Navigating the COVID-19 crisis: avoiding debt defaults and insolvencies as a ‘new normal’ emerges

3 April 2020

The effects of India’s 21-day lockdown are reverberating, with varying degrees of severity, across all the sectors of the Indian economy. As the world prepares for the ‘new normal’ after COVID-19, every stakeholder, from the government to promoters, corporates, and bankers, needs to take action to adapt.

By Manish Aggarwal, Partner and Head, Infrastructure M&A, Special Situations Group (SSG), KPMG in India

India was already in the throes of a slowdown when the COVID-19 pandemic struck, and now the country faces a period of significant economic disruption as the country locks down to slow the spread of the virus.

As the world scrambles to ease the immense healthcare burden of the virus, most economies are bracing for the havoc the virus is likely to leave in its wake. Many countries have already announced several rounds of ‘economic packages’ so far to aid businesses, workers and healthcare systems engulfed by the crisis. The Indian government and the RBI have also put in place a slew of measures to help fight the COVID-19 menace and ameliorate its economic fallout.

The effects of India’s 21-day lockdown are reverberating, with varying degrees of severity, across all the sectors of the Indian economy. The services sector, especially segments such as retail, aviation and entertainment, have been directly (and severely) hit. The manufacturing sector, too, has suffered. Production shutdowns, labour and supply chain disruptions - especially for companies exposed to international trade-as well as falling consumption, have raised serious concerns about the short- to-medium term viability of many businesses, including the MSMEs.

The infrastructure sector, which was already buckling under immense stress, has been among the worst hit; with stoppages in toll collections, discoms struggling to pay gencos, and the compete shut down of air travel hitting airport operators. The dramatic fall in demand across most infrastructure segments has further compounded the sector’s woes.

The current situation has also led to significant volatility in asset prices, especially for financial assets including publicly traded debt and equity. This, in turn, has had a mark-to-market impact requiring investors, such as global funds, to review the health of their portfolios. Falling asset and commodity prices (oil falling to USD25 per bbl) have directly impacted portfolios, which have also taken an indirect hit from investee companies. As a result, this situation will lead to repricing of financial assets and churning of fund portfolios, while generating new investment opportunities, as demand for alternative capital picks up and need-based M&A (disposal of non-core assets) gains momentum.

As we think of solutions, we must consider the nature and extent of the impact on business, from temporary challenges to long-term repercussions that will shape a new post-COVID reality for companies. Solutions and measures, in turn, need to be customised accordingly.
Loan deferment and interest moratoriums represent a good start, but the situation necessitates deep structural solutions. As the world prepares for the 'new normal' after COVID-19, every stakeholder, from the government to promoters, corporates and bankers, needs to take action to adapt to their new reality.

Government:

The government, along with the central bank, has already been working on multiple fronts to battle the pandemic. The following actions might help inject impetus into the economic recovery:

- Has the time come for government to consider direct infusion / investments — on the lines of Troubled Assets Relief Programme (TARP) targeted at specific sectors? Can an infra AMC / fund be set up to house stressed assets to get them back into the system?
- Infrastructure concessions would need ‘commercial breathers’ embedded into them depending upon the impact on each segment
- ‘Tax Free Bonds’ could help raise additional resources, apart from revisiting fiscal deficit targets and fast-tracking monetisation of operating assets across the infrastructure sector to raise required resources
- One-time restructuring window without asset reclassification can then help businesses focus on sharp recovery
- Bold reforms across the value chain starting with approvals, clearances, land, labour reforms to attract investment as India emerges as an alternative manufacturing base.

Lenders:

- Banks and NBFCs that have significant exposure to badly hit industries such as hospitality, tourism, real estate, construction, infrastructure, etc. may need to review their portfolios, conduct diagnostics and work out ‘sectoral relief packages’
- The entire restructuring framework needs to be revisited to make it more practical and facilitative to avoid multiple companies becoming NPIAs and/or hitting bankruptcy
- New structures/products at competitive pricing need to be thought through to support businesses that are backed by strong management.

Promoters/corporates:

The current situation will require companies to:

- Assess short term liquidity including cash balances to meet operational payments
- Reassess their business strategies in light of revised financial and operational forecasts to adjust to the post-COVID scenario
- Necessary adjustments to the capital structure factoring in potentially lower earnings
- Deferral of non-essential capex; and need to diversify funding sources
- Closely evaluating cost structures to cut down excess spend, and
- Explore potential disposals of non-core assets to optimise carrying costs and make balance sheets lean.

The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavour to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation.

© 2020 KPMG, an Indian Registered Partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative (“KPMG International”), a Swiss entity. All rights reserved. The KPMG name and logo are registered trademarks or trademarks of KPMG International.
In conclusion, the current situation is one that has a deep impact on key segments of the economy and is unlike anything we have seen in recent times. The global nature of the pandemic, coupled with its high intensity and long duration, will fundamentally alter the business landscape through changing trade flows, asset prices and consumption patterns. This will impact all key stakeholders, including banks, financial institutions, investors and corporates. The need of the hour is to put in place a comprehensive action plan that addresses potential impact, from short-term cash flow concerns to longer term balance sheet adjustments.