

Impact of Covid-19 on Banking Sector in India

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ARTICLE DETAILS

Article History

Published Online: 15 September 2020

Keywords

Covid-19, ICICI Bank, Indian Economic, Government Banking Sector, NBFCs, ATM

ABSTRACT

The Indian economy wasn't in great shape even before the Covid-19 outbreak, which has only made matters worse. The report by the Reserve Bank of India's (RBI) expert committee on a resolution framework, headed by former ICICI Bank chief K V Kamath, brings this out clearly. The report notes that the pandemic "has affected the best of companies" and businesses that were otherwise viable before the outbreak. Experts believe that banks may be more risk-averse to restructuring loans this time around, having already suffered big losses in previous restructuring efforts. In order to defeat the COVID-19, Pandemic, Indian Government announced complete lockdown in the country starting on March 24, 2020 & the same was extended to 3rd May, 2020 in the second phase. Though the lockdown was necessary & inevitable so as to prevent the faster spread of Novel Corona virus (Covid 19) & to save lives of people of the country. It is going to affect the various sectors of our economy severely. The Banking and Non-Banking finance companies (NBFCs) which are backbone of India's economy are not exception to the above.

This article is an attempt to assess the impact of the pandemic on Banks & NBFCs due to lockdown which has resulted into closure of all commercial organizations, public & private offices, educational institutions, suspension of means of transportations etc.

1. Introduction

COVID-19 is undoubtedly one of the biggest global events of our lifetimes, presenting unprecedented challenges to many industries, governments and people all over the world. The pandemic remains a health and humanitarian crisis, and the business and economic impact has been deep and far reaching. Financial services firms, in particular, have the opportunity to help consumers and businesses weather the economic downturn and navigate the current storm.

A lot has been done already. Banks in India have focused on maintaining critical staff at branches and have temporarily redeployed staff to manage online or phone enquiries from customers. They've also deployed mobile ATMs and implemented doorstep banking for senior citizens and other customers that need additional attention. We expect financial firms to implement video collaboration tools, new chat and messaging software and other fintech innovations to continue live interactions with customers who have been coping with social distancing norms, with some already making use of common consumer apps to that end.

Several banks have made investments in technology and digital transformation over the past couple of years. A lot of them, however, are still heavily reliant on face-to-face interactions, supported by paper processes. So, we expect to see renewed vigor in the Indian financial services industry with banks making a concerted effort to up their digital game. This will be critical as COVID-19 is likely to have a prolonged impact, and banking touches every part of our economy.

That said, most banks have addressed the immediate challenges of COVID-19, related to protecting staff and providing much needed services to customers. They now have the chance to be active participants to help mitigate this crisis,

and there are four key areas they can focus on to help navigate the current situation:

- **Customer Service and Advice:** As a result of social distancing, an increasing number of consumers are using online banking channels to manage their money. This is likely to result in a more permanent shift in customer preferences to digital channels and an increased demand for digital services. It's important for banks to be accessible to all consumers, including the elderly or those not familiar with digital banking, providing education on how to use digital tools, keeping ATMs stocked and operational. As customers seek help and advice on short-term cash management and re-planning their future, banks would need to prioritize live interactions through video collaboration tools. This increase in digital customer engagement must go hand in hand with a ramp-up of cybersecurity and fraud-protection tools to protect customers.
- **Credit Management:** Even with the Indian government's stimulus packages and Reserve Bank of India's (RBI) liquidity measures, banks can expect an increase in loan defaults as borrowers across customer groups struggle to make payments in the face of an economic crisis resulting from lost business and jobs. Besides the moratorium facility announced by the RBI for all term loans, as part of the COVID-19 package, lenders should consider proactively restructuring loans to reduce the cashflow burden in the near term, thus reducing defaults in the immediate future. The industry must work together to make the financial relief process quick and easy to deploy. Banks should proactively initiate credit forbearance

and modification programs using a data-driven approach to understand which customers need help and then rapidly reach out with tailored, relevant solutions. Even with these programs in place, some customers may still not be able to make their next payments. So, banks should prepare for losses and build capacity to deal with an increase in delinquent loans. As consumer demand picks up, albeit gradually, post lockdown, banks will need to repurpose their go-to-market and customer acquisition model, keeping in mind changing consumer behavior post COVID-19, as well as focus on digitally native journeys and re-look at underwriting norms for better risk discovery.

