Is borrowing relief ending too soon? Post-lockdown income recovery and loan moratoriums in rural India

Britta Augsburg (britta_a@ifs.org.uk) is with the Institute for Fiscal Studies, UK and Bansi Malde (b.k.malde@kent.ac.uk) is with the University of Kent and the Institute for Fiscal Studies[1].

The Reserve Bank of India's loan repayment moratorium, announced at the end of March 2020 and extended to 31 August 2020, was conceptualised and implemented as a coronavirus crisis-response measure. While the moratorium ended, the coronavirus crisis has not. This commentary reports findings from a survey of 1452 rural microfinance clients in Maharashtra, conducted in July-August 2020. A critical majority of borrowers continue to experience significant income deficits, and will not be in a position to service their debts for the foreseeable future.

Keywords: COVID-19, moratorium, RBI, microfinance, repayment, poverty

Stringent restrictions imposed by governments to control the spread of COVID-19 have halted many economic activities, leading to job and revenue losses at unprecedented scale. India, which implemented a strict lockdown, has been particularly badly affected. GDP fell by a staggering 23.9% in the April–June 2020 quarter, compared with 2019. Efforts have been made to reopen the economy. However, this is occurring amid sharply rising numbers of COVID-19 cases and the imposition of sudden local lockdowns to bring these under control.

Serious knock-on effects of the prolonged shutdown and continuing coronavirus crisis are unfolding, including for the microfinance sector, which counts over 50 million low-income Indians among its clients. Disrupted household and enterprise cash flows have significantly impacted borrowers' ability to repay loans. The debt repayment moratorium given by the Reserve Bank of India for initially three and later six months provided welcome relief to borrowers, allowing them to suspend repayments without risking black marks on their credit scores. This has, however, come at the expense of microfinance institutions, many of which have not received similar debt relief measures from their own lenders.

While the decision not to extend the moratorium beyond 31 August might at first seem to support the recovery of microfinance institutions, loan-retrieval rates are unlikely to bounce back to pre-crisis levels any time soon. Since loans continued to accrue interest through the moratorium, households that availed themselves of the moratorium face a larger debt burden, even though incomes have not yet recovered to expected levels. A large proportion of microfinance clients are likely to be in a precarious financial position as the repayment moratorium has been relaxed.

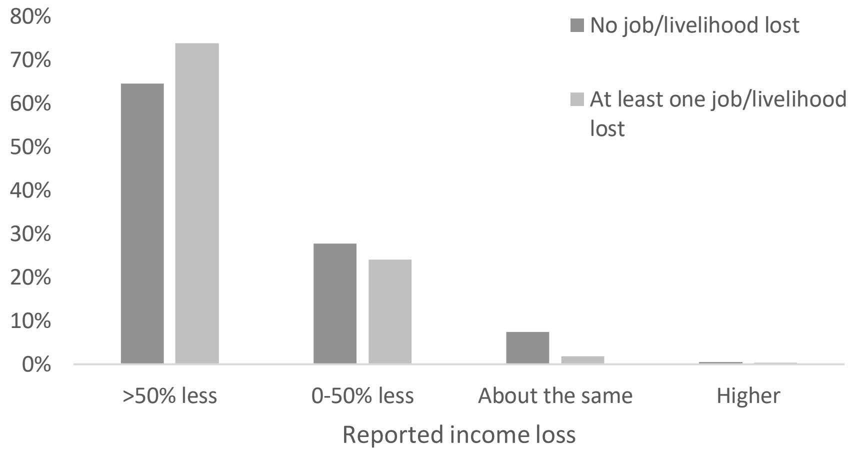
We reach this conclusion from a survey of 1,452 clients of a leading microfinance institution, living in rural areas of Latur and Nanded districts of Maharashtra state. These are areas dominated by agricultural activities: 35% of sample households receive their main income

[1] Contact details: Britta Augusburg, Institute for Fiscal Studies, 7 Ridgmount Street, London WC1E 7AE, UK. +442072914800; Bansi Malde, University of Kent School of Economics, Kennedy Building, Park Wood Road, Canterbury, Kent CT2 7FS, UK. Tel: +44 1227 816464

from cultivation of their own land, and a further 17% from agriculture and allied wage labour. Other households receive their primary income from other daily wage labour (18%), business ownership (16%) or salaried private jobs (11%).

