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IMPACT OF COVID-19 ON BANKING SECTOR IN INDIA

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Abstract

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. It could be the most serious challenge to financial institutions especially banking sector in nearly a century. As the economic fallout spreads, banks find themselves juggling some big priorities that require concrete steps to reposition now while also recalibrating for the future. They are working to keep their distribution channels open, despite social distancing advice and supervisory and compliance functions that were never designed for remote work. They are trying to manage revenue and customer expectations, despite near-zero interest rates and growing pressure on consumers. And, they need to keep an eye on strategy and brand issues that will define their future, as market forces and customer behaviors potentially change coming out of this crisis. Now, the banks can take concrete steps to support the communities and customers they serve while balancing medium to long term positioning. Hence, the paper will discuss about the impact of COVID -19 on banking sector and also give some suggested ways to recapture their position after COVID -19.

Keywords: *Covid-19, Consumer, Banks, Banking sector, Customer, Market.*

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. It has also emerged as the “black swan event which is going to require extraordinary measures from governments across the globe to help resume economic stability. Based on when the pandemic is likely to come under control, several economic scenarios indicate global recession of varying magnitudes. The situation has hit the Indian economy at a time when growth has slowed to the lowest in a decade. In the recent past, there were signs of green shoots of recovery in the Indian economy. However, the impending outbreak of the virus is likely to severely impact the recovery process. The government and the regulators have responded by providing an economic stimulus package with several measures to shore up liquidity and provide forbearance on several financial and compliance commitments. The banking sectors have taken responsive measures to the pandemic and aim to reduce in-person interactions, downsize operations while providing financial support to retail and institutional customers.

IMPACT OF COVID – 19

The pandemic is impacting the banking sector in multiple ways from business continuity issues and operational considerations to the overall financial outlook. As Banking companies are mobilizing and taking steps to minimize these impacts, they will likely face short and long-term implications on both profitability's as well as balance sheet items. A continued spread of the pandemic and its results will significantly slow down business, hence financial institutions particularly banks must take additional measures to ensure business continuity to remain relevant to their customers. Banks must also prepare for scenarios that might occur post the lockdown period as well. This would be essential in developing a flexible contingency plan that best equips the banks for crisis management and provides supportive solutions to its customers.

The Reserve Bank of India has taken certain measures to give some relief to the lending institutions in the areas of liquidity, regulation and supervision, and financial markets. The following are some of the business and accounting considerations for banks.

Credit risk assessment

The RBI has given certain waivers to the borrowers which include moratorium to pay principal and interest with relaxation on their classification as a non-performing asset or a restructured asset. This has been implemented to help borrowers tide over temporary financial difficulties. However, banks will have to identify and monitor the borrowers who are facing temporary and long-term financial difficulties. Such borrowers will be provisioned accordingly. Due to the pandemic, it might become too cumbersome or difficult for banks to determine the extent and adequacy of collaterals available with them and the subsequent provisioning. There may be additional disclosures required in the financial statements and the computation of capital adequacy for COVID-19. Banks would therefore be required to maintain robust risk management functions and track their borrowers individually to determine and segregate the permanent impact from the temporary impact and make appropriate provisions. The following are the some of the key areas that merit consideration.

Liquidity

Given the situation of the lock down in the country, the defaults may have increased substantially as many companies would have lost revenue for a long time. An increase in defaults is likely to cause issues in liquidity and capital adequacy. However, the RBI has come up with certain measures to provide liquidity to all the lending institutions.

Going concern and impact of subsequent events

Given the unpredictability of the potential impact of the out break of COVID-19, there may be material uncertainties that cast significant doubt on the entity's ability to operate under the going-concern basis. If the entity prepares the financial statements under the going-concern assumption, it will be required to disclose these material uncertainties in the financial statements to clarify that the assumption is subject to such material uncertainty. The degree of consideration required, the conclusion reached, and the required level of disclosure will depend on the facts and circumstances in each case. This is because not all entities will be affected in the same manner and to the same extent. Significant judgment and continual updates to the assessments till the date of issuance of the financial statements may be required, given the evolving nature of the outbreak and the uncertainties involved. Further the BFSI sector in India will need to ensure that effective processes are in place to identify and disclose material events such as bankruptcies of the borrowers or the impact on lending portfolio due to liquidity or business issues in particular sectors such as real-estate, Small and Micro Enterprises (SME), etc. after the reporting period.