- Revenue Compression:** Revenue from retail and commercial banking is falling sharply, as underlying consumption and transactions have seen an exponential dip. While central banks around the world slash interest rates, banks are reducing yields to generate business, thus significantly reducing net interest margins. Income from payments and other fee-based services are hit by a general decline in economic activity. With measures like moratorium periods provided on loans, banks' cashflow have also taken a hit. We expect an overall drop of up to 10% in banks' payments revenues, which means a USD 150 billion top-line decline for the industry globally, as demand in sectors like retail and entertainment falls sharply or moves to online channels, while activity in areas such as tourism and travel evaporates. There is little that banks can do to stop the overall drop in revenue, but they can focus on making payments safer by increasing limits on contactless payment channels and educating consumers on digital wallets. Banks can also focus on cashback and loyalty rewards to encourage spending in sectors that need it the most.
- Operating Model Adjustments, Cost Elasticity and Innovation:** Over the next few quarters, the banking sector will face a misalignment between short-term costs and revenues due to the economic impact of COVID-19. Banks would need to review and prioritize current projects to ensure allocation of resources to the most pressing needs. Banks should also focus on investing in areas that will outlive the current pandemic, including projects and initiatives that maintain or improve the customer experience such as a paperless utility, end-to-end digital advisory and lending capabilities, increased fraud and cybersecurity analysis and detection, etc. These new digital tools will make banks more efficient and resilient to future changes. Banks that haven't focused on remote working and virtual collaboration in the past should explore establishing elastic operations. This will insure banks against such unprecedented lockdowns and perhaps better manage cost overheads. COVID-19 will have long-lasting impact on many industries including banks. Post crisis, digital maturity and COVID-19 resiliency will determine strategy of banking players with three segments emerging: banks that are already future-ready with truly digital banking

capabilities and cost elasticity, banks that are digital laggards and that need to evolve and renew due to sub-par COVID-19 resiliency, and lastly banks that will struggle to survive as a result of being digital laggards with sub-par financial and operational resiliency. COVID-19 will change our behaviors as customers, citizens and employees in India and around the world. As people become more focused on their well-being, businesses will also need to understand how they can be part of a new health ecosystem that is likely to dominate customer thinking going forward. The idea that "every business is a health business" is already emerging in many corners of financial services, and that is perhaps one of the few positive lasting impacts to result from COVID-19. The Indian Banking Sector finds it difficult to maintain good assets and good earnings due to this pandemic. Due to the shutdowns & income slowdown many repayment of loans may cease leaving the banks dry. Banks in the country are to witness a spike in their non-performing assets ratio by 1.9% & credit cost ratios by 130 basis point in 2020, following the economic slowdown on account of COVID-19 crisis. In the medium term, both the volume and value of transactions is likely to decline with the prospect of a prolonged slowdown in the economy. Growth in the penetration of slowing transaction activity. The pandemic could have an impact on the choice of the mode of delivery of finance, and the nature and structure of financial products. However, COVID-19 or not, financial penetration in India is here to stay.

Is the Indian banking sector recovering from the impact of COVID-19 sooner than initially expected? There are a few recent data points worth looking at.

On Wednesday, the Reserve Bank of India in Indian economy could return to positive growth in Q3, a quarter earlier than initially. To be sure, the RBI said its Economic Activity Index estimates GDP growth at negative 8.6 percent in Q2, suggesting a contraction. This is still lower than the contraction projected in the October policy at negative 9.8 percent. And the RBI study talks about a likely recovery in Q3. Economic recovery is directly linked to asset quality of banks. When cash flows of companies improve, they employ people and resume repayments to banks. Projects that are on hold will be back on track.

Secondly, in a research report, State Bank of India's economists said the fear of huge spike in bad loans for the banking sector could be unfounded. Incoming data suggests that only very few applications have come to banks for loan restructuring so far. Only about Rs 1 lakh crore of corporate loans could go for restructuring compared with Rs 7 lakh crore estimated earlier. The RBI's NPA estimates could be an exaggeration and most of the past estimates have gone wrong, the SBI report said.

"It is now apparent that the big fear of large slippage in asset quality of banks is unfounded with Indian banks guiding at much lower credit cost than even their Asian counterparts! As far as our understanding goes, very few of the borrowers have till date applied for restructuring and incrementally such borrowers are likely to be much lower," the SBI report said.

2. Retail loans pick up

That's not all. On Wednesday, ICICI Bank said it managed to do home loan sales in October and crossed Rs 2 lakh crore mortgage portfolio. In a conference call with reporters, ICICI Bank management said there is a resurgence seen on the demand for home loans. Many banks have reported that there are only 'very few' applications so far restructuring or 'an insignificant number' to report. Most banks have already set aside extra provisions to cover the likely impact and almost all of them have seen regular growth trends in their retail loan portfolios.

According to CARE rating agency, during September 2020, the retail segment registered a growth of 9.2 percent in September 2020 on a Y-o-Y basis and accounted for 28.2 percent share of the total credit during the period as compared to 27.3 percent during the period one year ago.

3. NPAs improve

The GNPA ratio of SCBs improved to 7.7 percent in the quarter ended September 20 against 9.3 percent in the year-ago period and 8.2 percent in the June-end quarter which was largely driven by PSBs, CARE said. On an overall basis, PSBs accounting for about 75 percent share of GNPA of SCBs have experienced a drop in the GNPA ratio to 9.3 percent in the quarter ended September 20 against 11.6 percent in the year-ago period and 9.8 percent in the June 20 quarter.