Our data, collected in July–August 2020, shows that 54% of households experienced a job loss or earnings reduction since lockdown, with wage labourers, business owners and farmers worst affected. Though the national lockdown was relaxed at the end of May 2020, local lockdowns were imposed in Latur and Nanded districts with little warning in July, just prior to our phone survey. Consequently, incomes of the households in our sample lagged significantly behind what they would typically earn in July. Only 5% of households did not experience any income loss; and close to 70% reported income reductions of over 50% relative to the typical amount for July. Importantly, as Figure 1 reveals, income reductions are significant, even when households do not experience a complete job or livelihood loss. To cope with the income losses during lockdown, a third of households reported eating less food or skipping meals.

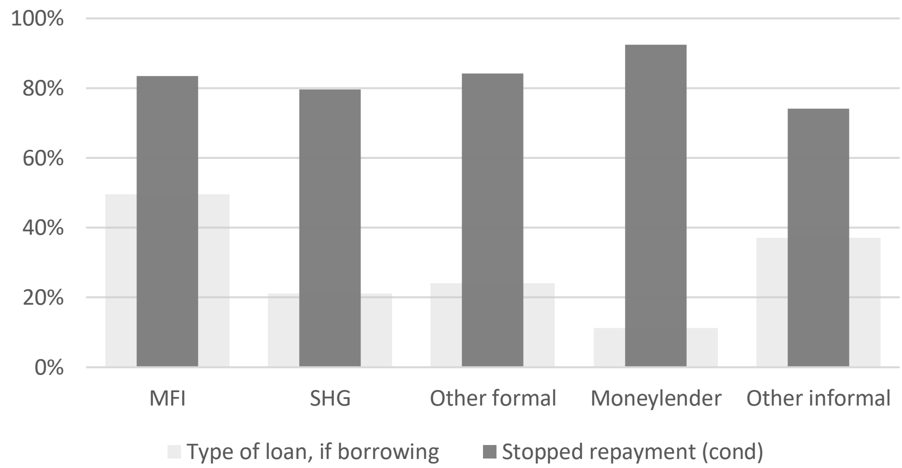
FIGURE 1: Distribution of total household income loss in past month by whether the household experienced any complete job, earnings or livelihood loss since start of lockdown



Notes: Source: Own phone survey. Percentage of households where at least one household member experienced a complete loss of job, earnings or livelihood (as compared to no loss with or without reduced income), by size of income loss.

Unsurprisingly, over four-fifths of households with an outstanding loan of more than INR 500 (80% of the sample) stopped making repayments during lockdown. Borrowers halted repayments on loans from formal and informal sources. Moneylenders, with whom 11% of borrower households had a loan outstanding (lightest grey bar in Figure 2), were those seeing the highest repayment stoppage rate, at 92% (darkest grey bar). Microfinance institutions (MFIs), with whom 50% of borrower households had a loan outstanding, saw 83% of their clients stop their repayments. Similar patterns have been documented by Malik et al (2020) for Pakistan.

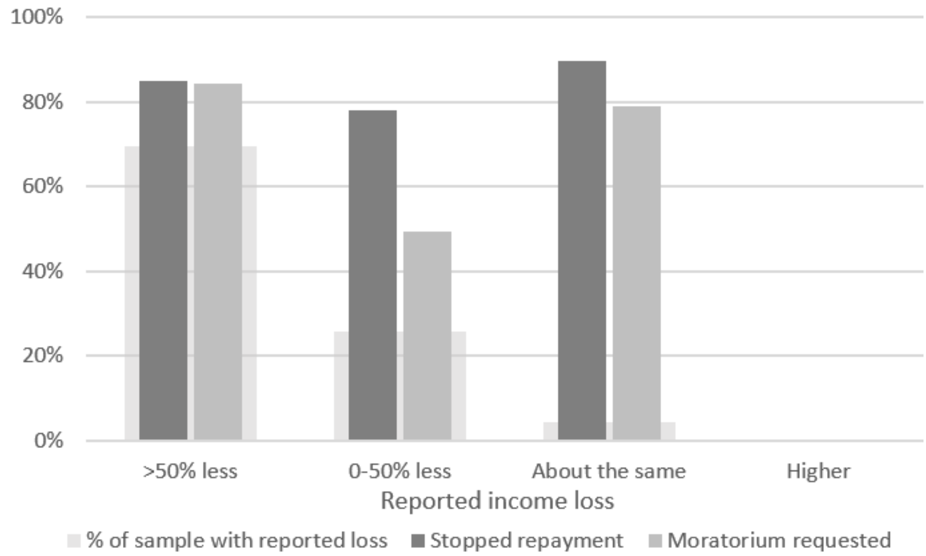
FIGURE 2: Loan repayment by lender type



Notes: Source: Own phone survey. The dark grey bars show the percentage of households that stopped repayment on an outstanding loan of more than INR 500 by lender type (conditional on having a loan outstanding). The light grey bars show the percentage of the sample that has a loan with the mentioned lender type outstanding. MFI = microfinance institutions; SHG = self-help groups.

