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How Independent Research Found a Fatal Flaw with Yes Bank

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Hemindra Hazari

Specialist in Indian banking and economic research

Yes Bank | ESG

Yes Bank - All That Glitters Is Not Gold

By Hemindra Hazari | 14 May 2017

EXECUTIVE SUMMARY

The dazzling glitter of new private sector banks is fast losing its glimmer with the shocking divergence of Yes Bank's March end 2016 (FY2016) non-performing assets, which dwarfed (in % terms) Axis Bank's alarming recent disclosure. The rot is deep and extensive in some of these new private sector banks and senior management and auditors are surprisingly not fired by their boards and regulators for such misreporting. When the same individuals are allowed to keep their posts despite certifying misleading accounts, subsequent accounts signed and certified by them have no credibility. Regulators in India need to wake up and haul up such banks or India will get de-rated by global credit rating agencies resulting in capital outflows by foreign investors and a flight of deposits from such poorly managed, non-transparent banks.

DETAIL

On May 12, 2017, Yes Bank, released its annual report for the year ended March 31, 2017 where the Reserve Bank of India's (RBI) mandatory disclosure showed that for the year ended March 31, 2016, the bank's gross non-performing assets (NPAs) was higher by 5.6x to Rs49.3bn instead of the reported Rs7.5bn. In percentage terms, the divergence exceeded that of Axis Bank and ICICI Bank.

Divergence in FY2016 Gross NPAs

Rsmn	Axis	ICICI	Yes
Gross NPAs Reported	60,876	262,213	7,490
Gross NPAs by RBI	155,656	313,263	49,257
Divergence	94,780	51,050	41,767
Change (%)	155.7	19.5	557.6

Source: Banks

The huge under-reporting of its NPAs in FY2016 transformed critical parameters of valuation for Yes Bank – net NPAs to CET-1 (Common Equity Tier-1 capital) shot up from 2% in the audited number to 27% in the revised number, consequently adjusted book value (ABV, assuming 60% haircut for net NPAs), a key indicator used by analysts declined by 19% to Rs224 from Rs276. In FY2015, the bank's ABV was Rs272 and hence the revised number for FY2016 had declined by 17.6%. A timely disclosure of such a deterioration will have resulted in a change of perception of the bank but the senior management of the bank in its wisdom withheld this critical disclosure till the release of its FY2017 annual report.

Yes Bank - Change in FY2016 on Account of RBI Divergence

	FY2015	FY2016	FY2016R	FY16R/FY16
Rsmn				**Change (%)**
Net Profits	20,054	25,394	19,784	-22.1
Annual Growth (%)		26.6	-1.3	
Gross NPAs	3,134	7,490	49,257	557.6
Annual Growth (%)		139.0	1,471.7	
Provisions	2,257	4,645	13,225	184.7
Annual Growth (%)		105.8	486.0	
Net NPA	877	2,845	36,031	1,166.5
Annual Growth (%)		224.4	4,008.4	
Tier-1	118,755	142,693	137,083	-3.9
Tier-1 (%)	11.5	10.7	10.3	-0.4
CET-1	114,086	137,064	131,454	-4.1
CET-1 (%)	11.0	10.3	9.9	-0.4
Net NPA/CET-1 (%)	0.8	**2.1**	**27.4**	25.3
BV (Rs)	**273.1**	**279.4**	**268.0**	**-4.1**
ABV (Rs) 60% w/o Net NPA	**271.8**	**275.9**	**223.9**	**-18.9**
ROE (%)		20.2	16.1	-4.1
Risk Weighted Assets	1,034,022	1,329,499	1,329,499	
No. of shares (mn)	417.736	490.532	490.532	

Source: Yes Bank

Lack of Transparency & Misleading Commentary by Senior Management

The senior management at Yes Bank, had cloaked the state of its asset quality in FY2016 with reassuring words providing comfort to the shareholders and the public. Yes Bank's FY2016 annual report in a section on "robust risk management" stated,

> *The risk management culture at YES BANK is top-down and bottom-up… The effectiveness of YES BANK's risk governance was reflected in best-in-class indicators – the Bank's Net NPA…was among the lowest in the industry at 0.29% even in an economically challenging FY 2015-16.*

The CEO and CFO even provided an impressive certification of conforming with Yes Bank's Code of Conduct and Ethics.

CEO / CFO Certification

We, Rana Kapoor, Managing Director & CEO and Rajat Monga, Chief Financial Officer, of YES Bank Limited hereby certify that:

a. We have reviewed financial statements and the cash flow statement for the year ended March 31, 2016 and that to the best of our knowledge and belief:

   i. these statements do not contain any materially untrue statement or omit any material fact or contain any statements that might be misleading;

   ii. these statements together present a true and fair view of the Bank's affairs and are in compliance with existing accounting standards, applicable laws and regulations.

Source: Yes Bank Annual Report FY2016 p. 173

We now know the hollowness of their"true and fair" claim to shareholders as the revised net NPA for FY2016 was 3.7% as compared with the reported 0.29%. More alarmingly, Yes Bank did not mention the RBI divergence in the risk factors in its preplacement document for a qualified institutional placement of US$750mn which closed on March 29, 2017 at a price of Rs1,500 per share which was lead managed by CLSA India Private Limited, DSP Merrill Lynch Limited, IIFL Holdings Limited and Motilal Oswal Investment Advisors Private Limited.

Lead merchant bankers are required to undertake a thorough due diligence and such a huge under-reporting of Yes Bank's FY2016 NPAs should have been disclosed in the preplacement document. Institutional investors in the issue may suffer losses if Yes Bank's share price collapses and they may initiate legal proceeding against Yes Bank and its lead managers for this critical non-disclosure.

Even during the 4QFY2017 results analysts conference call , on April 19, 2017, Rajat Monga, (CFO), Yes Bank never revealed the quantum of NPA divergence and instead cleverly stated,

> *There has been a recent circular issued by RBI on account of divergences in asset classification and provisioning so the bank has been able to incorporate all the financial impact rising out of the said circular in the current reported numbers...I will reiterate, divergence has been fully taken care of in this current [FY2017] financial presentation, our financials fully incorporate the divergence ask of RBI.*

Hence nobody suspected that the quantum of divergence was significant for FY2016.

Indeed, even in its latest FY2017 annual report, no mention or explanation is provided in the 'Management Discussion and Analysis' or in the 'Directors' Report' for the divergence in FY2016 NPAs and whether the board conducted an exercise in determining accountability. When there is such a significant NPA divergence, the needle of suspicion points toward rampant evergreening and the RBI appointed P.J. Nayak Committee to Review the Governance of Boards in India (May 2014) in its report stated,

> *"[if] significant evergreening is detected by RBI supervisors, it must mean that evergreening is wilful, with support from sections of the senior management of the bank."*

The integrity of Yes Bank's accounts is primarily the responsibility of Rana Kapoor, CEO and promoter, Rajat Monga, CFO, the audit committee and the auditor, Viren H Mehta (same individual who also certified Axis Bank's FY2016 and FY2017 accounts), partner Batliboi & Co. (a member firm of Ernst & Young). Such a huge divergence in NPA should have resulted in the removal of all the concerned individuals in FY2017 but instead not only did they retain their positions (exception of auditor as the term was over) but the key personnel were rewarded - Rana Kapoor's remuneration increased by 21.2% and Rajat Monga's by 7.2% (median remuneration increase of employees was 13.8%).

Remuneration Increase of Senior Staff at Yes Bank in FY2017

Sr. No.	Requirements	Disclosure	
I	The ratio of the remuneration of each director to the median remuneration of the employees for the financial year	MD & CEO	102.56x
		Radha Singh *	2.07x
		Ashok Chawla **	1.89x
II	The percentage increase in remuneration of each director, CFO, CEO, CS in the financial year	MD & CEO	21.20%
		CFO	7.20%
		CS	6.20%
III	The percentage increase in the median remuneration of employees in the financial year	The median remuneration of the employees in the financial year was increased by **13.8%**. The calculation of % Increase in Median Remuneration is done based on comparable employees. For this we have excluded employees who were not eligible for any increment.	

Source: Yes Bank Annual Report FY2017 p. 164

When the news finally broke on May 12, on the quantum of Yes Bank's NPA divergence and the share price fell by 5.5% to Rs1,491 the bank issued the following statement

> *The reported divergence was for the prior period ended FY 15-16. With ongoing remedial actions undertaken by the Bank during FY 16-17, there have been several reductions/ exits/partial sale to ARCs/ improvements in account conduct which significantly reduced the overall gross NPA outstanding to Rs 1039.9 Cr [Rs10.39bn] as on March 31, 2017.*

The bank's lame defence of saying that out of the total RBI divergence of Rs41.8bn in FY2016, only Rs10.4bn became NPA in FY2017 and hence is not a major issue is irrelevant. As on March 31, 2016, the Rs41.8bn should have been identified by the bank as NPA and the necessary provisions charged to profits, subsequent status change to these accounts has no bearing for FY2016. Moreover, the reputation of its senior management is under a cloud and the same key individuals lack credibility when they state that the majority of the divergence has been resolved in FY2017.

It is a matter of grave concern when the board of directors and the banking supervisor does not take stringent action against the senior management of Yes Bank for this significant mis-reporting of NPAs. Such leniency may result in huge costs for an emerging economy like India as global credit rating agencies may de-rate India on grounds of fraudulent accounts and poor standards of transparency and corporate governance which may result in foreign capital outflows and a flight of deposits from poorly-managed private sector banks.

Disclosure & Certification

- I/We have position(s) in one or more of the securities referenced in this insight
- Views expressed in this insight accurately reflects my/our personal opinion(s) about the referenced securities and issuers and/or other subject matter as appropriate.
- This insight does not contain and is not based on any non-public, material information.
- To the best of my/our knowledge, the views expressed in this insight comply with Singapore law as well as applicable law in the country from which it is posted
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- I/We have signed the Insight Provider Agreement and this insight does not violate any of the terms specified therein.

— Hemindra Hazari (14 May 2017)

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Yes Bank | ESG

Yes Bank - Top Heavy Swings in Organisational Structure

By Hemindra Hazari | 25 May 2017

EXECUTIVE SUMMARY

Credibility issues have plagued Yes Bank's asset quality disclosures in the earlier (year ending March 31, 2016) annual report, added to these concerns is a top heavy organisational structure with significant expansions and contractions in the "top management" category in the last 2 years without any explanation in the annual report. Contradictory data on its human capital have been presented in the bank's latest (year ending March 31, 2017) annual report which raises more questions about the veracity of the data, the management presents to its stakeholders. Investors, therefore, have to exercise caution when analysing data in Yes Bank's annual reports.

DETAIL

Shareholders of Yes Bank have barely recovered from the shock of the huge divergence in the bank's FY2016 non-performing assets (NPAs) between the audited accounts and the regulator's inspection when this writer has observed some major discrepancies in their "top management" data disclosed in the FY2017 annual report.

HUMAN CAPITAL DATA POINTS

A. EMPLOYEE STRENGTH

Particulars	FY 2016-17						
	Under 30		30-50		Above 50		Total
	Male	Female	Male	Female	Male	Female	
Top Management	0	0	76	6	16	3	101
Senior Management	0	0	195	19	7	0	221
Middle Management	54	14	2,529	354	3	2	2,956
Junior Management	2,684	805	5,075	832	3	0	9,399
General Management	4,399	1,428	1,379	241	1	0	7,448
TOTAL	**7,137**	**2,247**	**9,254**	**1,452**	**30**	**5**	**20,125**

Particulars	FY 2015-16						
	Under 30		30-50		Above 50		Total
	Male	Female	Male	Female	Male	Female	
Top Management	0	0	119	9	15	3	146
Senior Management	0	0	502	58	3	0	563
Middle Management	249	75	2,669	383	3	2	3,381
Junior Management	1,577	515	2,357	406	0	0	4,855
General Management	3,503	1,140	1,212	200	0	0	6,055
TOTAL	**5,329**	**1,730**	**6,859**	**1,056**	**21**	**5**	**15,000**

Particulars	FY 2014-15						
	Under 30		30-50		Above 50		Total
	Male	Female	Male	Female	Male	Female	
Top Management	0	0	89	4	8	2	103
Senior Management	0	0	397	44	1	0	442
Middle Management	225	48	1,847	261	3	2	2,386
Junior Management	1,010	351	1,619	268	0	0	3,248
General Management	2,587	780	1,089	175	0	0	4,631
TOTAL	**3,822**	**1,179**	**5,041**	**752**	**12**	**4**	**10,810**

Source: Yes Bank FY2017 annual report p. 74

In the FY2017 Yes Bank annual report, the bank disclosed 5 layers of management; top, senior, middle, junior and general. The human capital data disclosed throws up two major issues.

1. The large number of staff classified in top management which exceeds the number in much larger banks
2. Discrepancy in Yes Bank's own data, one set of tables reveals significant expansion and contraction in "top management", while another set of data contradicts this sharp volatility

In the last 3 years, Yes Bank has over 100 staff in its senior-most management cadre which it calls "top management". Larger banks have much smaller number of staff at the peak of their organisational structure as compared with Yes Bank e.g. in FY2016 ICICI Bank disclosed 32 while HDFC Bank and Axis Bank reported 25 and 16 respectively in their "top management" category. Why the much smaller Yes Bank needs to be so top heavy remains a mystery.

Comparative Size of "Top Management"

FY2016	Top Management	Assets (Rsbn)	Branches
Axis	16	5,255	2,904
HDFC Bank	25	7,088	4,520
ICICI Bank	32	7,207	4,450
Yes Bank	**146**	**1,653**	**860**

Source: Bank Annual Reports, FY2016

Discrepancy in human capital data

In Yes Bank's FY2017 annual report on page 74, in the top management category, the number increased from 103 in FY2015 to 146 in FY2016 and came down to 101 in FY2017. For a bank the size of Yes Bank, adding 43 staff in its top management cadre and in the subsequent year reducing it by 45 individuals is a notable event. However, in the ' B and C' tables titled attrition and hires shows a divergent number e.g. in FY2017 the net change in top management was +5 as compared with the -45 in 'Table A'.

B. TOTAL ATTRITION DURING THE YEAR

Particulars	FY 2016-17 Under 30 Male	Under 30 Female	30-50 Male	30-50 Female	Above 50 Male	Above 50 Female	Attrition Rates
Top Management	0	0	2	0	0	0	1.98%
Senior Management	0	0	14	1	0	0	6.79%
Middle Management	10	2	261	46	1	0	10.83%
Junior Management	660	225	1,103	165	0	0	22.91%
General Management	1,847	677	480	66	1	0	41.23%
TOTAL	**2,517**	**904**	**1,860**	**278**	**2**	**0**	**27.63%**
ATTRITION RATES	**35.27%**	**40.23%**	**20.10%**	**19.15%**	**6.67%**	**0.00%**	

Particulars	FY 2015-16 Under 30 Male	Under 30 Female	30-50 Male	30-50 Female	Above 50 Male	Above 50 Female	Attrition Rates
Top Management	0	0	5	0	0	0	3.42%
Senior Management	0	0	44	4	0	0	8.53%
Middle Management	59	7	399	62	0	0	15.59%
Junior Management	382	136	478	83	0	0	22.22%
General Management	1,261	399	355	58	0	0	34.24%
TOTAL	**1,702**	**542**	**1,281**	**207**	**0**	**0**	**24.88%**
ATTRITION RATES	**31.94%**	**31.33%**	**18.68%**	**19.60%**	**0.00%**	**0.00%**	

Particulars	FY 2014-15 Under 30 Male	Under 30 Female	30-50 Male	30-50 Female	Above 50 Male	Above 50 Female	Attrition Rates
Top Management	0	0	3	0	0	0	2.91%
Senior Management	0	0	17	6	0	0	5.20%
Middle Management	57	8	263	37	0	0	15.30%
Junior Management	224	85	273	54	0	0	19.58%
General Management	844	229	301	34	0	0	30.40%
TOTAL	**1,125**	**322**	**857**	**131**	**0**	**0**	**22.53%**
ATTRITION RATES	**29.43%**	**27.31%**	**17.00%**	**17.42%**	**0.00%**	**0.00%**	

The entire sales and operations force of YES BANK is on payroll. Some industry participants have separate entities that employ the direct sales force.

C. TOTAL HIRES DURING THE YEAR

Particulars	FY 2016-17						
	Under 30		30-50		Above 50		Hire Rates
	Male	Female	Male	Female	Male	Female	
Top Management	0	0	6	1	0	0	6.93%
Senior Management	0	0	26	0	1	0	12.22%
Middle Management	35	4	752	109	1	0	30.48%
Junior Management	2,133	563	2,099	283	0	0	54.03%
General Management	3,558	1,141	475	68	2	0	70.41%
TOTAL	**5,726**	**1,708**	**3,358**	**461**	**4**	**0**	**55.94%**
HIRE RATES	**80.23%**	**76.01%**	**36.29%**	**31.75%**	**13.33%**	**0.00%**	

Particulars	FY 2015-16						
	Under 30		30-50		Above 50		Hire Rates
	Male	Female	Male	Female	Male	Female	
Top Management	0	0	15	0	1	0	10.96%
Senior Management	0	0	95	12	1	0	19.18%
Middle Management	165	41	953	132	0	0	38.18%
Junior Management	1,314	353	866	132	0	0	54.89%
General Management	2,779	886	319	57	0	0	66.74%
TOTAL	**4,258**	**1,280**	**2,248**	**333**	**2**	**0**	**54.14%**
HIRE RATES	**79.90%**	**73.99%**	**32.77%**	**31.53%**	**9.52%**	**0.00%**	

Particulars	FY 2014-15						
	Under 30		30-50		Above 50		Hire Rates
	Male	Female	Male	Female	Male	Female	
Top Management	0	0	6	1	0	0	6.80%
Senior Management	0	0	33	2	0	0	7.92%
Middle Management	115	26	484	72	0	0	29.21%
Junior Management	680	230	461	78	0	0	44.61%
General Management	1,959	543	305	35	0	0	61.37%
TOTAL	**2,754**	**799**	**1,289**	**188**	**0**	**0**	**46.53%**
HIRE RATES	**72.06%**	**67.77%**	**25.57%**	**25.00%**	**0.00%**	**0.00%**	

Employee Profile analysis is based on the database maintained by the Bank's HCM unit, which may differ from the Bank's total headcount on a particular date. HCM data does not include employees of YES FOUNDATION and YES Securities Limited.

