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EMI MORATORIUM IN COVID CRISIS – THE EFFECTS ON INDIAN ECONOMY

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ABSTRACT

Moratorium period refers to the period of time during which you do not have to pay an EMI (Equated Monthly Instalment) on the loan taken. This period is also known as EMI holiday. Usually, such breaks are offered to help individuals facing temporary financial difficulties to plan their finances better.

The Reserve Bank of India (RBI) announced loan Equated Monthly Instalment (EMI) deferment primarily to provide relief to those whose loan repayment capacity has been severely impacted because of disruptions caused by the lockdown due to COVID-19. The customers can choose to defer their EMI payments scheduled from 1st March 2020 to 31st May 2020.

Though the specifics will vary across banks, borrowers are likely to be given three options by lenders. Moratorium does not mean a cancellation or waiver of interest. The moratorium is only an option to defer or postpone EMI repayment for the borrower. It does not mean the interest during this period is cancelled or waived off. If the individual avails the moratorium facility, the interest will continue to accrue or get added to the principal outstanding amount. Then, from June 2020 onwards, when EMI will be restarted, the interest will essentially be calculated on the higher principal amount. So, effectively an individual could end up paying a higher interest from June onwards. Hence, one should keep this in mind while deciding to avail the option of EMI moratorium.

KEYWORDS*:* EMI, loan moratorium, loan deferment, COVID impact

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1. INTRODUCTION

The entire world is battling from the pandemic of COVID-19 and this fight cannot be won if the countries will fight individually. It will take a joint effort by everyone to fight come out of it. While the fight is majorly for human survival but at the same time it is creating a major turmoil in the economies too. Every government's first priority is to keep its people safe and hence nationwide lockdowns have become the new normal. The economic activities have come to a standstill except for essential commodities and services. Manufacturing has been severely affected and this has created a ripple effect in the economy where the business and employees both are taking a hit on their earnings. The companies are making partial payment of remuneration to their employees or in worst scenario they are laid off.

Amid this crisis the Reserve Bank of India (RBI) announced the deferment of Equated Monthly Instalment (EMI) primarily to provide relief for those whose loan repayment capacity has been severely impacted because of economic disruptions caused by the lockdown due to COVID-19 (Economic Times, 2020). As RBI announced relief measures for the common man to deal with corona virus, several banks have come out with their explanations on what will the impact on the EMIs for the customers if they opt for deferring the EMIs by three months.

"However, those availing the deferment will continue to accrue interest on the outstanding amount of their term loans during this period. As the interest accrual will increase their total interest cost, existing borrowers' capable of servicing their term loans should continue with their original repayment schedule. This will save them from incurring higher interest costs on their loans. Only borrowers unable to service their terms loans because of restrained cash flows should opt for the loan deferment." says Naveen Kukreja – CEO & Co-founder, Paisabazaar.com

"The loan moratorium is a help for cash flow only, not a reduction in payable amounts. Hence, only those who have liquidity issues (lost a job, cut in salary, etc) should avail the loan moratorium; as they continue to pay interest on the loan outstanding -- and the tenure will be extended by the 3 months period too." said Lovaii Navlakhi, Founder & CEO, International Money.

With the intent to contain the spread of COVID-19, India's Prime Minister Honarable Mr. Narendra Modi with effect from March 25, 2020 announced a nationwide complete lockdown. India had the world's biggest lockdown that shut a majority of the businesses and factories, suspended domestic and international flight operations, stopped all passenger trains and restricted movement of majority of vehicles and peoples. 70 per cent of the economic activities, investments, exports and discretionary consumption came to a standstill. Analysts

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and industrial bodies have suggested, this biggest lockdown had cost the Indian economy lakh crore during this period. Only essential goods and services, such as agriculture, utility services, mining, some financial and IT services and many public services were allowed to operate. It is stated that this pandemic came at the most inopportune time for India, where economy was showing positive signs of recovery after some bold fiscal and monetary measures taken by the government.

