

BANKING

05 June 2020

Apex court raises troubling spectre of interest waiver

The SC in a recent hearing expressed concerns over banks charging interest on loans under moratorium but has sought the government's reply on the matter. While we expect more clarity in the next hearing on 12 June, our estimates suggest 4-11% erosion in net worth of private banks in the event of a waiver. Apart from the financial impact, the risk of moral hazard would also rise as borrowers opting for moratorium could surge. ICICIBC, HDFCB and KMB remain our top picks in the sector.

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SC against levying interest on loans under moratorium: As per [media reports](#), the Supreme Court (SC) in its recent hearing on a petition seeking interest waiver during the moratorium period slammed RBI for permitting interest to be levied on such loans. The SC's view was that the economic aspect cannot be placed above peoples' health and that permitting a moratorium without interest relief would be more detrimental. It has sought the finance ministry's reply on the matter and deferred its next hearing to 12 June.

Loans availing moratorium could increase sharply: We agree with RBI's view that a waiver of interest would damage financial stability of the banking sector as a whole, given that banks would suffer a ~Rs 2tn (~1% of India's GDP) hit to interest income over the six-month moratorium period. We could further see a sharp rise in loans availing moratorium as borrowers currently honouring their dues may also queue up to seek relief. Such a move could also have a long-tail impact on asset quality and credit costs alongside the risk of moral hazard.

Net worth of banks could be eroded by 4-11%: Based on current data of loans availing moratorium, the net worth of private banks under our coverage could be depleted by 4-11%. We recommend sticking to banks with a robust liability franchise and strong capital position. ICICI Bank (ICICIBC), HDFC Bank (HDFCB) and Kotak Mahindra Bank (KMB) are our preferred picks in the sector.



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BUY – Expected return >+15%

ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

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