Source: Yes Bank FY2017 revised annual report pgs 75-76

Moreover, in the original FY2017 annual report there were some more discrepancies in the % variance rate in attrition of the total workforce not tallying with the % attrition rate in the individual segments. A detailed questionnaire was sent to Yes Bank to understand the discrepancies in their human capital tables. Yes Bank responded with the following statement:

> *Question (xvi) – pertaining to Human Capital & Employee strength details*
>
> 1. *[Tables] A, B & D - We would like to bring to your notice that the decline in Top Management and Senior Management numbers being reflected in the Annual Report is owing to the fact that YES BANK has reclassified its Management bands during FY 2016-17. This re-classification has also impacted the numbers in the Junior Management and General Management bands.*

> 2. *[Table] C – The overall attrition rate of 24.88% is correct and the absolute numbers mentioned under the various heads are also correct. The discrepancy in the attrition rates is due to a typographical error, which we have now corrected in the Annual Report available at :https://www.yesbank.in/about-us/investors-relation/financial-information/annual-reports . Please note that this is not a statutory disclosure and YES BANK has declared these numbers in the interest of transparency and in accordance with the GRI disclosures for our Sustainability Review section. We thank you for bringing this to our notice.*

Yes Bank has devoted 11 pages on human capital in its FY2017 annual report but nowhere is it mentioned that the bank has reclassified its management bands. A reclassification of its management structure especially at the top of the hierarchy is a major exercise in human resource management which should have been disclosed to shareholders especially when the bank devotes so much attention in its annual report to human capital. And if indeed a reclassification took place, it implies that the structure was changed in FY2016 and it was again changed in FY2017 to explain the sharp expansion and contraction in two years.

Even though, Yes Bank is stating that there was a reclassification it appears that the top management number of 146 in FY2016 may have been an error as in its annual reports, Yes Bank devotes considerable space to providing photo profiles of its top management. Analysing the photo profiles data reveals that in FY2016, the number declined from 108 in FY2015 to 84 in FY2016 and it subsequently increased to 97 in FY2017. The photo profiles of its top management also contradict data in “Table A”.

Yes Bank - Executive Top Management

	FY2015	FY2016	FY2017
Senior Group President	4	5	5
Managing Director	3	0	0
Group President	15	19	20
Senior President	37	59	71
President	49	1	1
Executive Top Management	**108**	**84**	**97**
Increase		*-24*	*13*

Source: Yes Bank annual reports

Following this writer’s queries, Yes Bank had to change its recently released annual report and upload a rectified annual report which does not reflect well on the management, in fact-checking data that it is presenting to shareholders and the public.

The significant NPA divergence detected by the banking regulator in FY2016 casts the management of Yes Bank in poor light and combined with the discrepancies in the human capital disclosures in the FY2017 annual report indicates the quality of information provided to shareholders. Investors, therefore, must exercise caution when analysing Yes Bank's disclosures.

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— Hemindra Hazari (25 May 2017)

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Specialist in Indian banking and economic research

Yes Bank | ESG

Yes Bank Reports Handsome Growth in Misreporting

By Hemindra Hazari | 26 Oct 2017

EXECUTIVE SUMMARY

"After such knowledge, what forgiveness?" – T.S. Eliot, Gerontion

For the quarter ended September 30, 2017 (2QFY2018), Yes Bank joined Axis Bank in enjoying the dubious distinction of misreporting its financial statements for two consecutive years. It disclosed that it, too, had under-reported bad loans and overstated earnings for the year ended March 31, 2017. As with Axis Bank, the board of directors of Yes Bank seem content to allow the promoter-CEO, chief financial officer, audit committee and the auditor to continue in their posts, thus casting doubts on the credibility of FY2018 financial statements as well. What is even more amazing is that the banking and capital market regulators allow such individuals to continue to certify accounts; the only punishment is a nominal fine on the bank. Such actions by the regulators are merely symbolic and will instead encourage banks to repeatedly mislead investors and the public. Although Yes Bank reported a 25% yoy and 4% qoy increase in 2QFY2018 net profits, analyzing the numbers is meaningless in the light of the significant consecutive misreporting of earlier profits.

DETAIL

When Yes Bank reported its 2QFY2018 results, it also disclosed that it had repeated its performance of FY2016 and mis-reported its financial statements for FY2017 as well. In absolute terms, the misreporting in FY2017 was even higher than in FY2016 in terms of non-performing assets, provisions for bad debts and net profits. As with Axis Bank, this latest misadventure by Yes Bank should not have come as a surprise to investors as the board of directors of Yes Bank and the banking supervisor had benevolently allowed all those directly responsible for the financial statements -- the CEO, CFO, and the auditor -- to continue in their posts. With most of them continuing with their responsibilities in FY2018 as well, analyzing FY2018 financials without knowing what the regulator's inspection may subsequently uncover becomes irrelevant.

Mis-reporting of Financial Statements by Yes Bank

Rsmn	FY2016	FY2017
Gross NPAs Reported	7,490	20,186
Gross NPAs as assessed by RBI	49,257	83,738
Divergence in Gross NPA	**41,767**	**63,552**
Net NPAs Reported	2,845	10,723
Net NPAs as assessed by RBI	36,032	58,916
Divergence in Net NPAs	**33,187**	**48,193**
Provisions for NPAs	4,645	9,463
Provisions for NPAs as assessed by RBI	13,225	24,821
Divergence in Provisions	**8,580**	**15,358**
Reported Net Profits	25,395	33,301
Net Profits as assessed by RBI	19,784	23,161
Divergence in Net Profits	**-5,611**	**-10,140**
Divergence (%)		
Gross NPA	557.6	314.8
Net NPA	1,166.6	449.4
Provisions	184.7	162.3
Net Profits	**-22.1**	**-30.4**

Source: Yes Bank

The key management personnel responsible for the financial statements at Yes Bank are Rana Kapoor, the promoter-CEO, and Rajat Monga, CFO, who have held their positions since the bank's inception. Despite Yes Bank being audited by the Big Four firms (in FY2016 it was audited by S.R. Batliboi, a member firm of Ernst & Young and in FY2017 and FY2018 it is audited by B S R, associated with KPMG), the banking regulator is uncovering significant mis-reporting. The accounts are prepared by the CFO under the direction of the CEO, and approved by the audit committee of the board. Subsequently, they are approved by the entire board and finally certified by the auditor. When such an extensive misreporting takes place, all these individuals have to be held accountable. The fact that the board of directors at Yes Bank, like Axis Bank have taken no action against the individuals indicates the level of corporate governance and accountability at these banks.

Key Individuals in Yes Bank Responsible for the Financial Statements

Name	Designation	FY2016	FY2017	2QFY2018
Ashok Chawla	**Non-executive independent chairman of the board**	**No**	**Yes**	**Yes**
Radha Singh	Non-executive independent chairperson of the board	Yes	No	No
Rana Kapoor	**Promoter, managing director & CEO**	**Yes**	**Yes**	**Yes**
Rajat Monga	**Chief Financial Officer (CFO)**	**Yes**	**Yes**	**Yes**
Vasant V Gujarathi	**Chairman, audit committee, independent director**	**No**	**Yes**	**Yes**
Ajay Vohra	Chairman, audit committee, independent director	Yes	No	No
Manoj Kumar Vijai	**Auditor, partner BSR, affiliated with KPMG**	**No**	**Yes**	**Yes**
Viren Mehta	Auditor, partner S R Batliboi, member firm E&Y	Yes	No	No

Source: Yes Bank

When the board of directors does not take action in the light of such serious lapses, the regulatory authorities should take strong action. However, on October 24, 2017, the Reserve Bank of India (RBI), the banking regulator, imposed a monetary penalty of a paltry Rs 60 mn (US$ 0.9 mn) pertaining to the misreporting of NPAs in FY2016 and a delay in reporting a security incident across its ATM network in October 2016 . Given the huge gross NPA divergence of Rs 41.8 bn (US$ 630 mn) in that year, the penalty for the bank is inconsequential and will not be a deterrent for future mis-reporting. This is confirmed by the fact that the gross NPA divergence in FY2017 actually grew by 52%, to Rs 63.6 bn. (US$ 981 mn). To date, the Securities and Exchange Board of India (SEBI), the capital markets regulator, has remained silent and is not concerned that a prominent private sector bank is misleading the capital market with its inflated profits.

During FY2017, and more importantly, prior to the misreporting of FY2016 profits being made public, Yes Bank raised Rs 49 bn (US$ 756 mn) through a qualified institutional placement at a price of Rs 300/share (pre-split Rs 1,500/share) which was subscribed by prominent Indian and foreign institutional investors. It is only subsequent to the issue that investors have been made aware that Yes Bank misreported and inflated its profits for FY2016 and FY2017.

In an earlier insight, Yes Bank - All that Glitters is Not Gold, this writer had cautioned,

> *Regulators in India need to wake up and haul up such banks or India will get de-rated by global credit rating agencies, resulting in capital outflows by foreign investors and a flight of deposits from such poorly managed, non-transparent banks.*

By not taking stringent action even after the disclosure of massive misreporting, the regulators' reputation has been damaged, which will have an impact on investor confidence in Indian banks and the capital market.

Disclosure & Certification

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— Hemindra Hazari (26 Oct 2017)

Hemindra Hazari

Specialist in Indian banking and economic research

Yes Bank | ESG

Reliance Naval Sinking into NPA: Yes Bank To Take a Hit

By Hemindra Hazari | 18 Apr 2018

EXECUTIVE SUMMARY

Reliance Naval Engineering (RNE) will in all likelihood be classified as non-performing by all the concerned banks in the consortium for the quarter ended March 31, 2018. Long facing difficulty meeting its financial obligations, the company finally fell short in the December quarter. In the March quarter, banks in the consortium were unable to agree on a restructuring proposal and the account became 90 days' overdue; a press release by the company may compel the majority of banks to classify the account as non-performing.

Although the major hit from RNE will be borne by State Bank of India and IDBI Bank, Yes Bank also has a significant exposure of Rs 4.85 bn. outside the consortium of banks. Interestingly, till the December quarter, in the banking industry RNE was classified as a non-restructured standard asset, and was not included in any of the restructuring mechanisms/disclosures introduced by the regulator; hence it sailed below the radar of most analysts.

More than the size of the hit that Yes Bank will take, its conduct in the entire affair is worrying, for it unsettles confidence in its reporting. Senior Yes Bank officials, led by Rajat Monga, the former chief financial officer (CFO), and the official responsible for mis-reporting two consecutive years of results, had been informing sell-side analysts in the March quarter that they have nothing to worry from Yes Bank's corporate exposures. While the impact of RNE on credit costs of the bank is marginal and within the guidance provided by the bank, in this writer's opinion the bank should have forewarned analysts of the possibility of a large, poor quality standard account belonging to a cash-strapped business group being classified as a NPA, especially when analysts were concerned of worsening corporate asset quality in the industry in the March quarter. Is this deliberate obfuscation? Or does the bank, in defiance of the industry, plan to classify RNE as a standard asset when it reports results on April 26, 2018? If it is the latter, then nothing has changed for this serial misinformer.

DETAIL

The Indian banking industry has a large exposure of around Rs 90 – 100 bn on RNE (formerly, Reliance Defence and Engineering Limited/Pipavav Defence and Offshore Engineering Company). An *Economic Times* article dated September 15, 2017 quoted two unnamed bankers as stating,

> *Reliance Naval is classified as special mention account-2 or SMA-2 [not received dues for over 60 days but less than 90 days] with all banks. Somehow, in the past few months, the company has managed to make critical payment before the end of the 90-day deadline to prevent the account from slipping into the bad loan basket,*

Since then, according to bankers this writer interacted with, RNE was unable to service its interest for the December 2017 quarter and it was negotiating a restructuring with banks which did not materialise. Consequently, on March 1, 2018, RNE issued a disclosure to the stock exchanges which stated,

> We wish to inform you that the Company's loan accounts have either been irregular or sub-standard since September 2014, i.e. before the Company was taken over by Reliance Group in January 2016. Pursuant to Circular No DBR.No.BP.BC.101/21.04.048/2017-18 dated February 12, 2018 issued by the Reserve Bank of India, the said loans will either be classified as irregular or sub-standard, as the case may be.

Source: RNE

Some of the banks this analyst interacted confirmed that RNE has been classified as NPA by them for the quarter ended March 31, 2018 as a result of the RBI notification. The company has now 180 days for the creditors to accept the resolution plan, failing which the company will be admitted to the National Company Law Tribunal (NCLT). Government banks like State Bank of India (SBI) and IDBI have the largest exposures on RNE, but, interestingly, according to the Registrar of Companies (ROC), Yes Bank and HDFC also have exposures on the company.

HDFC & Yes Bank Exposures to RNE

Company CIN/FCRN/LLPIN/FLLPIN	L35110GJ1997PLC033193
Company / LLP Name	RELIANCE NAVAL AND ENGINEERING LIMITED

Charges Registered

SNo	SRN	Charge Id	Charge Holder Name	Date of Creation	Date of Modification	Date of Satisfaction	Amount	Address
1	G79460812	100160549	RELIANCE INFRASTRUCTURE LIMITED	07/03/2018	-	-	25000000000.0	H Block, 1st FloorDhirubhai Ambani Knowledge CityNavi MumbaiMa400710IN
2	C81910440	10602446	IL & FS TRUST COMPANY LIMITED	20/04/2015	14/07/2015	-	11330000000.0	IL & FS Financial Centre, Plot C - 22, G Block,Bandra Kurla Complex, Bandra EastMumbaiMH400051IN
3	C81928160	10601211	IL & FS TRUST COMPANY LIMITED	20/04/2015	14/07/2015	-	8020000000.0	IL & FS Financial Centre, Plot C - 22, G Block,Bandra Kurla Complex, Bandra EastMumbaiMH400051IN
4	C81921975	10601169	IL & FS TRUST COMPANY LIMITED	20/04/2015	14/07/2015	-	16890000000.0	IL & FS Financial Centre, Plot C - 22, G Block,Bandra Kurla Complex, Bandra EastMumbaiMH400051IN
5	C65759326	10594135	HOUSING DEVELOPMENT FINANCE CORPORATION LIMITED	23/03/2015	-	-	1700000000.0	RAMON HOUSE 169BACKBAY RECLAMATIONH T PAREKH MARGMUMBAIMH400020IN
6	C80688260	100053598	YES BANK LIMITED	12/03/2015	-	-	4850000000.0	9th Floor, Nehru Centre, Discovery of IndiaDr. Annie Besant Road, WorliMUMBAIMH400018IN
7	C35789569	10534920	Union Bank of India	24/09/2014	-	-	5350000000.0	Industrial Finance Branch, Union Bank Bhavan, 239Vidhan Bhavan Marg, Nariman PointMumbaiMH400021IN

Source: Registrar of Companies (ROC)

As per the ROC filing, Yes Bank, since March 12, 2015 has an exposure of Rs 4.85 bn. on RNE and there has been no change in the modification of charge since that date. The Yes Bank loan to RNE is at a coupon of 11% (spread of 0.25% p.a over YES Bank Base Rate), payable monthly. In RNE's FY2017 annual report, the auditors highlighted that the company had overdues in repayment of interest and principal aggregating to Rs 1.95 bn, including a default of less than 60 days to Yes Bank of Rs 73.3 mn.

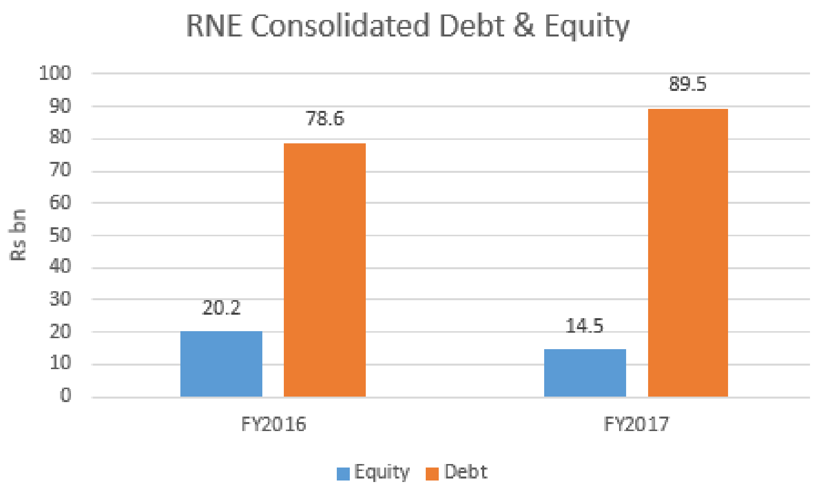
15.8 As at March 31, 2017, the Company has overdue of ₹ 8,403 Lacs (Previous Year: ₹ 8,225.07 Lacs) and ₹ 11,060.24 Lacs (Previous Year: ₹ 4,402.83 Lacs) towards the principal and interest respectively.

