



Mapping the Indian retail lending landscape – vol. 2.0

An overview of the sector's performance, impact of the COVID-19 second wave in Q1 FY22 and future trends

February 2022



Message from PwC



Asim Parashar
Partner, Financial Services
PwC India

Dear reader,

It is our pleasure to bring to you PwC's report on the performance of the retail lending sector in Q3 FY21 and Q1 FY22.

The report is part of a series of publications focusing on the evolution of India's retail lending sector during the COVID-19 pandemic. The last edition of the report covered the initial impact of the pandemic in the Indian retail lending space. As the sector was recovering from the pandemic's first wave, the country underwent a more devastating second wave in April–May 2021. This edition of the report covers the period between December 2020–June 2021 and analyses the retail lending sourcing and disbursement trends across several parameters like geography, product and lender type for both sourcing as well as delinquency. This report has been prepared in collaboration with our partner Equifax. The scope of this edition is limited to sourcing and delinquency trends in the retail lending market viewed across multiple lenses, including geographies, sectors, and products, covering in detail the actual mid-term impact of the pandemic.

While the industry is still plagued by the problems of suboptimal asset quality, we have also witnessed India becoming a global leader in terms of digital and technological innovation in the lending space. The pandemic has accelerated the digital transformation journey for lenders across the board.

As of January 2022, over 150 crore vaccine doses have been administered in India and 47% of the country's adult population is fully vaccinated.¹ The vaccination drive, coupled with digitisation adopted by lenders during the pandemic, will enable faster recovery. This will be a turning point for retail lending in India as financial institutions (FIs) gradually move towards adapting to newer ways of working and become resilient and agile.

We hope you find this report to be an informative and helpful read.

¹ <https://ourworldindata.org/covid-vaccinations?country=IND>

Message from Equifax



K. M. Nanaiah
Managing Director
Equifax Credit Information Services Pvt Ltd

The year 2020–21 was a challenging one for lenders and borrowers across the country due to the COVID-19 pandemic and subsequent lockdowns. Retail loans are the mainstay of the Indian lending sector. While the impact on the retail portfolio was minimised by the Reserve Bank of India’s (RBI) interventions through moratorium and restructuring, some underlying stress continues to exist in the repayment capacity of borrowers. This, coupled with the strain on the collection efforts, has resulted in an increased risk of slippages in retail portfolios of Indian lenders.

Equifax, in partnership with PwC, is pleased to bring to you the second edition of ‘Mapping the Indian retail lending landscape’. This report provides a comparative analysis of the pandemic’s impact on the Indian retail lending sector and insights into the trends in the Indian retail financial services industry – from disbursements to delinquencies by geography, product and lender type.

We sincerely believe that this report will provide insights into the lending industry and aid policymakers as we navigate the post-COVID impact and adopt the recovery strategies and policies for the new normal.

I would like to thank the teams from Equifax and PwC for their efforts in bringing out this report.



Table of contents

01	Introduction.....	05
	<ul style="list-style-type: none">• Macroeconomic impact of the second wave on the Indian economy• Retail lending scenario in India	
02	Comparative analysis of the impact of COVID waves on Indian retail lending...08	
	<ul style="list-style-type: none">• Geography-wise loan sourcing and delinquency trends• Product-wise trends• Loan portfolio based on FI type	
03	Key drivers of change.....	28
	<ul style="list-style-type: none">• Digitisation in retail lending• Embedded financing• Ecosystem buildout	
04	Conclusion.....	33

01 Introduction

The COVID-19 pandemic is one of the most important events in recent history which has had a profound impact on the global economy. It has affected global demand and supply worldwide, leading to a short-term recessionary trend in many countries, and cast a shadow on long-term growth. Both emerging and advanced economies were severely impacted in 2020 during the pandemic's first wave and the subsequent economic recovery was either slowed or severely affected with the outbreak of the second wave in 2021 across all major countries, including India. Disruptions and decreasing industrial output due to production cuts and workforce shortages led to business losses and liquidity crunches, resulting in layoffs and pay cuts, and increased unemployment. Apprehensive attitudes towards economic recovery have severely impacted consumption and investments. The pandemic-induced macroeconomic downtrends have deeply impacted the banking sector and the retail lending landscape.

Most countries worldwide have resumed their economic recovery journey post the second wave. The US economy grew at a rate of 6.7 % in the second quarter of 2021.² The economy of the European Union (EU) is also expected to grow by 5.0% annually.³ The Indian economy has also recovered well, registering a 8.4%⁴ annual growth in the second quarter of FY21.

1.1 Macroeconomic impact of the second wave on the Indian economy

The second wave of the pandemic affected India between the months of April–May 2021, resulting in severe consequences in the form of exponential growth in cases, reduced supplies of essential treatments, severely strained health infrastructure, and increased deaths, particularly among the young population.

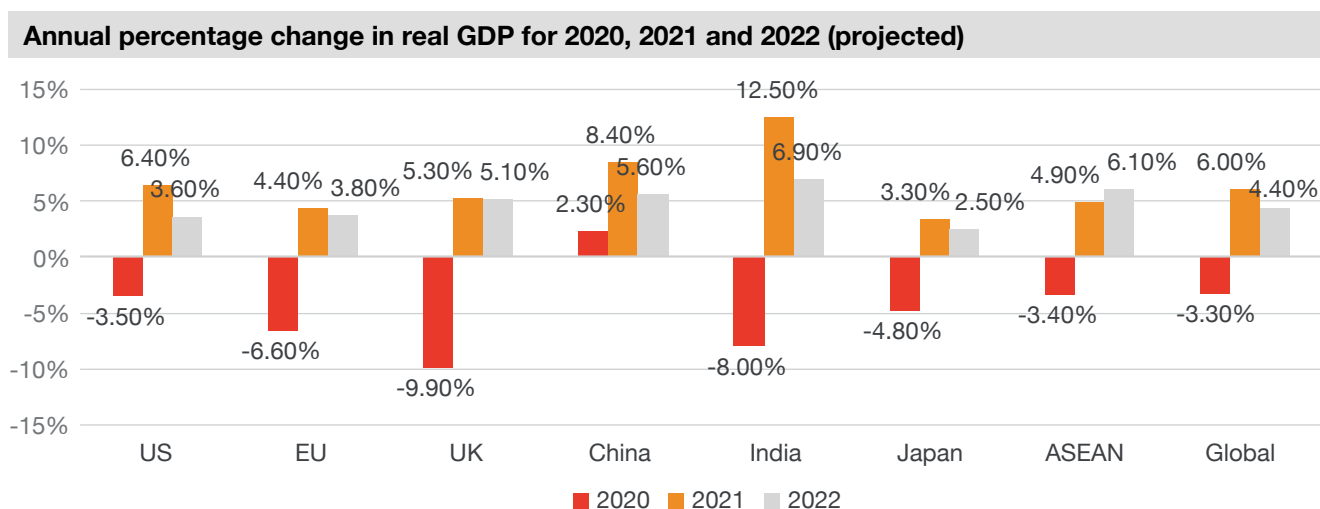
The second wave had a significant impact on India's economy as well, though quite different compared to that of the first wave. For instance, manufacturing and services, which fuel the urban economy, came to a grinding halt during the first wave while the rural economy continued to function because of less strict lockdowns. However, during the second wave, the share of COVID-19 cases in rural areas increased, resulting in rural economic activities being affected.

2 <https://www.bea.gov/news/2021/gross-domestic-product-3rd-quarter-2021-advance-estimate>

3 [https://ec.europa.eu/info/business-economy-euro/economic-performance-and-forecasts/economic-forecasts/autumn-2021-economic-forecast-recovery-expansion-amid-headwinds_en#:~:text=Growth%20in%20the%20EU%20is,euro%20area\)%2C%200.2%20pps.](https://ec.europa.eu/info/business-economy-euro/economic-performance-and-forecasts/economic-forecasts/autumn-2021-economic-forecast-recovery-expansion-amid-headwinds_en#:~:text=Growth%20in%20the%20EU%20is,euro%20area)%2C%200.2%20pps.)

4 <https://www.imf.org/en/Publications/REO/EU/Issues/2021/10/20/regional-economic-outlook-for-europe-october-2021>

GDP growth of major world economies



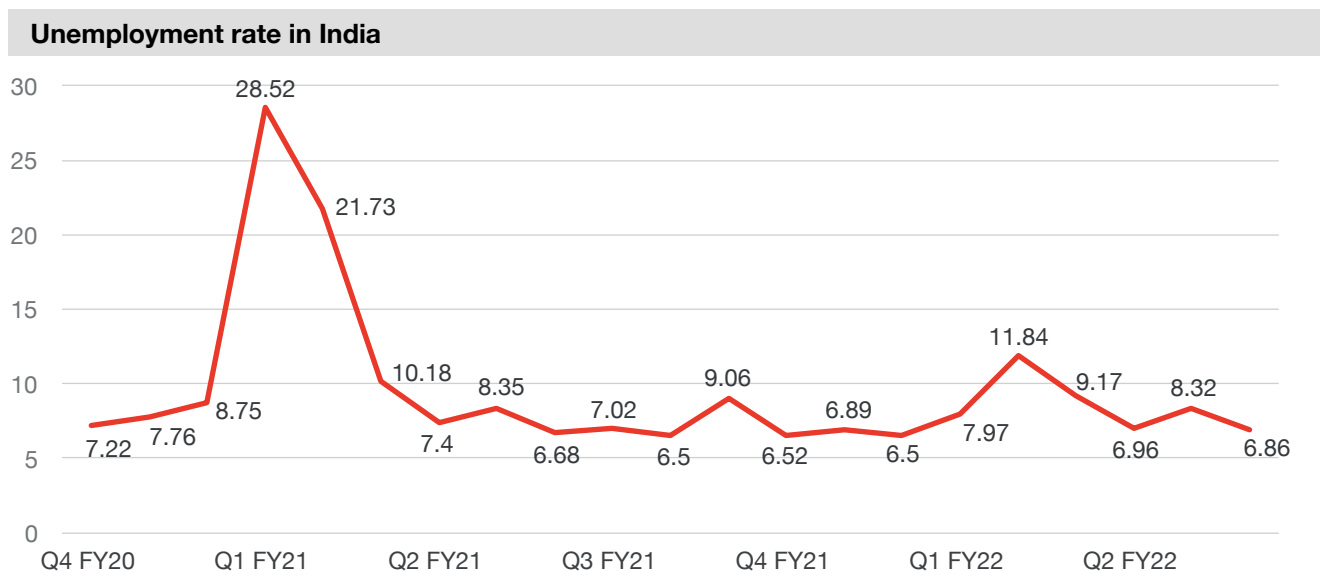
Source: International Monetary Fund (IMF)

The world nearly went into recession in 2020 with the global GDP growth shrinking by 3.3%. The pandemic led to cessation of activities across major economies, with only China registering a positive economic growth of merely 2.4%.⁵

Countries such as Italy and the UK were hit hard by the pandemic and saw major recessionary trends, with both of them registering 8.9% and 9.9% negative growth respectively.

