"Critical Analysis of Micro financial Development and COVID-19"

Dr. Mahadeo Kharade
Assistant Professor, Punyashlok Ahilyadevi Holkar Solapur University.

Dr. Mahadeo Kharade, Critical Analysis of Micro financial Development and COVID-19, -- Palarch's Journal Of Archaeology Of Egypt/Egyptology 18(2), 983-996. ISSN 1567-214x

Keywords: COVID-19, financial statement, impact, etc

Abstract
The occurrence of the coronavirus Covid-19 out has significantly disrupted the functioning of many commercial units. The impact on the banking and financial sector in terms of non-performing assets and low financial activity will only be known when the situation returns to normal. At the same time, some areas have had a positive impact, such as information technology and digital business, Given the outbreak of the e-commerce business, pharmaceuticals and life sciences business, healthcare business, and insurance business Covid-19 out, it is challenging at this moment to estimate the full scope and duration of its business and financial impact. In this situation, the elements are presented with challenges while preparing their financial statements and reporting their results.

Introduction
World economic activity makes an indecisive and uneven recovery from the unprecedented COVID-19 pandemic on the back of extraordinary policy responses by monetary, fiscal, and regulatory authorities, the focus is shifting to developing policies and strategies to nurse deleteriously affected sectors back to health and normalcy. The trade-off that will inevitably confront authorities and get sharper going forward is between cliff effects of terminating exceptional measures and risk a deterioration of the repair and healing that has been achieved so far, and ramp effects that involve more graduated withdrawal of policy support but also the moral hazard of making various economic agents more reliant on policy stimuli and for longer, eventually locking in authorities into forbearance and liquidity traps.
By all counts, police authorities have been able to restrain the immediate risks from the destructive macro-financial feedback loops of the pandemic, but incipiently pre-pandemic vulnerabilities have intensified and pose headwinds to a fuller recovery. Also, as stated earlier, support measures may have unintended consequences as reflected, for instance, in the soaring equity valuations disconnected from economic performance. These deviations from fundamentals, if they persist, pose risks to

financial stability, especially if recovery is delayed.

Against this backdrop, this chapter begins with an overview of global and domestic macroeconomic and financial market developments. addresses global macro-financial developments and the outlook. deals with domestic macro-financial developments, emerging fiscal and corporate sector risks, and the evolving dynamics of bank and non-bank financial intermediation. The chapter concludes by drawing on the responses to the Reserve Bank's half-yearly systemic risk survey.

Objectives.

1) To study and the Analysis of micro-financial Development
2) To study the major suggestions

Research Methodology

The Research is based on secondary data. For the Research paper data is collected from the Reserve Bank of India Website, the Reserve Bank of India Manual, Guideline provided by RBI in their manuscript, Books, Internet, Magazines and Newspaper.

Global Background

Macro financial Developments and Expectations

Global economic activity remained besieged by the COVID-19 pandemic, more recently by the second wave that has forced the re-clamping of lockdowns across Europe and a resurgence of infections in the US. This is casting a shadow on the strong rebound of economic activity in Q3:2020. The International Monetary Fund (IMF) placed global growth in 2020 at (-)4.4 percent, followed by a recovery in 2021 to 5.2 percent which is, nonetheless, insufficient to lift output above the 2019 level in most advanced and emerging markets and developing economies (EMDEs), excluding China (Table 1.1 and Chart 1.1). Optimism about global growth in 2021 (Chart 1.2), on the back of vaccine roll-out, is now tempered by the realization that production and distribution constraints will allow only a gradual move towards mass vaccination.

Table 1.1: Growth Projections for 2020 and 2021

(in percent)

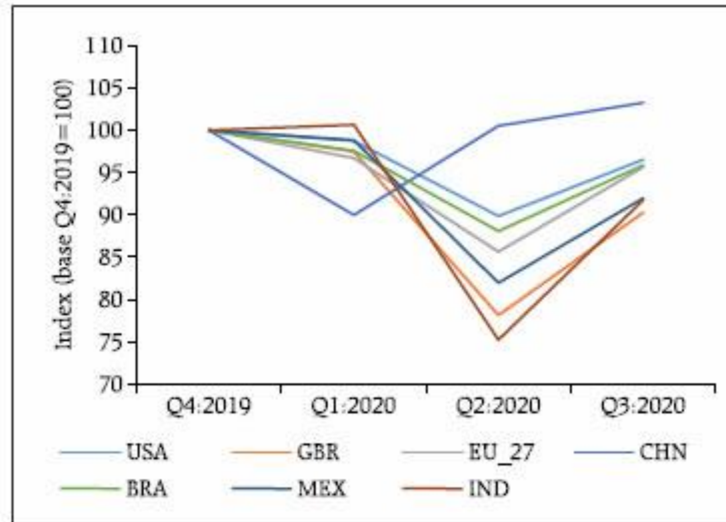
Release period	Advanced Economies		EMDEs		World	
	2020	2021	2020	2021	2020	2021
January 2020	1.6	1.6	4.4	4.6	3.3	3.4
April 2020	-6.1	4.5	-1.0	6.6	-3.0	5.8
June 2020	-8.0	4.8	-3.0	5.9	-4.9	5.4
October 2020	-5.8	3.9	-3.3	6.0	-4.4	5.2

Source: World Economic Outlook, IMF.

