

RBI in its annual report assesses that the global outlook has once again turned grim and overcast with extreme uncertainty and downside risks. Compared to financial crises, a health crisis can be more pervasive, persistent and debilitating in its impact on the real economy noted RBI and the report says that India's near-term outlook is clouded, with an accentuation of downside risks and potential externalities of global spillovers. Bringing some cheer, the RBI report highlights even though with the removal of interim stay on asset classification standstill by the Supreme Court and waiving of interest on interest charged on loans during the moratorium period impacting the banks finances and thereby asset quality, banks are well capitalised and as per the report according to the stress tests, banks have sufficient capital at the aggregate level even in a severe stress scenario.

Coming to RBI's finances, the rebasing of the balance sheet to Apr-Mar meant that RBI's accounts were finalised for only nine months. The impact of the COVID-19 on RBI's finances are visible. Income for the nine months was no doubt less. But the expenditure contracted sharply due to significant reduction provision towards Contingency Fund (CF), leading to a higher available surplus. The CF provision was required as the available realised equity on Mar'21 base had fallen to 5% of the total assets. Thus as per recommendations of the Jalan Committee, the above provision was made to keep it at a level of 5.39%, same as on the previous valuation date. Further since realised equity plus the reserves is within 20-25.5% of the total assets it implies entire surplus of Rs 99,122 crore was transferred.

The printing cost has marginally declined and now Rs 500 denomination notes have 68.4% share in the total value of bank notes in circulation, which is 28,268.6 billion (y-o-y increase: 16.8%). However, there was an increase of 31.3% in counterfeit notes detected in the denomination of Rs 500 [Mahatma Gandhi (New) Series]. In the last two financial years RBI/banks detected almost 70,000 pieces of Rs 500 counterfeit notes which had combined value of Rs 35 lakh.

The economic activity has continued to decline with SBI Business activity index dipping to 61.4 for the week ended 24 May'21, the lowest since 25 May'20. However, there is a positive development this week. The rural penetration of COVID-19 infection which during the last week reached near the maximum achieved in 2020, has now declined modestly. Share of rural districts in new cases has come down to 51.7% for the week ended 26 May, compared to last week's 53.6%.

We reiterate that vaccination is the best policy going forward. Centre and State should adopt a cooperative rather than combative strategy in vaccine procurement as vaccine is a public good. With around 15-17 crore children in the 12-18 age bracket, India can go for an advanced procurement strategy like that adopted by developed nations to inoculate this age-group.

- ◆ Today, the Reserve Bank of India released its Annual Report for 2020-21. The Report covers the transition period of nine months (Jul' - Mar'21)

GLOBAL ECONOMY

- ◆ RBI in its annual report assesses that the global outlook has once again turned grim and overcast with extreme uncertainty and downside risks. Compared to financial crises, a health crisis can be more pervasive, persistent and debilitating in its impact on the real economy noted RBI.
- ◆ The pandemic has turned out to be highly inequitable – it is estimated that around 95 million additional people around the world have been forced into extreme poverty during the year, with 80 million more undernourished, mostly in low-income countries.
- ◆ Under these conditions, the global economy is projected to grow at 6.0% in 2021 by the IMF in its April 2021 World Economic Outlook. Downside risks tilt the balance: pandemic resurgence; tighter financial conditions; extended scarring; intensified social unrest; and geopolitical and trade frictions.
- ◆ Global trade is expected to accelerate. The IMF projects an expansion of 8.4% in trade volumes of goods and services (the WTO's projection of merchandise trade volume is 8.0%), although they will remain below the pre-pandemic trend.
- ◆ Cross-border services trade (tourism and transportation) is likely to remain subdued until the pandemic recedes globally, pandemic-related restrictions on international travel ease and confidence returns.

INDIA'S FINANCIAL SAVINGS MAY REACH 11.2% OF GNDI IN FY21

- The financial savings in FY20 increased to 7.8% of GNDI (SBI estimate was 7.6%) which was highest in last four fiscals. In absolute terms financial savings increased by Rs 5 lakh crore to Rs 16.1 lakh crore since FY16. RBI's preliminary estimates indicate an upsurge in household financial savings to 21.0% of GDP in Q1 FY21 vis-à-vis 4.0% in Q1 FY20, owing to the COVID-19 led reduction in discretionary expenditure and the associated surge in precautionary saving despite stagnant/reduced income. However, the financial savings waned substantially and its rate dropped to 10.4% of GDP in Q2 FY21 as households switched from essential only spending to discretionary spending with gradual reopening/unlocking of the economy. Using RBI's Q1 and Q2 numbers, we have estimated the financial savings for FY21. According to our estimate net financial savings may reach Rs 22.4 lakh crore (or 11.2% of GNDI) in FY21 as compared to Rs 16.1 lakh crore in FY20 (or 7.8% of GNDI). The substantial amount of increase is expected in currency and deposits.

