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ICRA COMMENTS ON RBI'S MAY 5 STATEMENT ON COVID-19 RELIEF MEASURES

MEASURES PRIORITIZE CREDIT DELIVERY TO MEDICAL HEALTH CARE SERVICES; RESTRUCTURING GUIDELINES TO PROVIDE NEAR TERM RELIEF TO SOME BORROWERS

May 2021

Karthik Srinivasan
+91 22 6114 3444
karthiks@icraindia.com

A M Karthik
+91 44 4596 4308
a.karthik@icraindia.com

Aashay Choksey
+91 22 6114 3430
aashay.choksey@icraindia.com

HIGHLIGHTS

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With the resurgence of Covid-19, RBI has decided to take a more measured stance by prioritizing credit delivery to medical health care services, while continuing with the optionality to restructure loans as an immediate relief to various affected borrower groups.

The need to progressively supplement these with additional measures will depend on the duration and macroeconomic impact of the second wave.

The RBI came out today with its first set of measures to counter the impact of the second phase of the Covid pandemic prioritizing emergency healthcare services and MSME sectors. Some of the key measures include:

- RBI has announced a restructuring package to provide relief to those borrowers who were classified as 'Standard' a on March 31, 2021 and have not availed restructuring under the Resolution Framework 1.0 announced by RBI on August 6, 2020. The restructuring under the proposed framework can be invoked upto September 30, 2021 and will have to be implemented within 90 days after invocation.
- Loans restructured under the Resolution Framework 1.0 can be further restructured by extending the residual tenor (including the moratorium period) upto a total of two years for resolution plans where the original tenor extension (including the moratorium period) was less than two years. The modification can be approved by September 30, 2021.
- RBI has decided to extend an on-tap liquidity window of Rs.50,000 crore at repo rate, with a tenor of upto three years, that can be availed by bank's till March 31, 2022. This facility can be used to provide liquidity for ramping up the covid related health infrastructure and services. Fresh lending provided under this facility will be allowed to be classified as Priority Sector Lending (PSL) till the repayment or maturity of these loans. RBI has also allowed on-lending to other financial entities that are regulated by RBI. Further banks are eligible to park surplus liquidity equivalent to the loan amount in the reverse repo window at a rate that is 40 bps higher than the prevailing reverse repo rate.
- RBI has announced a special long-term repo operations (STLTRO) of Rs.10,000 crore at repo rate for Small Finance Banks. The facility can be utilized for fresh lending upto a ticket size of Rs.10 lakh per borrower till October 31, 2021. Additionally, RBI has allowed PSL classification benefits for on-lending done by SFB's to small Micro Finance Institutions (MFIs) with portfolio upto Rs. 500 crore as of March 2021.
- RBI has announced extension of the allowable deduction of fresh loans (upto Rs.25 lakhs) given to new MSME borrowers from the Net Demand and Time Liabilities (NDTL) for the purpose of CRR calculation till December 31, 2021 from the fortnight ending October 1,2021.

Outlook: The various policy measures announced by RBI on May 5, 2021 are aimed at addressing near term challenges like ensuring timely credit availability to the health care services as well as providing support to marginal and small borrowers. While the macroeconomic impact of the second wave is still evolving, we expect restructuring to provide near term relief to certain borrowers. While lenders may continue remain selective, we expect an increase in the overall restructured portfolio given the current situation. Moreover, depending on the severity of the impact in the coming months, additional measures may also be needed to provide relief to various affected stakeholders.