The economic outlook for 2021 has been optimistic so far, with India projected to grow at 12.5%.⁶ However, post the devastating second wave, the projected growth figure has been revised to 9.5%, a correction of 300 basis points.

Unemployment trends in India



Source: Centre for Monitoring Indian Economy (CMIE)

⁵ <https://www.imf.org/en/Publications/WEO/Issues/2021/10/12/world-economic-outlook-october-2021>

⁶ <https://theprint.in/economy/imf-projects-12-5-growth-rate-for-india-in-2021-6-9-in-2022/635195/>



The unemployment in India increased exponentially during the first wave to a record high of 28.52% in April 2020, eventually decreasing to 21.73% in May 2020.⁷ The increase in unemployment rate is attributed to the strict lockdown imposed during this period.

However, during the peak of the second wave in May 2021, the unemployment rate increased to a maximum of 11.84%. This is less than half the peak unemployment rate during the first wave. A possible reason for the low unemployment rate during the second wave could be the localised lockdowns which allowed economic activities to continue in areas with low infection numbers.

Since then, the unemployment rate has come down to pre-COVID levels. The national unemployment rate for September 2021 was at 6.86%.⁸ The vaccination rate has increased significantly since the peak of the second wave. The demand for goods and services has also picked up during the festive season, leading to increased job opportunities in the Indian market.

1.2 Retail lending scenario in India

- Loans disbursed towards agriculture and allied activities showed an uptick to the tune of 11.4% in June 2021 compared to 2.4% in June 2020.⁹
- Retail loans – covering housing and vehicle loans – witnessed an accelerated growth of 11.9% in June 2021 compared to 10.4% a year ago.
- Retail credit grew at a year-on-year (YoY) rate of 16.6% up to 2019–20. The present rate of growth in retail lending is expected to remain below the pre-pandemic levels.

A glance at the provisioning and NPA situation in the Indian banking ecosystem

The gross non-performing assets (GNPA) had peaked in FY18 at 11.2% before falling to 9.1% in FY19 and further declining to 8.2% in FY20, right before the onset of the pandemic's first wave.¹⁰ However, the ratio of GNPA came down to 7.5% in September FY21 despite the pandemic and its economic impact. This is due to the RBI's six-month moratorium announced during the first wave to cushion the economic impact on retail borrowers.

The second wave led to further decline in the capacity of retail lenders to repay the loans. As a result, the NPAs of scheduled commercial banks (SCBs) in India are expected to rise to the tune of 9.8% by March 2022 as against 7.5% in March 2021.¹¹ The repayment capacity of lenders is expected to recover from the third quarter onward with the resumption of economic activities.

7 <https://unemploymentinindia.cmie.com/>

8 Ibid.

9 <https://www.rbi.org.in/Scripts/PublicationReportDetails.aspx?UrlPage=&ID=1180>

10 Ibid.

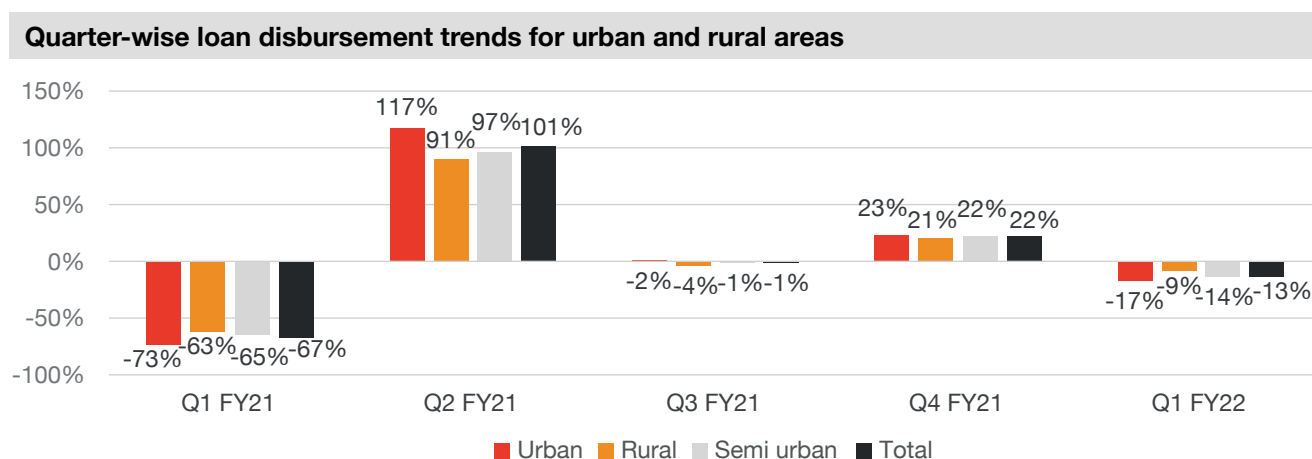
11 <https://rbi.org.in/Scripts/FsReports.aspx>

02 Comparative analysis of the impact of COVID waves on Indian retail lending

2.1 Geography-wise loan sourcing and delinquency trends

Since the outbreak of the pandemic in India, the country has seen two major waves, spaced roughly one year apart, during which the number of infections peaked. However, the impact has not been uniform across India as some states were significantly impacted while others managed the pandemic relatively better. Similarly, the impact on retail lending has varied across states as well as along the urban-rural divide. In the upcoming section, we will discuss how the pandemic impacted the retail lending ecosystem in India across various geographical differences and the factors contributing to this heterogeneous behaviour.

Urban vs rural trends of disbursement



Source: Equifax

Note: Data for retail lending products considered (auto, business, consumer, housing, personal, property, tractor, two-wheeler and used car loans)

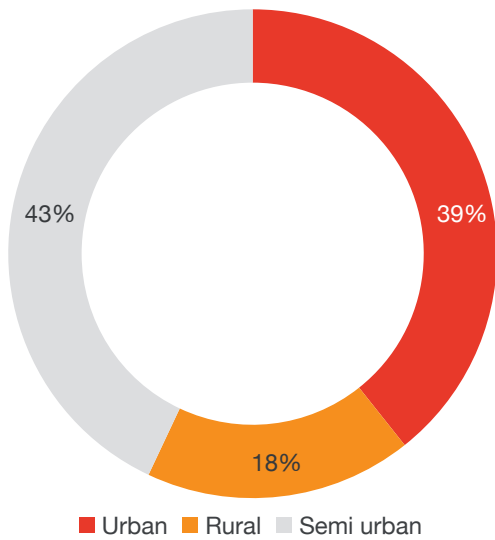
The number of new loans sanctioned decreased significantly across the spectrum with the onset of the pandemic. There was an overall decrease of 67% during the first quarter of FY21 owing to the lockdown and limited availability of a robust digital infrastructure.

The recovery in loans sanctioned started to improve from the mid of the second quarter, with September being the best month in the quarter. However, the stellar growth of 101% in sanctioned loans is largely owed to the low base effect from the previous quarter. The percentage of new loans sanctioned reached a healthy level of 22% by the fourth quarter owing to the announcement of a breakthrough in COVID-19 vaccines, opening of major activities of the economy and the commencement of the vaccination programme in India.

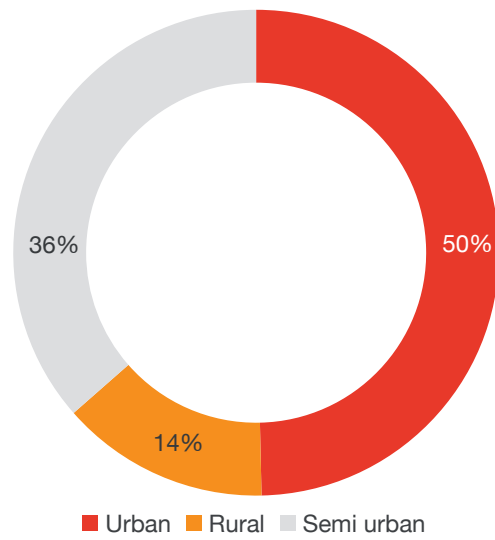
The growth in loans sanctioned grew to negative once again in the first quarter of FY22 due to the outbreak of the second wave. But compared to the average decline of 67%, the decline during the second wave was much lower at only 13%. From here onward, disbursements have picked up as the vaccination rate increased and the number of COVID-19 cases declined.

Urban vs rural trends for delinquency

Percentage distribution of delinquent accounts by rural/urban area



Percentage distribution of outstanding amount in delinquent accounts by rural/urban area



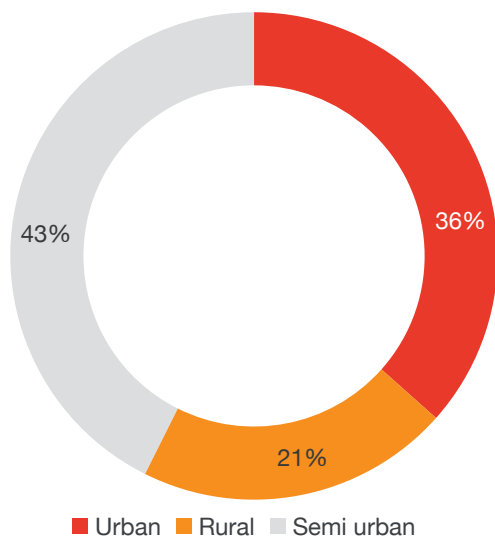
Source: Equifax

Note: Data for retail lending products considered (auto, business, consumer, housing, personal, property, tractor, two-wheeler and used car loans).

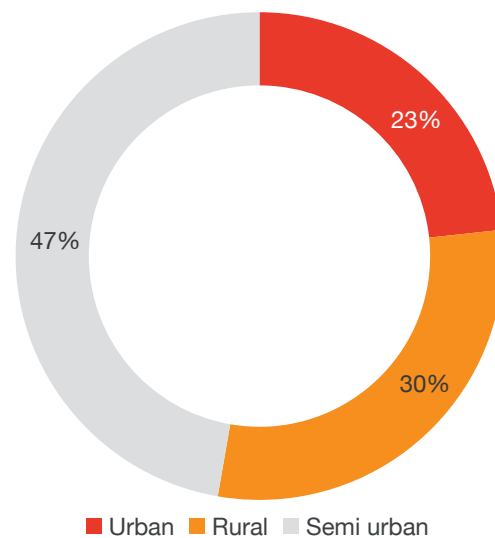
The highest number of accounts as well the amount outstanding in accounts that were restructured due to COVID-19 were the highest in semi-urban areas standing at 47% and 43% respectively.

