COVID-19- A BLESSING IN DISGUISE FOR DEBT RESTRUCTURING

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During the testing times, India has imposed the most stringent lockdown in the world in response to the COVID-19 pandemic. This pandemic can be stopped through containment- but at a significant economic cost. Uncompromising on the health of its Citizens the Government has ensured relief in as many ways as possible. Policymakers are supporting vulnerable households and smaller businesses to mitigate the impact of this severe shock.In this battle, The Reserve Bank of India has set out various developmental and regulatory policies that directly address the stress in financial conditions caused by COVID-19. The policies consist of :

a. expanding liquidity in the system sizeably to ensure that financial markets and institutions are able to function normally in the face of COVID-related dislocations;
b. reinforcing monetary transmission so that bank credit flows on easier terms are sustained to those who have been affected by the pandemic;
c. easing financial stress caused by COVID-19 disruptions by relaxing repayment pressures and improving access to working capital; and
d. improving the functioning of markets in view of the high volatility experienced with the onset and spread of the pandemic.

The first and foremost set of measures is intended to ensure that liquidity is sizeably expanded in order to ensure that Financial markets and Institutions and all related constituents are able to function as normally as possible in the face of the COVID-related dislocations.

The CRR (Cash Reserve Ratio) is the minimum amount of money that a Commercial Bank needs to keep with the RBI (Reserve Bank of India) which cannot be used for any of the commercial purposes of the bank, namely lending of loans to the corporations and individuals. As a one-time measure on 27th March 2020, to help banks tide over the disruption caused by COVID-19, it has been decided to reduce the cash reserve ratio (CRR) of ALL banks by 100 basis points to 3.0 per cent of net demand and time liabilities (NDTL) with effect from the reporting fortnight beginning March 28, 2020. This reduction in the CRR would release primary liquidity of about ₹ 1,37,000 crore uniformly across the banking system in proportion to liabilities of constituents. This dispensation will be available for a period of one year ending on March 26, 2021. Thus, the effects of reduction in CRR would lead to:

i. The Banks have to set aside lesser amount as deposits with the RBI and have more liquidity available which shall lead to reduction in lending costs,

ii. In order to boost growth and sustainability in the economy, the Banks will have more money to lend at a Lower interest rate which shall help Borrowers to continue their Businesses,

iii. Since Banks have more Liquidity it needs to be deployed in Investment grade Bonds, commercial papers and non-convertible debentures,

iv. On Real estate sector, customers will be able to get home loans at lower rate of interest rates thus facilitating the real estate sector to sell the ongoing projects, also expansion of 1year has been extended to developers for completion of their projects by NBFCs.

The long-term effect of this Pandemic is going to be massive and most unexpected. The COVID-19 induced economic as well as social uncertainty and consequences were absolutely not accounted for by any of the Countries. A necessary first step is required to be prepared by us once the Lockdown is lifted so that we can ensure minimum impact on our businesses and personal lives. In this regard, there are some notable challenges, we shall recognize them and try to lessen the impact as much as possible:

a. Most of us have availed Home Loans from various Banks, but how many of us have actually analysed the best Loan for us. Now that we have stayed in our Homes for the longest times in our lives , its time, to analyse what is the excess cost that we are paying in the form of Home loan interest in order to stay there. The most important questions to ask yourself is –

1. Is your Home Loan Rate of Interest the most competitive?

2. Recheck your Rate of Interest once every Six months to know the difference between the Rate of interest at which your loan was sanctioned and your ongoing Rate of Interest.

3. Do you really need a tenure of 20 years to repay your Home Loan?

Example I:

Vicky took a Home Loan of Rs.1,00,00,000 on 2/4/2018 from XYZ Bank @8%p.a for 20years. When asked for his EMI Statement for the period 1st April 2019-31st March 2020, he was surprised to find out that he has been paying the same amount of EMI of Rs.83,664 for an interest rate @8.65%. Pooja advised Vicky in a constructive manner that for a Loan of Rs.1 crore he was paying a total Interest of Rs.1,00,74,561 during the 20years as on 2nd April 2018. This amount increased by Rs.4,00,000 as on 1st April 2019 when his interest rate spiked up.

In the current scenario, since the RBI has cut the Repo rates, a marginal reduction in the home loan rates is expected. Hence, this is the best time to continue with your plan of buying your new home and making sure that you pay minimum interest on your Total Loan.