Centrum Institutional Research has projected the country again stares at the possibility of low or negative growth for FY2021 (April 2020 to March 2021). It was further estimated by Acuite Ratings & Research Ltd that "Nationwide complete lockdown is likely to shave off at least Rs 7-8 trillion," which implicates that the lockdown will cost the Indian economy almost USD 4.64 billion (over Rs. 35,000 crore) every day and the entire first phase of lockdown resulted in a GDP loss of almost USD 98 billion (about Rs 7.5 lakh crore).

The sectors that are most severely impacted are tourism, transportation, dine outs, multiplexes, cinema halls and real estate activities. Many relief packages have been announced by the government for the upliftment of these industries but the losses that these industries are facing are growing day after day. The Confederation of All India Traders estimates that the losses incurred by the retail trade of the country in the second half of March due to the COVID-19 pandemic were a massive USD 30 billion. The Indian retail sector comprising 70 million small medium and big traders employing 45 crore people, does a monthly business of approximately USD 70 billion. All India Motor Transport Congress (AIMTC) Secretary-General Naveen Gupta said that “The accumulated losses to truckers during the first 15 days of lockdown were about Rs. 35,200 crores given an average Rs. 2,200 loss to per truck per day. More than 90 per cent of the about one crore trucks in the country are off roads during the lockdown as truckers with only essential commodities are on the move," he said. "Even if the lockdown is lifted, it will take at least 2 to 3 months for truckers to limp to some normal scale as we apprehend consumption of nonessential items to remain hit on the account of lack of purchasing power." National Real Estate Development Council - a body of realtors, puts the loss in real estate sector at Rs. 1 lakh crore. "I am scared to estimate what the losses would be. I think, a potential loss of maybe Rs 1 lakh crore on a conservative basis on an all India basis. It is a conservative figure. I cannot think of the upper end of the figure. Based on thumb rule, at least Rs.1 lakh crore," said its President Niranjan Hiranandani (Economic Times, 2020).

A host of international rating agencies have cut India's economic growth estimate for FY21 on concerns about the fallout of COVID-19 outbreak. World Bank said earlier that India's economy is expected to grow 1.5 per cent to 2.8 per cent in financial year 2020-21. This will be the slowest growth rate recorded for Indian economy since the economic reforms of 1991. Asian Development Bank (ADB) estimated India's economic growth slipping to 4% in FY21, while S&P Global Ratings has further slashed their estimated GDP growth forecast for the country to 3.5 per cent from a previous downgrade of 5.2 per cent. Fitch Ratings puts its estimate for India growth at 2 per cent while India Ratings & Research has revised their FY21 forecast to 3.6 per cent from 5.5 per cent earlier. Latest rating given by Fitch Ratings for India is decline of 5 percent in its GDP (CNBC, 2020).Moody's Investors Service has slashed its estimate of India's GDP growth during the 2020 calendar year to 2.5 per cent, from an earlier estimate of

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5.3 per cent which was further reduced to 0.2 percent and said the corona virus pandemic will cause unprecedented shock to the global economy (Economic Times, 2020).

Moratorium period refers to that duration of time during which the customers do not have to pay their EMIs on the loan availed by them. This period can also be referred as EMI holiday. Usually, such breaks are offered by the financial institutions to help customers facing temporary financial difficulty so that they can plan their finances better.

Some deferments are automatically done by the financial institutions, such as in the case of student loans, where the EMIs are automatically deferred when students enroll themselves in a college or university degree/diploma program till the end of such course. In some cases it is further differed for next year till the student is able to get an employment. In other loan cases deferments needs to be proven to the lender with documentation support. The lender can decide to approve or deny the request of deferment based on the lender's policies, submitted documentation or opinion regarding the validity of the deferment request. Most of the deferments are not guaranteed by the financial institutions and borrowers need to be prepared to pay their loans or they risk going into default. Deferring any loan payments does not stop interest from accumulating, so it can be quite impactful on the interest owed on loan, depending on the loan's terms.