In response to the macroeconomic impact of the on-going second Covid-19 wave, RBI announced certain targeted policy measures aimed at alleviating financing constraints faced by the heath care services segment as well as affected individuals and small businesses. RBI has also decided to extend the option to restructure accounts, while staying away from any moratorium related measures for the time being. Some of the key measures and their impact is as under:

1) **Resolution framework 2.0 for COVID related stress:**

The resurgence of Covid-19 has led to lockdown and containment measures across states, which in turn has stalled the economic recovery process following the first wave in FY2021. RBI has announced a restructuring package to provide relief to those borrowers (including individuals, small businesses and MSME's having an aggregate exposure not more than Rs.25 crore) who were classified as 'Standard' on March 31, 2021 and have not availed restructuring under the Resolution Framework 1.0 announced by RBI on August 6, 2020. The restructuring under the proposed framework can be invoked upto September 30, 2021 and will need to be implemented within 90 days after invocation. RBI in its policy has also allowed some relief to borrowers who availed restructuring under the Resolution Framework 1.0. It proposed that the already approved resolution plans under framework 1.0 can be modified by extending the residual tenor (including longer moratorium, as the case may be) by upto two years. However, this relief is permitted only for those resolution plans where the original residual tenor extension was less than two years. These modifications can be approved upto September 30, 2021. Besides this, the process for invocation of restructuring as well as the asset classification and provisioning (10% provision on restructured exposures and the subsequent write back of half the provisions upon the borrower paying at least 20% of the residual debt) remain similar to framework 1.0 . RBI has also allowed lenders to review the working capital limits or drawing power for accounts that were restructured under Framework 1.0, without treating the same as restructuring.

Impact: RBI's decision to extend the option to restructure standard accounts as on March 31, 2021 will provide near term relief to borrowers as it will give them time to stabilize their cash flow. While overall restructuring under RBI's Resolution framework 1.0 remained low, overall percentage of restructured book is likely to increase. Lenders that are relatively stronger placed on capital could decide to take a more conservative stand by limiting overall restructuring to only viable borrowers and absorb potential impact of the stress, while those operating with comparatively weaker capital cushions are likely to encourage affected borrowers to restructure accounts.

2) **Incentivized Term Liquidity Facility of Rs.50,000 crore for bank's**

RBI, in light of its assessment of financial constraints being faced by the emergency health care services (like hospitals, pharmacies, medicine manufacturers or importers, medical oxygen manufacturers and suppliers and other operators engaged in the critical healthcare supply chain) has decided to extend an on-tap liquidity window of Rs.50,000 crore at repo rate, with a tenor of upto three years, that can be availed by bank's till March 31, 2022. Further, fresh lending provided under this facility will be allowed to be classified as Priority Sector Lending (PSL) till the repayment or maturity of these loans. RBI has also allowed on-lending to other financial entities that are regulated by RBI so that loans granted under the facility reach the intended beneficiaries efficiently. Further, banks that give 'Covid loans', given under this facility are eligible to park surplus liquidity equivalent to the loan amount in the reverse repo window at a rate that is 40 bps higher than the prevailing reverse repo rate.

Impact: The policy announcement is expected to facilitate credit delivery and provide relief to the health care services segment in the near term. Further, RBI in October 2020, announced facility of on-tap TLTROs for banks of upto Rs 1.0 trillion which was available at Repo rate for upto three years which was later on extended to 26 stressed sectors identified by the Kamath Committee. In its policy announcements of February 5, 2021, RBI further expanded the scope of lending under on-Tap TLTROs for lending to NBFCs and subsequently extended the availability of the said facility till September 30, 2021 in its announcement in April 2021. However, given the surplus liquidity position in the banking system, the outstanding balance against the said facility remained low. Against this backdrop, the linking of the Term Liquidity facility with additional incentives in the form of higher rates in the reverse repo window as well as eligibility for PSL classification is expected to ensure better utilization of the policy measure taken by RBI

3) Special Long-Term Repo Operation (SLTRO) of Rs.10,000 crore and PSL classification benefits for SFB's

In order to alleviate the financial conditions of customers of Small Finance Bank's, RBI has announced a special long-term repo operations (STLTRO) of Rs.10,000 crore at repo rate. The facility can be utilized for fresh lending upto a ticket size of Rs.10 lakh per borrower till October 31, 2021. Additionally, RBI has allowed PSL classification benefits for on-lending done by SBF's to Micro Finance Institutions (MFIs), which is aimed at incentivizing credit delivery to smaller MFIs (with asset size upto Rs.500 crore), which has been allowed by RBI till March 31, 2022.