The response of public authorities to the pandemic has varied across advanced economies (AEs) and emerging market and developing economies (EMDEs) (Chart 1.3). Since July 2020, policy measures have shifted to fine-tuning and extending strategies to nurse severely affected sectors back to health. Given the substantial risk of a looming solvency crisis eroding the strength of the business sector, authorities have turned to provide fiscal support to rebuild businesses. The

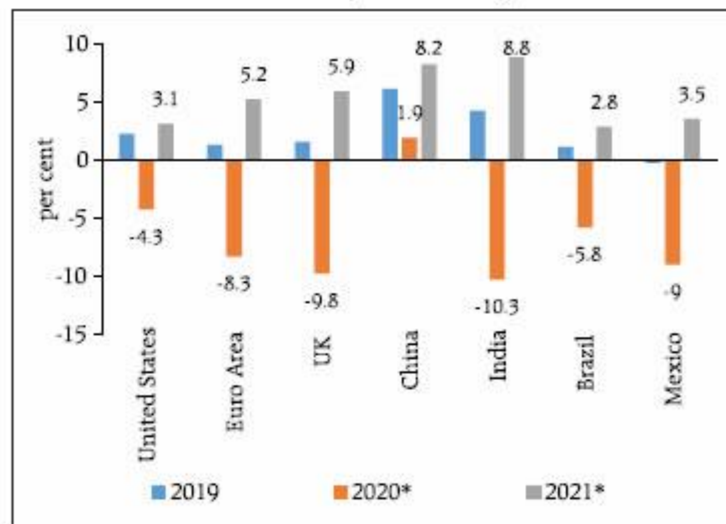
European Union (EU), through its long-term budget and other initiatives, has designed a fiscal package of Euro 1.8 trillion, the largest stimulus package ever to be funded through the budget. In Japan, fiscal authorities have introduced a fresh stimulus package of about Yen 73.6 trillion, of which about Yen 40 trillion is dedicated to fiscal spending on loans, investments, and other measures. The US has approved a US$ 2.3 trillion coronavirus relief and government spending package in the wake of a second resurgence of the pandemic and slowing employment numbers in November 2020.

Chart 1.1: GDP Growth in Major Economies



Source: Bloomberg.

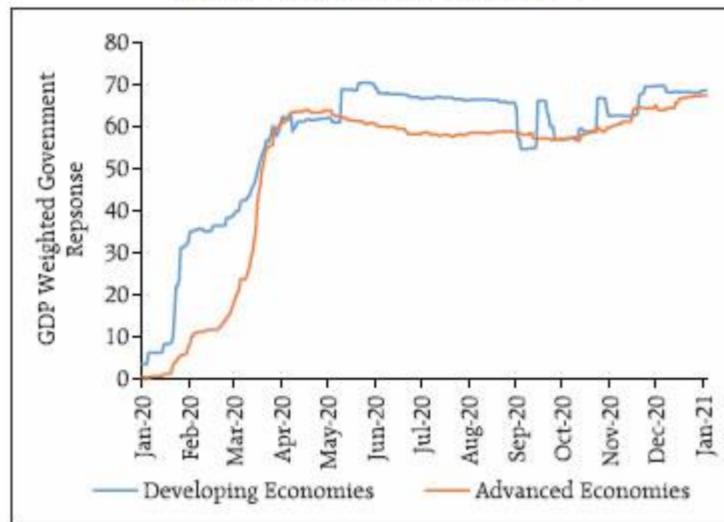
Chart 1.2 : Growth Projections for Key Economies



Note: * - Projected.

Source: World Economic Outlook (WEO)-October 2020 update, IMF.

Chart 1.3 : Policy Response to COVID-19



Note: 1. Updated till January 3, 2021.
2. Higher scores implying government response being more restrictive.
Source: University of Oxford's Coronavirus Government Response Tracker.

