

WORST IS FAR FROM OVER FOR INDIA'S INDEBTED TYCOONS

By James Crabtree

Risk remains that unexploded debt bombs could go off suddenly



Raghuram Rajan, India's central bank governor is concerned over rising corporate borrowing.

When Raghuram Rajan gives a warning, people listen. India's central bank governor is credited with foretelling the 2008 financial crisis, in a speech in 2005. What concerns him now is debt – specifically rising corporate borrowing in developing markets, fuelled by easy monetary policy in the industrialised economies.

“Across the emerging world, post financial crisis, there's been a sense that leverage has picked up,” he told the Financial Times last month, worrying about what happens when that liquidity suddenly dries up. “And, certainly, I think we have our own highly levered enterprises in India.”

That is something of an understatement. Indian business has been on a decade-long binge, more than doubling its debt to 50 per cent of gross domestic product last year. This jump has been especially pronounced among its 10 most indebted conglomerates: the likes of Adani, Essar or Vedanta, which owe more than \$100bn. The proportion of non-performing and restructured debt at Indian banks has spiked as well, reaching roughly a tenth of loans last year.

Statistics such as these looked especially grim as India's economy struggled, but Mr Rajan's warnings present something of a conundrum as growth finally ticks up, touching nearly 6 per cent in the last quarter. Should anyone still be worried about India's indebted industrialists?

Business confidence has improved since the election of Prime Minister Narendra Modi in May, and equity markets have reopened for fundraisings, too.

It is worth reflecting on this last development. Any analyst predicting that billionaire Anil Ambani's debt-laden Reliance Communications could raise \$800m in fresh equity would have been laughed out of town earlier this year. Then, in June, the resourceful tycoon – long shunned by investors – did just that, keeping creditors at bay.

However, any notion that the worst is over appears misplaced. The likelihood of a systemic crisis for state-backed banks has always been slim. But the risk remains that unexploded debt bombs could go off suddenly, damaging confidence in the country's financial system and its fragile recovery.

Indeed, a few shockwaves have already been felt. In August, the chairman of state-backed Syndicate Bank was arrested on suspicion of soliciting bribes from Bhushan Steel, a mid-tier steelmaker. Bhushan's shares crashed by two-thirds. That is a problem: the company had net debts of about \$5.7bn last year, on earnings before interest, taxes, depreciation and amortisation of \$445m. The odds of full repayment are slim.

True, few outside India have heard of Bhushan. But similar problems dog better known names too. Essar, for instance, had net debts of about \$14bn back in 2013, the last year for which it has provided figures. Since then, its fortunes in sectors such as power and steel have scarcely improved. But its borrowings have almost certainly grown.

This year it took on a \$1.2bn loan facility from Russia's VTB, partly to fund the delisting of its beleaguered Essar Energy subsidiary in London. Essar's billionaire founders have a reputation as canny operators. They will need to show that in spades to pay back their banks, which include global lenders such as Standard Chartered.

Myriad further examples litter India's corporate scene. Numerous other steelmakers are in financial difficulties. Dozens of private sector power stations are due to come online over the next few years, many with limited access to fuel, and thus little ability to service loans. All of this does not mean a crisis is imminent. Some indebted businesses will raise equity to tide themselves over. Others might tap foreign banks, swapping rupee loans for dollar debt – a path being pursued by Suzlon, a struggling wind turbine maker.

However, equity fundraising can refinance only a tiny portion of corporate India's roughly \$900bn of outstanding debts. Swapping rupee debt for dollars stores up trouble for later, if

the rupee depreciates. In either case, bad loan levels are set to keep rising, even if India's economy improves and companies patch up their balance sheets.

Mr Rajan's warnings on excessive indebtedness were not limited to his own country. Asian economies including China and Korea have seen sharper increases. But India looks vulnerable, especially to unexpected shocks. Mr Rajan is right to be worried. Others in India should be too.