Impact of COVID-19 on the Banking Sector

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Abstract

The corona virus (COVID-19) outbreak has snowballed into a global crisis causing immense personal and financial suffering for consumers, communities, and businesses. Banks have been hit since the unsettlingly rapid global spread of Covid-19. The banking industry is facing many challenges; they are expected to help customers during this time. The banking sector may have their well-defined plans, but it still may be difficult to handle a crisis of this scale. This paper highlights the extensive impact of COVID-19 on the Banking sector and some measures taken by the Reserve Bank of India to overcome the challenges. A consideration of possible impacts of COVID-19, either directly or indirectly, is outlined by drawing on a variety ofliteratures.

Keywords: ***Banking, Covid-19, Challenge, Pandemic.***

Introduction

On March 11, 2020, WHO officially declared COVID 19 outbreak as pandemic due to its global spread and seriousness of the disease. The name "corona virus" is derived from Latin corona, meaning "crown" itself a borrowing from Greek korṓnē. The name was first used in 1968 by an informal group of virologists. COVID 19 was first reported in Wuhan, China on 31st December 2019 and quickly started spreading all over the globe. Economist Robert J. Shiller has said that, COVID-19 is not the only one pandemic but it has one more with it. No doubt the first one is the health pandemic but the second one is namely the anxiety over the economic effect because of the pandemic. Almost every sector has been hit due to the outbreak. Effect of this outbreak has a negative impact on social life, commercial activities, service industries, manufacturing industry and various other ancillary industries. This pandemic can even lead to businesses closing down, due to which the unemployment rate will increase; many people will be losing on income sources and people might take any steps due to desperation of earning some income, in all of this the people might not take enough precautions against the spread of the disease. As the economic fallout spreads retail banks are struggling with their priorities of meeting customer's expectations, brand image, profits etc. RBI has introduced various economic and fiscal measures to overcome the COVID-19 crisis.

Objectives

- To understand the impact of COVID -19 on the Banking Sector.
- To identify the current challenges and barriers faced by the Banking Sector due to COVID-19.
- To identify different strategies framed by the Reserve Bank of India to deal with the pandemic.

Research Methodology

The study is descriptive in nature. The study focuses on the impact of COVID-19 on the banking sector. Secondary data has being used in this study. Secondary data includes various research papers, journals, newspapers, web contents etc.

Review of Literature

Author/year	Focus Area	Review
Kaushik Das (2020)	COVID-19 on Solar Energy Generation Sector	The sector is highly dependent on Chinese supplies, Economic activities will suffer huge losses and this pandemic shall have Multi-dimensional, multi sectorial, multi-regional effect.
CA Narendra Kumar Bansald et al. (2020)	COVID-19 on Indian Economy: GST	Government's funds in form of GST were leviable only on supply of goods or services. Now in nation wide lockdown, supply of goods and services are adversely affected, which in turn will affect GST collection.
Nuno Fernandes (2020)	Economic effects of COVID- 19 on the world economy	Countries highly dependent on foreign trade are more negatively affected. The results suggest that on average, each additional month of crisis costs 2.5-3% of global GDP.
Asger Lau Andersen Et. al. (2020)	Consumer Responses to the COVID-19 Crisis in Denmark	Aggregate spending was on average 27% below the counterfactual level without the pandemic in the seven weeks following the shutdown.

Effects of COVID -19 on the Banking Sector

- **Loans**

The pandemic has brought about a substantial change in the businesses and the employment environment due to which the demand for loans have decreased. Many people are losing their jobs due to which the repayment capacity of the people has reduced. Since at this point of time, the future is uncertain, providing further loans on the basis of their creditworthiness will be a challenge for the banks.

Digital Banking

Government agencies and banks are anticipating a shift towards digital banking. It is observed that there is a lot of growth in the activities of online banking and people are not visiting the banks physically. Due to the spread of the disease many customers are forced to register and adopt online and digital banking apps as a new way of banking. The availability of new digital capabilities means that banks can fundamentally change their response from previous issues. COVID-19 has accelerated digital transformation in the banking sector. The challenge will be faced by bank customers who are not technological literate.