Given the unprecedented nature of the crisis, central bank interventions spanned interest rate reductions, funding liquidity, and market liquidity expansion, asset purchases, credit easing, macroprudential policies, and swap lines. They have persisted with and in some jurisdictions intensified these measures since July 2020. Illustratively, in a series of measures, the European Central Bank (ECB) has ramped up its corpus for the purchase of sovereign bonds (including principal repaid), extended the horizon of such purchases, and recalibrated the conditions of targeted longer-term refinancing operations. As a result, policy rates have touched historic lows and have even descended to negative territory and balance sheets have expanded to levels hitherto unobserved (Chart 1.4).

These actions have eased financial conditions across the globe back to pre-COVID levels. The Office of Financial Research's Financial Stress Index1 (OFR FSI) moved further into negative territory since July 2020, indicating below-average stress levels (Chart 1.5). Easing financial conditions have also directly impacted insurance on corporate credit, with high-grade and high-yield credit default swaps (CDS) in the US back at their pre-COVID levels and the 3-year over 5-year CDS spread changing course after the COVID-19 induced inversion (Charts 1.6 & 1.7). European CDSs were similar, approaching pre-COVID levels. While easier financial conditions do support growth prospects in the short run, the longer-term impact in terms of encouraging leverage and inflating asset prices may give rise to financial stability concerns.

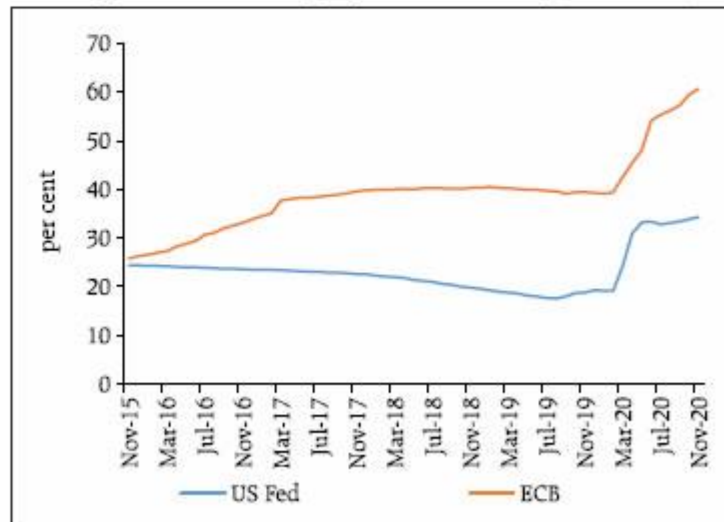


Chart 1.4 : Balance sheets of the US Federal Reserve (Fed) and European Central Bank (proportion to their respective GDPs)

Source: Bloomberg.

1.8 The massive infusion of central bank liquidity in the wake of the pandemic has led to a sharp decline in term rates (Chart 1.8), which has brought down borrowing costs substantially but has also compressed the net interest rate margins of banks, driving down their profitability2. Even as deposit yields have fallen, assets under Money Market Mutual Funds (MMMFs) have grown, indicative of a search for yield (Chart 1.9). Such risk-taking among institutional investors, specifically in illiquid investments to earn targeted returns, may lead to a build-up of financial vulnerabilities, with adverse implications for financial stability.

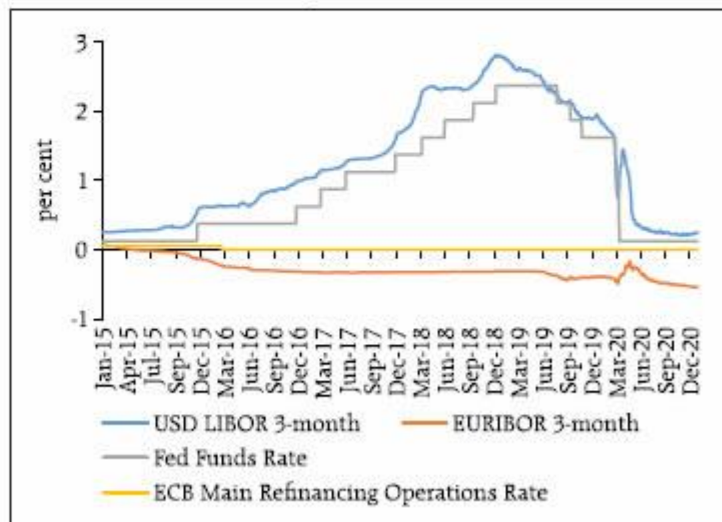
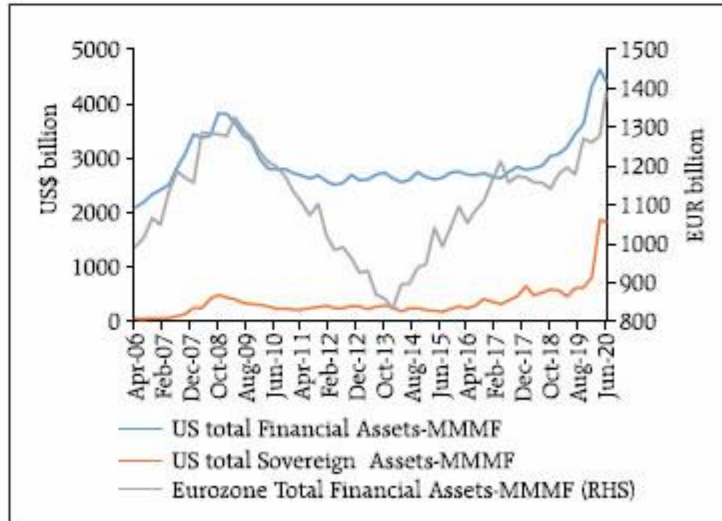