ASSET QUALITY IMPROVEMENT: A SILVER LINING

- Amidst the COVID-19 pandemic hitting the economy in FY21, banks were provided cushion owing to steps including easier access to working capital; loan moratorium; asset classification standstill; permitting restructuring of viable accounts; and also postponement of planned roll-outs of prudential norms. All these steps enabled the GNPA of Scheduled commercial banks to decline to 6.8% in Dec'20 compared to 8.2% in Mar'20.
- Additionally, there has been an overall improvement in the provision coverage ratio of SCBs to 75.5% at end-Dec'20 from 66.6% in Mar'20 owing to prudent provisioning by banks and even over and above regulatory prescriptions for accounts availing moratorium and undergoing restructuring. Adjusting for write-offs, the PCR was 88.0%, up from 81.3% in Mar'20. Furthermore, the capital to risk weighted assets ratio of SCBs increased further to 15.9% by end-Dec'20 from 14.8% at end-Mar'20.
- The RBI report highlights that with the removal of interim stay on asset classification standstill by the Supreme Court and waiving of interest on interest charged on loans during the moratorium period may impact the banks finances and thereby on asset quality. **However, banks are well capitalised and as per the report according to the stress tests, banks have sufficient capital at the aggregate level even in a severe stress scenario.**

Financial Savings of the Household Sector						
	FY16	FY17	FY18	FY19	FY20	FY21 P
In Rs Lakh Crore						
A. Gross financial saving	15.0	16.1	20.6	21.3	22.8	28.2
<i>of which:</i>						
Currency	2.0	-3.3	4.8	2.7	2.9	4.7
Deposits	6.4	9.8	5.3	8.1	8.7	10.6
Shares and Debentures	0.3	1.7	1.8	0.8	0.8	1.3
Claims on Government	0.7	1.2	1.6	2.1	2.7	3.0
Insurance Funds	2.6	3.5	3.4	3.6	3.1	4.0
Provident and Pension funds	2.9	3.3	3.7	4.0	4.6	4.6
B. Financial Liabilities	3.9	4.7	7.4	7.9	6.6	5.8
Net Financial Saving (A-B)	11.1	11.5	13.2	13.6	16.1	22.4
% of GNDI						
A. Gross financial saving	10.7	10.4	11.9	11.1	11.0	14.1
<i>of which:</i>						
Currency	1.4	-2.1	2.8	1.4	1.4	2.4
Deposits	4.6	6.3	3.1	4.2	4.2	5.3
Shares and Debentures	0.2	1.1	1.0	0.4	0.4	0.7
Claims on Government	0.5	0.7	0.9	1.1	1.3	1.5
Insurance Funds	1.9	2.3	2.0	1.9	1.5	2.0
Provident and Pension funds	2.1	2.1	2.1	2.1	2.2	2.3
B. Financial Liabilities	2.7	3.0	4.3	4.1	3.2	2.9
Net Financial Saving (A-B)	7.9	7.3	7.6	7.1	7.8	11.2

Source: RBI, SBI Research, FY21 is SBI estimate

- Furthermore, the resumption of IBC, introduction of a pre-packaged insolvency mechanism for MSMEs to provide an easier resolution channel, the envisaged bad bank, and measures for developing market-based mechanisms for credit risk transfer, such as securitisation, transfer of loan exposures and development of secondary loan market will further help in reducing the stressed assets on the banks' balance sheets.

TRANSFER OF PROFITS

- The rebasing of the balance sheet to Apr-Mar meant that RBI's accounts were finalised for only nine months. This had obvious implications both for income and expenditure and calculation of economic capital as of Mar'21, eventually affecting the transfer of profits.
- The impact of the COVID-19 on RBI's finances are visible. Income for the nine months was no doubt less. The expenditure contracted sharply leading to a higher available surplus as the Rs 20,710 crore provision towards Contingency Fund was significantly lower than last year. The CF provision was required as the available realised equity on Mar'21 base had fallen to 5% of the total assets. Thus as per recommendations of the Jalan Committee, the above provision was made to keep it at a level of 5.39%, same as on the previous valuation date. Further since realised equity plus the reserves is within 20-25.5% of the total assets it implies entire surplus of Rs 99,122 crore was transferred.
- The steep contraction in expenditure and higher income is what has driven the transfer of profit this year. It needs to be seen if the same amount can be done for a full year next year.