During these difficult economic situation RBI has allowed all Banks and other Financial Institutions to offer its customers, an option, of EMI moratorium up to 3 months. This means that a customer can choose to defer the payment of their EMIs scheduled from March 1, 2020 to May 31, 2020.

All those customers are eligible to avail moratorium who have existing over dues prior to 1st March 2020. Their requests shall be considered by the bank based upon its merits. For such customers, the extant IRAC norms will apply. Under the category all kinds of retail loans or Term loan like Car Loan, Personal Loan or any other retail credit facilities prior to 1st March 2020 are eligible. All Agri Loans (Kisan Gold Card) and Micro finance customers under the initiative of Bank's Sustainable Livelihood are also eligible. All Corporate customers as well as SME customers are eligible for moratorium. Customer can get information on the moratorium process by their respective branches or relationship managers. Business heads will share details with the branches and relationship managers on the process of availing corporate and SME moratorium.

Though the specifics of moratorium will vary across the financial institutions, borrowers are likely to be given three options by lenders.

• Option I: The borrower can make a one-time payment in June of the interest that accrues in April and May.

• Option II: The interest is added to the outstanding loan which will increase the EMI for the remaining months.

• Option III: The EMI is kept unchanged but the loan tenure is extended.

Suresh Sadagopan, Founder, Ladder7 Financial says: "If they have a regular income which is not expected to be interrupted or if they have liquidity enough to pay the EMIs irrespective of disruptions, they may continue with the loan repayments as before. Only those who are expected to be adversely affected in terms of cash flows need to opt for moratorium".

Explaining further as to how the stipulation by RBI will have an impact its customers? When a customer chooses EMI moratorium, then: Financial institutions will not ask for any EMI Payment until May31st, 2020. Though the interest will continue to accrue on the outstanding principal for the period of moratorium at the contracted rate of interest. Thus, loan tenure will get extended by the corresponding period for which the moratorium has been availed. For example, if a customer has paid the EMI for the month of March 2020 and has opted for moratorium for April & May 2020, then the loan tenure will get extended with only the corresponding effect of two months.

The EMI of a borrower is dependent on multiple factors, such as:

1. Principal borrowed
2. Rate of interest
3. Tenure of the loan
4. Monthly/annual resting period

For a borrower, loan taken at a fixed interest rate, the EMI will remain fixed for the entire tenure of the loan, provided there will be no default or part-payments in between. The EMI is used for paying off both the principal and interest components of an outstanding loan. The first EMI has the highest interest component and the lowest principal component. With every subsequent EMI, the interest component keeps on reducing while the principal component keeps rising. Thus, the last EMI has the highest principal component and the lowest interest component. In case where the borrower makes a pre-payment or part payment through the tenure of an existing loan, then either the subsequent EMIs get reduced or the original tenure of the loan gets reduced or a mix of both. The reverse will happen when the borrower skips an EMI throughout the tenure of the loan. Skipping of EMI can be for the reasons like EMI holiday or cheque dishonor/bounce or insufficient balance in bank account where EMI gets auto deducted or a default. In that case either the subsequent EMIs will rise or the tenure of the loan will increase or a mix of both. Also, there can be penalty from the financial institution for nonpayment of EMI on time.

Similarly, in the case of floating rate loans, if the rate of interest reduces throughout the tenure of the loan the subsequent EMIs will get reduced or the tenure of the loan will fall or a mix of both. The reverse will happen if the rate of interest increases. Suppose a person borrows Rs one lakh for one year at the fixed rate of 9.5 percent per annum with a monthly interest. In this case, the EMI for the borrower for 12 months (1-year X 12 months = 12 months) works out to approximately Rs. 8,768, divided between Principal and interest as shown in Table 1.