Chart 1.8 : Movement in Key Interest Rates in the US and Eurozone

Source: Bloomberg.

Chart 1.9 : Growth in Money Market Mutual Fund Assets in the US and Eurozone



Source: Federal Reserve Bank of St. Louis Economic Research & European Central Bank Statistical Data Warehouse.

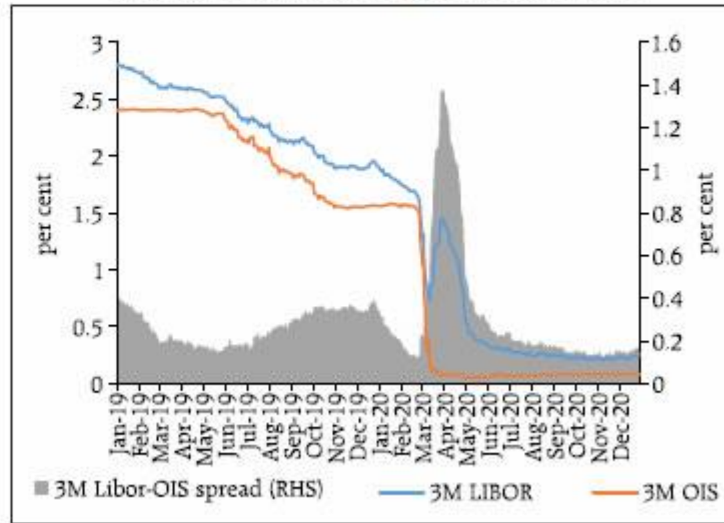
Table 1.2: Fiscal Deficit as a percent of GDP – Key Regions		
	2019	**2020***
Advanced economies	-3.01	-14.39
Emerging and Middle-Income Asia	-6.00	-11.40
Emerging and Middle-Income Europe	-0.65	-7.18
Emerging and Middle-Income Latin America	-4.00	-11.09
Emerging Market and Middle-Income Economies	-4.83	-10.72
Note: * - Projected. Source: IMF Fiscal Monitor;		

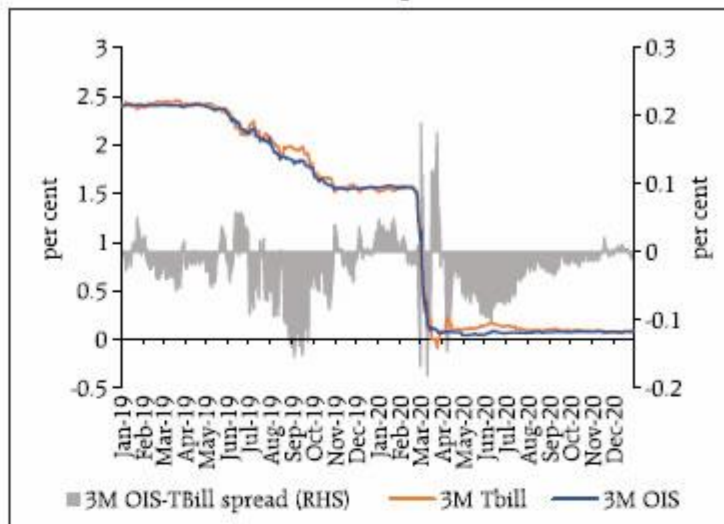
Other fault lines have also emerged in the wake of the COVID-19 pandemic-induced economic disruptions. For one, the pandemic has severely affected government revenue receipts which, in turn, has inflated sovereign borrowing to fund sharp increases in fiscal deficits across all geographies, especially in the advanced economies (Table 1.2). This has aggravated global debt vulnerabilities.