Such a trend can be attributed to the lockdown which caused the loss of daily/casual jobs in urban areas, inducing reverse migration of the workforce to their native semi-urban areas.

Percentage distribution of number of accounts restructured due to COVID-19



Percentage distribution of amount outstanding in accounts restructured due to COVID-19



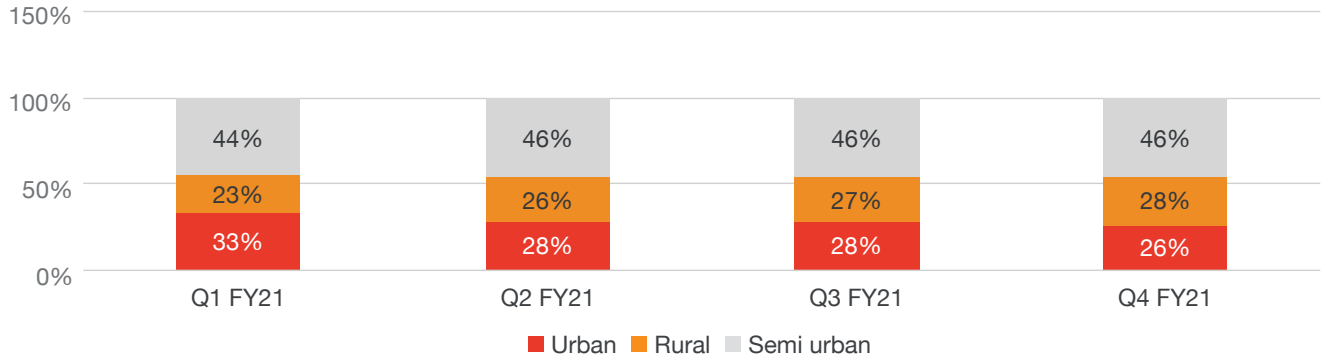
Source: Equifax

Note: Data for retail lending products considered (auto, business, consumer, housing, personal, property, tractor, two-wheeler and used car loans)

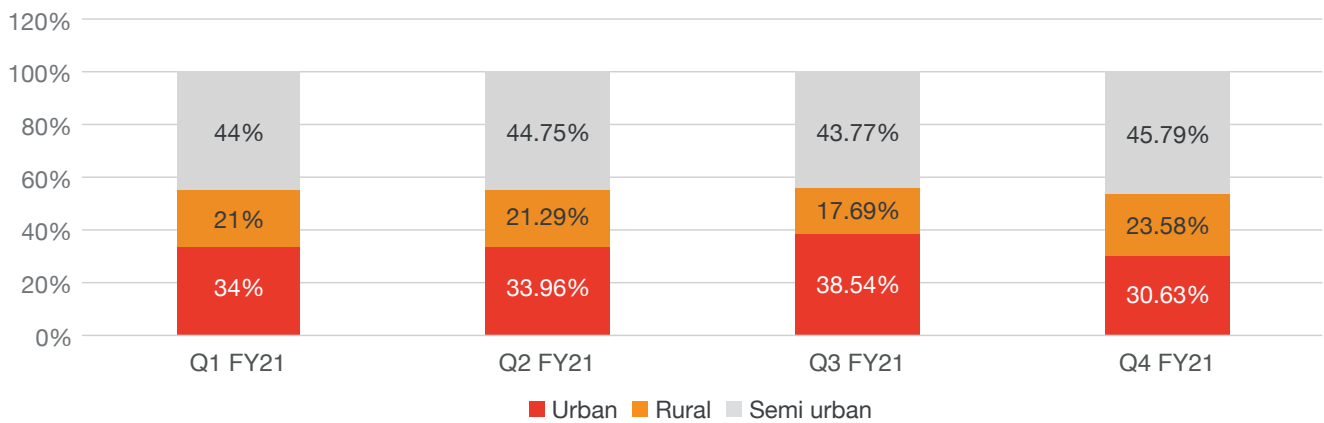
Looking at the quarter-on-quarter (QoQ) distribution of accounts in delinquency, the number of accounts in DPD 90 and DPD 120 is the highest among semi-urban and urban areas.

Such a high rate of delinquency among urban and semi-urban borrowers can be attributed to the higher dependency of urban household income on manufacturing and service sectors which were more severely impacted due to the pandemic and the subsequent lockdown, compared to agriculture. Job losses and reverse migration from urban areas are other two reasons for the high delinquency rate.

QoQ distribution of number of 90 DPD delinquent accounts by rural/urban area

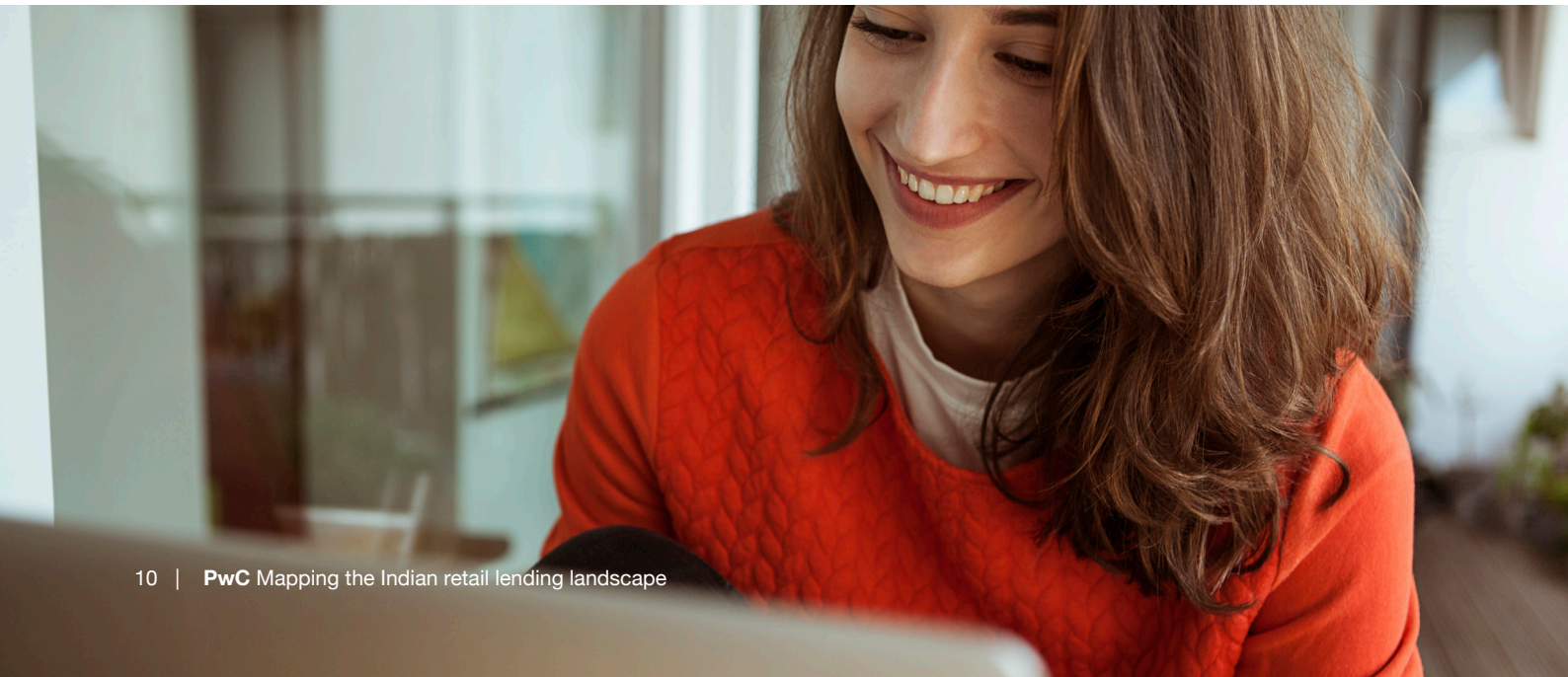


QoQ distribution of number of 120 DPD delinquent accounts by rural/urban area



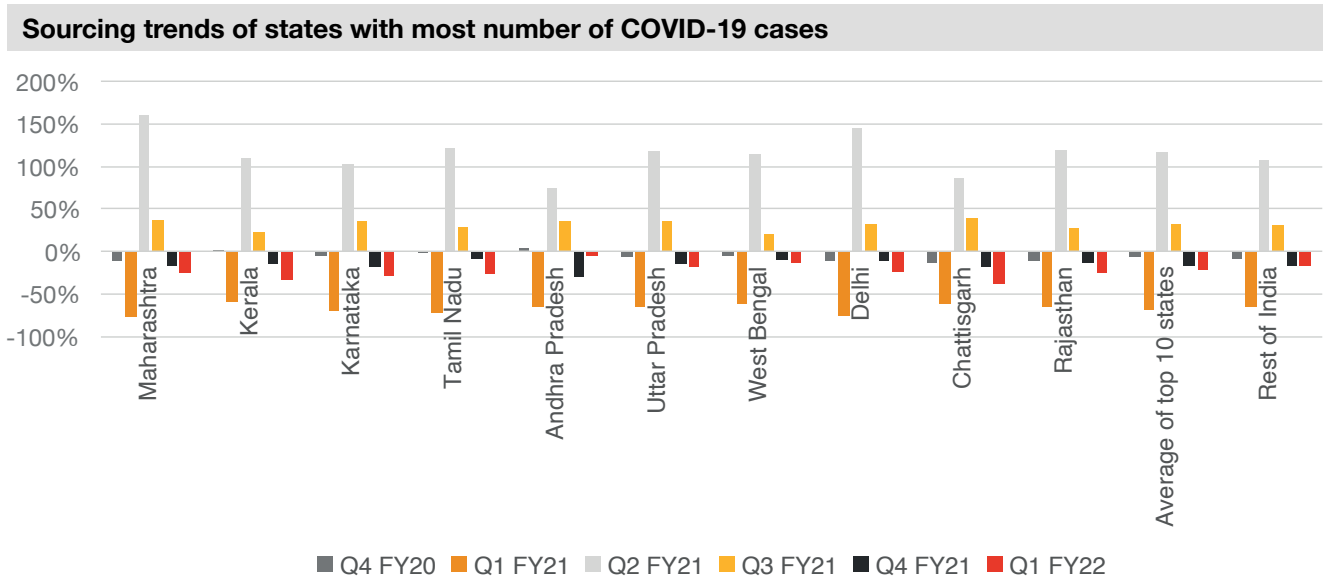
Source: Equifax

Note: Data for retail lending products considered (auto, business, consumer, housing, personal, property, tractor, two-wheeler and used car loans)