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Table 1

Month	Principal Outstanding	Interest	Balance Remaining
1	7977	792	92023
2	8084	729	83983
3	8103	665	75880
4	8168	601	67712
5	8232	563	59480
6	8297	471	51183
7	8363	405	42891
8	8429	339	34390
9	8496	272	25849
10	8563	205	17331
11	8631	137	8699
12	8699	69	0

Source: BankBazar.com

Here, during the entire tenure of twelve months it has been assumed that there is no default in payment of EMI.

Total Principal amount paid: Rs. 1,00,000

Total interest paid: Rs. 5,220

Now, for a borrower moratorium does not mean either cancellation or waiver of interest. It is only an option to defer or postpone, your EMI repayment. Thus, the interest accumulated during this period is not cancelled or waived off. If a borrower avails of the moratorium facility, the interest will continue to accrue and get added to your principal outstanding amount. When, from June 2020 onwards, the borrower restarts the payment of EMI, then the interest will essentially be calculated on a higher principal amount. So, effectively the borrower could end up paying a higher rate of interest from June onwards. A simple interest rate will be calculated by banks for the period in which loan repayment was due but was not paid under the scheme of moratorium. This interest would be added up into the borrower's principal at the end of three-month forbearance, raising their monthly payout.

So, if the customer is availing the moratorium facility and deferring their payment of an EMI of, say Rs. 1,000, and the bank is charging an interest of 10 percent on outstanding, then the borrower will end up paying Rs. 25 extra on each of the three EMIs which has not been paid during the moratorium. This additional interest may either be added up to all the future EMIs or to the loan tenure which can get extended at the same EMI level (Economic times, 2020).

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So, if the borrower is capable to pay the EMI amount for the next 3 months, then the experts suggest that the repayment of EMIs should not be avoided. Let us understand this via chart that how it is going to impact the borrower's loan (3 months EMI moratorium):

For Loan of Rs. 50,00,000 @ 8.5% p.a. for 20 years

EMI: Rs. 43,391/-

Total interest: Rs. 54,13,879/-

Table 2

Remaining Tenor	Outstanding	Additional Interest for three months	New Principal	New EMI (same tenor)	Total interest payable	Extra tenor if EMI unchanged
19 years	49,00,489	1,04,875	50,05,364	44,320	55,20,727	13 months
15 years	44,06,359	94,300	45,00,659	44,320	54,86,728	8 months
10 years	34,99,691	74,896	35,74587	44,320	54,50,412	4 months
5 years	21,14,936	45,261	21,60,197	44,320	54,24,328	2 months
1 year	4,97,492	10,647	5,08,139	44,320	54,14,369	1 month

Source: BankBazar.com

For Credit Card customers Kukreja says- "While credit card dues are also eligible for moratorium, it should be avoided to the extent possible. The interest cost, popularly known as finance charges, of credit card dues can range anywhere between 23-48% p.a., which is way higher than the usual loans. Instead, credit card holders unable to repay their dues should convert their bill amount to EMIs to repay back in smaller instalments. The interest rates of EMI conversions are much lower than the finance charges and the tenure usually ranges between 1-5 years."

2. IMPACT ON STAKEHOLDERS

Positive effects for borrowers

1. Banks are ready to offer easier credit to small and medium sized enterprises that are facing maximum pressure in the current quarter as sales have falter because of supply chain disruptions and lack of customers.
2. The moratorium offers some respite during these troubled times of a financial emergency. A borrower can defer their loan repayments during this period while diverting the funds for essential needs and sustainability of the business.
3. The bank will not be charging any penalty even though the borrower will not repay the loan during moratorium period.
4. Since it is a relief measure, the banks will not report the borrower as a defaulter to the credit bureau during the moratorium period. Even if you don't repay your loan, your credit

score and credit history will not see an adverse impact. This will help in the future when you need to take another loan and need a good credit history.

5. As the borrowers can differ their EMIs, the corporate as well as small businesses will now have excess liquidity which can be utilized for the development of the business or other business-related activities. It is estimated that the corporate will have an enhanced liquidity of Rs. 2.1 lakh crore during these three months (Economic Times, 2020).