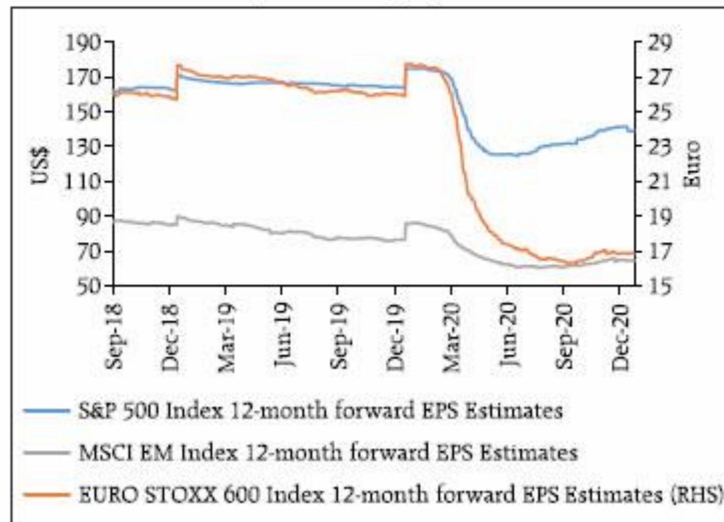
Second, it has exposed vulnerabilities in treasury markets. Following the onset of the pandemic, the 3-month overnight indexed swap (OIS)-US Treasury Bill (T-Bill) spread turned negative persistently, pointing to unprecedented illiquidity in US money markets which, in turn, had a cascading influence on global risk appetite, affecting borrowing rates and flows (Charts 1.10 & 1.11). The unsecured rate spread over the OIS rate also widened sharply. While these spreads have reverted to positive territory more recently, the developments brought into sharp relief the implications for emerging markets (EMs), should the frailties of the US treasury market give rise to US dollar shortages in non-US markets.

Third, COVID-19 has accentuated the credit risk of firms and households, which is impacting short-term corporate earnings. Yet, strong growth expectations remain firmly embedded in equity prices (Charts 1.12 & 1.13). Developments that lead to

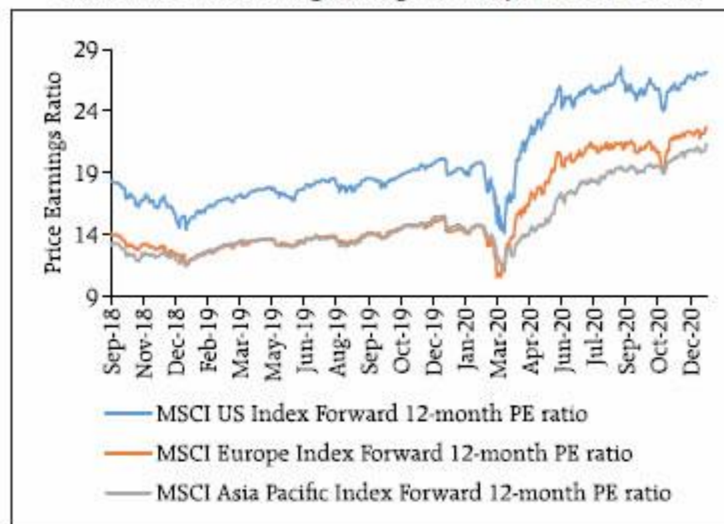
a re-evaluation of corporate earnings prospects will have significant implications for global flows, going forward.







1.12 The policy endeavor is moving from mitigating stress to repair and recovery. Accordingly, a policy shift is underway from broad-based liquidity support to more targeted measures to support households and firms and to maintain the health of the financial system (Box 1.1).



Capital Flows and Exchange Rate Volatility

1.13 After the unprecedented outflows in the earlier part of the year following the outbreak of the pandemic, a hesitant recovery in capital flows to emerging markets (EMs) began in June 2020 and picked up strongly following positive news on COVID-19 vaccines (Chart 1.14). The response of foreign investors to primary issuances from EMs has been ebullient (Chart 1.15). Anticipating the COVID-19 vaccine-induced economic boost, US yields of intermediate tenors (2– and 5-year)

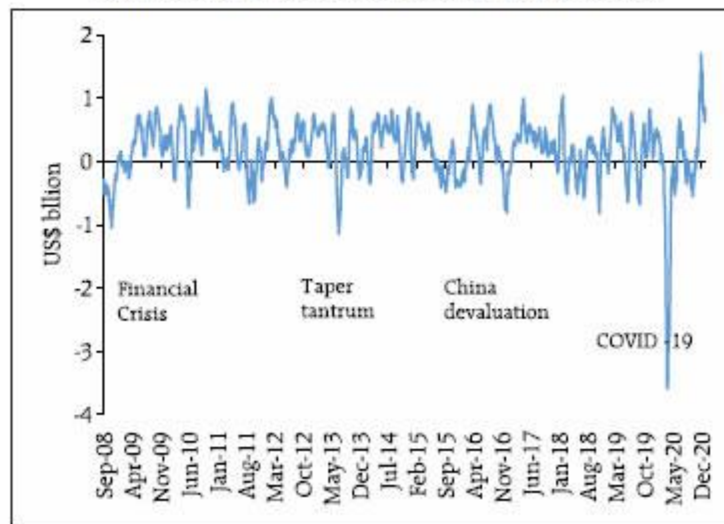
have started edging higher4. This could have implications for future portfolio flows to EMs.