₹ in Lacs

S. no	Name of Lender	Amount of Default	Period of Default
01	Bank of Maharstra	133.26	Less than 60 Days
02	Central Bank of India	807.14	Less than 60 Days
03	Corporation Bank	399.06	Less than 60 Days
04	EXIM	511.38	Less than 60 Days
05	HUDCO	13,471.53	More than 60 days
06	IDBI Bank	976.47	Less than 60 Days
07	IIFCL UK	127.56	Less than 60 Days
08	Jammu and Kashmir Bank	397.67	Less than 60 Days
09	Karnataka Bank Limited	54.78	Less than 60 Days
10	Karur vaisya Bank	54.48	Less than 60 Days
11	LIC of India	133.61	Less than 60 Days
12	Oriental Bank of Commerce	105.63	Less than 60 Days
13	Punjab National Bank	220.93	Less than 60 Days
14	UCO Bank	133.56	Less than 60 Days
15	Union Bank of India	1,021.75	Less than 60 Days
16	United Bank of India	144.34	Less than 60 Days
17	Vijaya Bank	36.62	Less than 60 Days
18	Yes Bank	733.47	Less than 60 Days

Source: RNE Annual Report FY2017 p 88

The debt of RNE has been mounting since FY2016, and in FY2017 the consolidated debt was Rs 89.5 bn, as compared to Rs 78.6 bn in FY2016, and its debt to equity is clearly unsustainable.



Source: RNE

The financial results of RNE in FY2018 has only got worse. Revenue has plummeted, interest costs have not only soared but are significantly higher than revenue and losses are mounting.

RNE - Financial Results Highlights in FY2018

Rs mn	1QFY2018	2QFY2018	3QFY2018	9MFY2018
Revenue	**1,648**	**833**	**540**	**3,021**
EBITDA	794	130	115	1,039
Interest	**-1,511**	**-1,677**	**-1,825**	**-5,013**
Depreciation	-493	-499	-499	-1,490
PBT	-1,210	-2,045	-2,202	-5,457
Exceptional item	-1,632	0	0	-1,632
Tax/DTA	538	539	539	1,616
Net Loss	-2,304	-1,506	-1,663	-5,473

Source: RNE

What is even more interesting is that in early to mid-March, i.e. after RNE had informed stock exchanges that it was going to be classified as irregular and/or non-performing by banks, Yes Bank officials were informing sell-side analysts that all was well, and shareholders had no reason to worry from any corporate accounts that may be classified as NPA. Sell-side analysts were concerned as an RBI circular dated February 12, 2018 compelled the industry to classify accounts as NPA which were under various corporate restructuring mechanisms, and hence the industry was expected to be badly hit with a surge in corporate NPAs.

A research note by *IIFL* on a management meeting with Yes Bank, rated a ‘Buy’, dated March 23, 2018 states,

> *Well-positioned to mitigate credit quality issues. Management insists that the RBI circular will not accelerate its delinquencies. It proactively identifies stress and has adequate safeguards in contracts.*

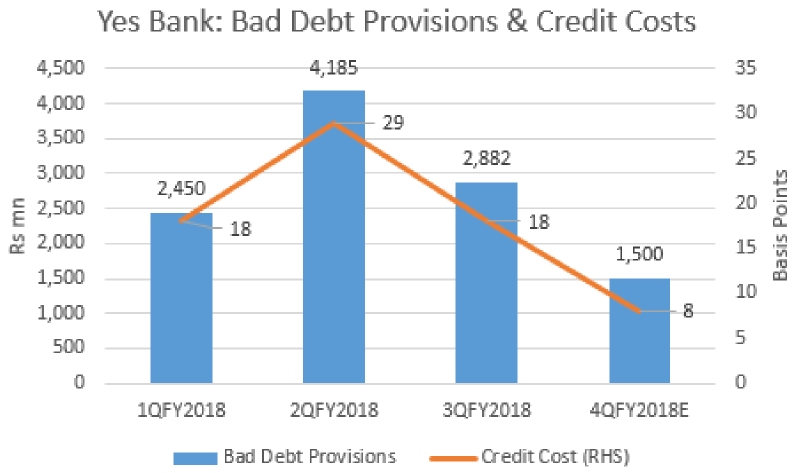
An *HSBC* note dated March 15, 2018 titled, "Buy: Management meeting reinforces positive outlook" said,

> *Our recent interaction with YES Bank's management (Mr Rajat Monga, CFO, and Mr Niranjan Banodkar, Head of Investor Relations) provided interesting perspectives on some key areas, and overall, it reinforced our view that the bank is in a strong position to sustain its market share gains while improving its core profitability.*

A note by *J M Financial* dated March 8, 2018, a week after RNE had informed the stock exchanges about it being classified as NPA, titled, "Yes Bank – Buy, Q&A with management," said

> *Q: What is the impact the recent RBI guidelines on stressed assets impacting Yes Bank and the credit costs outlook thereof?*
>
> *[A] For Yes Bank, the impact of the recent RBI guidelines on our Restructured Book as well as on exposures to entities with systemic exposures above INR1Bn is minimal and it doesn't alter the Bank's outlook on its credit / asset quality parameters.*

It is apparent from these research notes that senior officials of Yes Bank were not informing sell-side analysts about its significant RNE exposure of Rs 4.85 bn, despite the company informing the public on March 1, 2018 that banks will be classifying the account as irregular/NPA. The slippage of RNE to NPA for Yes Bank may marginally move the needle on the bank's overall credit costs, but nevertheless the size of the exposure is significant enough to forewarn analysts – a single account constitutes 16% of the bank's 3QFY2018 gross NPAs of Rs 29.74 bn. A fallout of the RNE non-disclosure is how many more of such accounts, maybe present in Yes Bank's portfolio that analysts have not unearthed? It is pertinent to remember that Mr Rajat Monga (the former CFO, a new CFO was appointed on April 3, 2018) has the dubious credibility of signing off on two consecutive years of untrustworthy accounts. If Yes Bank reports the RNE account as "standard" when it reports 4QFY2018 results on April 26, 2018, it reveals that issue of transparency of its asset quality remains and naming and shaming the bank by regulatory disclosures has no impact.



Source: Yes Bank

In the quarter ended March 31, 2018, the Indian banking and financial institutional industry is likely to add Rs 90-100 bn as NPA from this single account (RNE). The incremental bad debt provisions for the industry based on a minimum 15% provision will be around Rs 13.5 bn- Rs 15 bn, and for Yes Bank it would be around Rs 728 mn (around 25% of 3QFY2018 provisions from a single account). In 1QFY2018, Yes Bank had guided for FY2018 credit costs of 50-70 basis points (bps) and for the 9 month period ended December 2017, the bank achieved 64 bps. For the 4QFY2018, assuming the bank increases credit by 50% yoy and reports bad debt provisions of Rs 1,500 mn, assuming credit costs of 8 bps including RNA credit costs, then a single account will account for around half of the total credit costs for the bank. If Yes Bank adds the RNA credit costs to the Rs 1,500 mn for the entire bank, the overall credit costs increases to 12 bps from the earlier estimate of 8 bps.

More importantly though, trusting analysts who had faith in Yes Bank's earlier accounts, and who continue to rate the bank as a "Buy" as they meet the same officials who conjured the earlier accounts, may consider taking some effort in cross-checking prior to regurgitating management commentary to institutional investors.

Disclosure & Certification

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— Hemindra Hazari (17 Apr 2018)

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Yes Bank | ESG

Miracle at Yes Bank

By Hemindra Hazari | 01 May 2018

EXECUTIVE SUMMARY

It seems miracles do happen. The lame walk, the dying return to life, the blind see – well, maybe not the last, if they are sell-side analysts and the business media, in which case they keep their eyes closed for life. Had they attempted a close analysis of Yes Bank's 4QFY2018 results, they would have found that Reliance Naval Engineering (RNE) account of Rs 4.85 bn was classified by the bank as a standard performing asset -- a feat surely equaling the lame walking or the dead returning to life. This despite the fact that RNE's 4QFY2018 results, declared prior to Yes Bank's, show worsening financials, with most of the 20-member bank consortium of the company likely to classify the account as non-performing for the 4QFY2018.

An issue that naturally arises is how Yes Bank is able to get its loan serviced by RNE in the March quarter, when RNE was unable to service the consortium banks since the December quarter. Moreover, the precarious financial health of RNE indicates that it will be difficult for any bank to continue to classify the account as performing in 1QFY2019. Given that Yes Bank is a repeat offender, reporting untrustworthy accounts for FY2016 and FY2017, the regulator should examine how such an account has been classified as standard by the bank in the March quarter.

DETAIL

In an earlier insight, Reliance Naval Sinking Into NPA - Yes Bank to Take a Hit, on April 19, 2018, this writer had cautioned that RNE was a problem account in the industry and that most banks in the consortium would be classifying the account as a non-performing asset (NPA).

Standalone RNE Quarterly Results in FY2018

Rs mn	1QFY2018	2QFY2018	3QFY2018	4QFY2018
Revenue	**1,648**	**833**	**540**	**331**
EBITDA	794	130	115	**-2,145**
Interest	**-1,511**	**-1,677**	**-1,825**	**-1,960**
Depreciation	-493	-499	-499	-491
PBT	**-1,210**	**-2,045**	**-2,202**	**-4,596**
Exceptional item	-1,632	0	0	0
Tax/DTA	538	539	539	509
Net Loss	-2,304	-1,506	-1,663	-4,087

Source: RNE

Consolidated RNE Annual Results

Rs mn	**FY2017**	**FY2018**	**Change (%)**
Revenue	**5,641**	**3,786**	**-32.9**
EBITDA	733	**-1,002**	
Interest	**-6,255**	**-7,541**	**20.6**
Depreciation	-2,079	-2,077	-0.1
PBT	**-7,601**	**-10,620**	**39.7**
Exceptional item	0	-1,624	
Tax/DTA	1,828	2,125	16.2
Net Loss	**-5,773**	**-10,119**	**75.3**

Source: RNE

On April 23, 2018, RNE declared its results, which clearly showed a marked deterioration both in stand-alone quarterly results as well as the consolidated annual results. In consolidated annual results, revenue has fallen by 33%, while interest has risen by 21%, and in both years interest is more than revenue and losses have increased by 75%. Indeed, Pathak H.D. Associates, the company's auditor, commenting on certain observations, qualified the accounts and stated,

> *These conditions indicate the existence of a material uncertainty that may cast significant doubt on the Holding Company's ability to continue as going concern.*

RNE Auditor's Comment

5. We draw your attention to the:

a) Material Uncertainty Related to Going Concern
Note no. 3 to the statement regarding preparation of consolidated financial results of the Holding Company on going concern basis and also recognition of Deferred Tax Assets (DTA) on tax losses notwithstanding the fact that the Holding Company has been incurring cash losses, its net worth has been substantially eroded as on 31st March, 2018, loans have been called back by secured lenders, current liabilities are substantially higher than current assets, applications have been made to the National Company Law Tribunal (NCLT), Ahmedabad, under section 9 of the Insolvency Bankruptcy Code 2016 and winding up petitions been filed before Hon'ble Gujarat High Court for recovery of their dues by few operating creditors, for the reasons stated in the said note. The Holding Company is also of the view that no impairment of its noncurrent assets is required. These conditions indicate the existence of a material uncertainty that may cast significant doubt on the Holding Company's ability to continue as going concern. The appropriateness of assumption of going concern, recognition of DTA and evaluation of recoverable value of its noncurrent assets is critically dependent upon the approval of Holding Company's resolution plan by the secured lenders, the Holding Company's ability to raise requisite finance / generate cash flows in future to meet its obligations and to earn profits in future.

Source: RNE

When RNE's own auditor is questioning whether the company can continue as a going concern it is no surprise that the banks should be classifying the account as a NPA, especially when the company itself issued a press release on March 1, 2018 stating that banks will be classifying the account as NPA.

Yes Bank, as per the Registrar of Companies filing, has a sanctioned exposure of Rs 4.85 bn on RNE, and this account was classified by all the banks as a standard account as of 3QFY2018, although for most banks the company had not serviced interest dues as on December 31, 2017. Since as on March 31, 2018, it had become 90 days past due, most of the banks would classify the account as NPA -- with the notable exception of Yes Bank.

When Yes Bank reported its 4QFY2018 results on April 26, 2018, 3 days after RNE, it became apparent that the bank's RNE exposure was classified as performing, as the total corporate slippages to NPAs in the quarter was only around Rs 3.17 bn, lower than its RNE exposure.

Yes Bank: Slippages to Gross NPAs

	Corporate			Retail	Total
Rsmn	**Normal Corporate**	**Divergences for FY17**	**Restructured+NCLT**		
1QFY2018	1,280	0	0	730	2,010
2QFY2018	7,400	12,190	0	300	19,890
3QFY2018	2,146	0	2,454	349	4,949
4QFY2018	**3,170**	0	282	350	**3,802**
FY2018	13,996	12,190	2,736	1,729	30,651

Source: Yes Bank

Responding to a journalist's query during the results press conference on the status of the RNE account, Rana Kapoor, the promoter-CEO of the bank, said that the RNE account was performing for the bank and it was a well collateralized exposure which could be easily liquidated.

The Basel-3 disclosures pertaining to industry-wise loans and collateral held show that Yes Bank, under the shipyard classification, has a total fund-based exposure of Rs 4.6 bn, which is close to the ROC disclosure, and hence one can infer that the fund-based shipyard exposure is that of RNE. More importantly, it reveals that prior to the 4QFY2018, this exposure was not backed by lien but in 4QFY2018, a lien of Rs 4.45 bn suddenly appears.

Shipyard Exposure of Yes Bank as per Basle-3 Disclosures

Rs mn	4QFY2017	1QFY2018	2QFY2018	3QFY2018	4QFY2018
Fund-based	4,526	4,563	4,568	4,588	4,588
Backed by Lien	***0***	***0***	***0***	***0***	***4,445***
Non-fund based	1,827	2,452	2,456	2,532	2,292
Total Exposure	6,353	7,015	7,024	7,120	6,880

Source: Yes Bank

It appears that this lien of Rs 4.45 bn is the well collateralized security that Rana Kapoor is alluding to. The issue is by the 3QFY2018, all the banks were aware that RNE was a problem account and the likelihood of it becoming a NPA was very high. Not only was RNE cash-strapped and excessively leveraged, the Anil Ambani business group it belonged to was also experiencing financial difficulties. As per the bankers this analyst interacted with, RNE was unable to even pay for normal banking fees but yet miraculously, it was able to exclusively carve out a security of Rs 4.4 bn for Yes Bank, a non-consortium bank in a period of financial crisis when even the company's auditor was questioning its existence as a going concern.

This amazing feat of banking by Yes Bank needs to be investigated by the banking supervisor, as Yes Bank has supposedly not only been able to get its loans serviced when the company was unable to service loans from the consortium of banks, but it has also been able to extract a highly liquid security from the company during a period of acute financial crisis. Whether Yes Bank can continue to classify RNE as a standard account in FY2019 remains to be seen. It cannot be ruled out that it would instead contribute to a hat-trick in mis-reporting of the bank's accounts in FY2018.

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— Hemindra Hazari (01 May 2018)

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Yes Bank | ESG

Yes Bank's Matix Fertiliser Exposure Classified as Standard When Most Banks Treat It as NPA

By Hemindra Hazari | 30 May 2018

EXECUTIVE SUMMARY

It is an unusual development when a corporate account is classified as a non-performing asset by a group of banks while other banks classify the same account as performing. Earlier, in the absence of a database, banks were unaware how other banks were classifying the same account. But now, thanks to the Central Repository of Information on Large Credits (CRILIC), a database where all banks mandatorily have to submit their classifications for large corporate accounts, transparency has increased amongst banks. And this increased transparency is turning up new, worrying information about how some banks are following their own, novel methods of classifying problem loans. As the revelations unfold, who knows what more might be in store?

DETAIL

On April 19, 2018, in the case of Reliance Naval Engineering, this writer had highlighted how Yes Bank and HDFC were likely to classify the account as performing when the 20-member government bank consortium were expected to classify the same account as non-performing in the quarter ended March 31, 2018. This development became evident when Yes Bank,HDFC,Union Bank and Vijaya Bank declared their results. In such cases, the banks which continue to classify the account as performing and standard, need to be thoroughly investigated by the respective regulators on how defaulting companies were servicing the loans of these particular entities.

Matix Fertiliser and Chemicals has been in the news as a company linked with the Essar group and also linked to Nupower Renewables, which is controlled by Deepak Kochhar (spouse of ICICI Bank CEO, Chanda Kochhar). MFC's business plan was to purchase coal-bed methane from Essar group's Raniganj coal mine in West Bengal to produce fertilisers, but in February 2018, GAIL outbid MFC to purchase the entire production of the Essar Raniganj mine.

One of the lesser known facts about MFC is that it is a NPA with most of the banks that have granted loans to the company. As per CRILC, for the period ended March 31, 2018, Indian lenders have an exposure of around Rs 40.45 bn, and out of the 12 lenders, only 3 of them classify the account as standard: Punjab National Bank (Rs 1.74 bn), Vijaya Bank (Rs 1 bn) and Yes Bank (Rs 836 mn). In the case of Yes Bank, it is the only bank where it is classified as a non-CDR (corporate debt restructuring) standard loan and is part of its disclosed restructured standard loans as on March 31, 2018. While for 7 banks, MFC is a sub-standard NPA, for State Bank of India and Axis Bank, MFC is a doubtful account where the provisioning requirement is even higher than for a sub-standard account. When most banks are classifying the account as substandard and two banks have classified it as doubtful, it is extremely strange for the 3 banks to classify the account as a performing standard account. It is possible in the case of MFC, multiple tranches of loans were given by banks for project financing with different timelines for payment schedules and hence different banks classified it differently based on their payment schedules.