State-wise trends

State-wise trends for disbursement



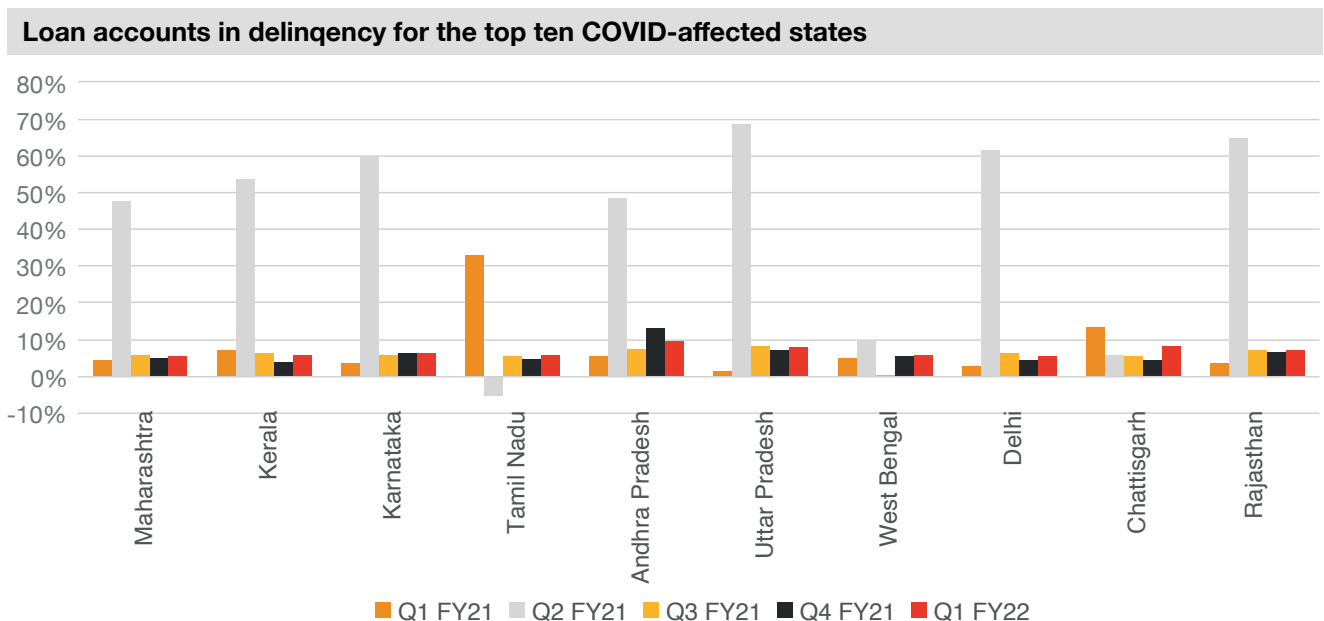
Source: Equifax

Note: Data for retail lending products considered (auto, business, consumer, housing, personal, property, tractor, two-wheeler and used car loans)

From the sourcing trends, it is evident that although the second wave was more severe than the first, the impact on lending was lesser compared to the first wave. The average decline in retail lending for the top ten COVID-19 impacted states during Q1 FY21 was -68.88% compared to 22.19% for Q1 FY22. The average for the rest of India stood at -65.00% and -15.78% respectively for the same period. This can be attributed to the fact that robust digital infrastructure was developed during the intervening period by most of the banks.

During the first wave, states like Maharashtra, Tamil Nadu and Delhi saw the highest contraction in loan disbursements, to the tune of 70% and more. During the outbreak of the second wave, states like Kerala and Chhattisgarh saw over 30% contraction in disbursements.

State-wise trends for delinquency



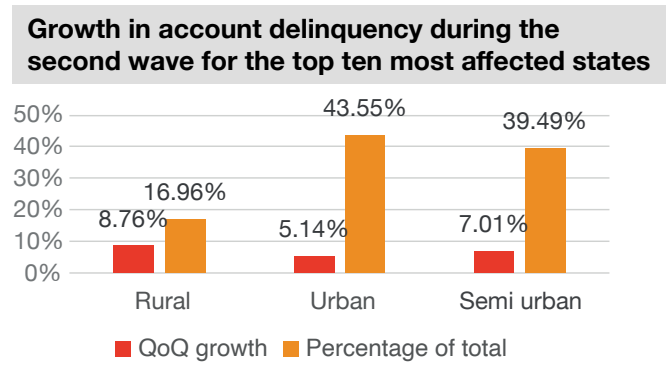
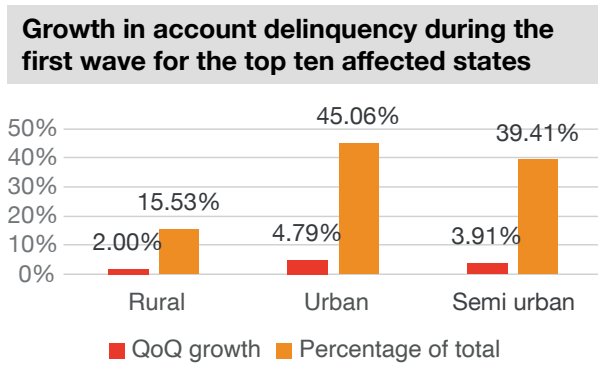
The number of delinquent accounts skyrocketed during the first wave, compounded by the nationwide lockdown which extended well into the second quarter of FY21, resulting in reverse migrations and halting of most economic activities barring the essential ones.

Due to the high number of job losses, a spike in auto-debit failures was also noticed, which indicate the pain for India's small borrowers during the pandemic.

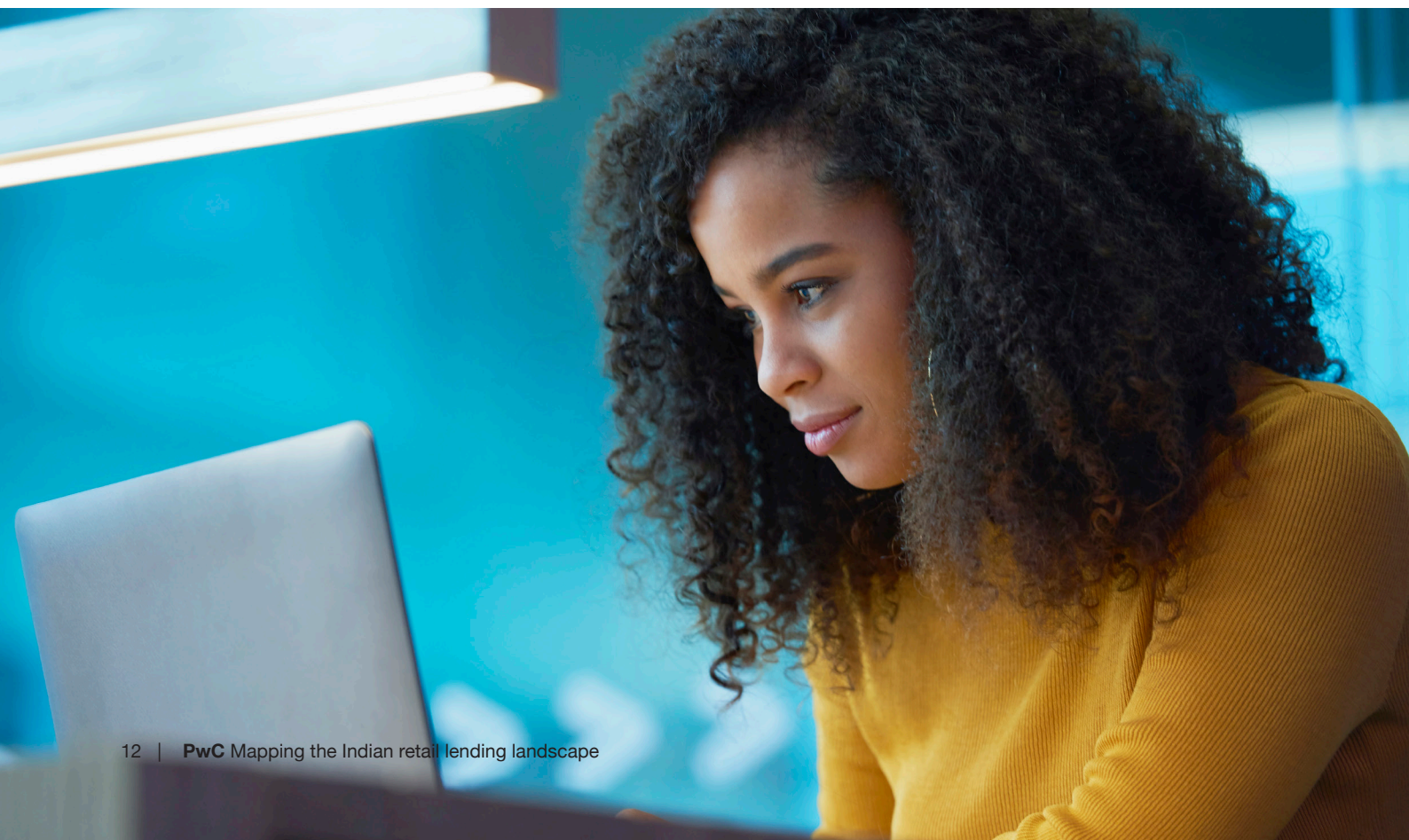
Another key attribute that has contributed to the higher delinquency rates is the hindrance to physical collections. The lack of digital infrastructure during the first wave compounded the problems for those who had the capacity to pay, but could not, due to severe restrictions in movement. Since then, the digital infrastructure has been ramped up, which could be one of the major reasons why the delinquency rates for retail loans was lower during the second wave.

Looking at the growth rates of accounts in delinquency for the top ten affected states, the share of the number of accounts in delinquency in rural, urban and semi-urban areas remained almost the same during both the waves.

However, the QoQ delinquency growth from Q4 FY21 to Q1 FY22 was the lowest for rural areas during the first wave while it was the highest for the same during the second wave. A similar uptick was noticed in the case of semi-urban areas.