Positive effects for financial institutions

1. The accrued interest will be collected by the lender institution in the form of additional EMIs from those borrowers who will opt for three months moratorium. For as example a borrower has taken a home loan of Rs 30 lakh with a maturity of 15 years at the rate of 8%, the net additional interest for the borrower would be approx. 2.34 lakh which will be equal to 8 EMIs for those borrowers who opt for the moratorium.
2. The three-month suspension of EMI payments might not result in significant gains for borrowers as they will get charged the additional interest for the moratorium period, as per the scheme announced by their banks. As the borrowers will get charged for 3 months interest the revenue earned will be beneficial for banks.
3. While the borrowers get immediate relief, banks will recover the entire cost once the moratorium is over, resulting in higher EMIs. In case the borrower can't afford higher EMIs, then the financial institutions will likely give them the option to increase the tenure of loan.

Negative effects for customer

1. Since the interest continues to accrue, during the moratorium period the borrowers' EMI could increase after June 2020. Hence, the borrowers need to make provision accordingly if they choose to avail the benefit of moratorium.
2. In the case the borrower is not able to increase the higher payout of EMIs then in such case the tenure of the loan will get increased. Thus, again a payment of higher interest to the financial institutions.
3. The borrower will not be able to use their credit card during the availed moratorium period.

Negative effects for financial institutions

1. As per an estimate if more than 50% of the borrowers opt for EMI moratorium, then the additional liquidity made available by the financial institutions through the RBI measures could be far less than the amount that they would not receive as principal repayments and interest payments from borrowers during the moratorium period. The reason being that the banks will have to continue to pay depositors the interest and principal amounts on their deposits. Such a situation will have a negative impact on the liquidity position of banks.
2. EMI moratorium can cause concern for the financial institutions over higher credit-deposit (CD) ratio. Under the present circumstances, the central bank of India might have to consider for opening a general line of credit to the financial institutions.

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3. With more and more borrowers opting of EMI moratorium the chances to these assets turning NPA for the banks also increase. The borrowers who opt for moratorium are already under financial stress and if there will be negative economic impact on them, the chances of repayment of loans further decreases.

Now the questions arise how to understand whether borrowers should opt for EMI Moratorium or not?

1. If borrower is salaried and the employer has announced a salary cut or if the borrower is businessman and the business has been shut down due to the lockdown, then there EMI can increase the financial burden. In such cases, the moratorium can provide financial relief. But, if the current finance permits the borrower to repay the loan, then they may continue to do so, as this will help avoiding additional interest burden on the loan amount.
2. If the borrower has more than one loan, then the moratorium should be availed based on the loan which is likely to see a bigger impact post the moratorium period. This decision will depend on the amount of loan, the interest rate and the residual loan tenure.
3. If the borrower's loan is in its initial stages, then it makes more sense for them to continue repaying their EMIs, as interest portion in the EMI during the initial period of the loan is considerably higher than the EMIs at a later stage. Hence, if the borrower defers their EMI at an initial stage, the impact on loan will be larger, than someone whose loan tenure is nearing the end.

3. CONCLUSION

The impact of EMI deferment on borrowers is mostly negative, as they have to pay higher rate of interest for the deferment of their existing EMIs. When the borrower avails the deferment of EMIs, that amount will be added to the total principal amount and therefore the interest on loan will increase. At the same time, there is also a positive impact on fund strapped borrowers as opting for moratorium will give must respite to them financially as they don't need to worry about payment of their EMIs and such funds can be utilized for other preferential decisions.

The impact of EMI deferment on financial institutions is mostly positive, as they will be earning higher income from the same assets. The interest rates charged will be higher for every EMI deferment thus, giving them higher income. However, there can be negative effect as well. The borrowers who will not have sound financial stability will tend to default of their EMIs once the moratorium period is over. This can lead to higher NPAs for the financial institutions which will be a burden on the financial stability of the institutions and for the country as a whole. There can be a possibility that the default will start not only for big credits but also for small credits.

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