

## Evergreening of Loans

### Why in news?

The Reserve Bank of India (RBI) Governor Shaktikanta Das raised red flags over banks adopting innovative methods for evergreening of loans.

### What does evergreening of loans mean?

- The evergreening of loans is a term in which banks try to revive a loan that is on the verge of default by granting further loans to the same borrower.
- It is a form of zombie lending in which banks provide more loans to the borrowers to stop them from turning into huge non-performing assets (NPAs).
- The process of evergreening of loans is typically a temporary fix for a bank covering up the real status of stressed loans.

*A loan turns into a nonperforming asset (NPA) if the interest or instalment remains unpaid even after the due date and remains unpaid for a period of more than 90 days.*

### Why do banks follow evergreening of loans?

- If an account turns into a non-performing asset (NPA), banks are required to make higher provisions which will impact their profitability.
- To avoid classifying a loan as an NPA, banks adopt the evergreening of loans.
- Banks offer fresh loans to borrowers on the verge of default to ensure they repay an old loan.
- Banks delay the recognition of losses through evergreening process.
- Banks also avoid provisioning to cover loan losses and increase their liquidity.

### What are the evergreening methods?

- Bringing two lenders together to evergreen each other's loans by sale and buyback of loans or debt instruments.
- Good borrowers being persuaded to enter into structured deals with a stressed borrower to conceal the stress.
- Use of internal or office accounts to adjust borrower's repayment obligations.
- Renewal of loans or disbursement of new/additional loans to the stressed borrower or related entities closer to the repayment date of the earlier loans.

### What do bankers say?

- It is difficult for banks to indulge in the evergreening of loans as the RBI monitors each

and every loan on a regular basis.

- Once an account is classified as an NPA, the situation will become worse.
- By evergreening, banks try to save a borrower from becoming NPA by extending temporary liquidity.

### **What is the problem with evergreening?**

- Bad loans are made to look good at the risk of additional lending to unviable borrowers.
- Evergreening of loans put lenders at risk of huge amounts of default.
- The RBI does not approve of evergreen loans and it is going against its norms.
- This is a misgovernance in banking.

### **How can evergreening be stopped?**

- The audit committee needs to be particularly vigilant.
- A significant evergreening is assumed to be wilful, with support from sections of the senior management of the bank.
- It then becomes necessary to levy penalties and action against the erring officers. Few are -
- Penalties should be levied through cancellations of unvested stock options.
- Claw-back of monetary bonuses on officers concerned and on all whole-time directors.
- The Chairman of the audit committee could be asked to step down from the board.

### **Quick Facts**

#### **Evergreen Loans - A type of loan**

- An evergreen loan is a type of interest-only loan in which principal payment is deferred.
- Typically, the repayment of principal is only expected at the end of the loan term.
- Until the interest is paid, the repayment of principal can be delayed indefinitely and it works like *revolving credit*.

### **References**

1. [IE - Are banks, corporates still window-dressing loans?](#)
2. [Zee Business - Evergreening of loans](#)