

Financial crisis in the banking industry: challenge or window of opportunity?

Since the end of 2014, banks have been facing increasing pressure on their assets and capital. Various estimates indicate that the volume of overdue debt at Russian banks at the beginning of 2016 is higher than in the 2008-2009 crisis. Retail lending was the first to notice the weakening market conditions. By the beginning of 2016, banks also started seeing outstripping growth of overdue loans in corporate portfolios. This business line includes the least transparent segment—related party lending—where recognition of a borrower's troubles can be deferred the longest. Due to the protracted nature of the present crisis, the banking sector can expect a delayed effect from the recognition of overdue receivables and write-offs in corporate portfolios. However, the current crisis can be a window of opportunity to restructure a business, review business models, and carve out non-core assets and businesses by creating a "bad assets bank" focused on restructuring or improving assets or realizing their liquidation value. Such an approach allows for retaining the most viable and promising business lines and focusing on their development. It is a difficult choice, but one that many will have to make. A plan for establishing a bad debt improvement structure should determine and substantiate the required amount, sources, and tools of recapitalization.

A purely "paper" solution that does not include robust measures will only suspend the problem and most likely contribute to difficulties in the future. In the current environment, banks should not expect a quick rebound in fundraising and loan volumes.

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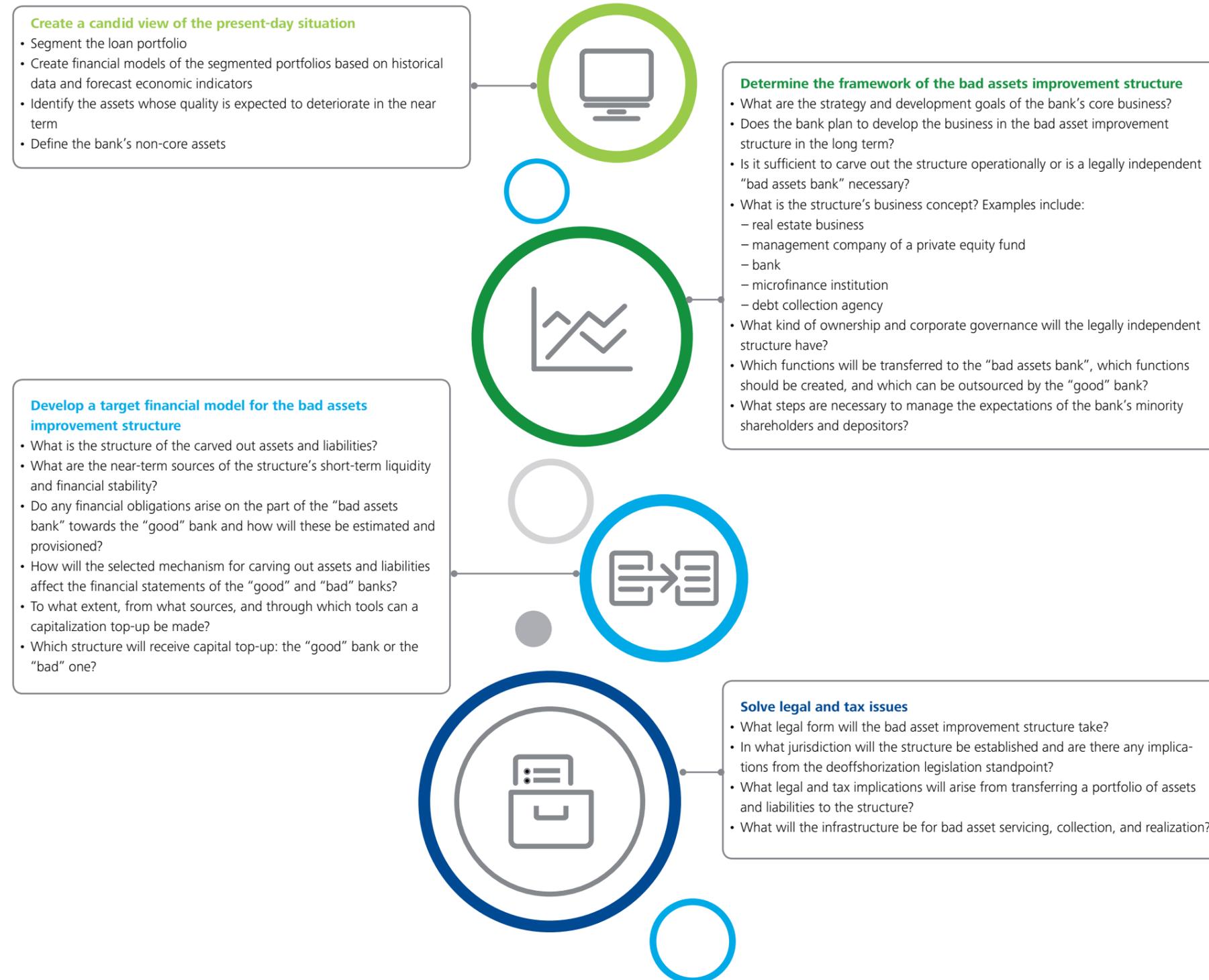


Banks: the good, the bad, the ugly?

2016



What should be considered when forming a bad asset improvement structure?



How can we help?

- 1 Determine the composition and structure of the bad assets to be carved out to the "bad assets bank", as well as assets that are non-core for the "good" bank but can support the financial sustainability of the "bad assets bank"
- 2 Valuation of assets to be carved out
- 3 Provide an independent analysis of the bank's large corporate borrowers' business to define priority methods of debt restructuring
- 4 Analyze the "good" bank's liabilities and provide recommendations on the portfolio of liabilities that can be transferred to the "bad" bank and used as a tool for indirect capitalization top-up
- 5 Prepare IFRS and RAS model financial statements for the "good" bank and the "bad" bank to be carved out, including a forecast balance sheet, statement of financial results, and statement of cash flows (for both the "good" and the "bad" banks separately and in consolidated form) in terms of potential structuring options
- 6 Assess the compliance of the selected bad assets improvement scenario with requirements of the Russian Central Bank
- 7 Develop the target legal and tax structure of the "bad" bank, select the structure's jurisdiction and participants as well as the transfer mechanism for assets and liabilities
- 8 Determine the need and provide recommendations for the form, timelines, and volume of financing coming from the "good" bank's shareholder(s) and third parties based on the developed financial models
- 9 Develop the operating model of the "bad" bank