Out of the three banks that have classified MFC as standard, Yes Bank has the highest market capitalization, price to book value and also foreign ownership. Hence institutional investor interest is the highest in Yes Bank as compared with PNB and Vijaya Bank. When an entity trades at a premium to others in its category, the market expects higher accounting standards, greater transparency and superior corporate governance apart from better financial performance. It remains a mystery of how and why Yes Bank classified even a small loan of Rs 836 mn as standard.

	Mkt Cap.	P/BV	Foreign Ownership
	Rs bn	x	%
Yes Bank	806.5	3.7	42.6
PNB	244.7	0.6	9.1
Vijaya	77.3	0.9	5.1

Source: Moneycontrol

Yes Bank has superior financial performance, which is reflected in its premium valuation multiple, but, sadly, in terms of accounting integrity it has been a major disappointment. Yes Bank stands guilty of mis-reporting its accounts for two consecutive years, (i.e for the year ended March 31, 2016 and 2017) by under-reporting its NPAs and over-stating its profits, and there was huge variance between the regulator's assessment of its NPAs and that of the bank's audited results. The accounts of a bank which reports two consecutive years of NPA 'divergence' and still retains its chief executive officer, cannot be trusted as the CEO is directly accountable for the NPAs and profits reported by the bank.

Following considerable anguish by sell-side analysts and the business media, Yes Bank assured the public that it had rectified its NPA reporting issues in the year ended March 31, 2018. However, not much seems to have changed for the bank as it reported its Reliance Naval Engineering loan of around Rs 4.85 bn as a performing asset when banks like Union Bank and Vijaya Bank reported it as NPA, and all the other government banks in the RNE consortium are expected to report the account as NPA when they report their results. Even the auditor of RNE qualified the company's accounts and questioned it as a going concern. But Yes Bank steadfastly classified the account as performing. For Yes Bank, RNE is not an exception for in MFC it is also in the minority of 3 banks who have classified the account as performing and standard when all the other lenders have classified it as NPA. It is possible that Yes Bank may classify MFC as NPA by June 2018 as it was classified as SMA-2 (overdue between 61-90 days) in March 2018.

As the French critic, journalist and novelist, Jean-Baptiste Alphonse Karr famously remarked in the mid 19thcentury, "plus ça change, plus c'est la même chose" (the more things change, the more they stay the same).

Disclosure & Certification

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— Hemindra Hazari (29 May 2018)

Hemindra Hazari

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Yes Bank | ESG

Will India's Banking Regulator Approve a Serial Mis-Reporter for One More Term?

By Hemindra Hazari | 14 Jun 2018

EXECUTIVE SUMMARY

Yes Bank shareholders with an "overwhelming majority" approved the reappointment of Rana Kapoor as managing director and CEO for another 3 years effective September 1, 2018. Such is the abysmal state of corporate governance: the prominent institutional shareholders of Yes Bank, who are merely managers of other people's monies, have apparently turned a Nelson's eye to not one but two successive years of dodgy accounts under the leadership of Rana Kapoor. A company's annual accounts are sacrosanct, as they are the bedrock for market valuation and determining senior management compensation. Suppressing non-performing assets and inflating net profits are cardinal sins, demanding the instant removal of the CEO, the Chief Financial Officer (CFO), the head of the audit committee of the board and the auditor. But in India, bank CEOs can defy the banking regulator and merrily produce fudged accounts without any fear of censure. Worse, shareholders not only fail to punish the CEO, but actually reward the individual with another term. It remains to be seen whether the Reserve Bank of India approves Rana Kapoor for another term. If it does, this will be one more nail in the coffin of the banking regulator's credibility, as it will be endorsing fictitious accounts by the banks.

DETAIL

On June 12, 2018, Yes Bank issued a statement,

> *The shareholders supported the resolutions for re-appointment of Mr. Rana Kapoor as MD & CEO of the Bank for a further period of 3 years, effective September 1, 2018, with an overwhelming majority. The re-appointment is subject to final approval by the Reserve Bank of India (RBI).*

The approval by shareholders is shocking as during the year ended March 31, 2018 (FY2018), following a new regulatory disclosure, Yes Bank revealed that it significantly under-stated its NPAs and inflated its net profits for 2 consecutive years i.e. in FY2016 and FY2017.

Two Successive Years of Mis-reported Accounts by Yes Bank

Rsmn	FY2016	FY2017
Gross NPAs Reported	7,490	20,186
Gross NPAs as assessed by RBI	49,257	83,738
Divergence in Gross NPA	**41,767**	**63,552**
Net NPAs Reported	2,845	10,723
Net NPAs as assessed by RBI	36,032	58,916
Divergence in Net NPAs	**33,187**	**48,193**
Provisions for NPAs	4,645	9,463
Provisions for NPAs as assessed by RBI	13,225	24,821
Divergence in Provisions	**8,580**	**15,358**
Reported Net Profits	25,395	33,301
Net Profits as assessed by RBI	19,784	23,161
Divergence in Net Profits	**-5,611**	**-10,140**
Divergence (%)		
Gross NPA	**557.6**	**314.8**
Net NPA	**1,166.6**	**449.4**
Provisions	**184.7**	**162.3**
Net Profits	**-22.1**	**-30.4**

Source: Yes Bank

Yes Bank reported a 'divergence' of gross NPAs in FY2016 of 558% and in FY2017 of 315% and its net profits should have lower by 22% and 30% respectively in those years. The percentage variation is huge, and such mis-reporting should impact market valuation and perception of the management, as it reflects extremely poorly on the CEO. India's NPA identification is rule-based and hence there should be minimal divergence between the regulator's assessment and that of the bank.

Yes Bank argued that the impact of the divergence was minimal, as the bank was able to recover most of the 'divergent' loans after the closure of the annual accounts. Such an explanation is irrelevant, as the bank should have first classified and provided for the bad loan and then it could have subsequently written back the provisions when it was able to recover it.

Responding to a Bloomberg article , Yes Bank stated, Responding to a Bloomberg article , Yes Bank stated,

> *We would like to highlight that Bank remains committed to fullest compliance with RBI regulations or norms and with further learnings from past risk-based supervisory exercises is confident of ensuring full conformity to all RBI guidelines*

Contrary to Yes Bank claims, this writer highlighted that even in FY2018, the bank had classified two corporate accounts, Reliance Naval Engineering and Matix Fertiliser, as performing when most of the banks who had exposure had classified the companies as NPA. This impacts the credibility of the bank's FY2018 accounts as well.

Mis-reporting of accounts in a bank by under-stating NPAs and over-stating profits is a serious offence, and shareholders should immediately remove CEOs who have signed off on such accounts, as subsequent accounts under the same CEO lack credibility. It is therefore surprising that shareholders voted with an "overwhelming majority" to give Rana Kapoor an additional 3-year term as CEO. As per Yes Bank's shareholding pattern as on March 31, 2018, foreign portfolio investors held 42.6%, insurance companies 14.2% and domestic mutual funds 10.3%. The majority ownership is therefore held by investment managers of other people's money. Since the majority of shareholders endorsed Rana Kapoor, it seems they have no objection to being shareholders in a bank which consistently mis-reports its accounts. It remains to be seen how such investment managers can justify to their investors (a significant component of whom are foreign) that their savings are being invested in a bank where the accounts are untrustworthy.

Prominent Non-Promoter Share Holders in Yes Bank as on March 31, 2018

	%
Life Insurance Corporation of India	9.68
Birla SunLife Trustees Company	2.30
ICICI Prudential Life Insurance Co.	2.01
Franklin Templeton Mutual Funds	1.76
Franklin Templeton Investment Funds	1.48
Vanguard Emerging Market Stock Index Fund	1.20
T Rowe Price Emerging Stock Market Funds	1.01

Source: Yes Bank

While Yes Bank shareholders are happy to endorse a CEO who has a track record of inflating profits, the RBI, the banking regulator, is entrusted with the responsibility of financial stability and protecting depositors. It is because of the RBI notification that the public is aware of which banks flagrantly violate the RBI norms of income recognition and asset classification. For a bank CEO who has presided over 2 consecutive years of mis-reported accounts to be endorsed by the RBI for another 3-year term would demolish what little is left of RBI's credibility as a banking supervisor, and destabilise the financial system, as the banking regulator will be seen as endorsing fudged accounts in the banking sector.

For the sell-side, a bank which habitually mis-reports its accounts is par for the course. According to Bloomberg, 52 analysts maintain a recommendation on Yes Bank, with 45, the overwhelming majority with a 'Buy', 5 with a 'Hold' and only 2 maintaining a 'Sell'.

Sadly, the Yes Bank episode totally exposes the hypocrisy of institutional investors, who are supported and advised by experienced analysts and who regularly preach the virtues of corporate governance and transparency. As custodians of public funds, their commitment is found wanting.

Disclosure & Certification

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— Hemindra Hazari (13 Jun 2018)

Hemindra Hazari

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Yes Bank | ESG

Yes Bank to Be Headless?

By Hemindra Hazari | 04 Sep 2018

EXECUTIVE SUMMARY

While the Reserve Bank of India (RBI) has put Yes Bank on tenterhooks by refusing to endorse a fresh three-year term as Chief Executive Officer (CEO) for the serial mis-reporter Rana Kapoor, no one has noticed the perfect storm this unleashes on the bank. A 2015 Bombay High Court judgement laid down that whole time directors in the bank could only be appointed jointly by the two promoters. This is highly unlikely, as the two promoters are currently at war. The remaining board members are either too old or not qualified to hold the post. This raises the prospect that Yes Bank may soon become headless.

DETAIL

In the dying hours of August 31, 2018, the date on which the term of Mr Rana Kapoor, the promoter-CEO of Yes Bank, ended, the bank issued a terse press statement, stating,

> *YES BANK has received Reserve Bank of India's approval that Shri. Rana Kapoor may continue as the MD & CEO of the Bank, till further notice from the RBI.*

The capital market had been sensing for some time the regulator's reluctance to endorse the decision of the Yes Bank board to renew Rana Kapoor's tenure for another 3-year term. The bank's shareholders at the annual general meeting of June 12, 2018 had approved Kapoor's re-appointment, and the bank thereafter had sent the proposal to the RBI for approval. More than two months later, on August 29, 2018, CNBCTV18 reported that the RBI, apparently having reservations about giving its approval, had asked Yes Bank whether they wished to reaffirm their appointment of Rana Kapoor, to which the board had again reaffirmed its commitment to renew Kapoor's term.

By not endorsing a 3-year tenure for Rana Kapoor and instead stating, "till further notice," the RBI clearly indicated its displeasure regarding the board's decision to provide Kapoor with a full 3-year term. This writer has been highlighting in numerous insights (here and here) that the bank's accounts are untrustworthy. For two consecutive years (FY2016 and FY2017) the bank had understated non-performing loans and overstated net profits. In FY2018, this writer had highlighted how two corporate accounts in Yes Bank, Reliance Naval and Matix Fertiliser were classified as performing and standard when most banks having the exposure had classified the accounts as NPA, thus casting doubts on even the bank's FY2018 accounts. Under such circumstances, it would have been improper for the regulator to endorse another term for the CEO.

The capital market and sell-side research reacted negatively to the news of an uncertain tenure for Rana Kapoor, as the bank has been identified with Rana Kapoor since its inception and he is seen to be the major driving force. Investors are facing uncertainty with no definite term for Rana Kapoor, and without information in the public domain about whether the RBI has made it conditional on the bank achieving certain benchmarks of accounting accuracy and corporate governance. However, the market seems to have ignored a material development of the past which makes the issue even more complex and uncertain.

The uncertainty on the bank's future leadership is compounded by a Bombay High Court Order of June 4, 2015, which makes it difficult to appoint a suitable candidate for the CEO's post or even appoint a whole time (executive) director. A dispute had arisen between the Indian promoters of Yes Bank, Rana Kapoor and the successors of Ashok Kapur (who was killed in the Mumbai terror attacks in November 2008) on the appointment of whole time directors and directors representing the Indian promoters. The High Court judgement was unsatisfactory for both the disputing promoters and the matter was appealed to the Supreme Court of India, where it is currently being heard.

Some critical aspects of the Bombay High Court judgement have a direct bearing on the issue at hand and investors should be made aware of these issues. The judgment interpreted the Articles of Association which governed the promoters conduct in recommending whole time directors.

> *8.17 The amended Article [of Association] 127A also gave the Indian Partners the right to recommend Whole Time Directors to the Board of Yes Bank.*
>
> *8.44 This takes us immediately to the second question: how is that right to be exercised? I believe this question more or less answers itself. The right in Articles 110(b), 127(b) and 127A(a) must be exercised jointly or not at all. Nothing in either of those Articles lends itself to an understanding that each Indian Partner was entitled to exercise that right unilaterally, i.e., to the exclusion of the other.*
>
> *8.45 …Nothing in these Articles suggests that either of these two men [Rana Kapoor and Ashok Kapur] could have done so. They were entitled to exercise that right jointly or not at all. Finding that the right passes on to their successors does not and cannot alter this position. The rights in the Articles are, consequently, are ones that can only be exercised jointly, never singly.*
>
> *(c) Another argument raised is that should, for ig [sic] any reason, Rana Kapoor cease to be the Managing Director/CEO, Yes Bank would be in an unviable position, being unable to appoint suitable employees to whole time directorship; and Section 203 of the 2013 [Companies] Act requires a whole time director where there is no Managing Director. This argument by the directors proceeds on too stretched a hypothetical, and indeed there is nothing that prevents the company from appointing a suitable candidate from among the 15 who serve on its Board.*

Hence according to the High Court judgement, which Yes Bank and the RBI have to currently abide by, whole time directors can only be appointed by a joint recommendation of both the warring promoters and a managing director/CEO can only be appointed from the existing board members, which currently consist of 9 directors. The Yes Bank board can appoint non-whole time directors which do not require the recommendation and approval of the promoters.

The problem is that the promoters of Yes Bank, Rana Kapoor and the successors of Ashok Kapur, have been unable to come to an understanding on jointly recommending whole time directors or on any major issue in the management of the bank, and hence it is extremely unlikely that in future they can jointly recommend a whole time director.

With the current uncertainty regarding Rana Kapoor's future tenure as CEO, shareholders are in a predicament on the succession issue. If the RBI does not consider Rana Kapoor 'fit and proper' to continue as a CEO or considers that he will be permitted a tenure of less than 3 years, his replacement can only come from the existing nine directors of Yes Bank's board.

Yes Bank Board of Directors

Yes Bank Board of Directors

	Name	Designation	Age	Appointment	Background
1	Rana Kapoor	CEO-Promoter	60	2003	Commercial Banking
2	Lt Gen. (retd) Mukesh Sabharwal	Independent	66	25 April 2012	Indian Army
3	Brahm Dutt	Independent	68	24 July 2013	Indian Administrative Service
4	Vasant V. Gujarathi	Independent	67	23 April 2014	Accounting
5	**Ajai Kumar**	**Non-executive non-independent**	**65**	**29 January 2016**	**Commercial Banking**
6	Ashok Chawla	Chairman, independent	67	30 October 2016	Indian Administrative Service
7	**Subhash Kalia**	**Non-executive non-independent**	**67**	**03 April 2018**	**Commercial Banking**
8	Pratima Sheorey	Independent	Late 40s	26 April 2018	Academia, Marketing
9	Rentala Chandrashekhar	Independent	65	26 April 2018	Indian Administrative Service

Source: Yes Bank , Bloomberg

Even though Yes Bank has 9 directors, their age and background deters them from being considered by the RBI for the appointment of a CEO and a replacement for Rana Kapoor. As per Section 10B of the Banking Regulation Act, 1949, (BRA) only a banker or an individual having, "financial, economic or business administration" background can qualify for the post of whole time chairman or managing director. Serving and former government bureaucrats have served as CEOs in banks, notably, P.J. Nayak in Axis Bank (January 2000 – April 2009) but they had been appointed at a much younger age. The problem with the Yes Bank board is that it is mainly filled with retired professionals from government banks or from the Indian bureaucracy, and barring Rana Kapoor and Pratima Sheorey, all the individuals are in their mid to late 60s. The RBI had increased the retirement age for private sector bank CEOs from 65 to 70 years, and hence it is unlikely to approve a CEO who is over 65 years of age at the time of appointment. Pratima Sheorey, in her late 40s, has a marketing background and lacks banking experience; hence she will not qualify for the post of bank CEO as per the BRA. In a worst case scenario, despite their advanced age, the two former government bank officials, Ajai Kumar and S C Kalia, can qualify as CEOs to succeed Rana Kapoor if the RBI cuts short his tenure.

Rana Kapoor's uncertain tenure as CEO, coupled with the Bombay High Court judgment of 2015 pertaining to the appointment of whole time directors, has caused a perfect storm in the succession issue at Yes Bank. The ageing composition of Yes Bank's board of directors and the complete absence of whole time directors apart from Rana Kapoor exposes the bank to leadership risk. Sadly, neither the banking regulator nor the board can do anything about it. The only solution is for either the promoters to bury their differences and jointly recommend whole time directors or for the promoters to reduce their shareholding to below 10%, thereby automatically removing themselves from recommending whole time directors and allowing the board to take the necessary decisions.

In such a precarious situation it remains to be seen how long the RBI will allow Rana Kapoor to continue as the CEO.

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— Hemindra Hazari (04 Sep 2018)

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Yes Bank | ESG

Finally, the Regulator Regulates, Pushes Kapoor Out as CEO of Yes Bank

By Hemindra Hazari | 19 Sep 2018

EXECUTIVE SUMMARY

On the evening of September 19, 2018, Yes Bank informed the stock exchanges that the Reserve Bank of India (RBI) had instructed the bank that Rana Kapoor's term as CEO must end on January 31, 2019. Like Shikha Sharma of Axis Bank, Kapoor misreported accounts for two consecutive years; like Sharma, he has been given the boot by the RBI.

