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COVID-19: Realigning your borrowing requirements

Impact on the Indian economy and liquidity challenges

With the ongoing COVID-19 crisis, the Indian economy is already grappling with a sharp reduction in economic activity. Businesses are expected to face considerable liquidity challenges amidst concerns of weaker demand for at least next few quarters. Forecasters are slashing growth estimates for FY2020-21 (starting 1 April), expecting a severe contraction in the June quarter output.

Consumer demand is likely to remain soft even after the COVID-19 crisis ebbs, due to bankruptcies and job losses and the resulting psychological scars. S&P Global Ratings has cut its estimate for India's GDP growth to 3.5%, from its earlier estimate of 5.2%, as it expects damages to the economy for the Asia-Pacific region to be as severe as the one during the Asian financial crisis of 1997-98.

Indian policymakers have announced several measures to counter the impact on the economy and more are likely to be announced in coming weeks.

Borrowers need to HALT and consider the following short term priorities during these uncertain and challenging times:

Evaluate actual impact

To be done from an operating and financial perspective

Manage debt obligations

Review debt repayment obligations and covenants

Prepare for bounce-back scenarios

Adapt resources to business needs of the near future

Ensure cost discipline

Reorganise procurement strategy and set up control tower to promote a cost-conscious culture in the organisation

Manage cash and liquidity

Prepare for amended cash conversion cycle

Revise financial plan of the business

Perform financial and stress tests to check assumptions, variables and weaknesses and develop rolling forecasts

RBI's COVID-19 relief package[1]

The RBI has announced economic assistance to businesses with the objective of easing liquidity in the system and ensuring no defaults in short term. The assistance is applicable to all commercial banks, small banks, co-operative banks, all-India financial institutions and NBFCs.

- Permitted to grant a moratorium of three months for instalments due between 1 March 2020 and 31 May 2020
- Repayment schedule/residual tenor to be shifted by three months after moratorium period
- Lending institutions to satisfy themselves if reschedule is necessary due to COVID-19
- Interest on term loans to accrue, however working capital interest to be paid at the end of moratorium period
- Recalculation of 'drawing power' by reducing margins and/ or reassessing working capital cycle
- Moratorium/ deferment/ recalculation of 'drawing power' not to be treated as concession or change in terms and conditions
- No asset classification downgrade and impact on credit history of borrowers

(1) RBI announcement dated 27 March 2020.

Concerns related to the economic relief package

The relief provides discretion to lenders and is primarily a deferment of liability and not a waiver.

For lenders

- Impact across sectors/geography: Resource constraint towards evaluation and sanction
- Financial impact, justification and validation: Independent vetting of the need to be carried upon
- Consortium lending situations – common and timely approach required for all members
- MSME vs. large cap: One size fits all approach might not be effective, specialised approach towards MSME

For borrowers

- Rescheduling does not address the immediate funding gap – revenue and profit impact on corporates due to lockdown is irrecoverable
- Three-month moratorium may be insufficient considering the likely impact
- For WC facilities, accrued interest shall be recovered immediately after the completion of this period
- Reducing margins/extending working capital cycle, may not be enough in all situations – additional credit line/ WCTL may be required for short-term

Issues to be addressed in banking facilities

Working capital

Here are key fund and non-fund based working capital issues that need to be addressed in the current situation:

- **Fund-based working capital**
  - Expected elongation of working capital cycle: Non-realisation of receivables or conversion of work in process as well as funding the supply chain including key vendors
  - Immediate liquidity requirement to sustain one working capital cycle: supporting an entity's liquidity in case of temporary cash flow mismatches
- **Non-fund based working capital**
  - Maturity cycle of LCs: Cash flow mismatches due to elongated working capital cycle; expect crystallisation of liability under usance LCs i.e. bills payable by the buyer/importer at a specified period after date/ sight of the bill
  - Invocation of bank guarantees: Invocation due to performance breach and taking possession of the collateral, against which the guarantee has been issued.

Term loan

Here are key term loan related issues that need to be addressed in the current situation:

- Debt servicing requirements in next 6-12 months: EBITDA and working capital may not be sufficient, refinance opportunities also limited, demand on fresh equity infusion by promoters
- Project under implementation: Expected execution delays and related cost overruns, impact on drawdown schedule
- New fund requirement: Due to prolonged shut down/ kick-starting of expenses

Potential impact and recommended resolution approach

We suggest the following short- and medium-term revival plan/ approach with respective benefits over the next 3-6 months and 6-12 months respectively for organisations during this challenging period.