Source: Equifax

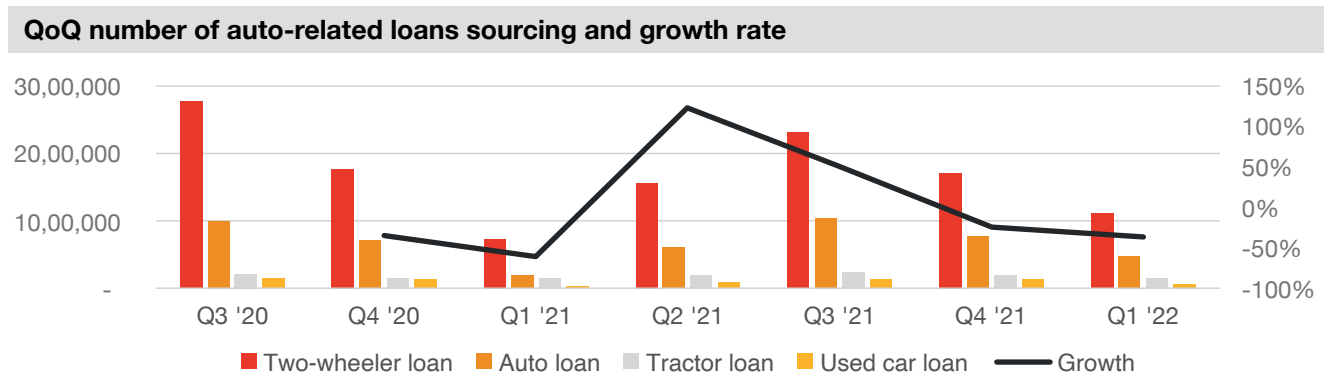


2.2 Product-wise trends

The pandemic has impacted different customer segments differently, affecting both sourcing as well as delinquency behaviour. In the upcoming section, we have broken down and analysed the sourcing and delinquency trends across different product types bucketed as auto-related loans, business and personal loans, and home and property loans.

2.1.1 Auto-related loans

Disbursement



Source: Equifax

The recovery in disbursements which started in Q1 FY21 continued till Q3, but the fear of a second wave and imminent lockdown had halted the growth with Q1 FY22 disbursement numbers clocking less than 50% of pre-COVID levels.

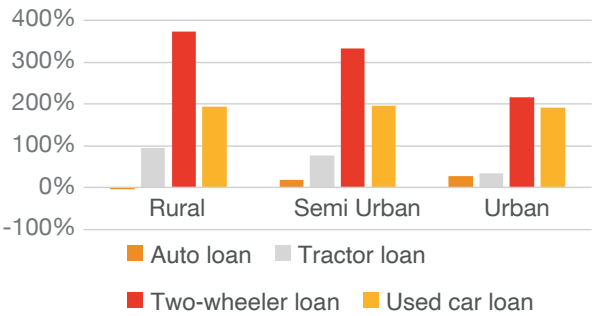
Two-wheeler loans lead the number of disbursements with an overall share of 64%. Post the first wave, consumers are spending more money on purchasing four wheelers with the average ticket size of auto loans growing year on year (YoY) by 22%, currently standing at INR 6.35 lakh. The lockdown induced reverse migration of salaried urban youth and subsequent decrease in monthly household expenditure could have attributed to this trend.

In the tractor loan segment, barring during the onset of the pandemic, there was no radical variation in terms of the number of tractor loan disbursements. This can be attributed to the higher-than-average rainfall, lower impact of lockdowns in rural areas and exclusion of agriculture from lockdowns.



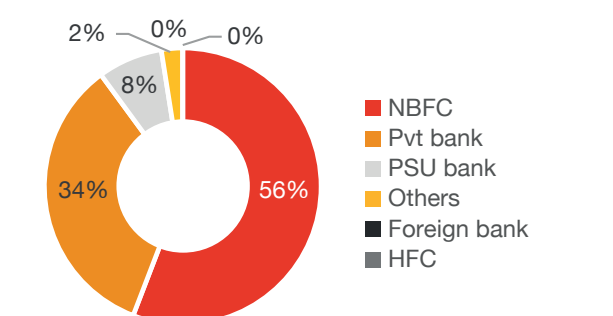


YoY (Q1 FY21 to Q1 FY22) growth rate of auto-related loans geography wise



Source: Equifax

YoY (Q1 FY21 to Q1 FY22) growth rate of auto-related loans geography wise

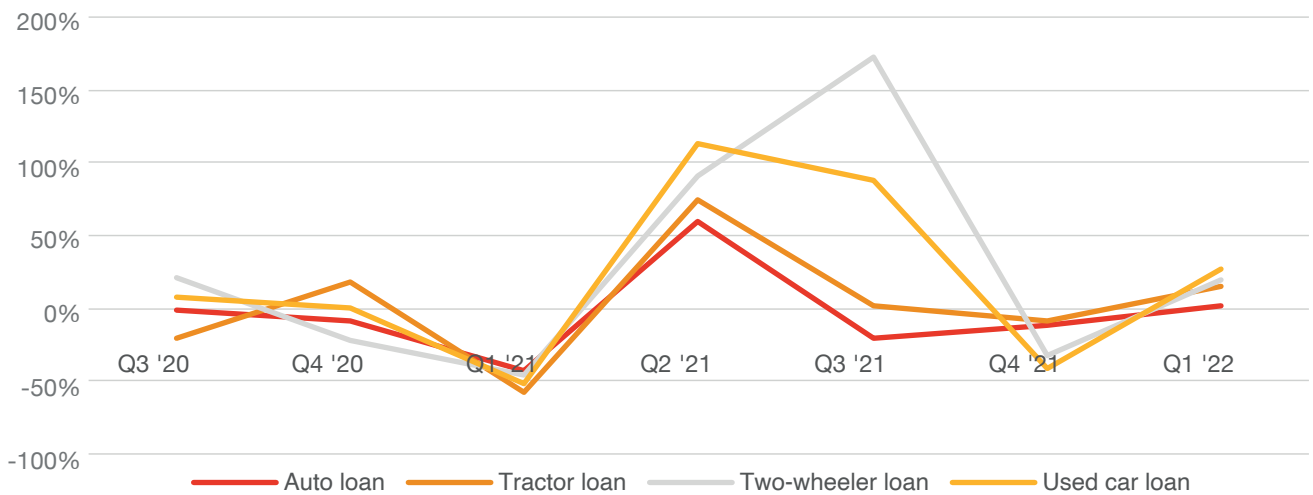


Source: Equifax

With customers moving away from public transportation and giving priority to safety and convenience, the number of auto-related disbursements have gone up by 200% with the highest increase seen in two-wheeler and used car loans. A higher number of used car loan disbursements was visible across geographies, possibly indicating these are first-time car buyers, while purchasing a new car has been the trend among urban customers.

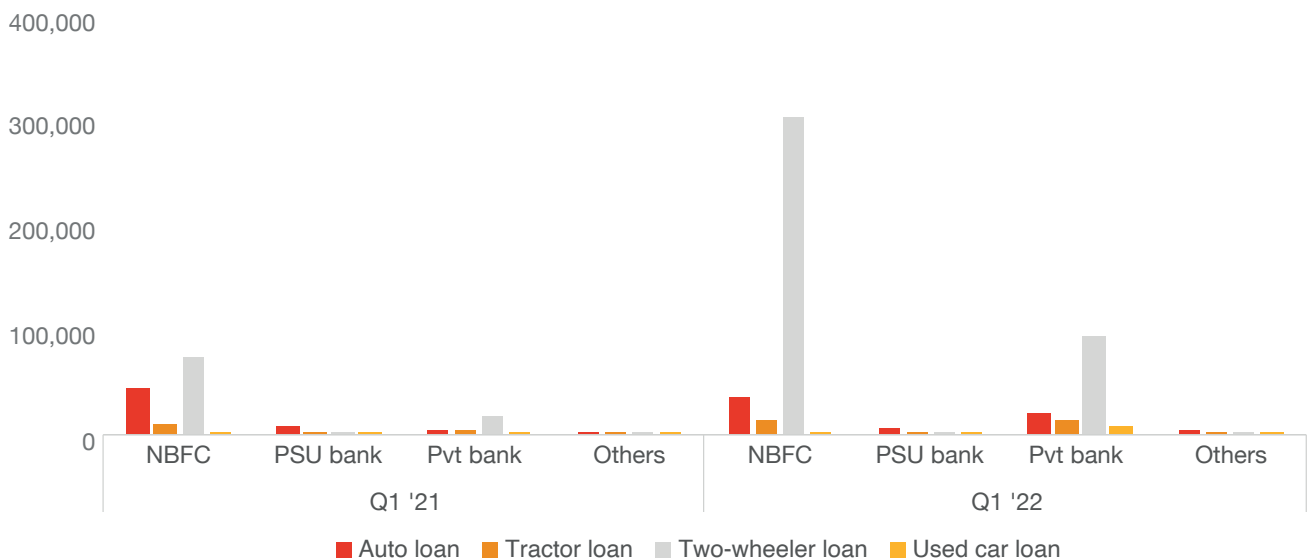
Non-banking finance companies (NBFCs) and private banks with their quicker processing time and wide distribution network have a combined share of 90% in the auto segment. Private banks have been able to leverage existing customer relationships and use data and analytics capabilities to provide preapproved offerings with minimal documentation.

QoQ growth rate for the number of DPD 90–120 accounts for auto-related loans



Source: Equifax

YoY (Q1 FY21 to Q1 FY22) sector wise number of auto related loans in DPD 90–120 category

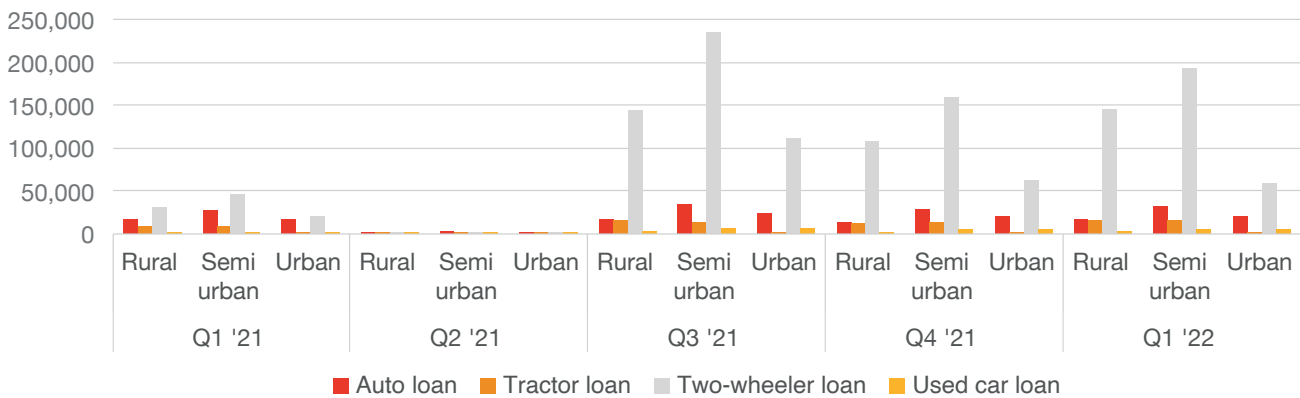


Source: Equifax

For the QoQ growth rate of delinquent accounts in the DPD 90–120 bucket, there was a dip in the growth rate in Q1 FY21 and a sharp rise in Q2 and Q3. This sharp rise in delinquent accounts post Q1 FY20 can be attributed to the end of the moratorium period in August 2020. The highest jump in delinquent accounts was observed for two-wheeler loans in the semi-urban geography, which can be attributed to the income loss for blue-collar workers and people working in the manufacturing sector which was significantly affected by the lockdowns. The work from home (WFH) option provided by major companies and online classes initiated by almost all educational institutions badly impacted the auto, cab and transportation sector, with assets lying idle and operators unable to make timely repayments. All this coupled with lower travel requirements of citizens, driver unavailability and localised lockdowns impacted the transportation industry negatively. With cashless repayment not reaching the desired level of penetration, a considerable number of lenders still rely on physical collection which was adversely impacted during the lockdowns.