This is largely because of recoveries, CARE said.

4. Is recovery in sight?

To be sure, these are early projections and could be misleading. An actual picture of the restructuring loan accounts could emerge only by December, banking analysts say. But if the growth momentum continues across sectors, banks could be looking at a lower damage due to the pandemic than initially expected by the analysts. More numbers are awaited but, for now, there are indications that the COVID impact could be less severe than expected.

RBI Governor addressed the media for the second time since the nationwide lockdown was imposed on March 25. Among other important announcements, he announced a reduction in reverse repo rate by 25 basis points from 4 per cent earlier to 3.75 per cent now.

Here's a look at key announcements, RBI Governor Das made in today's media address.

Governor Das started with the macroeconomic situation and mentioned that it has worsened since he last spoke.

However, he did mention some improvement in the situation and talked about IMF's data according to which India is among the very few countries which are likely to tenuously stick to 1.9 per cent GDP growth.

Besides, India is expected to stage a smart recovery to grow at pre-corona virus pace of 7.4 per cent in FY22 according to IMF.

5. Research Problem :

On 31 December, 2019, first of all the news came on Novel corona virus outbreak from Wuhan City of China. This corona virus is a new virus that has not been identified in human so far. Literature indicates that corona virus is a large family of viruses that causes illness. This disease may cause

from the cough, cold and breathing problem, to combat with COVID-19. Indian Government announced complete lockdown in the country. WHO has appreciated the timely action in the form of lockdown by Indian Prime Minister - Narendra Modi and many others as it seems best alternate to stop the spread of the virus in the absence of any cure or vaccine of this disease. However, the Transnational institutions like IMF and World Bank, Central Bank of Various countries, economists and consulting firms have expressed their fear regarding the devastating effect of lockdown on GDP world over in general and emerging economies like India in particular. IMF made a projection of 1.9 % growths in GDP for India in 2020 because the global economy is affected by the COVID pandemic, the worst recession since the Great Depression in the 1930s. However different experts and authorities have given different opinions about the impact of pandemic COVID-19 caused lockdown on current position and future of Indian Financial Sector, primarily on Banks and NBFCs. So, the flooding of information has confused investors, depositors, borrowers and other stakeholders in this sector of high importance.

6. Review of Literature :

The studies relates to find the impact of this pandemic, COVID-19 on Indian Banking Sector during the time of lockdown & for this research work will be reviewed. There are various studies at different point of time as the government extends the time of lockdown due to the situation of COVID-19 is out of control and the vaccine of COVID-19 is still not introduced.

7. Research Methodology :

The present paper is aimed to assess the impact of COVID-19 & lockdown on India's Banking Sector. To achieve this objective some extracts have been drawn from the existing literature available on various sites of internet in the form of interviews of renowned economists, economic and financial advisors, chamber of commerce and industry, authorities of International institutions like World Bank and IMF and so on. Further, research articles and reports of diversified groups like consulting firms, transnational institutions, central banks, regarding the impact of corona on financial sector of India were referred. Presently, there is no factual data regarding impact of COVID-19 on various sectors of economy including banks & only the initiative estimates are available. On account of non-availability of quantitative data, the use of statistical tool was not possible, hence a descriptive article has been prepared with the help of online views of experts regarding impact of ongoing pandemic.

8. Conclusion

The corona virus crisis has left some banks struggling to hang on to deposits, as funds migrate to the perceived safety state-owned lenders. Liquidity conditions of smaller private banks could force them to reduce lending. And in this situation the companies may default on loans. RBI has given all banks a three-month grace period during which they have some relief from rules governing bad loans recognition. But from September onward, non-performing assets are likely to surge if the crisis is still acute. It is well know by the bankers that since the imposition of lockdown by the Government of India on

March 25, 2020, the RBI has taken numerous requisite steps to ensure normal business functioning by the entire banking sector in India. Even after withdrawing lockdown, the banking sector will take a long time to revert to any normalcy. Financial Institutions need to plan for a multiple scenario till operations are normalized keeping both their customers as well as employees needs at the centre of their businesses. It is expected that the government stimulus will plan to address the broader economic challenges. There will be disruptions and delinquencies; however these challenges will open up choices for deepening customer relationships, investments in technology of the future, shift in mind-sets to truly adopt and

execute future of work. Financial institutions need to evaluate, test and implement business continuity and contingency plans along with building business innovations and operational flexibilities. Institutions that take sensitive measures to ensure customer and employee reliefs, will be able to truly differentiate and eventually grow and sustain themselves. In summary, times will be tough but by adopting a vigilant short, medium and long-term action plan, financial services players will emerge from this crisis as stronger, confident and socially responsible institutions. Institutions which use the downturn to sharpen their business models are likely to gain more from the impetus which the government stimulus is likely to provide.

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