1.14 EM local currency bond portfolio returns in US$ terms have been lower than local currency as well as hedged returns since early 2020 as emerging market currencies have softened against the US$ (Chart 1.16). This has led to sluggishness in EM local currency bond flows even as global bond markets have been pricing in a prolonged economic slowdown and benign inflationary conditions in Europe and the US. In this scenario, any significant reassessment of either growth or inflation prospects, particularly for the US, can be potentially destabilizing for EM local currency bond flows and exchange rates.

COVID-19 and Bank Capital

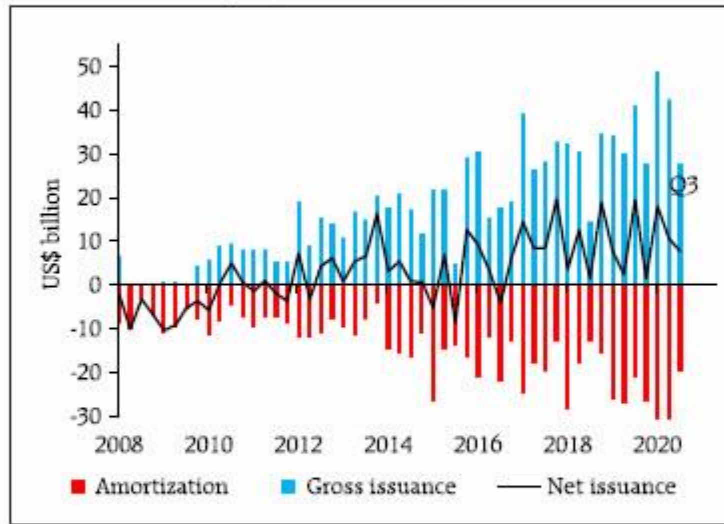
The world faced the COVID-19 crisis with much better-capitalized banks than was the case during the global financial crisis of 2008; the latter provided an impetus for stronger capital buffers. The COVID-19 crisis has significantly altered the capital costs of banks and has posed challenges for both banks and prudential authorities. Bank stock prices plummeted as the crisis unfolded (BIS, 20205) and their subsequent recovery was subdued as they generally remained well below other global stock prices and also below their pre-crisis levels. Similarly, price-to-book ratios fell, plateauing at around unity, on average, for banks outside Europe. Less profitable banks in Europe and Japan had ratios below unity pre-crisis and they deteriorated even further thereafter. Although US and European banks' Contingent Convertible (CoCo) bonds have recovered sharply from COVID-19 induced lows (Chart 1.18), funding costs for such instruments are still recovering and are high relative to their pre-COVID levels (BIS, op. cit).

Chart 1.14 : EMs' Daily Flows (28-day moving average)



Note : Till December 28,2020.
Source : International Institute of Finance (IIF).

Chart 1.15 : Net Issuance of EM Bonds Abroad



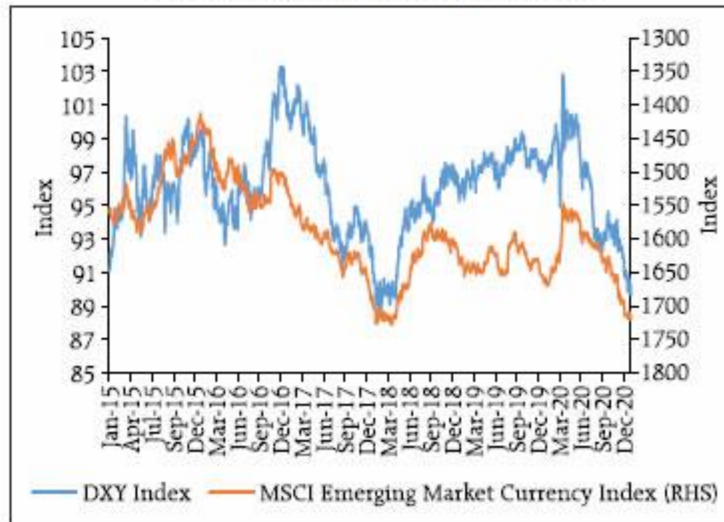
Source: IIF, Bloomberg.

Chart 1.16 : Emerging Market Bond Returns (Annualised)

Note: Information has been obtained from sources believed to be reliable, but J.P. Morgan does not warrant its completeness or accuracy. The index is used with permission. The index may not be copied, used or distributed without J.P.Morgan's prior written approval. Courtesy J.P. Morgan Chase & Co., Copyright 2020.