For some time now, I have been harping on the point that bank CEOs who misreport accounts need to be sacked. Unfortunately, I have had little or no company in this activity. I have also sharply criticised the regulator for failing to intervene. The forced departures of Sharma and Kapoor are promising signs that the RBI is getting tough with serial misreporters.

In Yes Bank, the CEO succession is more complex on account of a High Court judgement in 2015 which stated that wholetime (executive) directors on the board can only be nominated jointly by both the Indian promoters. However, the two promoters have been warring with each other and have been unable to agree on any major issue. As Rana Kapoor is the sole wholetime director, the bank has three choices: (i.) promoters have to temporarily call a truce and jointly nominate an individual as a CEO (ii.) Promoters can sell their individual stakes in order to reduce their stakes to below 10%, thereby losing their right to recommend wholetime directors (iii.) the board can select one of its (ageing) members to replace Kapoor. As the suitable candidates on the board are all over 65 years of age and RBI's norms caps the retirement age of CEOs at 70 years, such a candidate can only be temporary.

It is pertinent to note that in both Axis Bank and Yes Bank, the board of directors were rewarding their CEOs with another term for misleading shareholders and the public for two consecutive years, and it was the banking regulator who was compelled to step in and end the fiasco. The RBI's decision is a warning shot to the new private sector banks that they can no longer continue to mismanage their operations, that the regulator's writ reigns supreme, and that bank CEOs violate it at their peril. Such a decision, though causing

uncertainty for shareholders, reinforces the banking regulator's credibility as a supervisor and as the sentinel of financial stability.

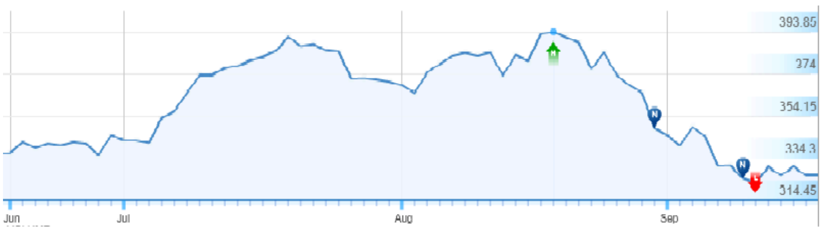
DETAIL

On September 19, 2018, Yes Bank informed the stock exchanges the,

> *Reserve Bank of India has vide letter dated September 17, 2018 received today, intimated that Shri Rana Kapoor may continue as the MD&CEO till 31 January 2019, and the Board of Directors of the Bank are scheduled to meet on September 25,2018 to decide on the future course of action.*

In an earlier insight dated September 4, 2018, titled, Yes Bank To Be Headless?, this writer had cautioned shareholders of such an event and why in Yes Bank's case, CEO succession is fraught with uncertainty and risk on account of a Bombay High Court judgement of 2015. In choosing a successor, either the two warring promoters; Rana Kapoor and the successors of Ashok Kapur have to bury the hatchet and jointly nominate a successor or the board will have to select one of its ageing directors as the future CEO. But, as the eligible directors are all 65+ years of age and RBI compels bank CEOs to retire by 70 years of age, such an individual can only be a temporary choice. This will create considerable uncertainty and confusion with investors inevitably resulting in erosion in the bank's share price. Since August 20, 2018, Yes Bank has under-performed the CNX NIFTY by 16.3%.

Yes Bank Share price Since June 2018



Source: Moneycontrol

As per the High Court judgment, which cannot be overruled by the RBI, either the Indian partners have to jointly recommend the candidate for wholetime director, or the individual promoter groups have to bring down their shareholding to below 10%, thereby ceasing to have the joint right to recommend wholetime directors.

The RBI's decision to cut short the tenures of Shikha Sharma as CEO of Axis Bank and now Rana Kapoor is a loud and clear signal to the public and the capital markets that mis-reporting of accounts will not be tolerated and the heads of bank CEOs will roll. This writer has been the sole analyst in the capital market highlighting that bank CEOs must be sacked for reporting fudged accounts. It is extremely unfortunate that sell-side analysts treated such events as par se and were willing to ignore such grave malpractices.

In the opinion of this writer, the new private sectors banks were getting away with fudged accounts, evergreening of non-performing loans, and CEOs who were managing the banks as personal fiefdoms with no accountability and oversight from the board of directors. It is pertinent to note that despite both Shikha Sharma and Rana Kapoor reporting two consecutive years of mis-reported accounts, the board of directors of both banks were rewarding the CEOs by renewing their term for another three years. This highlights the complete lack of corporate governance in these boards of directors.

It is gratifying to note that the RBI finally acted decisively and correctly in not renewing the three year term for such CEOs, thereby restoring the credibility of the RBI as a banking supervisor.

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— Hemindra Hazari (19 Sep 2018)

Hemindra Hazari

Specialist in Indian banking and economic research

Yes Bank | ESG

Fudge the Books? Join the Board: Yes Bank's Curious Promotion Policy

By Hemindra Hazari | 21 Oct 2018

EXECUTIVE SUMMARY

Corporate governance and the competence of the boards of directors at India's much-fancied new private sector banks keep touching new lows. The Reserve Bank of India has twice rejected Rana Kapoor's continuance as CEO of Yes Bank beyond January 31, 2019, leading to a collapse in the bank's share price. That Yes Bank's board of directors proposed this twice reveals its abject dependence on its promoter-CEO.

What has largely gone unnoticed has been the reward given by the board to Rajat Monga, the discredited former Chief Financial Officer (CFO). Monga has been elevated to the board, subject to RBI's approval. He has also been given a prominent role in explaining the current controversies to the public. For his role as CFO in certifying two consecutive years of fudged accounts, he should have been sacked, but instead the ever grateful board of directors has asked him to join them at the directors' table. Such an individual is not 'fit and proper' to grace any corporate board, and the RBI will do well to reconsider his appointment.

DETAIL

Rajat Monga joined Yes Bank in 2004, and was the CFO till April 2, 2018, when he stepped down, as the regulator insisted CFOs must have a minimum qualification of Chartered Accountancy. As the CFO, whose primary responsibility was the integrity of accounts, he had certified Yes Bank's accounts for the year ended March 31, 2016 and 2017 as 'true and fair' and said,

> *these statements do not contain any materially untrue statement or omit any material fact or contain any statements that might be misleading.*

CEO / CFO Certification

We, Rana Kapoor, Managing Director & CEO and Rajat Monga, Chief Financial Officer, of YES Bank Limited hereby certify that:

a. We have reviewed financial statements and the cash flow statement for the year ended March 31, 2016 and that to the best of our knowledge and belief:

   i. these statements do not contain any materially untrue statement or omit any material fact or contain any statements that might be misleading;

   ii. these statements together present a true and fair view of the Bank's affairs and are in compliance with existing accounting standards, applicable laws and regulations.

b. There are, to the best of our knowledge and belief, no transactions entered into by the Bank during the year which are fraudulent, illegal or violative of the Bank's Code of Conduct.

c. We accept responsibility for establishing and maintaining internal controls for financial reporting and that we have evaluated the effectiveness of internal control systems of the Bank pertaining to financial reporting and have disclosed to the Auditors and Audit Committee, deficiencies in the design or operation of such internal controls, if any, of which we are aware and the steps we have taken or proposed to take to rectify these deficiencies.

d. We have indicated, to the Auditors and the Audit Committee:

   i. significant changes in internal control over financial reporting during the year;

   ii. significant changes in accounting policies during the year and that the same have been disclosed in the notes to the financial statements; and

   iii. instances of significant fraud of which we have become aware and the involvement therein, if any, of the management or an employee having significant role in the Bank's internal control system over financial reporting.

Yours faithfully

Rana Kapoor
Managing Director & CEO
(DIN No: 00320702)

Rajat Monga
Chief Financial Officer

Place: Mumbai
Date: April 27, 2016

Source: Yes Bank FY2016 annual report p. 173

CEO / CFO CERTIFICATION

We, Rana Kapoor, Managing Director & CEO and Rajat Monga, Chief Financial Officer, of YES Bank Limited hereby certify that:

a. We have reviewed financial statements and the cash flow statement for the year ended March 31, 2017 and that to the best of our knowledge and belief:

   i. these statements do not contain any materially untrue statement or omit any material fact or contain any statements that might be misleading;

   ii. these statements together present a true and fair view of the Bank's affairs and are in compliance with existing accounting standards, applicable laws and regulations.

b. There are, to the best of our knowledge and belief, no transactions entered into by the Bank during the year which are fraudulent, illegal or violative of the Bank's Code of Conduct.

c. We accept responsibility for establishing and maintaining internal controls for financial reporting and that we have evaluated the effectiveness of internal control systems of the Bank pertaining to financial reporting and have disclosed to the Auditors and Audit Committee, deficiencies in the design or operation of such internal controls, if any, of which we are aware and the steps we have taken or proposed to take to rectify these deficiencies.

d. We have indicated, to the Auditors and the Audit Committee:

   i. significant changes in internal control over financial reporting during the year;

   ii. significant changes in accounting policies during the year and that the same have been disclosed in the notes to the financial statements; and

   iii. instances of significant fraud of which we have become aware and the involvement therein, if any, of the management or an employee having significant role in the Bank's internal control system over financial reporting.

Yours faithfully

Rana Kapoor
Managing Director & CEO
(DIN No.: 00320702)

Rajat Monga
Chief Financial Officer

Place: Mumbai
Date: April 19, 2017

Source: Yes Bank FY2017 annual report p. 228

Both these certificates endorsed by the CEO and his loyal CFO proved worthless, as subsequent Reserve Bank of India inspections revealed that the bank had cooked its books in both years, significantly under-reporting non-performing loans and inflating net profits

RBI Detects Significant Under-reporting of NPAs by Yes Bank

Rsmn	FY2016	FY2017
Gross NPAs Reported	7,490	20,186
Gross NPAs as assessed by RBI	49,257	83,738
Divergence in Gross NPA	**41,767**	**63,552**
Net NPAs Reported	2,845	10,723
Net NPAs as assessed by RBI	36,032	58,916
Divergence in Net NPAs	**33,187**	**48,193**
Provisions for NPAs	4,645	9,463
Provisions for NPAs as assessed by RBI	13,225	24,821
Divergence in Provisions	**8,580**	**15,358**
Reported Net Profits	25,395	33,301
Net Profits as assessed by RBI	19,784	23,161
Divergence in Net Profits	**-5,611**	**-10,140**
Divergence (%)		
Gross NPA	**557.6**	**314.8**
Net NPA	**1,166.6**	**449.4**
Provisions	184.7	162.3
Net Profits	**-22.1**	**-30.4**

Source: Yes Bank Annual Reports

On October 24, 2017, the RBI imposed a penalty of Rs 60 mn on Yes Bank for various transgressions, including mis-reported accounts. Cooking bank books is an extremely serious offence; indeed Indian law regards it as a criminal offence punishable with a jail sentence.

Section 46, Banking Regulation Act, 1949 , which deals with penalties, states:

> *(1) Whoever in any return, balance-sheet or other document 1[or in any information required or furnished] by or under or for the purposes of any provision of this Act, wilfully makes a statement which is false in any material particular, knowing it to be false, or wilfully omits to make a material statement, shall be punishable with imprisonment for a term which may extend to three years 2 [or with fine, which may extend to one crore [ten million] rupees or with both].*

It is shameful for any bank to report untrustworthy accounts for even a single year and be penalised by the regulator for the same. Yet, despite two consecutive years of fudged accounts, the bank's board of directors and the shareholders with an "overwhelming majority" endorsed Rana Kapoor as the CEO for another 3-year term. Fortunately, the RBI overruled the board and the shareholders of Yes Bank, and only extended his term till January 31, 2019. As per Yes Bank's own certificate of authenticity, the CEO and the CFO are to be held accountable for its accounts. Since the board of directors was not even remotely inclined to sack Rana Kapoor for such serious omissions, the RBI was compelled to protect the depositors and the public interest.

The board of Yes Bank, not content with renewing Rana Kapoor's term further, extended its generosity to the other culprit of the fudged accounts as well. It decided in its wisdom on September 30, 2018 to elevate Rajat Monga as an executive director of the bank.

This is the second time Rajat Monga will have been elevated to the board. He was appointed as an executive director during 2013-2015 but, a Bombay High Court judgement compelled him and others to step down, as they had been recommended by Rana Kapoor without the approval of the co-promoters, the successors of Ashok Kapur.

Now, not only has Yes Bank elevated Rajat Monga to the board, but he has also become the official spokesperson (here and here) for addressing sensitive issues to the public. According to media reports he is the point person for negotiating a settlement on behalf of Rana Kapoor with the successors of Ashok Kapur to bring about an amicable settlement to appoint a new CEO for the bank. According to a Macquarie report cited in the media, Rajat Monga may be even considered to succeed Rana Kapoor as CEO.

The decision to induct Rajat Monga as an executive director should have been recommended by the Nomination and Remuneration Committee (NRC) of the board which in FY2018 consisted of Brahm Dutt, independent director and chairman NRC, Lt. Gen. (Retd.) Sabharwal, independent director and Ajai Kumar, non-executive, non-independent director. To select the CEO, two external members will also assist the NRC, T.S. Vijayan, former chairman, Insurance Regulatory Authority of India (IRDAI) and O.P. Bhatt, former chairman, State Bank of India. If the selection of Rajat Monga is an example of how the board identifies a candidate as executive director, stakeholders and the regulator should be extremely concerned how Yes Bank selects the successor to Rana Kapoor as CEO.

The benevolent gaze of boards towards CFOs who have certified fraudulent accounts appears to be the norm in new private sector banks. Indusind Bank and Axis Bank are two other banks which reported two successive years of fudged accounts by the same CFOs. Neither CFO was fired or penalised and in both cases (here and p.38 of Indusind annual report) they were rewarded and received handsome increments.

The standards of corporate governance at Yes Bank are so abysmal that the board brazenly displays unflinching loyalty to a promoter-CEO and his loyalist, the former CFO. These are the very individuals directly responsible (by their own certification) for the two consecutive years of fraudulent accounts. The regulator was compelled to overrule the board and shareholders, and denied another term for Rana Kapoor as CEO. It appears it will also have to reject Rajat Monga as an executive director. If the RBI does not take a firm stand, it will be seen as rewarding CFOs who certify fraudulent accounts.

Disclosure & Certification

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— Hemindra Hazari (21 Oct 2018)

Hemindra Hazari

Specialist in Indian banking and economic research

Yes Bank | ESG

Yes Bank's Dwindling Directors Make Strange Selections for the Board

By Hemindra Hazari | 16 Nov 2018

EXECUTIVE SUMMARY

Leadership is unravelling at Yes Bank and the stock is tanking. In the dark hours of November 14, the bank announced the immediate resignations of Ashok Chawla, its non-executive, independent chairman, and Vasant Gujarathi, an independent director and head of its important audit committee. The directors of Yes Bank appear to have joined the ranks of endangered species. In June 2015, the Mumbai High Court revoked the appointment of 3 executive directors in Yes Bank; on September 19, 2018, the regulator had disallowed the continuance of founder-CEO Rana Kapoor from February 1, 2019; and director heads continue to roll at this beleaguered bank.

As investors lose hope, the bank must hurriedly appoint competent, independent-minded bankers in the board who can restore the regulator's confidence and withstand the incessant pressure from the founders. The abrupt resignation of an external expert on November 15, to select a new CEO further muddies the water. The immediate appointment of Uttam Prakash Agarwal, a former president of the Institute of Chartered Accountants, as an independent director and probable future head of the bank's audit committee may not be the most appropriate choice. The concerned individual has dabbled in politics and failed to be elected from a suburb of Mumbai in a 2014 Maharashtra state election as a representative of a political party. Appointing chartered accountants-cum-politicians may not be the best way to restore confidence in the bank at such a critical stage.

DETAIL

Corrigenda: There is an error in this insight. Please note the correction.
Correction: In the third to last paragraph, the phrase "...Bhatt should reason at this stage..." should read "...Bhatt should resign at this stage...".

On November 14, 2018 at 8:21 pm, Yes Bank informed the stock exchanges that its chairman, Ashok Chawla, had submitted his resignation with immediate effect. Chawla's resignation was inevitable, since he was named in a chargesheet filed by the Central Bureau of Investigation (CBI), India's premier federal investigation police, on July 19, 2018. The criminal investigation pertained to the time when Chawla was the Secretary of Economic Affairs in the Ministry of Finance. The moment he was charge sheeted by the CBI, his days as a director on Yes Bank were numbered, as RBI's 'Fit and Proper' Criteria for Directors on the Boards of Banks, IV b disqualified him as a director on any bank. In fact, Chawla should have resigned immediately when the CBI filed the charge sheet, but, sadly, he waited nearly 4 months to take this decision.

IV.	Proceedings, if any, against the director	
	a.	If the director is a member of a professional association / body, details of disciplinary action, if any, pending or commenced or resulting in conviction in the past against him / her or whether he / she has been banned from entry of at any profession / occupation at any time.
	b.	Details of prosecution, if any, pending or commenced or resulting in conviction in the past against the director and / or against any of the entities listed in II (b) and (c) above for violation of economic laws and regulations
	c.	Details of criminal prosecution, if any, pending or commenced or resulting in conviction in the past against the director
	d.	Whether the director attracts any of the disqualifications envisaged under Section 274 of the Company's Act 1956?
	e.	Has the director or any of the entities at II (b) and (c) above been subject to any investigation at the instance of Government department or agency?