While some sector experts are concerned that the moratorium might threaten repayment discipline and trigger moral hazard – with borrowers choosing not to repay loans even if they can afford to --, our data suggests that such concerns are overblown for rural microfinance clients. For the most part, households stopped repayments because they experienced significant income losses. As seen from Figure 3, households experiencing larger income losses are more likely to stop making loan repayments. We see a very similar pattern for moratorium requests. Households experiencing larger income losses are more likely to have requested a repayment moratorium. It is also true that households reporting no change in their incomes also stop making repayments and request a moratorium, but they comprise less than 5% of our sample.

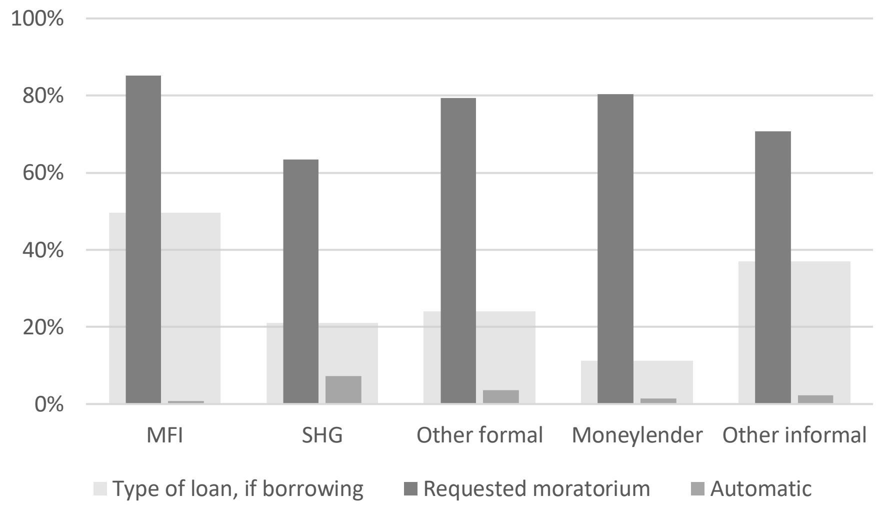
FIGURE 3: Loan repayment and requested moratorium by size of income loss



Notes: Source: Own phone survey. The dark and medium grey bars show respectively the percentage of households that stopped repayment on an outstanding loan of more than INR 500 by the size of their reported income loss and those that asked for a moratorium on it. The light grey bars show the percentage of the sample reporting the respective income loss category.

Overall, among those with an outstanding large loan at the onset of lockdown, 74% of households requested a moratorium, and a further 3% received one automatically from their lender (Figure 4). Take-up of loan repayment moratoriums was very high (80–85%) among borrowers with microfinance loans and loans from formal lenders other than MFIs or self-help groups (SHGs). Take-up was lower, though still high in absolute terms, among borrowers with SHG loans, with 60% requesting one and a further 7% receiving one automatically. Informal lenders also provided repayment moratoriums, with over 80% of borrowers with a moneylender loan receiving one and over 70% with loans from other informal lenders (i.e. family, friends and acquaintances).

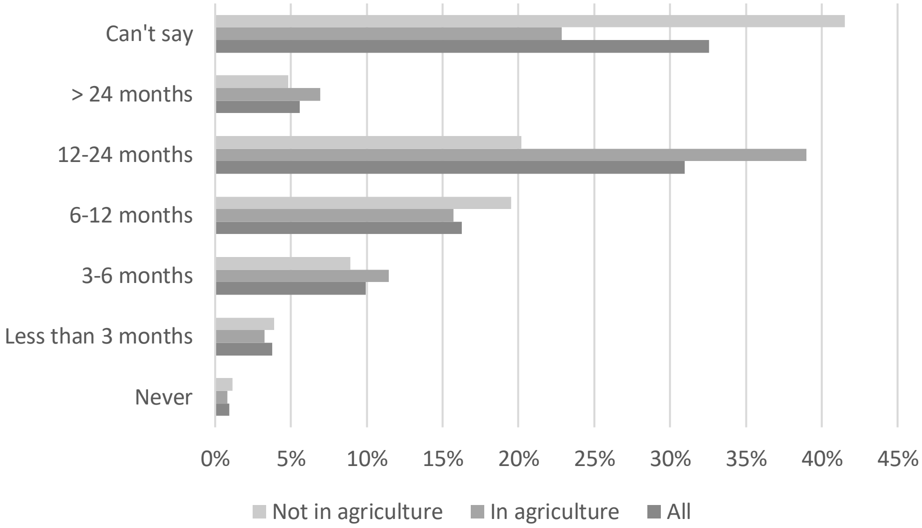
FIGURE 4: Moratorium by loan type



Notes: Source: Own phone survey. The dark and medium grey bars show respectively the percentage of households that requested a moratorium on an outstanding loan of more than INR 500 and the percentage that received one automatically, by the type of lender of the outstanding loan. The light grey bars show the percentage of the sample with a loan from that lender type. MFI = microfinance institutions; SHG = self-help groups.