Source: JP Morgan.

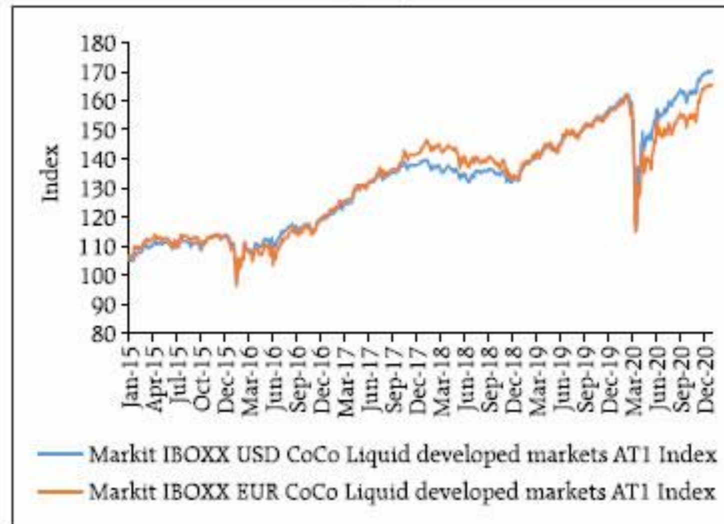
Chart 1.17 : Exchange Rates in AEs and EMs



Source: Bloomberg.

While globally regulators have encouraged banks in their jurisdictions to dip into their buffers to support the local economy, this has not yielded desired results uniformly. An analysis of key balance sheet parameters of banks across regulatory jurisdictions through the pandemic throws up interesting contrasts. While the growth in bank loans in Asia remained robust (largely driven by a sharp recovery in China), US banks have been aggressive in loan loss provisioning and the UK and European banks lead in common equity tier-1 (CET-1) capital augmentation (Charts 1.19 to 1.21).

Chart 1.18 : US and European Contingent Convertible Additional Tier-1 (AT-1) Index



Source: Bloomberg.

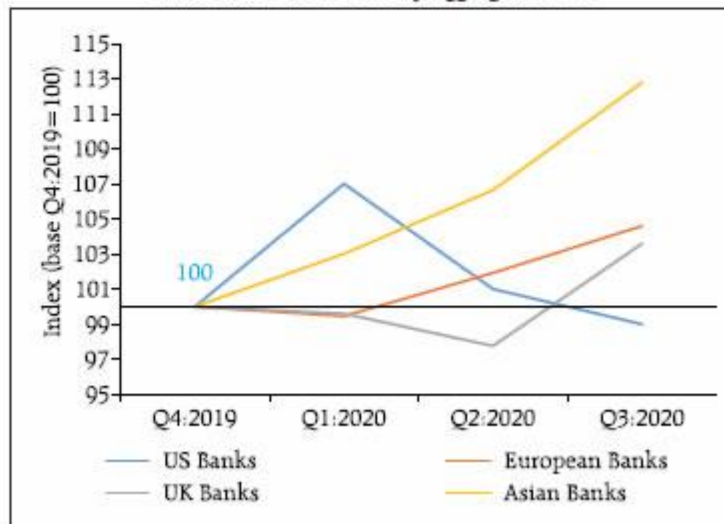


Chart 1.19 : Cross-Country Aggregate Loans

Source: Bloomberg.

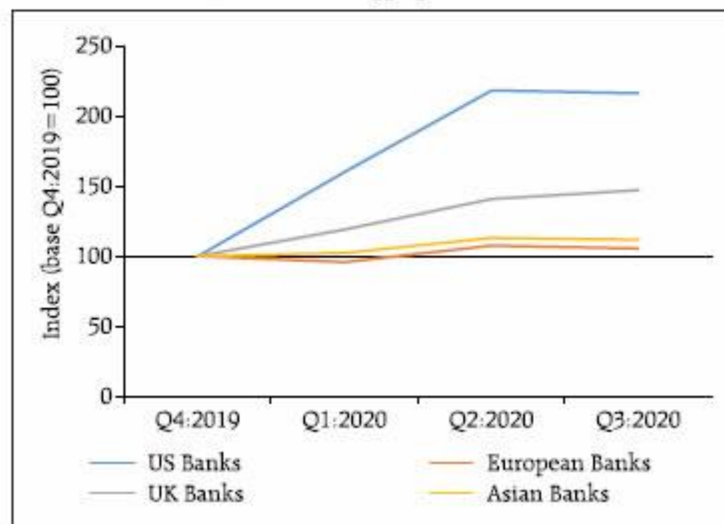


Chart 1.20 : Movement in Aggregate Loan Loss Reserves

Source: Bloomberg..