If Vicky hired Pooja as a consultant, she would ensure that he is paying the minimum interest amount for his total Loan, by reducing his Total Rate of Interest, as she analyses the rates of all the major Bank players. Due to COVID we have to ensure that we minimize these costs, which can be done only by generating more financial awareness.

The next question that arises in the minds of most of our clients is regarding availing the facility of Moratorium provided by the Banks, this is a very subjective question which I shall again explain through few examples:

Example II

Ramesh has an ongoing Term loan for which he is paying regular EMIs, he asked Pooja his financial Consultant the benefit of the moratorium facility. Since, Ramesh is a businessman with enough savings ,Pooja recommended him to continue paying the EMIs without availing of this benefit, as this would lead to a deferment of the payment , however he would end up paying higher interest on his existing loans as interest would be levied on every deferred payment.

Conclusion- Moratorium is harmful for Ramesh.

Example III

Sid is a businessman with Home Loan EMIs linked to his Working Capital Loan. Since, the Rate of Interest of Working Capital Loan is always higher as compared to Home Loans ,Pooja advised Sid to defer his EMIs as he would save on the differential interest and the end result would be a benefit for Sid without affecting his CIBIL score.

Conclusion- Moratorium is beneficial for Sid.

Example IV

Adarsh is an exporter, due to the COVID situation, all his orders are on Hold. He has availed Letters of Credit from Banks against his orders, he shall avail the Moratorium benefit as once the lockdown is lifted he can start processing his orders and the Bank shall defer his tenure for 3months while his business in non-operational.

There are innumerous examples and every case is different, we as professionals and businessmen shall realize that in coming times the need of Loan from Banks will be indispensable as our expenses for Rent, Salaries, electricity and other Administration related shall continue as earlier. Also, we can expect delayed payments from our Debtors due to close down of the businesses for a long tenure. Here I would remind you that As Mahatma Gandhi said in his famous address at Kingsley Hall, London in October 1931:

"……In the midst of death life persists, in the midst of untruth truth persists, in the midst of darkness light persists."

Our Government, financial Institutions, Banks and all functionaries are working in their maximum potential so that we can stay safe during this pandemic, and provide us sufficient ray of hope in order to fight and overcome these dark times. On 17th April, the Governor of RBI addressed the nation and revealed that the IMF (International Monetary Fund) on 14th April 2020 released its global growth projections, revealing that in 2020, the global economy is expected to plunge into the worst recession, yet India is among the handful countries that is projected to cling on to positive growth at 1.9%. It was shared that the regional offices of RBI have supplied fresh currency of Rs.1.2lakh crore from 1st March till 14th March to currency chests to meet the increased demand of cash, hence increasing liquidity in Banks. This will lead to excess funds available with Banks and hence relaxing norms for providing Loans, reducing margins and increase in activity in corporate Bonds market.

In such a situation, our means of finance shall resort to Loans in different forms- like Working Capital to meet our Short term expenses as banks have eased their criterions for Working Capital financing by reassessing the Working Capital cycle of Borrowers and reducing margins, Bank Guarantees can be availed to complete the contracts in hand as margins for these financing have been reduced, Home Loan as the Government will provide the lowest rates for availing the same.

Due to continuing expenses for businesses and professionals, people with existing loans will have higher chances of defaults in payments, which will lead to high NPAs in Banks; the RBI has relaxed norms for qualification of an NPA for an account and specifically stated not to include the moratorium period while calculating the NPA. There are various ways through which an NPA account can be settled, such as the Banks and Financial Institutions are currently required to hold an additional provision of 20% if a resolution plan has not been implemented within 210 days from the date of such default. Settlement of NPA’s is subjective to each case and each Bank, but it is very important to receive a settlement ensuring maximum benefit of the client.

The decision in respect of Finance is essential for development of businesses as well as to ensure financial stability and liquidity for smooth functioning of all vulnerable stakeholders. Hence, alongside liquidity measures , efforts have been undertaken to diminish the burden of debt servicing brought about by disruptions on account of the fall-out of the COVID-19 pandemic.Such efforts, in turn , will prevent the transmission of financial stress to the real economy, and will ensure the continuity of viable businesses and provide relief to borrowers in these extraordinarily troubled times. It is our decision to make the sure that even though social distancing seperates us, we understand the resolute of our Government and support them in order to support ourselves. As our Prime Minister, Narendra Modiji said: “Jaan Bhi aur Jahaan Bhi”, we have to prepare for the upcoming times by protecting each other from the unseen viruses- Corona Virus and the Financial Virus.