THE WEEK

COVID-19 second wave may lead to rise in stress in retail segment, MSMEs

The pandemic has affected smaller businesses and individuals much harder

By Nachiket Kelkar | June 22, 2021 20:16 IST

On March 23, 2021, the Supreme Court lifted the interim ban under which banks were prohibited from classifying loans that hadn't been classified as bad loans as of August 31.

These are loans essentially not repaid for 90 days or more. Last year, as the country went into a strict lockdown amid the COVID-19 pandemic, borrowers were offered a relief in the form of a moratorium on their repayments for six months.

Banks heaved a sigh of relief following the Supreme Court verdict in March as they could now start recognising bad loans. As the economy starting reopening slowly from June 2020 and at a faster clip post September, banks have seen a pickup in credit growth.

However, banks are bracing for fresh set of challenges in the wake of the second wave of COVID-19 that led to lockdowns in many states over April and May.

The pandemic has affected smaller businesses and individuals much harder, and not just from a health perspective. Many people have lost jobs or have had to take home reduced salaries. Many smaller businesses, traders, retailers, restaurant owners etc have had to down shutters. Many of them had barely begun to stand up again post the lockdowns last year, that the latest round of restrictions hit. This has raised worries about rising levels of stress in these sectors.

Ratings agency ICRA points out that the monthly collection efficiency in SME loan pools that picked up close to 100 per cent in March weakened to below 90 per cent in April and is likely to have further slipped to around 80 per cent in June.

Collection efficiencies in retail loan pools, which had touched pre-pandemic levels in the March quarter also declined in the range of 8-20 per cent in April, it said.

“Measures taken by state governments such as lockdown/ restrictions to contain the precipitous rise of the fresh COVID-19 cases beginning April 2021, have impacted the operations and collection activities of the non-banking finance companies/ housing finance companies. Further, the repayment capability was also affected as the income-generating ability of the underlying borrowers was impacted,” said ICRA.

The lockdowns in April-May were milder than the complete lockdowns in the same period last year, and the number of companies that were allowed to operate this time was also higher. But the worry is for firms in segments such as travel and tourism, some commercial real estate, jewellers, hospitality, food and entertainment, says Jindal Haria, director at India Ratings and Research.

“The impact for MSMEs operating in these segments will be stronger,” he said.

In the wake of the crisis last year, the government had announced an emergency credit line guarantee scheme (ECLGS), which guaranteed collateral free credit at capped interest rates to firms in various sectors. This scheme was recently extended till June 30.

In the quarter ended March 31, 2021, most banks have reported a rise in gross non-performing assets. This was expected following the Supreme Court lifting the ban on classifying NPAs. The impact of the second COVID wave on NPAs will be visible in the June quarter results due next month.

The Reserve Bank of India in its last financial stability report has projected gross NPAs of all scheduled commercial banks may increase to 13.5 per cent by September 2021, from 7.5 per cent in September 2020. Under a severe stress scenario, this could further escalate to 14.8 per cent, it added.

“COVID has had a huge impact on the repayment abilities of individual borrowers as well as MSMEs as the cheque bounce rates are still about 20 per cent higher than their pre-COVID levels and with the second wave of COVID, are expected to go up,” said Anshuman Panwar, co-founder Creditas Solutions, a company providing technology for debt recoveries and delinquency management.

According to a survey by LocalCircles in May, 37 per cent of startups and MSMEs said they will scale down their operation, 14 per cent said they might shut down, whereas, 8 per cent would sell off their business in the next 6 months.

Bad loans may not be the only thing lenders have to worry about. The pandemic driven uncertainties also slowed down demand for loans. In the year-ended March 2021, non-food credit of all banks rose just 4.9 per cent from a year ago to Rs 96.6 lakh crore, according to latest RBI data. This was the slowest pace in the past four years.

Banks had hoped that with the economy expected to rebound in double digits in 2021-22, credit demand would pick up. However, with the renewed restrictions and uncertainties, credit demand may yet remain weak. Banks are also likely to be cautious this year, as they take stock of the pandemic situation, do their checks and balances on businesses and lend only if convinced on their growth prospects.

“I don't think banks are going to chase growth at the risk of asset quality deterioration,” said Ramya Muraledharan, director – ratings at Brickwork Ratings.

She felt there may be a deterioration in the MSME portfolio of banks and non-banking finance companies (excluding the ECLGS portfolio guaranteed by the government), with banks/ NBFCs having a higher percentage of MSME portfolio being affected more.

Thankfully, COVID cases have declined in June, prompting most states that had announced lockdowns, to relax many of the restrictions. While, this has generally lifted the mood in the market, experts have predicted a third wave of COVID is likely in the coming months. If those expectations do come true, then MSMEs and small retail borrowers and their lenders could be in for another blow.