Impact: The second wave of Covid-19 and the consequent partial lockdowns across states is likely to impact livelihoods of small and marginal borrowers, and the policy announcement will remain a positive for individuals and small businesses. Given the pandemic, many lenders turned risk averse and especially small MFIs faced challenges in raising funds in the last fiscal. RBI's announcement of priority sector tag to SFB's lending to small MFIs is a welcome move and is expected to enhance liquidity support to MFIs.

4) **Extension in allowable deduction in CRR calculation**

RBI has announced an extension of the allowable deduction of fresh loans (upto Rs.25 lakhs) given to new MSME borrowers from the Net Demand and Time Liabilities (NDTL) for the purpose of CRR calculation till December 31, 2021. The earlier dispensation allowed deduction till the fortnight ending October 1,2021.

Impact: The measure is unlikely to result in increased credit flows to MSME borrowers, however it may encourage some targeted lending to certain affected borrowers

5) Relaxation extended for utilization of floating provisions

Banks will be allowed to utilize upto 100% of their floating/countercyclical provisions held as on December 31, 2020 for making specific provisions for non-performing assets, subject to the approval of the Board of the bank. The utilization of these provisions has been allowed till March 31, 2022.

Impact: The measure is majorly expected to benefit large private sector banks that have managed to create sizeable floating provisions over Q4FY2020-FY2021. The utilization of these provisions will largely help address incremental stress that could arise if the second wave sustains for a longer duration. The measure will help reduce the impact on the earnings profile of lenders in the near term.

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Business Contacts

Mr. L. Shivakumar
E-mail: shivakumar@icraindia.com
+91 22 6114 3406 / +91 98210 86490

Mr. Jayanta Chatterjee
E-mail: Jayantac@icraindia.com
Tel: +91 80 4332 6401/ +91 98450 22459

Media and Public Relations

Ms. Naznin Prodhani
E-mail: Communications@icraindia.com
Tel: +91 124 4545 860

Registered Office

1105, Kailash Building, 11th Floor,
26, Kasturba Gandhi Marg, New Delhi - 110 001
Tel: + 91 11 2335 7940-50

Corporate Office

Building No. 8, 2nd Floor,
Tower A, DLF Cyber City, Phase II,
Gurgaon - 122 002
Tel: +91-124-4545300

Ahmedabad

1809-1811, Shapath V,
Opp: Karnavati Club,
S.G.Highway, Ahmedabad - 380015
Tel: +91 79 4027 1500/501

Bengaluru 1

'The Millenia', Tower B Unit No. 1004,
10th Floor, 1 & 2 Murphy Road,
Bengaluru - 560 008
Tel: +91 80 4332 6400

Bengaluru 2

2nd Floor, Vayudooth Chamber
15-16, Trinity Circle, M.G. Road,
Bengaluru - 560 001
Tel: +91 80 4922 5500

Chennai

5th Floor, Karumuttu Centre
634, Anna Salai, Nandanam
Chennai - 600 035
Tel: +91 44 4596 4300

Hyderabad 1

4th Floor, 'Shoban'
6-3-927/A&B. Somajiguda
Raj Bhavan Road,
Hyderabad - 500 082
Tel: +91 40 4067 6500

Hyderabad 2

No. 7-1-58, 301, 3rd Floor, 'Concourse',
Above SBI-HPS Branch, Ameerpet,
Hyderabad - 500 016
Tel: +91 40 4920 0200

Kolkata

A-10 & 11, 3rd Floor,
FMC Fortuna 234/3A,
A.J.C. Bose Road,
Kolkata -700 020
Tel: +91 33 7150 1100/01

Mumbai

3rd Floor, Electric Mansion
Appasaheb Marathe Marg,
Prabhadevi,
Mumbai - 400 025
Tel: +91 22 6169 3300

Pune

5A, 5th Floor, Symphony, S. No. 210
CTS 3202 Range Hills Road,
Shivajinagar, Pune - 411 020
Tel: +91 20 2556 1194

Email: Info@icraindia.com
Helpdesk: 9354738909
Website: www.icra.in/ www.Icraresearch.in