- **Security Issues**

It's an unfortunate fact that fraudster's tend to take advantage of unexpected events or challenges. Cyber security is a challenge that the banking sector will face. Few of the common cyber security attacks aimed at banks include Phishing, Cross site scripting, Cyber- squatting, Botnets, Spoofing, etc. This causes a tremendous loss of money to the customer and bank, declines bank's reputation and decreases the trust that users place in a bank. The pandemic has generated significant demand for cyber security technologies.

- **Supply Chain Disruption**

Interruption of production and distribution does not have that much effect on banks like how it does for companies. But these companies are funded in the form of loans from the banks. So it is a concern for the banks in terms of recovering the loans provided. Several Indian industries have a significant direct dependence on supplies from China; this will lead to fall in production which will hinder the supply chain.

Difficulty in funding / providing loans

Banks provide loans on the credit worthiness of the customer. Due to the unpredictable job market and volatile business environment banks might find it different or rather risky to provide loans. Both the corporate and the banks are making their own assessment of the impact and the measures required to address the situation during the pandemic. In accordance to it RBI has announced several measures, including special lines of liquidity, loan moratorium, and easier asset quality norms, to help the economy tide over the crisis stemming from the novel corona virus pandemic.

- **Reduction in Income**

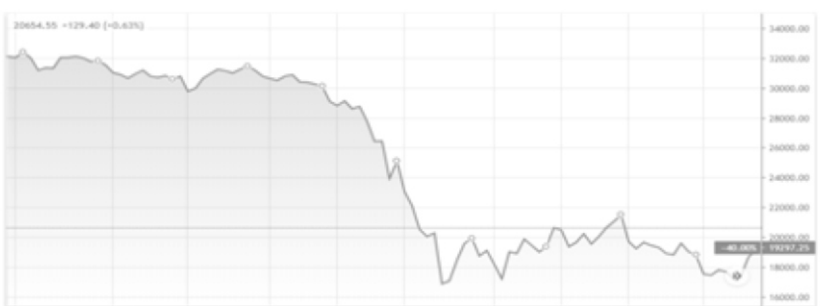
Banks get their income from interest income and other income. Since the lockdown period most of the income generated by the banks will reduce, due to reduction in banks daily transactions and RBI's measure of the moratorium period, it will have a major impact on the income generated by the bank especially for the quarters during the lockdown.

- **Effect on Credit Rating**

The Indian banking sector has been affected given the disruptions to India's economic activity from the corona virus outbreak, which will weaken the borrowers. The effect of COVID-19 will accelerate deterioration in the banks' asset quality and profitability. Global rating agency Moody's has downgraded ratings for State Bank of India and HDFC Bank's long-term local and foreign currency deposit from “Baa2” to “Baa3”. This is part of rating action on 11 banks, after Moody's downgraded India's sovereign rating from “Baa2” to “Baa3” with a negative outlook. They also revised the long-term issuer rating of Export and Import Bank of India (EXIM India) from “Baa2” to“Baa3”.

- **Share Prices**

The stock market is witnessing a tremendous shift in the prices after the corona virus pandemic. Bank nifty index has 12 most liquid and large capitalized stocks from the banking sector which trade on the National Stock Exchange (NSE). It provides investors and market intermediaries a benchmark that captures the capital market performance of Indian Banking sector. The figure below shows the trend from January to May 2020. It can be seen that there is a sharp decline in the trend after March.



Source: https://in.tradingview.com/symbols/NSE-BANKNIFTY/

Measures taken by the RBI and Banks

- **Rate reduction**

On the quantum of reduction, the Monetary Policy Committee had voted and has a majority of 5-1 in order to reduce the rate by 40 basis points that are from 4.4 percent to 4.0 per cent. Even the Marginal Standing Facility rate and the bank rate were reduced from 4.65% to 4.25 percent. The reverse repo rate was reduced from 3.75 percent to 3.35 percent. (On 22nd May 2020)

- **Pre-shipment and Post-shipment Export Credit – Extension of Period of Advance**

RBI has given permission for a period of realization and repatriation from nine months to 15 months for the export proceeds from the date of export in respect of exports made up to July 31,2020. The maximum permissible period of pre-shipment and post shipments credit that RBI has sanctioned has increased from 1 year to 15 months, for the disbursements made up to July 31,2020.

The period of pre-shipment and post-shipment export credit sanctioned by banks from the existing one year to 15 months, for disbursements made up to July 31, 2020. From the date of shipment all the imports made on or before July 31, 2020 there was an extension of the time for payment for imports extended from 6 months to 12 months excluding imports of gold/diamond and precious stones/ jewellary.