The NBFC sector has been impacted more in the number of delinquent cases. Localised presence of smaller NBFCs, lack of a pan-India collection infrastructure and manual recovery processes could be some of the reasons for this trend.

Geography wise number of auto related loans in DPD 90-120 category

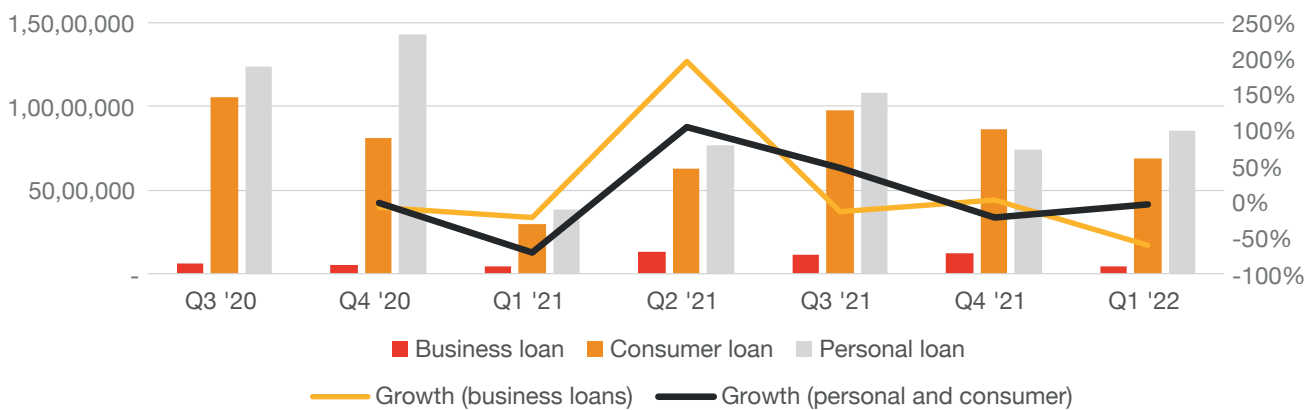


Source: Equifax

2.1.2 Personal, consumer and business loans

Disbursement

QoQ number of personal, consumer and business loans sourced and growth rate



Source: Equifax

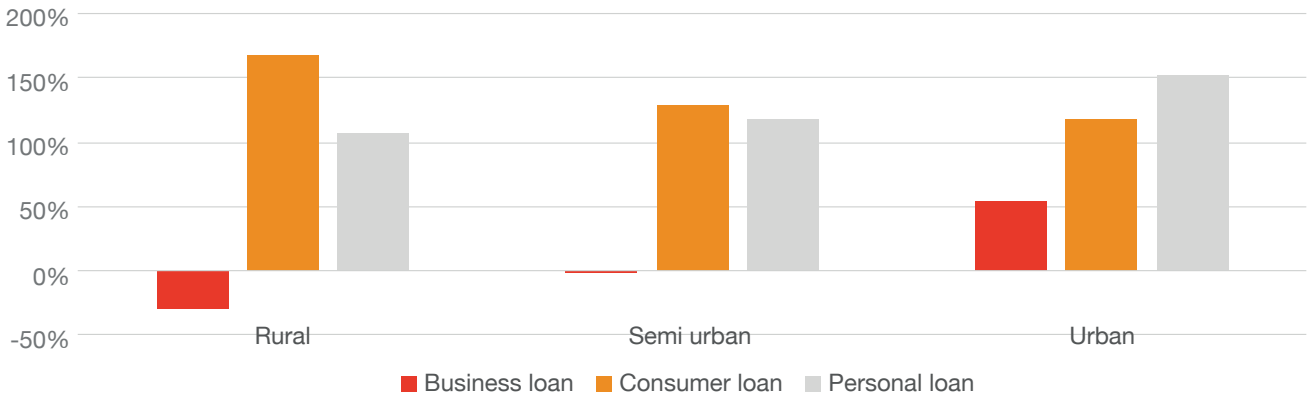
The pandemic and subsequent imposition of lockdowns have impacted small and medium enterprises (SME) owners the most. As state governments started to withdraw restrictions by the end of Q1 FY21, the subsequent quarter saw a 200% increase in the number of SME business loan sourcing, with sourcing levels in Q4 reaching two times compared to pre-COVID levels. However, the second wave severely impacted the business loan demand, with sourcing dropping by more than 50%. Various measures taken by the Government as a part of its Aatmanirbhar Bharat initiative to spur demand had a positive impact in the recovery journey post the first lockdown.

The pandemic resulted in 97%¹² of the households in the country reporting a decline in household income. Personal and consumer durable loans were negatively impacted in Q1 FY21 primarily because of the lack of contactless disbursement capabilities among FIs. However, this segment is picking up pace and is on track to attain pre-COVID disbursement levels. Even during the second wave, the sourcing of personal loans grew steadily while other product lines showed muted growth. The growth in personal loans can be attributed to the increased need-based demand coming in from educational and medical expenses.

FinTech NBFCs have led the charge in digital loan disbursements with smaller ticket sizes, customised product offerings and faster turnaround.

12 <https://www.cmie.com/kommon/bin/sr.php?kall=warticle&dt=20210517161425&msec=876&ver=pf>

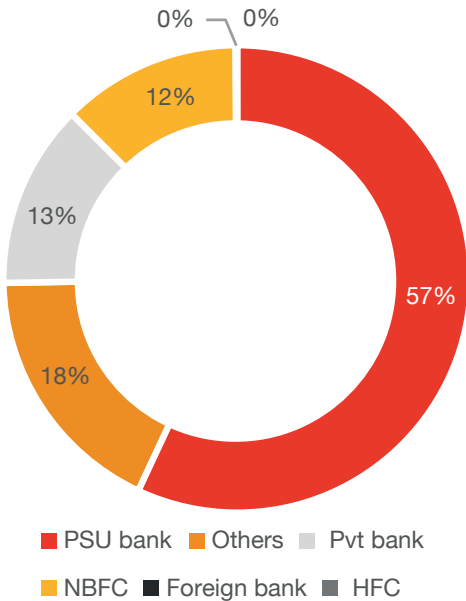
YoY (Q1 FY21 to Q1 FY22) growth rate of personal, consumer and business loans geography wise



Source: Equifax

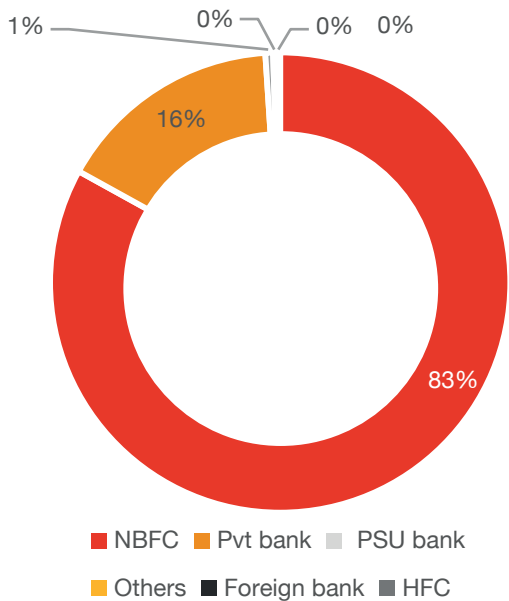
Consumer and personal loans have shown significant growth across geographies from the first wave till now. The demand for business loans has come down by 30% in rural areas and remained the same in semi-urban locations. With the prolonged lockdowns during the second wave, non-essential businesses were completely closed, thereby reducing the demand for business loans.

Share of business loan disbursement as on Q1 FY22



Source: Equifax

Share of personal and consumer loan disbursement as on Q1 FY22



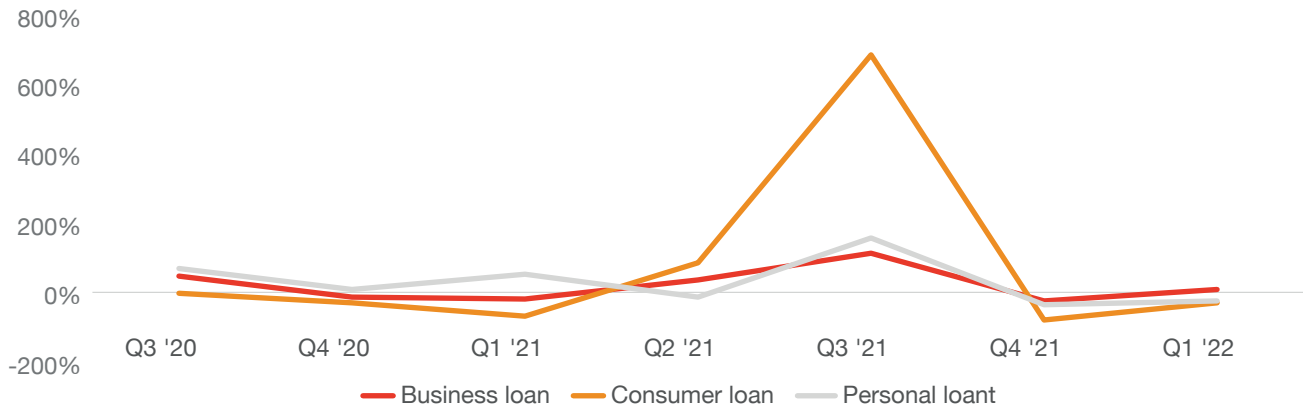
Source: Equifax

PSU banks have been key for pushing various Government schemes targeted at micro, small and medium enterprises (MSMEs). During the first wave, the Government had launched multiple schemes to help MSMEs tide over the crisis. Some of these schemes are the Credit Linked Capital Subsidy Scheme (CLCSS), overdraft interest rate rebate, collateral free loans and Emergency Credit Line Guarantee Scheme (ECLGS). The 57% share of PSUs in business loan disbursement is a testimony to the fact that PSU banks have played a key role in ensuring that these schemes reach end users.

