Impact of Covid-19 on Indian Financial System – A Study

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Abstract :

This paper attempted to study the monetary policy of RBI in addition to this it focuses on analyzing India's monetary policy framework has emerged in the last few decades due to financial developments and changing economic conditions. The framework of monetary policy has also undergone significant changes in the tools and methods of identification. The introduction of the Reserve Bank of India (RBI) Act, 1934 was also amended in 2016, which now explicitly provides for the authority of the RBI. It reads: "Managing the banking notes and the preservation of the palaces for the purpose of financial stability in India and the general use of the currency and the credit system to its advantage; to have a modern monetary policy framework to meet the challenge of a complex growing economy; to maintain price stability while keeping in mind the purpose of growth. "

The objective of monetary policy in the early years of the establishment of the RBI was primarily to maintain excellent equity, with the exchange rate becoming the basis of monetary policy. Liquidity was regulated by open market performance (OMOs), bank rate and savings rate (CRR). Soon after independence and in the late 1960's, the role of the central bank was in line with the nation's planned development agenda in line with its five-year plans. Therefore, it has played a major role in regulating credit access, using OMOs, banking rates, and the need for savings to achieve this.

Keywords : RBI, Monetary Policy, COVID-19, Cash Reseerve Ratio, Working Capital,

1. INTRODUCTION

With the centralization of the central banks in 1969, the main objective of monetary policy in the 1970s to the mid-1980s was debt management in line with the country's development needs. This period has been marked by monetization due to a lack of funding while the effects of inflation on high government spending need to appear regularly in CRR. In 1985, on the recommendation of the Committee established to Review the Performance of the Financial System (Chairman: Dr. Sukhamoy Chakravarty), a new financial policy framework, response funding was initiated based on strong evidence of a stable financial need. function. However, the introduction of finance in the 1990s meant that the need for money could be affected by things other than income. In addition, interest rates were withdrawn in the mid-1990's and India's growing economy combined with the global economy. Therefore, the RBI began to emphasize the role of monetary estimates and applied the MIA system in the 1998 fiscal policy which included all economic and financial variables that impact the main

objectives set out in the Preamble of the RBI Act. This is done in two phases — initially MIA and later expanded MIA (AMIA) which combines forward-looking variables with time series models.

2. OBJECTIVES OF STUDY

1. To study the monetary policy of RBI
2. To analyze the measures taken by the RBI in the post COVID-19 period.

3. RESEARCH METHODOLOGY

In order to accomplish the said objectives researcher collected data from the secondary source such as RBI websites, Newspaper, Financial Magazines and Research Articles. Researcher employed the analytical research technique in order to study the monetary policy and analyse the measures taken by the RBI in the post COVID-19 period.

4. COVID-19 – RBI Regulatory Package

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

In respect of working capital facilities sanctioned in the form of cash credit/overdraft ("CC/OD"), lending institutions are permitted to allow a deferment of another three months, from June 1, 2019 to August 31, 2019, on recovery of interest applied in respect of all such facilities. Lending institutions are permitted, at their discretion, to convert the accumulated interest for the deferment period up to August 31, 2019, into a funded interest term loan (FITL) which shall be repayable not later than March 31, 2019.

- **Easing of Working Capital Financing**

In respect of working capital facilities sanctioned in the form of CC/OD to borrowers facing stress on account of the economic fallout of the pandemic, lending institutions may, as a one-time measure,

(i) recalculate the 'drawing power' by reducing the margins till August 31, 2019. However, in all such cases where such a temporary enhancement in drawing power is considered, the margins shall be restored to the original levels by March 31, 2019; and/or,

(ii) review the working capital sanctioned limits upto March 31, 2019, based on a reassessment of the working capital cycle.

The above measures shall be contingent on the lending institutions satisfying themselves that the same is necessitated on account of the economic fallout from COVID-19. Further, accounts

provided relief under these instructions shall be subject to subsequent supervisory review with regard to their justifiability on account of the economic fallout from COVID-19.

Lending institutions may, accordingly, put in place a Board approved policy to implement the above measures.

5. RBI MEASURES POST COVID-19

Since March 2019, the Reserve Bank of India (RBI) has taken numerous measures to fight the COVID-19 at the financial front. These measures also form part of the Special Economic Package and the 'Atmanirbhar Bharat Abhiyaan' recently announced by the Hon'ble Prime Minister of India, Narendra Modi.

Various developmental and regulatory policies undertaken by the RBI to address financial stress caused by COVID-19 include:

- Liquidity Management
- Regulation and Supervision
- Decisions in respect of Financial Markets

5.1 Liquidity Management

Liquidity availed under the scheme by banks has to be deployed in investment grade corporate bonds, commercial paper, and non-convertible debentures over and above the outstanding level of their investments in these bonds as on March 27, 2019. Banks shall be required to acquire up to fifty per cent of their incremental holdings of eligible instruments from primary market issuances and the remaining fifty per cent from the secondary market, including from mutual funds and non-banking finance companies. Investments made by banks under this facility is classified as held to maturity (HTM) even in excess of 25 per cent of total investment permitted to be included in the HTM portfolio. Exposures under this facility also not be reckoned under the large exposure framework.

