



## Warning of Higher NPAs

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### Why in News

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Recently, the **Reserve Bank of India (RBI)** Governor has warned that the economic impact of the **Covid-19 pandemic** would lead to higher **Non-performing Assets** and capital erosion of banks.

### Key Points

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- **Reasons:**
  - Just in a span of decade, Indian economy has been hit by the **global financial crisis of 2008-09** and the **Covid-19 pandemic in 2020**.
  - The current crisis may leave a longer impact on Indian economy, which is predicted to contract in the Financial Year (FY) 2020-21 for the first time in the past four decades.
  - Uncertainty about:
    - Full restoration of supply chains.
    - Normalisation of demand conditions.
    - Long term impact of the pandemic on India's potential growth.
- **Issues Involved:**
  - Banks have poor asset quality, lack of profitability, loss of capital, excessive risk exposure, poor conduct, and liquidity concerns.
  - There is also a **lack of a mechanism** to address bank failures.
  - Stress on **Non-banking Finance Companies (NBFCs)** and **mutual funds** are emerging as crucial stress points in the financial system.

- **Suggestions:**

- The RBI Governor has advised all financial intermediaries to assess the impact of Covid-19 on their balance sheet, asset quality, liquidity, profitability and capital adequacy for the FY 2020-21 and to work out possible mitigating measures.

The idea is to ensure continued credit supply to different sectors of the economy and maintain financial stability.

- Financial intermediaries should **make risk management** in tune with the emerging contingencies.

The risk management includes, building buffers and raising capital, which will strengthen the internal defences of banks against the risks posed by Covid-19 also ensure credit flow.

- **Recapitalisation plan** for Public Sector Banks (PSBs) and private banks since the **minimum capital requirements** of banks may no longer be sufficient enough to absorb the losses.

The minimum capital requirements of banks are calibrated based on historical loss events.

**Source: TH**