

# Course correction

## IL&FS resolution has lessons

**O**n April 2, the troubled Infrastructure Leasing and Financial Services Limited (IL&FS) will see a major transition of power. After more than three years, the government appointed non-executive chairman, banker Uday Kotak, will exit his role. His replacement, as chosen by the Union ministry of corporate affairs, is former officer of the Indian Administrative Service C S Rajan, who has been managing director of the group since April 2019. Mr Rajan's last post in government was as chief secretary of Rajasthan, and he retired in 2016 after which he served on the state chief minister's advisory council. The handover of power is the appropriate time to assess how the recovery efforts for IL&FS have progressed, and what the lessons of this unfortunate episode might be.

The IL&FS companies' default and near-collapse in late 2018 was a landmark moment for both the infrastructure sector in India and non-banking financial companies (NBFCs). Fund flow in the latter began to dry up, with major macroeconomic consequences. The hollowness of IL&FS, long viewed incorrectly as practically a quasi-government organisation, also revealed continuing problems in how India was financing its infrastructure build-out through the shadow banking sector rather than transparently. Government has since taken steps to rectify both the problems. The NBFC sector is to be regulated more in line with major commercial banks, particularly for companies of systemic importance. And, the government has sought to find new pipelines for infrastructure finance, including by setting up a new development finance institution. Excessive structural complexity in infrastructure finance allows for the risk, inherent in project finance, to be concealed or deflected with consequent systemic risk. It is essential that transparency about risk be enhanced through world-class regulation if private infrastructure finance is to revive to desired levels.

The takeover of IL&FS' management and the supercession of its board in October 2018 was the most influential such move since the rescue of Satyam Computer following the discovery of large-scale fraud a decade earlier. Although delayed, it is fair to say that the IL&FS intervention has done better than most expected. Mr Rajan has said that 90 per cent of the debt the management hoped to resolve has been resolved, amounting to ₹55,000 crore. This has come as a relief to many creditors of IL&FS, especially public sector banks. Overall, the resolution ratio of the troubled assets is over 60 per cent, according to the management —about twice as much as the average for companies that have been put through the insolvency and bankruptcy process. This suggests that the efforts made to ensure that the company stays a going concern and that asset value is preserved have paid off. The government-appointed board can be pleased. Addressing a press conference this week, the departing non-executive chairman has highlighted some problems that, had they been addressed at a systemic level, would have raised the resolution ratio further. For one, several state governments and state-controlled utilities have delayed or cancelled payments, including dues and annuities. Chasing down such missing payments by governments in the Indian courts is particularly difficult, and this is a structural bottleneck that must be urgently addressed. Organs of the state do not have a special right to break contracts or avoid payments.

*Disclosure: Entities controlled by the Kotak family have significant holding in Business Standard Pvt Ltd*