The first TLTRO auction held today (March 27, 2019). Following a review of the outcome of this auction, the subsequent TLTRO auctions announced. Details about this facility are being issued separately.

➢ **CASH RESERVE RATIO**

a. Liquidity in the banking system remains ample, as reflected in absorption of surpluses from the banking system under reverse repo operations of the LAF of the order of ₹ 2.86 lakh crore on a daily average basis during March 1-25, 2019. It is observed, however, that the distribution of this liquidity is highly asymmetrical across the financial system, and starkly so within the banking system.

- **Marginal Standing Facility**

Under the marginal standing facility (MSF), banks can borrow overnight at their discretion by dipping up to 2 per cent into the Statutory Liquidity Ratio (SLR). In view of the exceptionally high volatility in domestic financial markets which bring in phases of liquidity stress and to provide comfort to the banking system, it has been decided to increase the limit of 2 per cent to 3 per cent with immediate effect. This measure applied up to June 30, 2019. This is intended to provide comfort to the banking system by allowing it to avail an additional ₹ 1,37,000 crore of liquidity under the LAF window in times of stress at the reduced MSF rate announced in the MPC's resolution.

- **4. Widening of the Monetary Policy Rate Corridor**

In view of persistent excess liquidity, it has been decided to widen the existing policy rate corridor from 50 bps to 65 bps. Under the new corridor, the reverse repo rate under the liquidity adjustment facility (LAF) would be 40 bps lower than the policy repo rate. The marginal standing facility (MSF) rate would continue to be 25 bps above the policy repo rate.

5.2 Regulation And Supervision

All commercial banks (including regional rural banks, small finance banks and local area banks), co-operative banks, all-India Financial Institutions, and NBFCs (including housing finance companies and micro-finance institutions) ("lending institutions") are being permitted to allow a moratorium of three months on payment of instalments in respect of all term loans outstanding as on March 1, 2019. Accordingly, the repayment schedule and all subsequent due dates, as also the tenor for such loans, may be shifted across the board by three months.

5.2.1.1 Deferment of Interest on Working Capital Facilities

In respect of working capital facilities sanctioned in the form of cash credit/overdraft, lending institutions are being permitted to allow a deferment of three months on payment of interest in respect of all such facilities outstanding as on March 1, 2019. The accumulated interest for the period paid after the expiry of the deferment period.

In respect of paragraphs 5 and 6 above, the moratorium/deferment is being provided specifically to enable the borrowers to tide over the economic fallout from COVID-19. Hence, the same not be treated as change in terms and conditions of loan agreements due to financial difficulty of the borrowers and, consequently, not resulted in asset classification downgrade. The lending institutions may accordingly put in place a Board approved policy in this regard.

5.2.1.2 Easing of Working Capital Financing

In respect of working capital facilities sanctioned in the form of cash credit/overdraft, lending institutions may recalculate drawing power by reducing margins and/or by reassessing the working capital cycle for the borrowers. Such changes in credit terms permitted to the borrowers to specifically tide over the economic fallout from COVID-19 not treated as concessions granted due to financial difficulties of the borrower, and consequently, not result in asset classification downgrade.

The rescheduling of payments wnot qualify as a default for the purposes of supervisory reporting and reporting to credit information companies (CICs) by the lending institutions. CICs shall ensure that the actions taken by lending institutions pursuant to the above announcements do not adversely impact the credit history of the beneficiaries.

5.2.1.3 Deferment of Implementation of Net Stable Funding Ratio (NSFR)

As part of reforms undertaken in the years following the global financial crisis, the Basel Committee on Banking Supervision (BCBS) had introduced the Net Stable Funding Ratio (NSFR) which reduces funding risk by requiring banks to fund their activities with sufficiently stable sources of funding over a time horizon of a year in order to mitigate the risk of future funding stress. As per the prescribed timeline, banks in India were required to maintain NSFR of 100 per cent from April 1, 2019. It has now been decided to defer the implementation of NSFR by six months from April 1, 2019 to October 1, 2019.

Highlights of study

- **Deferment of Interest on Working Capital Facilities:** RBI also permitted all lending institutions to allow a deferment of three months on payment of interest in respect of working capital facilities sanctioned in the form of cash credit/overdraft of all such facilities outstanding as on March 1, 2019
- **Easing of Working Capital Financing:** All lending institutions are permitted by RBI to recalculate drawing power by reducing margins and/ or by reassessing the working capital cycle for the borrowers in respect of working capital facilities sanctioned in the form of cash credit/overdraft.
- **Support to Real Estate Sector:** RBI has permitted an additional time of one year for the extension of the date for commencement of commercial operations (DCCO) in respect of all loans provided by NBFCs to the real estate sector.
- In recent times, RBI has recognized the growth of the offshore Indian Rupee (INR) derivative market - the Non-Deliverable Forward (NDF) market and decided to remove segmentation between the onshore and offshore markets.

- RBI has now permitted banks in India to participate in the NDF market from 1st June 2019 through their branches in India, their foreign branches or through their International Financial Services Centre (IFSC) Banking Units (IBUs).

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