Revisiting hedging strategies

Business transactions may be postponed or cancelled, or they may occur in significantly lower volumes than initially forecasted due to COVID-19 lockdown. If an entity has designated a transaction such as the expected issuance of debt, as a hedged forecasted transaction in a cash flow hedge, the entity will need to consider whether the transaction is still a highly probable forecasted transaction. This includes whether the volume or amounts involved will be lower than how they were forecasted or whether there is uncertainty on the duration about the forecasted transaction. Currently, increased volatility and decline in prices across many asset classes have impacted the trading books of banks and consequently, the capital allocated to address such market and counterparty credit risks. Firms will need to consider how quickly they can adjust their hedging strategies across forex, commodities, equities or fixed income as the COVID-19 situation evolves.

Adverse impact on specific loan covenant ratios being triggered

Given the current crisis and its impact on capital markets and businesses across, banks and NBFCs will face clients who are potentially experiencing stressed financial conditions, including deterioration of their credit ratings and credit quality. In certain cases, there is a like illness of borrowers to breach certain covenants linked to ratios like the current ratio, profitability ratios, return on equity (ROE), debt coverage ratios, etc. In some cases, the covenants breach could lead to classification of a loan as a non-performing asset.

MEASURES TO BE TAKEN FOR RECAPTURE THEIR POSITION

While it may be early to foresee a post COVID-19 Era, especially since we are facing an uncertain future, it is important for Banks to keep tackling the challenges on an ongoing basis to stay relevant and to continue business as usual.

- Shorter Perspective: Returning to Business As Usual
- Safety & Trust: Ensuring the safety of employees and all other stakeholders should be the top priority in addition to returning to BAU and gaining the trust of employees/ customers. Normally, trust cannot be built overnight. However, in a moment of crisis, minds too can change quickly, and hence, now is the right time to build Trust.
- Communication: Develop exclusive Communication Strategy and enhance channels to engage with all the stakeholders and specifically develop ad hoc

channels to manage and overcome temporary disruptions.

- Profitability: Multiple factors will test the Banks profitability in the coming Quarters and will put it under tremendous pressure. All possible efforts (lowering the cost of funds, booking profits from SLR portfolio, cost optimization, digitization, squeezing other income streams) should be taken to offset these challenges and to retain/enhance profitability.
- Stress: Impact of the heightened delinquencies, may surface by Q2 and Q3 of FY 21 and all major industries are likely to face the wrath of COVID 19. The adequate focus must be laid on addressing these challenges. Additionally, collective efforts should be made to seek regulatory approvals for one-time restructuring or relaxation in asset classification.
- Recovery: Focus should be given on revamping digital channels for recovery processes. This may be the right time to think about creating a digitalized Operational Models for collection and recovery.
- Cost: All possible cost-saving measures, be it reducing paper usage, reduction in electricity consumption, avoiding travel or strategic calls such as pay cut, should be adopted.
- Longer Perspective: Seven ways to consider crisis as an opportunity to do things could not do before
- Creating a flatter organization with a matrix structure for agility, swiftness in decision making, and faster response to the crisis.
- Rationalize costs on an ongoing basis: Centralization, reducing brick and mortar setup and its related overhead costs, going digital, Employee Cost, etc.
- Promoting virtual work, extensive use of collaboration tools, and changing the way work.
- Transforming: Work (humans with machines), People (getting right Talent and reskilling/upskilling existing Talent) and Workplace (Optimal blend of the physical and virtual workspace)
- Reinforcing hygiene, wellness, and healthcare.
- Permanent Crisis Management Team to be developed and their scope to be made broader.
- Developing a strong policy for ESG and become a Socially Responsible organization.

CONCLUSION

Banks must sustain the momentum gathered in breaking stereotypes (even though out of fear and desperation) and keep improvising. In short, by the time, COVID-19 situation is past, the crisis should be used as an opportunity to do things that could not do before and create a gamut of new normal that will shape the future of Banking.

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