Impact of Lockdown on Banks

Part of: GS Prelims and GS-III- Economy -Bank

Banks are concerned about the build up of Non-performing Assets (NPAs) as the disruption caused to business operations and supply chains during the 21-day lockdown period will take time to repair.

- This is despite the fact that the Reserve Bank of India (RBI) has injected fresh liquidity into the banking system and given banks leeway to deal with potential stress in loan accounts.

What is NPA?

NPA refers to a classification for loans or advances that are in default or are in arrears on scheduled payments of principal or interest. In most cases, debt is classified as non-performing, when the loan payments have not been made for a minimum period of 90 days.

- Gross non-performing assets are the sum of all the loans that have been defaulted by the individuals who have acquired loans from the financial institution.
- Net non-performing assets are the amount that is realized after provision amount has been deducted from the gross non-performing assets.

Concerns of Bankers

- Fresh NPAs
  - The 21-day period lockdown would cause pain to lenders, especially in loan accounts from sectors including Micro, Small & Medium Enterprises (MSMEs) airlines, real estate, auto dealers, gems and jewellery, metals among others.
  - Banks are concerned about MSME loans and those extended to manufacturing sectors, such as auto, steel, renewable energy, as those where fresh NPAs are looming.
  - According to the RBI’s financial stability report, the share of large borrowers in scheduled commercial banks' total loan portfolios and their share in GNPAs was at 51.8% and 79.3% respectively, in September 2019.

- Problems Within Different Sectors
  - Even if the lockdown is lifted on April 14, operations of a number of companies in specific sectors will not see business getting back to normal as the labour has moved out and the production may not be able to restart.
  - Apart from these, capital intensive sectors such as aviation, real estate, consumer durables, and jewellery may take a long time before there is a demand revival.
  - Renewable power is struggling because of complete disruption of supply chains from China, as a result of which they are way behind on project schedules and could face payment issues from their customers, the power discoms.

- Fear of Extended Lockdown: Measures by the RBI will provide banks some relief during the next three months, but a buildup of bad loans looks inevitable. While moratorium provides temporary relief to borrowers and helps check the NPAs during that period, an extended lockdown is expected to have a significant adverse effect on the economy.
Analysis By Different Rating Agencies

- **Moody’s Investors Service**: It expects deterioration in banks’ asset quality due to disruption in economic activity. It has changed the outlook for Indian banking system to negative from stable.

- **According to a report released by Crisil**: The asset classes will see continuing pressures on asset quality due to weaker profiles of borrowers and expectation of only a gradual economic recovery. In study of 35 sectors, both from manufacturing and services, there is a sharp variation in resilience in a post-Covid-19 landscape.

  - **High Resilience Category**: Pharmaceuticals, telecom, Fast Moving Consumer Goods (FMCG), fertiliser, oil refineries, power & gas distribution and transmission are among the sectors comprising nearly 44% of the debt.
  - **Moderate Resilience Category**: Another 52% debt is in sectors such as automobile manufacturers, power generators, roads and construction.
  - **Least Resilient Category**: Around 4% of debt in sectors such as airlines, gems and jewellery, auto dealers and real estate, given the discretionary nature of goods and services, and weak balance sheets.