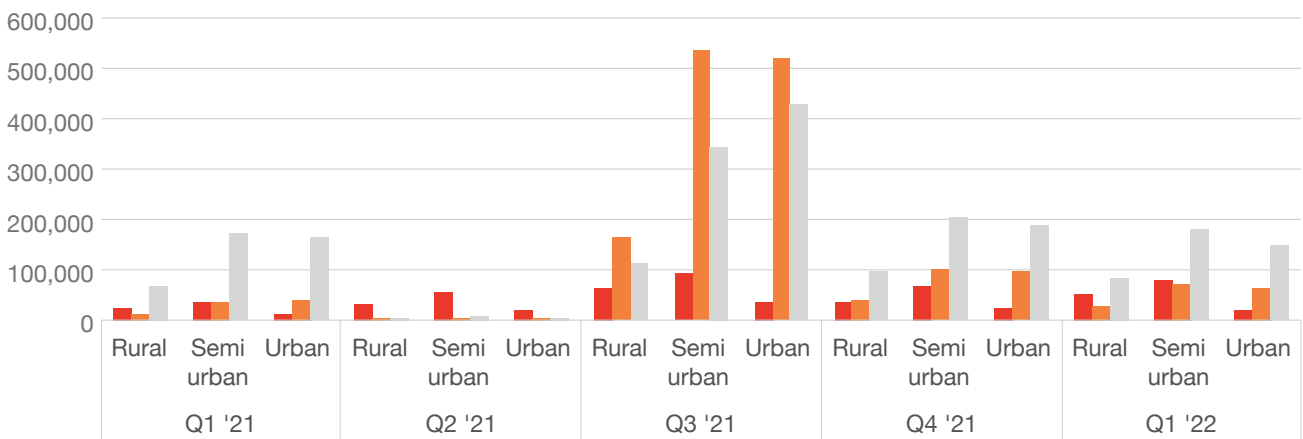
NBFCs have the highest share of personal and consumer durable loans. During the first wave, NBFCs and FinTechs were able to make quick changes in their existing processes and policies, and provide end-to-end digital experience to customers, thereby increasing efficiency and ensuring disbursement without face-to-face interaction. The period also saw the emergence of an increased number of FinTech NBFC players, especially in the personal loans and consumer durable space, providing a variety of targeted offerings to customers, including buy now pay later (BNPL) and credit line-based offerings. FinTech NBFCs saw increased disbursement but the average ticket size has decreased to 9,000. This segment saw 30% growth during the COVID period, with customers adopting mobile-only zero-contact offerings from FinTech players.

Delinquency

QoQ growth rate for the number of DPD 90–120 accounts for business, consumer and personal loans



Geography wise number of personal, consumer and business loans in DPD 90–120 category

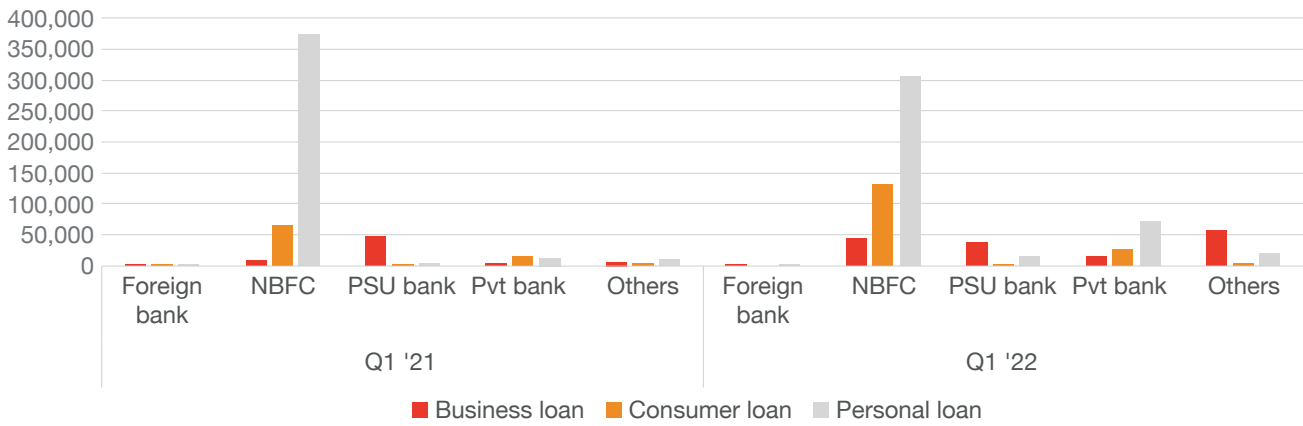


Source: Equifax

Delinquency cases were observed to be the highest in low ticket size loans like consumer and personal loans. The dependence on the manufacturing sector and agricultural income, and the subsequent reduction in household income during lockdowns can be attributed to the higher delinquency among the rural and semi-urban population. Fintech NBFCs, who have been leading the disbursements in the unsecured personal loans and consumer durable category with digital offerings like BNPL, have borne the maximum brunt. Business loans which have much more stringent credit policies coupled with physical verifications saw lower delinquencies. Also, this segment has better customer stickiness with customers opting for repeat loans, which might also be a contributing factor.



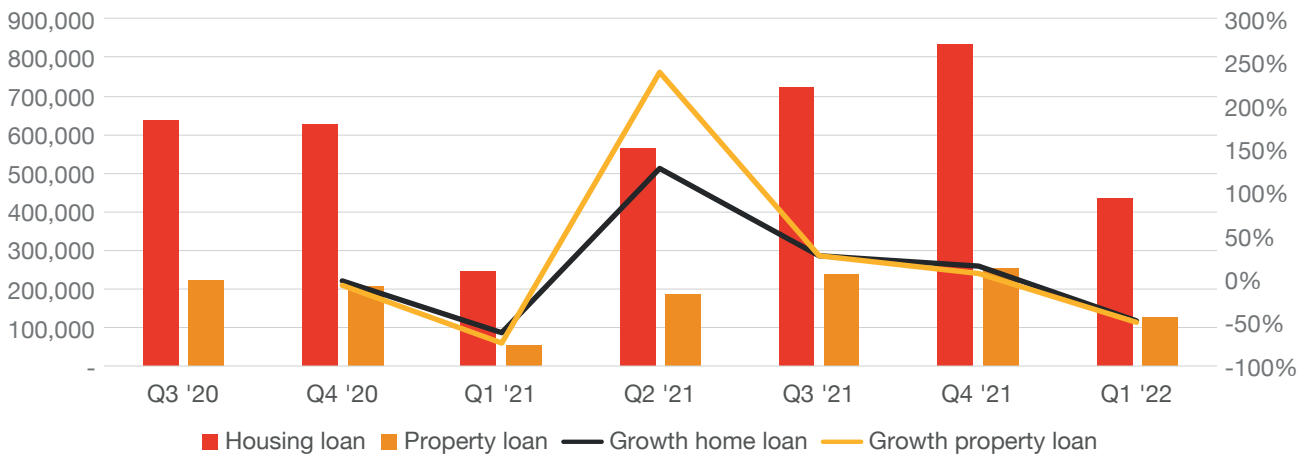
YoY (Q1 FY21 to Q1 FY22) sector-wise change in the number of loans in the DPD 90–120 category



2.1.3 Home loans and LAP

Disbursement

QoQ number of home loans and LAP sourced and growth rate



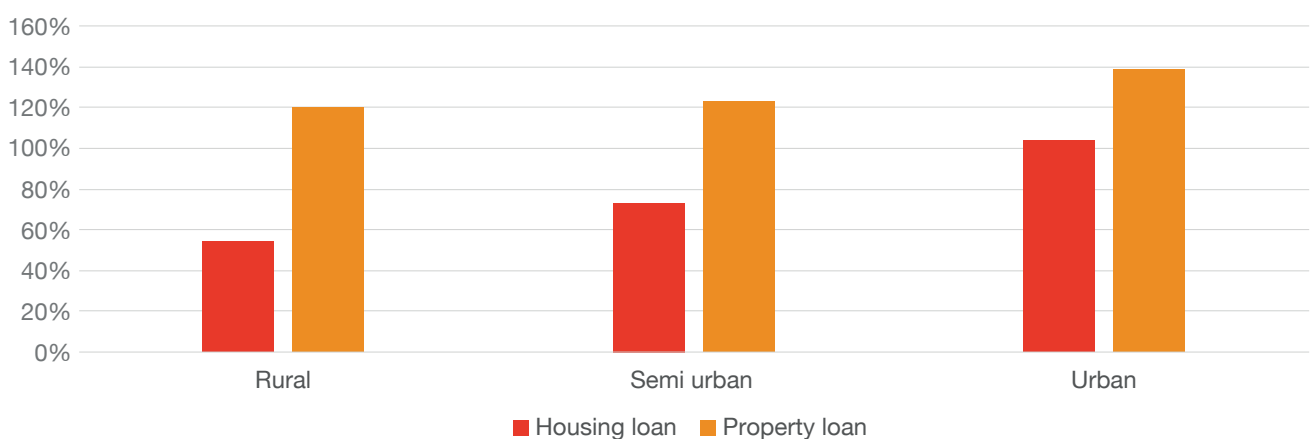
Source: Equifax

With uncertainties around the pandemic and an impending next wave, the demand for housing had declined to almost 60% during the first wave. The fall in interest rates coupled with various state governments reducing the stamp duty gave the much-needed push to home buyers and the demand increased continuously from Q2 FY20 and sourcing saw double digit growth till Q4 FY20, with 30% more disbursements in Q4 FY20 compared to the pre-COVID levels.

However, Q1 FY21 saw the demand crashing down by 50%. Onset of the second wave, lockdown-induced restrictions, unavailability of labour and increase in the price of raw materials could have contributed to customers postponing their purchase decisions.