- **Refinancing Facility for Small Industries Development Bank of India(SIDBI)**

In case of on-lending/refinancing the RBI had already announced a special refinance facility of Rs 15,000 crores to SIDBI at the repo rate offered by RBI for a period of 90 days. Inorder to provide greater flexibility to SIDBI, it has been decided to roll over the facility at the end of the 90th Day for another period of 90 days.

- **Liquidity Facility for EXIM Bank of India**

EXIM bank always has to meet its requirements of foreign currency resources hence; it was decided to extend the credit line which was Rs 15,000 crore to the EXIM bank for a period of 90 days which can have a rollover up to 1 year.

- **Rescheduling of Payments – Term Loans and Working Capital Facilities**

Banks providing loans including agricultural term loan, crop and retail loan, RBI has instructed all the commercial banks (local area banks, small finance banks, regional rural banks), co-operative banks, all-India Financial Institutions and nonbanking financial companies to extend the moratorium for another 3 months from June 1, 2020 to August 31, 2020 for the payment of installments due to the extension of the lockdown on account of COVID-19. The repayment schedule for such loans as also the residual tenor, were placed across the board. The outstanding portion of the term loan during the moratorium period, interest on that amount will continue to accrue.

- **Easing of working capital financing requirements by reducing margins or reassessment of working capital cycle**

RBI has taken a onetime measure for the leading institutions with respect of the stress in the economy due to the pandemic with special reference to the working capital facilities sanctioned in the form of OD/CC to the one who borrow. The first step being to recalculate the drawing power by reducing the margin till August 31, 2020. But, in all such cases where such a temporary enhancement in drawing power is to be taken into account, the margins shall be restored to the original levels by March 31, 2021; and/or, to review the working capital sanctioned limits up to March 31, 2021, which will be based on a reassessment of the cycle of the working capital.

Impact of the measures taken by RBI on general public

- Income stream may not reach its original place because of the lockdown and many companies, entities and even individuals will not be able to repay their debt. The Moratorium period will have a positive impact and would be a very practical approach by the Reserve Bank on the pubic as availing of this benefit will reduce their financial burden.

- The reduction in the various rates was taken by the central bank due to the corona virus pandemic, which has hurt the global economy. Slashing of bank rates indicate that banks will be able to provide loans at a cheaper rate. The rate at which RBI lends money to other banks it's called the Repo rate. When this rate reduces, it means that other banks can now borrow money from RBI at a much lower interest rate. The commercial banks usually pass this benefit on to their customers by reducing the interest rates on the loans they offer.

- Special liquidity facility for mutual funds will bring a liquidity window and it will act more as a psychological signal to mitigate investors panic by providing assurance of adequate money to meet redemption pressure.

Suggestions

- The bank must focus on survival and continuity planning. They can close some branches temporarily, following a hub and spoke model to emphasize flagship branches while closing smaller, less used / retail outlets in similar vicinity. The banks can even adjust branch hours and staffing mix and times.

- How banks respond to their customers could be pivotal to how their brand is seen for years to come. Many banks already have mountains of customer segmentation data that can play a critical role in determining and even meeting customer needs. Therefore the banks must show empathy to their customers while making decisions.

- It has always been a good idea to minimize spending on activity that doesn't build the core capabilities. But the current situation makes this act more important than ever. The banks have to work on trying to reduce their cost. There are various focus areas like procurement, back office functions, information technology, marketing, customer service etc, which the bank must focus on.

- It may seem early to be imagining a post COVID-19 world, but it's important for the banking sector to take a long view. The banks must think on strategies to be adopted post COVID-19. They can adapt to a new customer norm with new business models, restructure the addressable market to grow beyond the core and reprioritize capital allocation plans and mergers and acquisitions.

Conclusion

Covid-19 has been an unprecedented challenge for India. The Reserve Bank of India has recognized the challenges and has responded but this response should be just the beginning and they still have a long way to go. These are testing times and banks will need to quickly take measures to ensure seamless delivery of services to customers with minimal disruptions. They will have to frame solutions that provide rapid or quick resolutions to the problems created by the COVID-19 crisis. It is a tough challenge for the financial institutions, and collaborating with a trusted service provider may be the way forward.

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