CURRENCY COMPOSITION AND MANAGEMENT

- The number of banknotes has grown by 7.2% to 124.4 billion pieces as on Mar'21. Rs 2000 denomination notes have not been printed with its number going down to 2.5 billion pieces as on Mar'21, from 2.7 billion pieces in Mar'20. The biggest increase is in the printing of Rs 500 denomination notes, which rose to 38.7 billion pieces as on Mar'21, from 29.4 billion pieces in Mar'20. The number of small denomination notes (upto 100) has declined from 78.4 billion pieces as on Mar'20 to 77.4 billion pieces as on Mar'21, with the biggest decline in Rs 10 denomination followed by Rs100. Rs 200 denomination notes have seen a yearly increase of 0.5 billion pieces to 5.8 billion pieces in Mar'21. Denomination-wise the biggest number of banknotes in circulation is Rs 500 followed by Rs 100.
- The % composition of bank notes in value terms shows that Rs 500 denomination notes have 68.4% share in the total value of bank notes in circulation, which is 28,268.6 billion (y-o-y increase: 16.8%). The share of Rs 2000 denomination notes has come down to 17.3%. This was 50.2% in 2017, as the major focus was on remonetizing the economy. With printing of Rs 500 denomination notes taking precedence, due to ease of use, the value of Rs 2000 denomination notes has declined by Rs 1669.1 billion in the economy, from Mar'17 to Mar'21. The combined share of Rs 500 and Rs 2,000 banknotes was 85.7% in the total banknotes in circulation. Thus, the share of small denomination notes has come down to 14.1% as on Mar'21 from 16.6% as on Mar'20. However, it is still higher than the pre-demonetization level of 13.6%. But given the trend, it is quite likely that their share comes down even further next year.

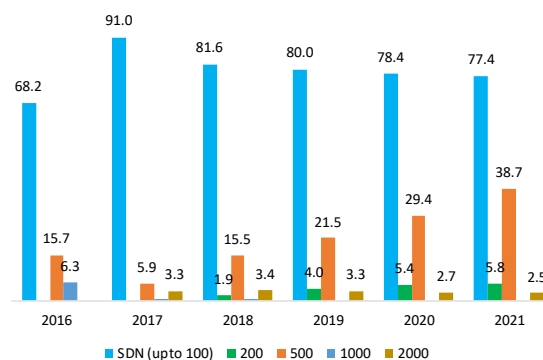
COUNTERFEIT NOTES

- Though there was a significant decline in counterfeit notes detected in FY21 (29.7%), there was an increase of 31.3% in counterfeit notes detected in the denomination of Rs 500 [Mahatma Gandhi (New) Series]. In the last two financial years RBI/banks detected almost 70,000 pieces of Rs 500 counterfeit notes which had combined value of Rs 35 lakh.

Disclaimer:

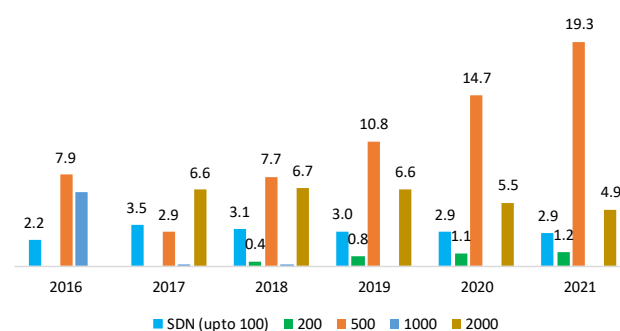
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Banknote Composition (billion pieces)



Source: SBI Research

Banknote Composition (Rs trillion)



Source: SBI Research

Denomination-wise Counterfeit Notes

Denomination (Rs)	Number of pieces			% YoY Change	
	FY19	FY20	FY21	FY20	FY21
2 & 5	-	22	9	-	-59.1
10	345	844	304	144.6	-64.0
20	818	510	267	-37.7	-47.6
50	36,875	47,454	24,802	28.7	-47.7
100	2,21,218	1,68,739	1,10,736	-23.7	-34.4
200	12,728	31,969	24,245	151.2	-24.2
500	971	11	9	-98.9	-18.2
500	21,865	30,054	39,453	37.5	31.3
1,000	717	72	2	-90.0	-97.2
2,000	21,847	17,020	8,798	-22.1	-48.3
Total	3,17,384	2,96,695	2,08,625	-6.5	-29.7

Source: RBI, SBI Research

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