors are weighing on people's minds. And therefore, we need to spur animal spirits. I genuinely believe that this is the time to be investing. The investment cycle has to get wider, if few people alone do the investments... that is not how we will have many flowers bloom. We need to have broader Corporate India really get the animal spirits back, because I think the time is good.

Indian banking has been a weak spot since 2015, when the asset-quality review happened. How is it positioned to lend for capex?

We are in what I call a Cinderella time. This is the sweetest credit cycle I have seen for the last many years. And for



ON CREDIT CYCLE

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all the fears of Covid when massive pumping of money happened, the credit cost post-Covid has been very benign. So, we are in a sweet spot. The question is what time of the day is it in Cinderella time? I still think it is afternoon, early evening. So now midnight is far. But, at some point of time, the clock does strike midnight. So we need to be prepared for that. I think this is a good time to underwrite well and grow the economy.

How much are banks responsible for the delay? Most banks are focusing only on retail and top-rated borrowers.

I think there are a few factors. One, you've got a lot of alternate instruments which are now in the market competing with banks. The well-known ones are alternative investment funds. And that's a huge window of money coming through alternate funds. In Kotak's own case nearly \$4 billion of new money has come through AIFs (alternative investment funds).

Funds may be flowing through AIFs. But what about the banking

industry itself?

Indian banks are losing big time to international banks. As a banker with adequate margin, I would have been very comfortable to lend against the security of Ambuja Cements and ACC shares (for the Adani acquisition). But in this case foreign banks have lent the money. It had to be an off-shore transaction because no bidder in India could get money from Indian banks. In India, as a banker I can't lend more than ₹20 lakh against shares. This rule was fixed in 1992 during the Harshad Mehta scam.

Is there a need to review some of these rules?

If we are ultimately going to see the animal spirits of corporate India back, you have to combine it with capacity building in Indian banking and the financial sector. You want growth, you want large capacity to be put up, you want a semiconductor facility. Most banks are going to hit group limits on three or four large corporates. So, what do bankers do? Either you keep lending for regular working capital and some project finance at lower and lower spreads, or you go retail. If we envision an India which is going to invest big and get the animal spirits of

ON STARTUPS

You will now see fundamentally sound business models play out. My sense is there will be a few winners and many losers

ON SUCCESSION

Whatever we do will be consistent. And our interests will be exactly aligned with the smallest shareholder of the bank

corporate India, it has to be combined with the ability of Indian banks to expand at scale.

What are those issues we need to immediately address that would prepare banks as well as the corporate world?

Bankruptcy code. Some group resolutions have gone through in a muddled manner where creditors have got single-digit recovery like in Videocon or Lanco. Where there are conglomerates, the overall resolution for creditors has been very poor. And a lot of it is in the infrastructure sector. Group resolution mechanism under IBC (Insolvency and Bankruptcy Code) leads to disproportionate pain for stakeholders and creditors. Under IBC, we are finding a big challenge for group resolution. And so far, even the NBFC (non-banking finance company) resolutions under IBC have gone through their own challenges. Bids are significantly lower than liquidation value. This is a very illiquid market, so if there is an infrastructure asset there may be one or two bidders, so they get it whatever price they bid.

What is the way out?

The IL&FS solution may be the fair solution. Look at the resolution value. It's in excess of 60%, nearly ₹61,000 crore. On the other hand, we have a conglomerate situation with the examples of Videocon and others where the resolution is less than 10%. Overall, IBC resolu-

tions are now less than 30%. If I'm a creditor, there's a huge difference between getting 50 or 60% versus getting 10 or 20%. Are we as a society getting much less for creditors and stakeholders through this resolution process?

Are you suggesting a public interest board for IBC type cases?

Yes, it can be looked at for larger cases where the debt is more than ₹25,000 crore or ₹50,000 crore. I am not saying we need to junk the IBC option, but at least we have to sit back and ask the question. If finally I'm getting a valuation which is significantly lower than liquidation value or in the case of a group, which is an NBFC with a group, which is more what Srei is, is the current IBC methodology for NBFCs a sustainable solution? There has to be a policy think on this. We have to figure out that for large national assets, we must think about the public interest route. The objective of the public interest board is to optimise value for stakeholders, which we have demonstrated in IL&FS. And IBC may not be the only route. And IBC needs to be relooked at even for NBFC resolutions.

Does the IBC need a complete overhaul?

I frankly believe the principles of IBC are excellent. You've moved the control away from debtor to creditor. So I'm saying keep the good principles of IBC in any resolution process. But, we need some really out-of-the-box thinking when I look at the next five or 10 years for India's financial landscape. The power of creditors in control is a big plus. Because every borrower is scared about losing the company.

Continued on ►► Smart Investing