Source: RBI

Yes Bank also announced the immediate resignation of Vasant Gujarathi, independent director and head of the audit committee of the board, who was appointed on April 23, 2014 to the board. Although his resignation was attributed to "personal commitments", Gujarathi was a member of the audit committee since his appointment on the board, and was the chairman of the audit committee since April 27, 2016. It appears that his belated resignation may be on account of the regulator pulling up the bank for fudged accounts for the years ended March 31, 2016 and March 31, 2017. In a strange anomaly, Rajat Monga, the Chief Financial Officer who certified those years of fudged accounts, was rewarded with a board seat, subject to RBI approval.

Yes Bank simultaneously announced the appointment, with immediate effect, of Uttam Prakash Agarwal as an independent director for a term of 5 years, subject to shareholder approval. The bank's press release on his appointment as a replacement for Gujarathi focused on his professional experience as a chartered accountant and the "the youngest President of ICAI [Institute of Chartered Accountants of India] 2009-10". Strangely, and perhaps intentionally, the bank omitted to mention that Agarwal had contested the Maharashtra state elections in 2014 for the assembly seat of Borivali, a suburb of Mumbai, as a candidate of the Shiv Sena party, but had lost the elections. Interestingly, during that election, media had documented that

> *Some students [below 18 years of age] of a local school in school uniform and during school hours were seen holding up placards and Shiv Sena flags, urging people to elect Agarwal.*

Although the said article quoted Agarwal as stating that the party had not asked any student to campaign for him, it also quoted an election official stating that election laws in India prohibit the participation of students in election campaigns.

While it is commonplace for corporate chiefs to cultivate the ruling party, it is not the normal practice for private sector banks, or private corporate sector entities in general, to nominate politicians as directors, as this adds an additional dimension of political risk. Investors should be cautious regarding Agarwal, a chartered accountant-cum-politician, replacing Gujarathi on the audit committee. Indeed, Agarwal may be even be appointed as the chairman of this important sub-committee of the board.

On November 15, 2018 at 7:58pm Yes Bank announced the resignation with immediate effect of O.P. Bhatt as an external expert of the 'Search and Selection Committee' for appointing a new CEO of the bank. This committee worked along with the bank's nominations and remuneration committee to select a new CEO and it is strange that Bhatt should reason at this stage citing "potential conflict of interest". All these departures in such a short time frame do not bode well for the bank.

Reacting to the resignations of the bank's chairman and the head of its audit committee, Yes Bank's stock tanked by 7% to Rs 206 on November 15, 2018 and is currently down a further 8% during market hours on November 16. The bank is now plunging into the new year without a chairman, and with its promoter-CEO being forced by the regulator to step down as CEO on January 31, 2019. The status of the appointments of its executive directors also remains uncertain as it requires the approval of the successors of Ashok Kapur as joint founders and the approval of the RBI, both of whom have had reservations pertaining to the choices of Rana Kapoor.

Yes Bank Last 6 Months Share Price Chart

Source: Moneycontrol

Yes Bank's stock has halved since August 20, 2018 on leadership concerns, and the nominations by the board of new appointees such as Rajat Monga, the former CFO who signed off on two successive years of fudged accounts, and now Uttam Prakash Agarwal, do not inspire confidence regarding the quality of leadership at this troubled bank.

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— Hemindra Hazari (16 Nov 2018)

Hemindra Hazari

Specialist in Indian banking and economic research

Yes Bank | Equity Bottom-Up

Yes Bank's Fate Is in the Hands of the Ordinary Depositor

By Hemindra Hazari | 30 Nov 2018

EXECUTIVE SUMMARY

The downgrade by Moody's of Yes Bank's rating to below investment and changing the outlook to negative, followed by the Indian rating agencies downgrade will bring liquidity risk and asset-liability management to the fore at this beleaguered bank. Corporate treasuries, sensitive to ratings will pull out their deposits from the bank, if they have not already done so, and the bank will be compelled to increase its rates to attract funds. In such a bleak environment, and with the daily barrage of negative news on the bank, the market must also be apprehensive of any spark triggering a retail run on deposits. However, it is pertinent to note on reported numbers there should be no reason for major concern. Even the best case scenario for the bank would see rising cost of funds, a compression on its net interest margin with an adverse impact on earnings until the leadership issue is resolved.

DETAIL

On November 27, Moody's downgraded Yes Bank's foreign currency issuer rating to Ba1 from Baa3 and changed the outlook from stable to negative. With the downgrade, the bank slipped from investment grade to non-investment grade. Worse, with the outlook changed to negative, it is unlikely to come back to investment grade for another year, and there exists a high probability of further downgrades. Those debt investors who hold Yes Bank foreign debt paper are now stuck, and now only those investors investing in junk debt will be interested in the debt of the bank. In terms of its foreign borrowing, normally there is a clause that if the rating slips below investment grade there is an automatic and sharp increase in the interest rate. Hence there should be a sharp and immediate increase in Yes Bank's foreign borrowing costs.

Subsequently, on November 28, Indian credit rating agencies ICRA and CARE also downgraded Yes Bank's domestic currency rating, but it remained in the investment grade (here and here). Here too the bank will be compelled to offer higher rates on its borrowing and on its deposits to attract funds.

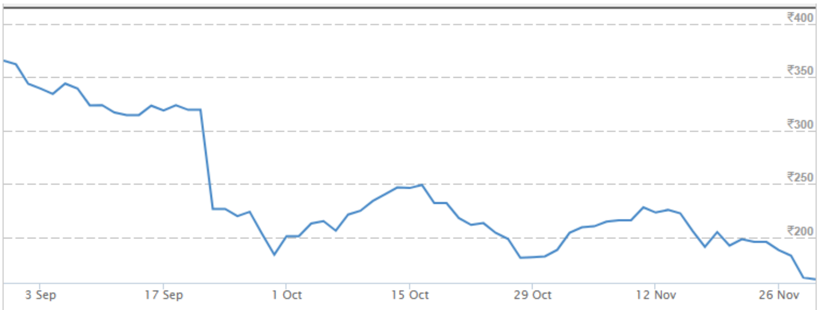
Corporate treasuries which park their short term funds with banks are extremely sensitive to downgrade in ratings, as they have stringent internal norms, and in the light of the ongoing leadership and boardroom crisis and with the daily barrage of negative news on Yes Bank, they would be pulling out (or not rolling over) their funds from the bank.

An *Economic Times* article dated November 30, 2018 titled, "MFs Stare at M2M Losses After ICRA Cuts Yes Bank Rating", states,"About a dozen mutual funds houses including Reliance MF, UTI MF and Franklin Templeton" have debt exposure to Yes Bank and debt-market dealers say that the bank's cost of funding "may rise upto 50 basis points."

In such an environment, the bank will now be faced with liquidity risk and its asset-liability management will be crucial. To stem the likely outflow of corporate and wholesale deposits, the bank will have to sharply increase rates on wholesale and also retail deposit rates. However, in the short term, retail deposits take time to mobilise. Hence for its immediate requirement of funds the bank may have to approach the RBI repo window and borrow against their excess government securities holding. If the outflow of wholesale funds becomes acute, the bank may have to sell its high quality loans to raise funds, thus impacting the residual quality of its loan book.

The problem for Yes Bank is that all this happening in an environment of global and domestic tightness in liquidity, with a capital outflow from emerging countries. In India, on account of the IL&FS fiasco and the related non-bank finance company (NBFC) liquidity and solvency issue and problems with real estate companies, the liquidity tightness is magnified.

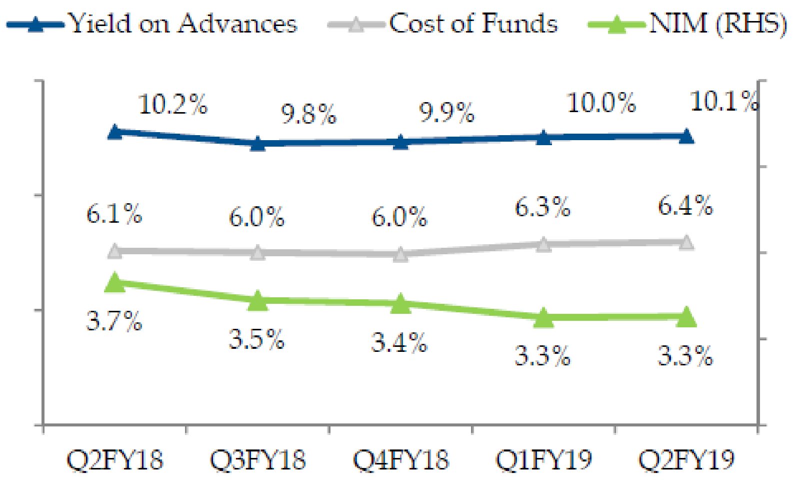
Yes Bank 3-Month Share Price Chart



Source: Moneycontrol

The 56% fall in Yes Bank's share price in the last 3 months also adds to the concern, the scrip touched its 52-week low of Rs 147 on November 29, prior to recovering to close at Rs 160. Yes Bank's capital adequacy is comfortable with CET1 at 8.3% (Rs 250 bn) and there is no major concern on its reported numbers. The bank, however, is at a very critical stage, because any spark may trigger a retail run on the bank, which may result in a full blown crisis for the bank and for the entire private banking sector. In India, even if government banks report negative net worth, huge losses and large frauds, retail depositors repose confidence in the banks because of sovereign ownership. The same faith is not extended towards private sector banks. After all, more than a decade earlier, ICICI Bank, despite reporting strong capital adequacy, experienced two runs, in 2003 and 2008. This shows the retail perception on private sector banks and how vulnerable they are to rumours.

Yes Bank Cost, Yield and Net Interest Margin



Source: Yes Bank

Even the best case scenario for Yes Bank would see a sharp increase in its cost of funds and a compression of its net interest margin. Investors must also expect the growth rates in loans to fall, as the bank requires to conserve liquidity at such a crucial juncture. Earning is naturally going to be a casualty, but investors need to be wary of how the retail depositor of Yes Bank behaves, as the immediate future of Yes Bank maybe in the hands of the ordinary faceless retail depositor

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— Hemindra Hazari (30 Nov 2018)

Hemindra Hazari

Specialist in Indian banking and economic research

Yes Bank | Equity Bottom-Up

Yes Bank's New CEO Should Not Be a Yes Man

By Hemindra Hazari | 28 Jan 2019

EXECUTIVE SUMMARY

Yes Bank has appointed Ravneet Gill as the bank's CEO, effective latest from March 1, 2019, for a 3-year term. The announcement led to a spurt in the bank's share price, as the leadership issue was finally resolved. While investors rejoiced, it remains to be seen whether the new CEO will be influenced by Rana Kapoor, who will step down as founder-CEO on January 31, 2019. Normally, in India, founders are reluctant to cede managerial control, and in banks, their influence often disrupts operational management even when the regulator has compelled founders to step down from the board. It is therefore imperative that once Rana Kapoor steps down as CEO his role should only be restricted to a founder shareholder without any operational involvement even as an advisor. Gill's actions as Yes Bank CEO will need to be closely monitored as some board appointees have already been made prior to his taking charge. In particular, we need to closely watch how he manages the close associates of Rana Kapoor, one of whom has been elevated to the board, subject to the regulator's approval. If Gill starts inducting experienced bankers from outside in senior positions in Yes Bank, it will demonstrate to the public that he is not under the yoke of the founder, but if he continues with the existing team of senior executive management or permits an advisory role for the departed founder-CEO it will indicate the continued strong influence of Rana Kapoor on the bank he co-founded.

DETAIL

On January 24, 2019, during market hours, Yes Bank announced that the RBI had approved the appointment of Ravneet Gill as CEO of Yes Bank. By January 25, the share was up 12% from the close of January 23, as investors rejoiced, although his name was reported in the media for some days prior to the announcement as the probable successor. On January 25, Yes Bank announced the appointment of Maheshwar Sahu (former bureaucrat), Anil Jaggia (formerly from HDFC Bank) as independent directors and Ashish Agarwal, chief risk officer (CRO) as an executive director (subject to RBI approval). One wonders the urgency in appointing directors just prior to the new CEO taking charge and whether these appointees have also been approved by Ravneet Gill.

To date, the conduct of the independent directors and the nomination and remuneration committee (NRC) has been disappointing, and it remains to be seen how the new independent directors contribute to improving corporate governance at the bank. On September 25, 2018, the bank had announced the appointment of Rajat Monga and Pralay Mondal as executive directors, subject to RBI approval, to ensure long term succession planning. But Mondal resigned from Yes Bank and is reported to be joining Axis Bank, while the RBI has not yet approved Monga as an executive director, probably on account of his being the chief financial officer when the regulator detected that the bank had fudged its accounts for two consecutive years. Hence the NRC has selected Ashish Agarwal, the CRO, as an executive director. All the senior executive management in Yes Bank owe their positions to Rana Kapoor, and hence it appears that the board will be favourably inclined towards Rana Kapoor even after he steps down as CEO.

It is therefore imperative for Gill to select experienced senior bank executives from outside Yes Bank and induct them into critical posts in Yes Bank, as well as on the board, to restore confidence with the regulator as well as with investors. Gill should also ensure that Rana Kapoor has no operational role to play as an advisor once he steps down as the CEO. It is equally important for Yes Bank's NRC to be completely overhauled to improve board oversight, compliance and performance, which were sadly missing all these years. If Gill continues to depend on the existing senior management at Yes Bank and allows an advisory role for Rana Kapoor it is clear that not much has changed and the status quo remains undisturbed.

It is interesting to note that the new CEO at Axis Bank has been inducting experienced bankers from outside, and that the coterie of the earlier CEO has either left or will be marginalised if they stay. When banks have had long periods of mis-governance, leadership has to be sought from outside the bank as the internal selection of leadership has clearly failed. Moreover, a new CEO will want a new cadre of leaders who will owe their loyalty to him and whom he can trust, and will not want to depend on executives who owe their loyalty to the previous leader. Similarly, Gill has to induct from outside experienced bankers in credit appraisal and monitoring, risk management, compliance and financial accounting, all critical areas where Yes Bank has been found wanting.

Yes Bank's share price bounced up smartly with the announcement of Gill's appointment as CEO. If the share price has to show a sustainable upward momentum, Gill has to demonstrate that he is not a CEO on a string.

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— Hemindra Hazari (28 Jan 2019)

Hemindra Hazari

Specialist in Indian banking and economic research

Yes Bank | ESG

Yes Bank: In the Cross Hairs of the Regulator

By Hemindra Hazari | 17 Feb 2019

EXECUTIVE SUMMARY

Yes Bank is in the cross hairs of the Reserve Bank of India (RBI), the banking regulator. On February 13, 2019, the bank issued a press release stating that the regulator's risk assessment report (RAR) for the year ended March 31, 2018 revealed nil divergence, i.e. the bank's net profits and asset quality were in conformity with the regulatory norms, unlike in FY2016 and FY2017. However, on February 15, 2019, the bank released a note stating that the RBI had pulled up the bank, as publicly disclosing a part of the RAR breaches regulatory confidentiality and is in violation of regulatory guidelines. **While the RAR is indeed confidential, the RBI did not publicly admonish other banks like HDFC Bank, Axis Bank and Kotak Mahindra Bank (KMB) when they had publicly revealed nil divergence from their RARs.** It is apparent that Yes Bank is the bad boy in the eyes of the regulator, and the bank will have to renew its efforts to change that perception. Shareholders have to therefore exercise caution and take the surge in the share price with a pinch of salt.

DETAIL

On February 13, 2019, Yes Bank issued a notice to the exchanges stating,

> *YES Bank has received the Risk Assessment Report for FY2018. The report observes NIL divergences in the Bank's asset classification and provisioning from the RBI norms.*

In certain sections of the market there was a perception that Rana Kapoor, the earlier CEO, was not given another term by the RBI as the RBI had detected divergence in FY2018 as well, and hence these sections believed that the bank would report divergence in FY2018 as well. Indeed, this writer had pointed out that in FY2018, two corporate accounts, Reliance Naval and Matix Fertilisers, were classified at Yes Bank as standard when most banks who had exposure to these companies had classified the accounts as non-performing, thereby raising the probability of the bank reporting divergence in FY2018.

The market was euphoric over the news of nil divergence in FY2018, and the stock closed 31% up, at Rs 221 on February 14. To the market it appeared that the bank's issues with the regulator had been finally resolved, while some sections questioned why then had the regulator refused permission for Rana Kapoor's new term as CEO. This writer has always argued that two successive years of divergence should immediately disqualify the CEO, the Chief Financial Officer (CFO), the head of the audit committee of the board and the auditor of the concerned bank.

However, it appears the regulator took offence at Yes Bank's decision to specially release a press note stating nil divergence, and on February 15, 2019, the bank in a filing to the exchanges stated,

1. As the RAR report was marked "confidential", it was expected that no part of the report and information contained therein be divulged except for the information in the form and manner of disclosure prescribed by Regulations. Therefore, the Press Release breaches confidentiality and violates regulatory guidelines. Moreover, NIL divergence is not an achievement to be published and is only compliance with the extant Income Recognition and Asset Classification norms. The RAR also identifies several other lapses and regulatory breaches in various areas of the Bank's functioning and the disclosure of just one part of the RAR is viewed by RBI as a deliberate attempt to mislead the public.
2. The issuance of the Press Release has, therefore, been viewed seriously by the RBI and could entail further regulatory action/s.

Source: Yes Bank

While the RAR report is confidential, Yes Bank is not the only bank which disclosed that it had nil divergence. Kotak Bank in its 2QFY2018 results analysts' conference call held on October 25, 2017 had informed analysts that the RBI had detected nil divergence.