Revival timeline

Lockdown/Revival timeline	3 - 6 months	6 - 12 months
Till 30 April	Gap funding might resolve the liquidity	Correction in working capital finance combined with deferment of term debt obligations
Till 30 June	Gap funding combined with correction in working capital finance	Deep restructuring of capital – new equity and/or mezzanine funding requirement

Impact

Need to re-visit your financing structure

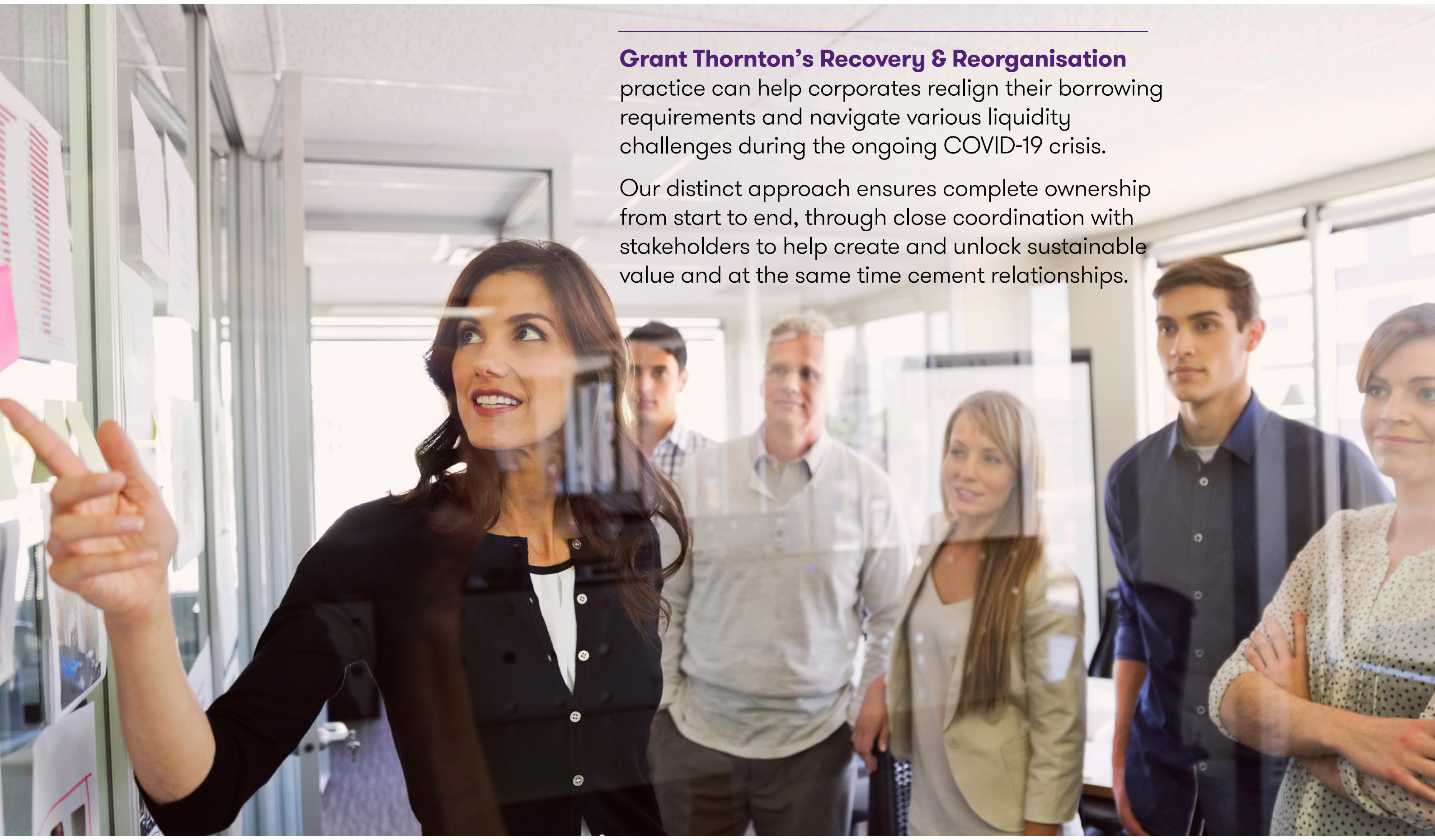
- Realignment of debt commitments in line with sustainable operational cash flows
- Reassessment of working capital finance addressing the gap and drawing power
- Customising the borrowing structure as suitable, in agreement with lenders jointly or bilaterally

As the current situation unfolds further, it is crucial that stakeholders HALT and assess their liquidity positions and accordingly plan their short- and long-term actions .

The need of the hour is to arrive at a funding gap/resolution package evaluating the following four vital parameters:

- EBITDA and free cashflows forecast
- Capex commitment
- Debt profile
- Short to medium term debt servicing committments

To help us understand your borrowing requirements and how we can help, please **download and complete this brief form** and email it to Sanjay Mishra (sanjay.mishra@in.gt.com).



Grant Thornton's Recovery & Reorganisation practice can help corporates realign their borrowing requirements and navigate various liquidity challenges during the ongoing COVID-19 crisis.

Our distinct approach ensures complete ownership from start to end, through close coordination with stakeholders to help create and unlock sustainable value and at the same time cement relationships.

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Click here to download the recently released Grant Thornton Halt-Plan-Refresh Guide on revisiting business priorities and plans

For more insights on the COVID-19 crisis, scan this barcode to see continuous updates on our website