Summary

The adverse impact on government revenue and the resultant increase in sovereign borrowing in a period when fiscal authorities are also required to provide stimulus to economic growth is increasing sovereign debt to levels that have intensified concerns relating to sustainability with crowding out fears in respect of the private sector in terms of both volumes of financing and costs thereof.

The growing disconnect between certain segments of financial markets and real sector activity pointed out in the last FSR, has got further accentuated during the interregnum, with abundant liquidity spurring a reach for returns. Within the financial market spectrum too, the divergence in expectations in the equity market and the debt market has grown, both globally and in India.

Since the publication of the Financial Stability Report (FSR) of July 2020, there is

a much better assessment of the spread and depth of COVID-19 risks and their broader impact on global and domestic economic conditions. Although there has been a rapid recovery in economic activity from the lows of March and April, major non-financial indicators remain below pre-pandemic levels.

Domestically, corporate funding has been cushioned by policy measures and the loan moratorium announced in the face of the pandemic, but stresses would be visible with a lag. This has implications for the banking sector as corporate and banking sector vulnerabilities are interlinked. While the post-global financial crisis (GFC) prudential measures have ensured stronger capital buffers in the banking sector, which have stood banks in good stead in the face of the pandemic, the imminent crystallization of financial stress may test their resilience, especially for individual banks which, in turn, can have systemic implications. Banks need to prepare for these adversities by augmenting their capital bases to support their business plans and the broader economic recovery process in the post-COVID period. Moreover, while easy financial conditions are intended to support growth prospects they can have unintended consequences in terms of encouraging leverage, inflating asset prices, and fueling threats to financial stability. The pandemic has altered behavior and business models fundamentally. Policy authorities are striving to stay ahead by designing suitable responses.

Conclusion

Financial Institutions facilitate a conducive healthy environment for the employees and reskilling of the employees on new processes for ways of working. They enhancing customer-centric approaches through digital channels. RBI frame the policy for ensuring business continuity, Engage in partnership to optimize the process and enhance the experience. Reprioritize sectors and customer segments based on growth and risk profile. As the situation change due to the COVID-19 pandemic government encouraging people to design an innovative business model for the new industry environment. Focusing on build a robust digital ecosystem leveraging the latest technology.

References

1. Profit before Interest, depreciation, tax, amortization, and other adjustments
2. SEBI (2020): Circular no. SEBI/HO/MIRSD/CRADT/CIR/P/2020/53 dated March 30 2020 on “Relaxation from compliance with certain provisions of the circulars issued under SEBI (Credit Rating Agencies) Regulations, 1999 due to the COVID-19 pandemic and moratorium permitted by RBI“
3. The OFR FSI published by the Office of Financial Research, an independent bureau within the United States Department of the Treasury, incorporates five categories of indicators: credit, equity valuation, funding, safe assets, and volatility. The FSI shows stress contributions by three regions: the United States, other advanced economies, and emerging markets.
4. Bank for International Settlements (2020): “Box A: Banks through Covid-19”, BIS Quarterly Review, September 2020.
5. The G30 is an independent global body of economic and financial leaders from the public and private sectors and academia.
6. Observations based on the US yield curve as of December 3, 2020.

7. BIS (2020): “Markets rise despite subdued economic recovery”, BIS Quarterly Review, September.
8. The FAO Food Price Index (FFPI) is a measure of the monthly change in international prices of a basket of five food commodity groups, viz., vegetables, sugar, cereals, dairy, and meat. It consists of the average of five commodity group price indices weighted by the average export shares of each of the groups over 2014-2016.
9. Measured by debt to equity ratio and the debt to asset ratio.
10. For this SMA classification, for a borrower with exposure across multiple banks, the worst reported SMA status is considered as the applicable SMA position on a given date.
11. Based on summary monthly data from select 33 scheduled commercial banks, accounting for about 90 percent of the total non-food credit deployed by all scheduled commercial banks
12. Consumer credit includes home loans, loans against property, auto loans, two-wheeler loans, commercial vehicle loans, construction equipment loans, personal loans, credit cards, business loans, consumer durable loans, education loans, and gold loans.
13. A credit inquiry is created when any borrower applies for a loan and permits the lender to pull their credit record. Inquiries are among the first credit market measures to change in credit record data in response to changes in economic activity.
14. Commercial loans classified into various segments basis credit exposure aggregated at entity level. Micro less than ₹1 Crore, SME ₹1-₹25 Crores,
15. For a detailed methodology and basic indicators used under different BSI dimensions please refer to Annex 2.
16. This includes absorption / injection of daily liquidity, standing liquidity facility availed from RBI and Cash balance held in Central bank in excess / deficit of CRR requirements
17. MCLR of a large PSB.
18 .Details are given in Annex 1.