As the moratorium is lifted, our data indicates that households will struggle to repay their loans. 44% of households were not able to meet their basic needs in late July/early August, and most households (96%) did not expect their incomes to recover to typical levels within the next three months. Figure 5 shows by when households expect their incomes to recover – for the whole sample and by whether households get income from agricultural activity or not. Only a third of respondents expect incomes to rebound within a year, with a further third expecting rebounds within 1–2 years. The remaining third of households are uncertain about when incomes will recover. The majority of those working in agriculture expect their incomes to recover within the next 12-24 months, in line with agricultural cycles. By contrast, households relying on incomes from the non-agricultural sectors are more uncertain about their economic prospects, with 42% unable to predict when their earnings will recover.

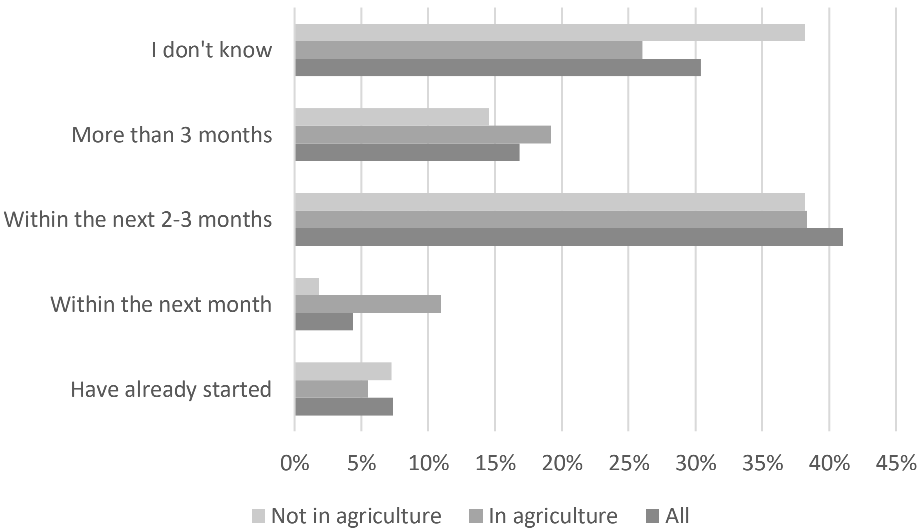
FIGURE 5: Expectations of when incomes will recover



Notes: Source: Own phone survey. The dark grey bars show responses for the whole sample, medium and light grey, respectively, for those for whom agricultural activities were the main income source, and those for whom agricultural activities were not the main income source.

Nonetheless, a majority of households with repayment moratoriums expect to start making repayments within the next three months (Figure 6). Without further Government support, it is likely that these repayments may be made at the expense of basic needs. Importantly, close to a third of households with repayment moratoriums, more so among those in non-agricultural sector, remained unsure about when they would be able to resume repayments, further underscoring the need for further Government support.

FIGURE 6: Expectations of when repayments will resume



Notes: Source: Own phone survey. The dark grey bars show responses for the whole sample, medium and light grey, respectively, for those for whom agricultural activities were the main income source, and those for whom agricultural activities were not the main income source.

Overall, the data indicates that concerns about moral hazard due to the loan repayment moratorium are overblown for rural microfinance clients. A critical majority of households continue to experience significant income deficits, and will not be in a position to service their debts. Rather than being pushed to make repayments, these households require support to manage their larger debt burdens. Such help should involve restructuring or rescheduling of loans, interest wavers, as currently being considered by the Government of India, and support to manage the debts. Fiscal measures targeting households served by microfinance institutions, including cash transfers, grants to micro and small enterprises or sustaining the expansion of the Mahatma Gandhi National Rural Employment Guarantee scheme are also needed. At the same time, support is also needed for smaller MFIs, who rely on loans from larger lenders as their key source of capital. The recently announced debt restructuring scheme from the RBI may help with this.

References

Malik, K., Meki, M., Morduch, J., Ogden, T., Quinn, S., and F. Said (2020), "COVID-19 and the Future of Microfinance: Evidence and Insights from Pakistan", Oxford Review of Economic Policy, Forthcoming.