



Mains Practice Question

Q. Evaluate the effectiveness of the Insolvency and Bankruptcy Code (IBC) in addressing non-performing assets (NPAs) and its implications for asset reconstruction companies (ARCs) in India. **(250 Words)**

13 Mar, 2024 GS Paper 3 Economy

Approach

- Start the answer by introducing the Insolvency and Bankruptcy Code (IBC).
- Discuss the effectiveness of the Insolvency and Bankruptcy Code (IBC) in addressing non-performing assets (NPAs).
- Highlight the implications of IBC for asset reconstruction companies (ARCs) in India.
- Conclude as per the requirement of keywords.

Introduction

The Insolvency and Bankruptcy Code (IBC) was introduced in 2016 to address the issue of non-performing assets (NPAs) in India. It aimed to expedite the resolution process for insolvent companies and improve the recovery of bad loans. Asset Reconstruction Companies (ARCs) play a crucial role in the resolution of NPAs by acquiring these assets from banks and attempting to recover dues.

Body

Effectiveness of IBC in Addressing NPAs

- **Resolution of Stressed Assets:** The IBC has expedited the resolution process for stressed assets by providing a time-bound framework. Till September, 2022, the creditors have realised Rs 2.43 lakh crore under the resolution plans.
- **Increased Recovery Rates:** The recovery rates under the IBC have been higher compared to other resolution mechanisms. The recovery rate for cases resolved under the IBC was around 42%, which is significantly higher than the earlier recovery rates.
 - However, Recovery rates under the IBC have fallen from 43% to 32% between March 2019 and September 2023.
- **Improved Credit Culture:** The IBC has also contributed to improving the credit culture in the country by instilling discipline among borrowers and lenders. The fear of losing control of their companies has made defaulting borrowers more willing to settle their dues.
- **Reduction in NPAs:** The IBC has contributed to reducing NPAs in the banking system. Gross NPAs have reduced from Rs. 8.96 lakh crore in March 2018 to Rs. 5.77 lakh crore in December 2020.
- **Resolution of Large Corporate Defaults:** The IBC has been effective in resolving large corporate defaults such as Bhushan Steel, Essar Steel, and Jaypee Infratech, among others. These resolutions have helped in recovering significant amounts for banks and financial institutions.

Implications for Asset Reconstruction Companies (ARCs)

- **Increase in Business Opportunities:** The IBC has led to an increase in business opportunities for ARCs as banks are more willing to sell their NPAs to these companies for resolution. This has helped ARCs in acquiring a larger number of assets for reconstruction.

- **Challenges in Resolution:** ARCs face challenges in resolving assets acquired under the IBC due to various reasons such as litigation, lack of buyers, and delays in the resolution process. This affects their ability to recover dues and generate profits.
- **Capital Requirement:** The IBC requires ARCs to have a minimum net owned fund of ₹300 crore, which can be a challenge for smaller ARCs. This requirement limits the entry of new players in the ARC sector.
- **Need for Innovation:** ARCs need to innovate and adopt new strategies for asset resolution to improve their recovery rates and profitability. This includes exploring options such as asset securitization, co-lending, and partnering with other financial institutions.
- **Regulatory Environment:** The regulatory environment for ARCs is evolving, and there is a need for clarity on certain aspects such as treatment of tax benefits and regulatory capital requirements. This uncertainty can impact the growth and operations of ARCs.

Conclusion

The Insolvency and Bankruptcy Code (IBC) has been effective in addressing NPAs in India by expediting the resolution process and improving recovery rates. However, there are challenges and implications for ARCs, which need to be addressed to further enhance the effectiveness of the IBC in resolving NPAs and strengthening the banking sector.

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