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Foreign debt bill for firms: $45 bn by ’09

Pressure on Indian banking system, which is seeing spurt in credit as cos substitute foreign debt with local funding

By *Satish John* and *Nesil Staney*, October 31st, 2008

MUMBAI: Indian companies have to redeem around $44.57 billion of overseas debt between now and December 2009 in an economic environment where money has become scarce and costly. This debt funded domestic expansion and overseas acquisitions.

The list of around 60 such firms includes leading Indian companies and commercial banks. Companies that are part of the Tata group, Aditya Birla group and Sterlite group feature in it. So do the Mukesh Ambani-controlled Reliance Industries Ltd and Reliance Petroleum Ltd, and the Anil Ambani-run Reliance Infrastructure Ltd. India’s two largest banks—State Bank of India and ICICI Bank Ltd—also appear on the list, culled from *Bloomberg* data.

“This is a pretty big issue, as the cost of borrowing could remain high for some time to come,” said Anindya Dutta, managing director and head of capital markets in India for Calyon Bank. The French bank is one of the biggest players in the loan syndication business in the region.

Also See List of the companies that need to repay overseas debt by December 2009

To be sure, some of the companies, such as Hindustan Zinc, say they have repaid their loans ahead of schedule. *Mint* couldn’t independently ascertain how many companies had done so. Most companies, however, usually pay their debts only when they are due or, if the foreign currency is appreciating, replace foreign debt with local borrowings.

There has been a spurt in credit in the Indian banking system this month and, according to the Reserve Bank of India, or RBI, this is on account of “substitution” of overseas debt with local borrowing. This will intensify further and put pressure on the local banking system which is already experiencing a liquidity crunch.

RBI last week raised the borrowing cost for overseas loans of more than five-year tenure to 500 basis points over the six-month London interbank offered rate, or Libor, an international benchmark rate for such loans. For three-five-year overseas loans, companies have been allowed to pay 300 basis points over Libor. One basis point is one-hundredth of a percentage point. Six-month Libor is now veering around 3.48%.

Also See Debt Dampener (PDF)

However, according to investment bankers and arrangers of overseas loans, even after this relaxation, Indian firms will not find it easy to borrow funds overseas. According to the treasury head of a large company which is planning to raise foreign debt, there is “simply no money around”.

“It (interest rate) is quoting 500-600 basis points over Libor,” said this person who did not want to be named.

This means Indian firms will find it difficult to roll over their old debt and raise new debt. This will affect their expansion plans as bankers do not expect the scenario to change anytime soon. Apart from the cost of borrowings, Indian firms also need to take forward cover for their overseas loans to hedge the currency fluctuation risk when they pay back their loans by buying dollars from the market. The local currency has lost at least 20% against the greenback this year.

“We don’t see borrowing costs coming down anytime soon,” said Thio Tse Chong, managing director and head of international sales at DBS Bank Ltd in Singapore.

The inability to repay overseas debt by borrowing afresh or from internal accruals will also affect the profitability of firms.

According to Rohit Kapur, executive director, advisory and head of corporate finance, at KPMG, an audit and consulting firm, some Indian companies may have to delay their expansion plans. JSW Bengal Steel Ltd is one such firm: it has revised its plans to set up a 10 million tonne steel plant in Salboni in West Bengal. Seshagiri Rao, director, finance, at JSW Steel Ltd, told *Mint* last week that the group has drastically scaled down the Rs30,000 crore plan for its subsidiary JSW Bengal Steel—to Rs4,000 crore, with the equity component pegged at Rs1,300 crore.

The liquidity crunch has forced Tata Chemicals Ltd to put on hold a few expansion plans that will not deliver quick returns, according to R. Mukundan, executive vice-president in charge of the chemicals business.

For some companies, money for domestic expansion will come from internal accruals. Tata Steel Ltd is one such. It has spent about Rs1,000 crore on domestic expansion in the first half of this fiscal. “The cost of capital globally has increased...,” said Koushik Chatterjee, group chief financial officer, Tata Steel.

Tata Steel does not feature in the list of companies whose loans are due by December 2009 as it has already made arrangements to fund its acquisition of Corus Group Plc. of the £3 billion term loan taken for buying Corus, Tata Steel has pre-paid £300 million in the first six months from the excess cash it held, Chatterjee said. Other firms of the Tata group, including Tata Sons Ltd, Tata Technologies Ltd and Tata Chemicals feature in the list.

Greg Moore, Singapore-based vice-president and director of international fixed income and foreign exchange trading at The Toronto-Dominion Bank, said: “It will take many months for banks to regain lost confidence” and until then, money could remain expensive.

Arup Rakshit, head of treasury advisory group at HDFC Bank Ltd said the lesson from the current turmoil is “how and what leverage can do to you.” The bank has a term loan of $93 million due for repayment in November.

At least some of the Indian banks that have overseas operations are apprehending asset-liability mismatches if they are unable to roll over their existing overseas debt. They have approached RBI seeking a dollar line of credit.

Some experts say things will improve. According to Jon Thorn, chief executive of Hong Kong-based India Capital Management Ltd, a foreign institutional investor, globally, policy has been focused on providing money to banks so far but the second round of policy measures will focus on “decreasing the cost of borrowing money for companies and other institutions”.

In a study titled *The Current Liquidity Crunch in India, Diagnosis and Policy Response*, released on 20 October, economists Jahangir Aziz, Ila Patnaik and Ajay Shah have said the global financial crisis has impacted the Indian money market and local firms.

“When the Libor rose sharply—reflecting the rise in credit risk in London—the rates at which the Indian firms had borrowed went up. Beyond the rise in debt servicing, Indian firms and banks also saw the cost of rolling over their maturity debt rise sharply as the money market in London dried up,” they wrote. According to the trio, as the costs of rolling over debt rose sharply, Indian firms borrowing in London found themselves structurally short of dollars. They responded by borrowing in the Indian short-term money market, converting the funds into dollars, using the proceeds to meet external debt obligations.