Kotak 2QFY2018 Results Analysts Conference Call

Coming specifically to Kotak, I think the earnings update must be with you. We are beginning to see a pretty reasonable stability on the quality of our credit. And at the outset, let me also share this disclosure with you which is that we have received the RBI inspection report for March 2017. We do not have anything to report on divergence.

Source: Kotak Mahindra Bank p. 3

HDFC Bank in its 3QFY2019 results on January 19, 2019 had disclosed in its mandatory filing with the exchanges that it had nil divergence.

8 There was no divergence observed by RBI for the financial year ended March 31, 2018 in respect of the Bank's asset classification and provisioning under the extant prudential norms on income recognition, asset classification and provisioning pertaining to advances.
9 Figures of the previous periods have been regrouped / reclassified wherever necessary to conform to current period's classification.
10 ₹ 10 lac = ₹ 1 million
₹ 10 million = ₹ 1 crore

Place : Mumbai
Date : January 19, 2019

Aditya Puri
Managing Director

Activa
Go to Se

Source: HDFC Bank

Similarly Axis Bank in its 3QFY2019 results on January 29, 2019 disclosed some contents of its interim (not even final) RAR report to the public.

Axis Bank 3QFY2019 Results

The Bank has received an indicative list from RBI relating to asset quality divergence for the fiscal year ending 31st March 2018. The Bank has been asked to classify 2 accounts as NPA, with an outstanding amount of ₹225 crores, which constituted less than 0.7% of last year's slippages of the Bank. Both of these accounts have already been downgraded in H1 FY19. In addition, the Bank has been asked to make

Page 3 of 7

AXIS BANK

additional provisions of ₹100 crores on 2 accounts already NPA as of March 2018. This provision has been incorporated in Q3 financials.

Source: Axis Bank

The issue naturally arises that when at least 3 other banks had selectively disclosed contents of the RBI's confidential RAR prior to Yes Bank's disclosure, why is it that the regulator has taken offence at Yes Bank's disclosure, and may even penalise the bank for the same, while ignoring the disclosures by the other banks?

A possible explanation is that Yes Bank, unlike the other banks, specifically issued a press release regarding nil divergence, and it was given wide publicity, while in the other banks it was part of their results, and it is possible that the RBI remained ignorant of the other banks' disclosure. Another explanation could be that that the regulator believed that the bank had released the nil divergence but ignored to mention the other breaches and regulatory lapses as a deliberate ploy to mislead the public and boost the share price. **But nevertheless, the RBI should be uniform regarding any violation of its norms, and hence should also pull up KMB, HDFC Bank and Axis Bank and any other banks which have publicly disclosed the contents of the confidential RAR.**

Even though RBI's RAR found nil divergence, the regulator's response to Yes Bank issuing a press release indicates its apprehension regarding Yes Bank even after the founder-CEO was compelled by the RBI to step down. Shareholders in banks should be cautious when banks run foul of the regulator, as the regulator's influence is all encompassing.

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— Hemindra Hazari (17 Feb 2019)

Hemindra Hazari

Specialist in Indian banking and economic research

Yes Bank | ESG

Yes Bank Fiasco Brutally Exposes Sell-Side Business Model

By Hemindra Hazari | 01 May 2019

EXECUTIVE SUMMARY

After the announcement of Yes Bank's fourth quarter results, the stock fell an astounding 29% in a single day, vaporising US$ 2.3 bn of market capitalisation. The bulk of sell-side research, those sentinels protecting shareholder wealth, supposed watchers on the wall, were bullish on the bank prior to the results. Once the bank itself released its results, these same pundits did a volte-face and turned their bubbling optimism into bleak pessimism. In their earlier published research, the sell-side, with a few exceptions, had deliberately chosen to ignore the many early warning signals. Instead they parroted the bank's management commentary that all was well. It was only when the new CEO publicly and candidly revealed the obvious, that the bullish sell-side scurried to downgrade the bank.

The Yes Bank event, resulting in a huge loss to shareholders, has not only exposed the rot in the bank's innards, but also exposed the sell-side research's business model, which, for its viability, depends on corporate access and, inevitably, uncritical analysis of companies under coverage. Alas, despite the Yes Bank debacle, analysts are unlikely to discard the rose tinted lens through which they fondly peer at companies. There is a lack of accountability when bullish calls go horribly wrong. In an environment which encourages reverence towards prominent companies under coverage and a culture of corporate public relations instead of critical research, investors are abandoned to their own devices.

DETAIL

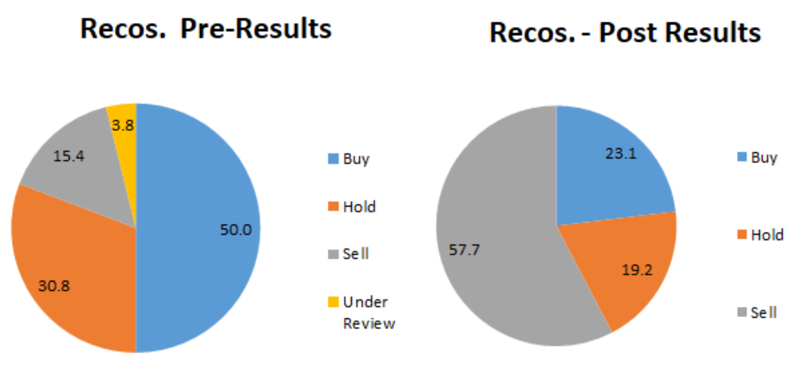
On April 26, 2019, Yes Bank declared its 4QFY2019 results. Contrary to the consensus expectation of a decline of around 27% in net profits to Rs 8.6 bn, the bank reported a loss of Rs 15 bn, which included a contingency provision of Rs 21 bn for stressed standard loans of Rs 100 bn, and a reversal of corporate fees of Rs 2.8 bn. The bank also guided for a ROA of 1% by FY2021. The huge loss and weak earning visibility resulted in significant downgrades by sell-side analysts.

As per a media report citing Bloomberg, out of the total 50 analysts covering Yes Bank, 20 have a ‘buy’ rating, 12 ‘hold’ and 18 ‘sell’. A year ago, in March 2018, the consensus was overwhelming bullish, with 44 analysts having a ‘buy’ rating, 7 ‘hold’ and 4 ‘sell’.

This writer analysed a smaller sample of 26 prominent sell-side analysts on Yes Bank who cater primarily to institutional investors, and documented the change in their pre- and post- result recommendations (see Annexure 1).

Pre-results, 50% of the analysts were bullish, while only 15% were bearish; but after the results, only 23% of analysts remained bullish, while 58% had become bearish. Interestingly, pre-results, many of the foreign brokerage houses and prominent domestic brokers having significant institutional business (e.g. Kotak, IDFC) were either bearish or had a neutral (sometimes a euphemism for sell) call. However, while consensus was expecting a decline in profits, the size of the loss and the poor future earnings visibility came as a shock to the sell-side.

Prominent 26 Sell-side Recommendations on Yes Bank - Pre & Post 4QFY2019 Results



Source: Media & sell-side reports

The most famous of the about turns was Macquarie’s double downgrade from ‘Outperform’ to ‘Underperform’ and a reduction in the price target by nearly 40%, to Rs 165. Their report candidly summed up the sell-side’s bullish stance prior to the results when it stated,

> *Over the past eight years we have been constructive on YES Bank’s ability to not just survive, but to thrive in a risky business segment like structured finance. Despite our anxious scepticism at times, YES has built a track record of handling multiple challenging accounts well. RBI’s clean chit in FY18 divergence audit seemed to ratify our understanding of the business model.*

The issue was that there were plentiful warning bells that Yes Bank's loans were much weaker than reported, and the entry of a new CEO to clean up the bank's accounts and its governance issues should have immediately turned the consensus sell-side view to be majorly negative, but they patiently waited for the results to be announced.

For many years, within financial circles, the credibility of Yes Bank's accounts and the actual quality of its loans was a topic of discussion, but nothing was visible in its reported accounts. That was till UBS published its critically acclaimed incisive report titled, "Deep dive into lending practices – differentials not priced in" dated 7 July 2015, where it boldly stated ,

> *We believe YES is most vulnerable to a prolonged weak credit cycle and consensus may not be ready for a sharp increase in the company's credit costs. We downgrade YES to a Sell…*

Nearly two years later, on May 15, 2017, this writer published the first of many notes cautioning investors on the credibility of not only Yes Bank's accounts but its entire senior management. Yes Bank's dismal saga continued with it reporting 2 consecutive years (FY2016 and FY2017) of fudged accounts and the regulator fining it for the same. In FY2018, this writer even highlighted a specific large account of Reliance Naval Engineering which the banking industry had classified as non-performing but which the bank continued to classify as performing. The media also raised alarming issues pertaining to corporate governance and the dealings of Yes Bank with the family offices of the daughters of Rana Kapoor which the bank denied. Not only did the sell-side not give these issues the importance it deserved, but it also ignored the divergent trajectories in asset quality between Yes Bank and Axis Bank, which had a similar corporate exposure.

Yes Bank's Asset Quality & Credit Cost

%	FY2015	FY2016	FY2017	FY2018	9MFY2019
Gross NPA	0.4	0.8	1.5	1.3	2.1
PCR	72.0	62.0	46.9	50.0	44.2
Credit Cost	**0.50**	**0.50**	**0.53**	**0.76**	0.64

Source: Yes Bank

Axis Bank's Asset Quality & Credit Cost

%	**FY2015**	**FY2016**	**FY2017**	**FY2018**	**9MFY2019**
Gross NPA	1.3	**1.7**	**5.0**	**6.8**	5.8
PCR	78.0	72.0	65.0	65.0	75.0
Credit Cost	**0.61**	**1.11**	**2.82**	**3.57**	2.17

Source: Axis Bank

The performance clearly showed that while in Axis Bank, corporate loans contributed to asset quality and credit costs significantly deteriorating from FY2017, in Yes Bank, which also had large corporate exposures, there was no major deterioration even till December-end 2018. Given such a history, it should have been obvious to the sell-side that once a new CEO from outside took charge at Yes Bank, a major overhaul of the bank and its accounts was inevitable. Yet the majority of sell-side analysts continued to remain bullish, and even the more experienced analysts with the prominent brokers preferred to keep a neutral stance till the bank reported its results, instead of loudly sounding the alarm with aggressive price targets to exit the stock.

In justifying drastically reducing their earnings forecasts and price targets post the results, the sell-side are not only merely reacting after the event, but are regurgitating management commentary of the weak earnings forecast. Essentially, the majority in the sell-side have been reduced to being reporters, who are completely dependent on being spoon-fed management guidance to form a view. Unlike the reporters, they rarely break news, and are grossly overpaid.

The pitifully situation in sell-side research is on account of their inability to publicly question or even condemn the management of the companies they cover and expose accounting fraud, mismanagement and mis-governance. The business model of the sell-side is critically dependent on access to regular information from corporate managements, and, more importantly, arranging meeting for their institutional clients with the management, and inviting managements for the conferences they regularly host for their clients. In such an environment it is best to remain bullish or maintain a neutral call on prominent companies where impending problems are likely to surface, and then feign surprise when it happens. There is no accountability or penalty for bullish calls going horribly wrong, and no incentive to publicly forewarn clients. Whereas the downside is that the tap of corporate access may be closed. That investors may face huge losses on account of their silence is par for the course.

Annexure – 1. Prominent Sell-side Research Recommendations on Yes Bank

		Pre 4QFY19 Results		Post 4QFY19 Results		PT Change
		Recommendation	PT (Rs)	Recommendation	PT (Rs)	%
1	Axis Capital	Buy	240	Sell	205	-14.6
2	B&K	Under Review	-	Sell	160	-
3	BOB Capital	Buy	275	Sell	210	-23.6
4	**Edelweiss**	**Buy**	**279**	**Hold**	**250**	**-10.4**
5	Ellara	Buy	362	Sell	192	-47.0
6	ICICI Securities	Buy	324	Sell	197	-39.2
7	**Macquaire**	**Outperform**	**270**	**Underperform**	**165**	**-38.9**
8	PL	Accumulate	245	Reduce	190	-22.4
	Average		**285**		**201**	**-29.4**
9	**Citi**	**Neutral**	**240**	**Sell**	**180**	**-25.0**
10	Emkay	Hold	260	Sell	155	-40.4
11	**HSBC**	**Hold**	**243**	**Reduce**	**164**	**-32.5**
12	**Jefferies**	**Hold**	**265**	**Underperform**	**155**	**-41.5**
	Average		**252**		**164**	**-35.1**
13	**Credit Suisse**	**Neutral**	**205**	**Neutral**	**205**	**0.0**
14	**Goldman Sachs**	**Neutral**	**248**	**Neutral**	**225**	**-9.3**
15	**JP Morgan**	**Neutral**	**225**	**Neutral**	**215**	**-4.4**
16	**Nomura**	**Neutral**	**245**	**Neutral**	**230**	**-6.1**
	Average		231		219	-5.2
17	**Kotak Institutional**	**Sell**	**210**	**Sell**	**170**	**-19.0**
18	**Morgan Stanley**	**Underweight**	**160**	**Underweight**	**125**	**-21.9**
19	**UBS**	**Sell**	**170**	**Sell**	**170**	**0.0**
20	**IDFC**	**Underperform**	**170**	**Underperform**	**155**	**-8.8**
	Average		178		155	-12.7
21	**Deutsche**	**Buy**	**330**	**Buy**	**245**	**-25.8**
22	Equirus	Buy	340	Add	260	-23.5
23	Investec	Buy	320	Buy	240	-25.0
24	JM Financial	Buy	275	Buy	265	-3.6
25	**Motilal Oswal**	**Buy**	**270**	**Buy**	**280**	**3.7**
26	**IIFL**	**Buy**	**237**	**Add**	**220**	**-7.2**
	Average		295		252	-14.8
	AVERAGE OF TOTAL		**248**		**198**	**-20.2**

Source: Media & sell-side reports

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— Hemindra Hazari (01 May 2019)

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Yes Bank | Equity Bottom-Up

Yes Bank's Hike in Deferred Tax Assets: Short-Sighted Policy

By Hemindra Hazari | 21 May 2019

EXECUTIVE SUMMARY

Yes Bank's loss in 4QFY19 would have been much higher, by Rs 16.6 bn, and its annual profit significantly lower, had it not been for the increase in the net deferred tax asset (DTA) of the same amount. The huge increase in the DTA partly offset the large provision the bank made for standard and non-performing assets. Although such accounting is permissible under regulatory norms, it inflates current profits, and depresses future profits. In the opinion of this writer, it is not a prudent practice. The management probably were of the view that reporting a larger loss than what they reported in the 4QFY19 would unnerve shareholders and depositors; as it is the stock market immediately reacted to the results with a 29% fall in the share price. The bank, though, has merely deferred the negative impact, and shareholders should be enlightened about the accounting treatment. The saving grace is that the new CEO is cleaning up the bank and its bad assets will become more transparent than in the past.

DETAIL

Yes Bank shocked the stock market in its 4QFY2019 results on April 26, 2019, when it reported a loss Rs 15.1 bn. Consensus estimates had been that the bank would report a profit, albeit lower. The actually reported loss resulted in the share price falling an alarming 29% on the trading day following the results. A major contributing factor for the unexpected loss was the Rs 21 bn in provisions for stressed standard loans which the bank expects to become non-performing and the Rs 12.7 bn in bad debt provisions.

However, a closer examination of the accounts reveals that, to partly offset the large increase in provisions, the bank increased its net DTA by Rs 16.6 bn, thereby deferring the tax provision to a future year and inflating the profits in FY2019 by a corresponding amount.

18.7 Income Taxes

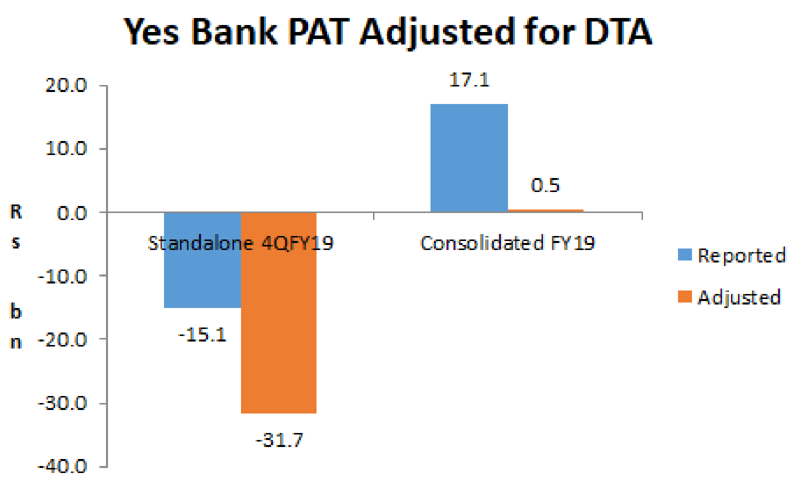
Provisions made for Income Tax during the year

(₹ in million)

Particulars	For the year ended March 31, 2019	For the year ended March 31, 2018
Current income tax expense	23,009.69	22,439.16
Deferred income tax credit	(16,612.30)	(2,726.00)
TOTAL	**6,397.39**	**19,713.16**

Source: Yes BankFY2019 Annual Report p. 290

As a result of huge surge in the DTA, the standalone loss in 4QFY19 would have been higher at Rs 31.7 bn, as compared with the loss of Rs 15.1 bn reported by the bank, and the consolidated profit for FY2019 would have been a mere Rs 0.5 bn, as compared with the Rs 17.1 bn reported.



Source: Yes Bank, HKH Research

In Yes Bank's case the significant increase in the DTA in FY2019 was on account of the sharp rise in bad debt and standard loan provisions.

