RBI's move on 90 per cent LTV on gold loans to heighten credit risk for banks: **Brickwork Ratings**

Mumbai , August 7: Brickwork Ratings has said that an increase in loan to value (LTV) ratio to 90 per cent for borrowers increases the credit risk for banks as the collateral available in the form of gold ornaments or jewellery may not be sufficient to fully cover both principal and interest components on these loans.

As part of its monetary policy announcements on Thursday, the Reserve Bank of India (RBI) allowed banks to increase the LTV ratio for loans to borrowers against the pledge of gold ornaments and jewellery for non-agricultural purposes from 75 per cent to 90 per cent for all incremental lending up to March 31 next year.

This comes as a positive for individual borrowers as it provides an interim liquidity buffer to tide over the crisis related to the COVID-19 pandemic. But it also increases collateralised retail lending avenues for banks that have been sitting on excess liquidity.

"Gold loans with an LTV of 90 per cent will result in a negative carry for banks as the total exposure will exceed the value of the pledged gold," said Brickwork Ratings Director Vydianathan Ramaswamy.

"It could adversely impact the recoverability and asset quality of banks in case of a weakening in borrower credit risk profile or sharp decline in gold prices, which have seen a strong rally over the last few months."

However, the risk on the portfolio is for a limited period given that the applicability of the scheme of a higher LTV is allowed only till March 31, 2021. Moreover, gold loans are mostly short-tenure loans of anywhere between three months to two years.

"Given that the RBI's announcement on higher LTV gold loans is limited to the banking sector, banks are bound to garner a larger market share vis-a-vis their non-bank peers in loans against the pledge of gold in fiscal 2021," said Ramaswamy.