The components that give rise to the deferred tax asset included in the balance sheet are as follows:

(₹ in million)

Particulars	As at March 31, 2019	As at March 31, 2018
Deferred tax asset		
Depreciation	597.38	418.59
Provision for gratuity and unutilized leave	395.53	213.48
Provision for Non-performing Assets	9,779.42	2,930.53
Amortization of premium on HTM securities	1,035.72	1,025.76
Provision for standard advances	11,119.17	3,220.59
Other Provisions	2,447.48	953.47
Deferred tax asset	**25,374.70**	**8,762.42**

Source: Yes BankFY2019 Annual Report p. 299

Deferred tax assets and deferred tax liabilities are created on account of the difference between accounting income (reported in the books of accounts disclosed to shareholders) and taxable income in the same period as the revenue and expenses to which they relate. As per the Indian Accounting Standard (IAS)-22,

> *6. The differences between taxable income and accounting income can be classified into permanent differences and timing differences…*
>
> *7. Timing differences are those differences between taxable income and accounting income for a period that originate in one period and are capable of reversal in one or more subsequent periods. Timing differences arise because the period in which some items of revenue and expenses are included in taxable income do not coincide with the period in which such items of revenue and expenses are included or considered in arriving at accounting income…*
>
> *12. Permanent differences do not result in deferred tax assets or deferred tax liabilities.*

In banks, the main difference between book income and taxable income arises on account of loan loss provisions and depreciation on investments. While loan write-offs lower taxable income, loan loss provisions, with few exceptions, are not tax deductible, and hence when there are large loan loss provisions, taxable income may not get reduced to the same extent as book income.

The creation of a net DTA in a bank, though classified as an asset, does not provide the bank with either liquidity or with income generating capacity, and therefore is an intangible asset. The Reserve Bank of India (RBI), the banking regulator, in a March 29, 2003 notification had stated,

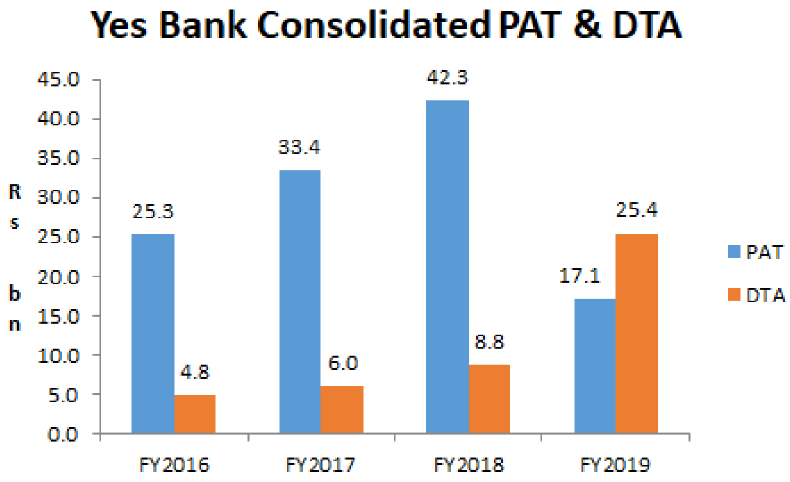
> *Creation of DTA results in an increase in Tier I capital of a bank without any tangible asset being added to the banks' balance sheet. Therefore, in terms of the extant instructions on capital adequacy, DTA, which is an intangible asset, should be deducted from Tier I Capital.*

However, with the deteriorating asset quality in the banking industry straining capital adequacy, the RBI relaxed the treatment of net DTA in a notification on March 1, 2016 and stated,

> *2.3(i) Deferred tax assets (DTAs) associated with accumulated losses and other such assets should be deducted in full from CET1 capital.*
>
> *(ii) DTAs which relate to timing differences (other than those related to accumulated losses) may, instead of full deduction from CET1 capital, be recognised in the CET1 capital up to 10% of a bank's CET1 capital, at the discretion of banks [after the application of all regulatory adjustments mentioned from paragraphs 4.4.1 to 4.4.9(C)(ii) of the Master Circular].*

Despite the regulatory forbearance, as a matter of prudence, analysts should deduct net DTA from CET 1 capital and from book value.

As on March 31, 2019, Yes Bank has a net DTA of Rs 25.4 bn which will have to be written off from future profits, thereby depressing future ROE. Sell-side analysts have tended to ignore the importance of DTA in inflating current profits, while depressing future profits and profitability, and the market should factor the impact of DTA in the bank's future.



Source: Yes Bank

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— Hemindra Hazari (20 May 2019)

Hemindra Hazari

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Yes Bank | Forensic Accounting

Legacy of the Past? Yes Bank's Divergence Should Alarm the Market

By Hemindra Hazari | 20 Nov 2019

EXECUTIVE SUMMARY

In a significant set-back, Yes Bank (YES IN) reported that its accounts for FY2019 were fudged: the banking regulator had detected under-reporting of non-performing loans and credit costs and over-stating of profits by the bank. **This development is disturbing, as it undermines the credibility of Ravneet Gill, the new CEO (took charge on March 1, 2019), the audit committee (chaired by independent director, Uttam Prakash Agarwal), Venkataramanan Vishwanath, partner, B S R & Co. (member firm of KPMG) and the office of the Chief Financial Officer (the then CFO, Raj Ahuja was replaced in August 2019).** The timing of this development is particularly unfortunate, as the bank desperately seeks additional equity capital and has to date not finalised the issue. This news will cast a negative light on the credibility of its accounts.

The only charitable explanation is that, since Gill took charge on March 1, and the accounts were finalised on April 26, he may have had inadequate time and exposure to closely monitor some of the corporate accounts which the bank had imprudently classified as performing. **Nevertheless, given the bank's legacy of dodgy accounts (in FY2016 and FY2017) and various publicly documented corporate governance lapses by Rana Kapoor, the erstwhile founder-CEO, Gill should have exercised extra caution and been more prudent in maintaining the integrity of the bank's accounts. It is shameful for any bank and its CEO to be publicly hauled up by the banking regulator for fraudulent accounts, and wilful mis-reporting by a bank is a criminal offence as per the law of the land.** Stakeholders can only hope that, as Gill settles down, he will restore the sanctity of the bank's accounts and that FY2019 was the departing legacy of the past.

DETAIL

In a nasty surprise, Yes Bank informed the stock exchanges on the evening of November 19, 2019 that the banking regulator had found that the bank's FY2019 accounts were untrustworthy, that its gross NPAs were 42% higher than reported, and its net profits were 37% lower. The news was unexpected, as the regulator had cleared the bank's FY2018 accounts after having detected 2 consecutive years of fudged accounts in FY2016 and FY2017. With the entry of a new CEO, Yes Bank reported a significant increase in credit costs and a loss in 4QFY2019, which the market interpreted as a cleaning up of the accounts.

Yes Bank's History of Dodgy Accounts

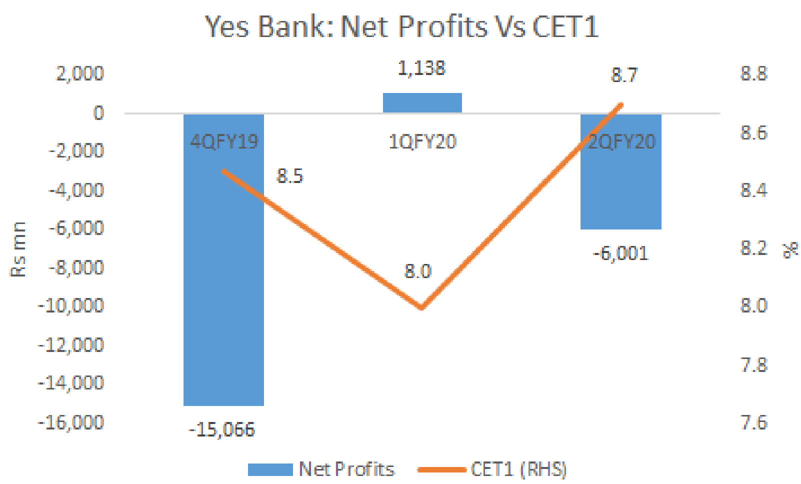
Rsmn	FY2016	FY2017	FY2019
Gross NPAs Reported	7,490	20,186	78,826
Gross NPAs as assessed by RBI	49,257	83,738	1,11,596
Divergence in Gross NPA	**41,767**	**63,552**	**32,770**
Net NPAs Reported	2,845	10,723	44,848
Net NPAs as assessed by RBI	36,032	58,916	67,838
Divergence in Net NPAs	**33,187**	**48,193**	**22,990**
Provisions for NPAs	4,645	9,463	33,977
Provisions for NPAs as assessed by RBI	13,225	24,821	43,757
Divergence in Provisions	**8,580**	**15,358**	**9,780**
Reported Net Profits	25,395	33,301	17,203
Net Profits as assessed by RBI	19,784	23,161	10,840
Divergence in Net Profits	**-5,611**	**-10,140**	**-6,363**
Divergence (%)			
Gross NPA	**557.6**	**314.8**	**41.6**
Net NPA	**1,166.6**	**449.4**	**51.3**
Provisions	184.7	162.3	28.8
Net Profits	**-22.1**	**-30.4**	**-37.0**

Source: Yes Bank

Yes Bank clarified that, of the total Rs 32.8 bn additional gross NPAs detected by the RBI in FY2019, the bank had classified Rs 12.6 bn as NPA by 2QFY2020, and hence was to classify the residual Rs 20.2 bn in 3QY2020. This pertained to 4 accounts, of which Rs 10.4 bn (across 3 accounts) was internally rated as 'BB&Below' as on September 30, 2019. **There is, however, no explanation of the single account of Rs 9.8 bn internally rated as 'BB+&Above' as on 2QFY2020, which was classified as an NPA by the regulator 6 months earlier. It defies explanation how the bank's internal rating can classify an account as 'BB&Above' when the RBI determines the same account to be NPA much earlier. Hence it casts credibility issues on its internal rating which in this case appears to be in sharp variance to the regulator's norms on asset classification.**

That the RBI has determined that Yes Bank's FY2019 accounts are untrustworthy undermines the credibility of Ravneet Gill, the CEO; the audit committee chaired by independent director, Uttam Prakash Agarwal); Venkataramanan Vishwanath, partner, B S R & Co. (member firm of KPMG); and the office of the Chief Financial Officer (the then CFO, Raj Ahuja was replaced in August 2019 by Anurag Adlakha). **The integrity of the accounts is the responsibility of all these individuals, and the board of Yes Bank has to demand accountability and implement systems to prevent the recurrence of such divergence.** It is particularly unfortunate that this development has taken place at a time when the bank is strapped for equity capital, and is desperately seeking capital from institutional investors, which till date has not materialised. In such a perilous time, it is vitally important that a bank's accounts be trustworthy, for investors to estimate its valuation.

The dilemma for Yes Bank is between maintaining the credibility of its accounts and reporting acceptable levels of CET1 to the stock market and it appears that for FY2019, the latter took precedence. The main issue is that in 3QFY2020, in addition to the fresh slippages to loans as a result of a rapidly deteriorating economy, the bank has to provide for Rs 6.32 bn for its 'divergence' for FY2019 which will put further pressure on net profits and CET1.



Source: Yes Bank

The only charitable explanation is that FY2019 is the legacy of the bank's past, when Yes Bank took on high-risk corporate exposure (at a time when most banks were severely reining in their corporate loan growth). Perhaps Gill had inadequate time to fully evaluate the bank's corporate exposure prior to the finalisation of the accounts. **But nevertheless, mis-reporting of information is a very serious offence, and as per Section 46(1) of the Banking Regulation Act, 1949 (BRA), wilful mis-reporting by a bank is a criminal offence.**

Since Gill has taken charge, the market capitalisation of the bank has collapsed, the erstwhile founder CEO has sold off virtually his entire holding, and the bank is struggling to raise capital as the economy spirals downwards and asset quality woes mount. It is therefore vitally important for Yes Bank to restore the sanctity of the accounts to improve the valuation and perception of the bank.

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— Hemindra Hazari (20 Nov 2019)

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Yes Bank | ESG

Will a Desperate RBI Allow Shadowy Investors to Take Over Yes Bank?

By Hemindra Hazari | 02 Dec 2019

EXECUTIVE SUMMARY

On November 29, 2019, Yes Bank (YES IN) finally revealed the names of the prospective investors for its US$ 2 bn equity issue. Unfortunately, 90% of the issue consisted of family offices and the 3 family offices which accounted for 85% of the issue were relatively unknown names. It is apparent that global institutional investors have decided to stay away from the issue, and this is likely to disappoint the market, which was expecting marquee names to enter and turnaround the bank. Not only was there a dearth of public information about the family offices, but, more worryingly, they also had a dubious track record of backing out of deals, and one even went through bankruptcy proceeding in the late 1990s. Hence their source of funding for the Yes Bank transaction is suspect.

It is strange and perhaps an act of desperation that the Yes Bank board approved such names as possible investors, especially when it has R Gandhi, who was appointed by the banking regulator, on the board. Gandhi was the deputy governor, RBI, in-charge of currency management (and an active participant in the demonetisation fiasco). As the joint bid by the family offices of Erwin Singh Braich and SPGP Holdings would eventually hold around 27% of the bank, while the bid by Citax Holdings Ltd & Citax Investment Group would possibly hold an additional 11% of the shareholding, RBI's approval would be required (as for any individual holdings above 5%). The RBI would face a considerable loss of credibility if it were to permit such names to hold in excess of 5% in any Indian private sector bank.

DETAIL

Post market hours on November 29, 2019, Yes Bank issued a statement revealing the names of prospective investors who were bidding for the equity issue aggregating to US$ 2 bn. The Yes Bank stock closed nearly 3% down on November 29, in anticipation that the news may be disappointing. The disclosure of the names finally revealed that marquee global institutional investors, with the possible exception of an undisclosed "top tier US fund house", were uncomfortable in placing a bid for the bank, and 90% of the issue size was by family offices.

Investors for Yes Bank's US$ 2 Bn Equity Issue

Name of the Investor	
Institutional Investors	Amount
Top Tier US Fund House *(Name disclosure early next week)*	$120 Mn
Discovery Capital	$50 Mn
Ward Ferry	$30 Mn
Family Offices	
Aditya Birla Family Office	$25 Mn
Citax Holdings Ltd & Citax Investment Group	$500 Mn
GMR Group and Associates	$50 Mn
Erwin Singh Braich / SPGP Holdings *(Discussions with Investor ongoing and expected to be concluded shortly. In the meantime the Binding Term Sheet extended till December 31, 2019)*	$1200 Mn
Rekha Jhunjhunwala	$25 Mn

2. In light of the above, the Board of Directors has today taken a decision to raise upto USD 2 Billion through preferential allotment at a price in accordance with Chapter V of the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 [Higher of 2 weeks or 26 weeks average price]. None of the Investors will be allotted equity shares such that their holding exceeds 25% of the share capital of the Bank.

Source: Yes Bank

What is disturbing is that three relatively unknown family offices, Erwin Singh Braich, SPGP Holdings and Citax Holding have bid for 85% of the issue. A *Bloombergquint* media story highlighted not just the opacity of these family offices but also that Erwin Singh Braich went through bankruptcy proceedings in the late 1990s and was declared bankrupt. SPGP Holding, after showing initial interest in Reid and Taylor in the bankruptcy proceeding, later backed out, as it did not pay the earnest money. Citax Holding also after initially bidding for Nagarjuna Oil Corporation in the bankruptcy proceedings, later backed out of the bid. There is also limited financial information on these entities in the public domain, and the *Bloombergquint* story states that the latest 30 June filing of Citax Holding balance sheet reveals total fixed assets of 6.6 mn pounds, and total shareholder funds of only 20,107 pounds, indicating the high leverage in the company.

What is even more unusual is that all three family offices have negligible exposure to commercial bank investments. In an interview with CNBCTV18, Somitra Agrawal, MD and CEO, SPGP Holding, Hong Kong acknowledges that the Yes Bank investment would be,

> *globally...our first investment in a bank.*

In the same CNBCTV18 interview, Srinivas Solaraj, executive chairman, Citax Holdings commenting on the Yes Bank investment says,

> *We are currently a small shareholder in a private bank in Switzerland and we plan to expand in the financial services space shortly.*

SPGP Holdings has jointly bid with Erwin Singh Braich US$ 1.2 bn, and Citax Holding has bid US$ 500 mn in Yes Bank. These are substantial investments for these entities. It is strange that these family offices lack exposure and possible expertise in investing in banks, but are willing to invest a large amount of funds for a troubled bank in India which has a significant corporate asset quality problem, which would normally require investors having specialised expertise to turn it around.

Despite the sketchy background of these family offices and the lack of credibility of some of their earlier bids for Indian companies facing bankruptcy proceedings, the board of directors of Yes Bank has endorsed such investors taking a sizeable stake in the bank. What is even more bizarre is that R Gandhi, former deputy governor, RBI and appointed by the regulator on the board of Yes Bank, has also approved these family offices' investment bids (in Indian banks, if the RBI appointed director dissents on any proposal, the board approves the proposal at its peril). It should be noted that R Gandhi as deputy governor was in-charge of currency management during the demonetisation fiasco, during which RBI's credibility reached new lows as it bungled the entire exercise, resulting in huge job and income losses for the low income and the unorganised sectors.

As per regulatory norms, RBI has to approve any investment by an entity exceeding 5% in a private sector bank, and therefore the investment bids by Erwin Singh Braich/SPGP Holdings and Citax Holding will have to be approved by the RBI, as collectively these entities will account for around 38% of the post issue shareholding of the bank. Given the opacity of these entities, their lack of managing commercial banking investments, and their track record of backing out of bids, it will be highly irregular if the banking regulator were to approve these entities owning more than 5% in any private sector bank.

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— Hemindra Hazari (02 Dec 2019)

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