YoY (Q1 FY21 to Q1 FY22) growth rate of home and property loans (geography wise)

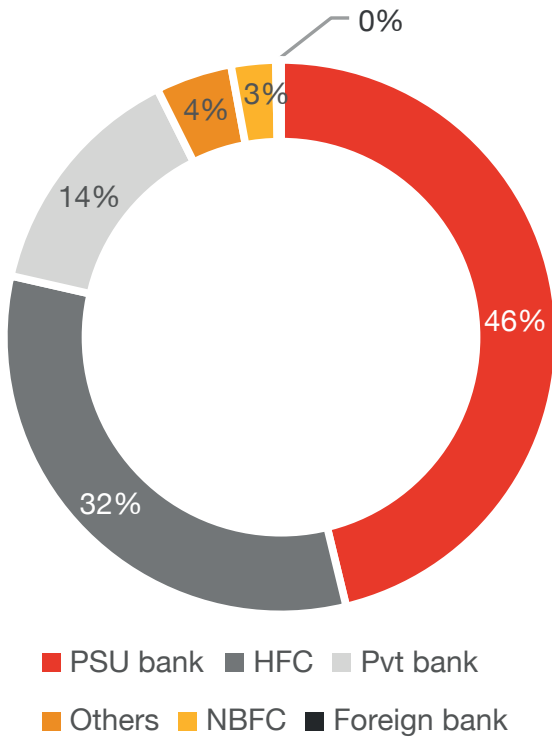


Source: Equifax

Demand for both home and property loans saw an uptick across geographies.

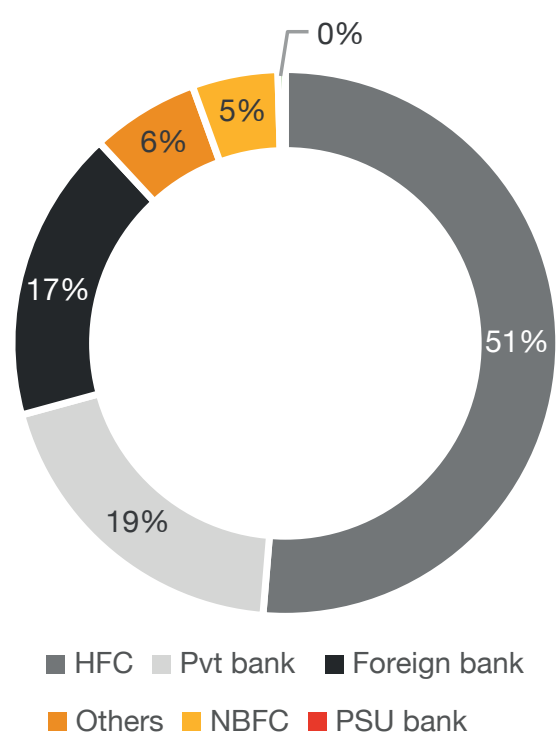
The average ticket size for home loans has gone up by 14%. The extension of WFH could be one of the reasons behind the increased need for spaciousness among consumers. The average ticket size for LAP has gone down by 7%, with businesses focusing on survival rather than expansion.

Share of business loan disbursement as on Q1 FY22



Source: Equifax

Share of personal and consumer loan disbursement as on Q1 FY22



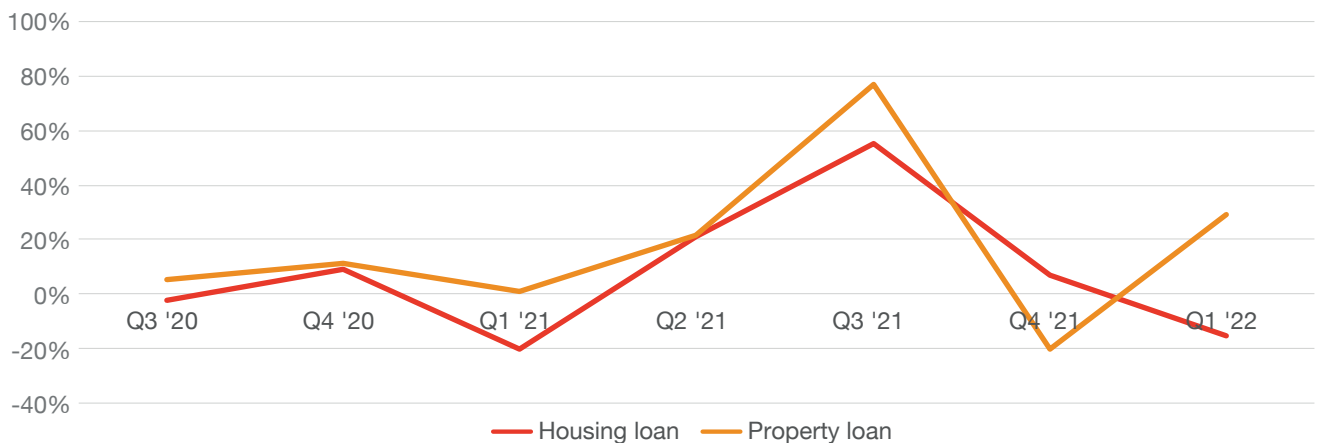
Source: Equifax

PSU banks were the first to pass on the benefit of reduced interest rates to their customers. Such banks (followed by housing finance companies [HFCs]) lead the home loan segment with reduced interest rates and a wide distribution network. Leading PSU banks have also launched credit score based differential interest rate schemes where customers with higher credit scores (>750) are offered better interest rates.

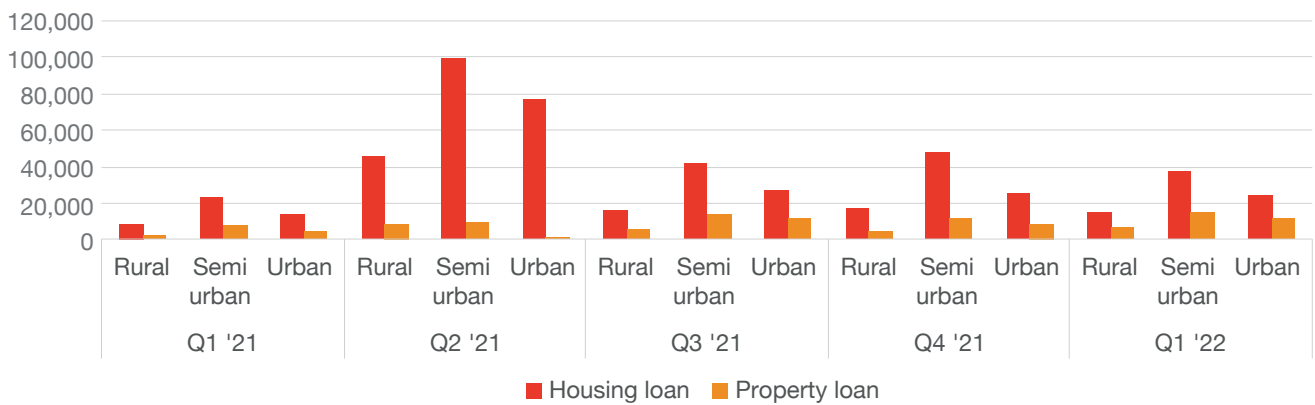
In the case of loan against property (LAP), the primary consumers are small business owners who often don't prefer going through the detailed documentation process and opt for an HFC or a private bank which disburses the loan amount faster. HFCs and private banks have a combined share of 70% in this segment.

Delinquency

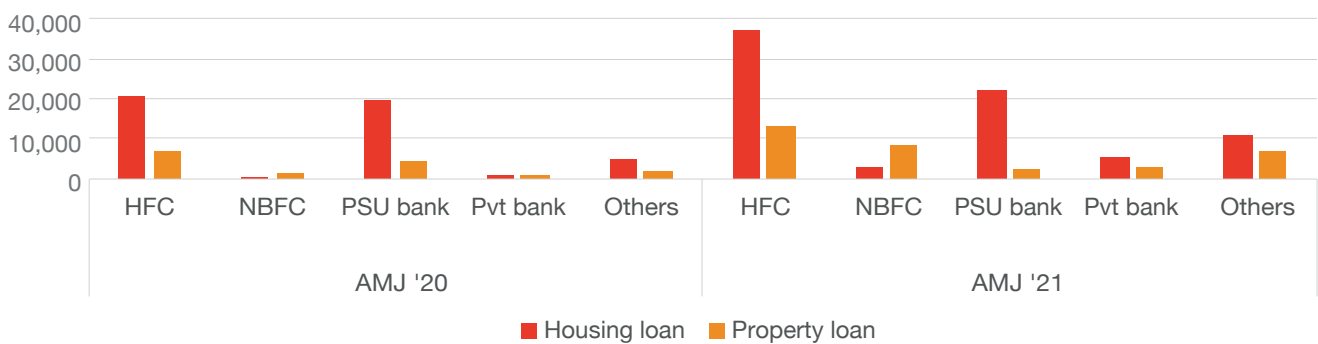
QoQ growth rate of DPD 90–120 accounts for home and property loans



Geography wise number of personal, consumer and business loans in the DPD 90–120 category



YoY (Q1 FY 21 to Q1 FY22) sector-wise change in the number of loans in the DPD 90–120 category



Source: Equifax

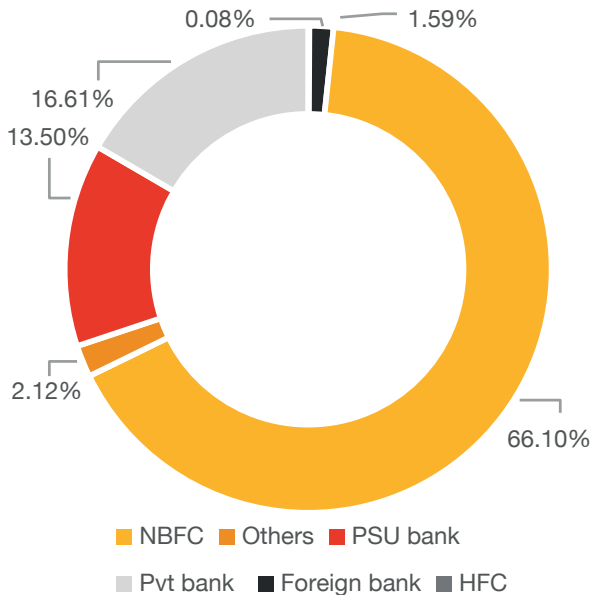
With small business owners being the primary consumers of property loans and their livelihoods being adversely affected by the pandemic, this segment saw a 165% growth in delinquency compared to pre-COVID levels. Most of the impact was observed in the urban and semi-urban geographies where the lockdowns were much harsher.

The HFC and PSU sectors which have the highest share of home loans have shown an uptick in the number of delinquent cases.

2.3 Loan portfolio based on FI type

While the impact of the pandemic was felt across the industry and all types of FIs were affected, the impact was not the same for all categories of institutions. Even for similar product lines, the behaviour in sourcing and delinquency has greatly differed for different lenders.

Distribution of loans sourced across FIs in FY22



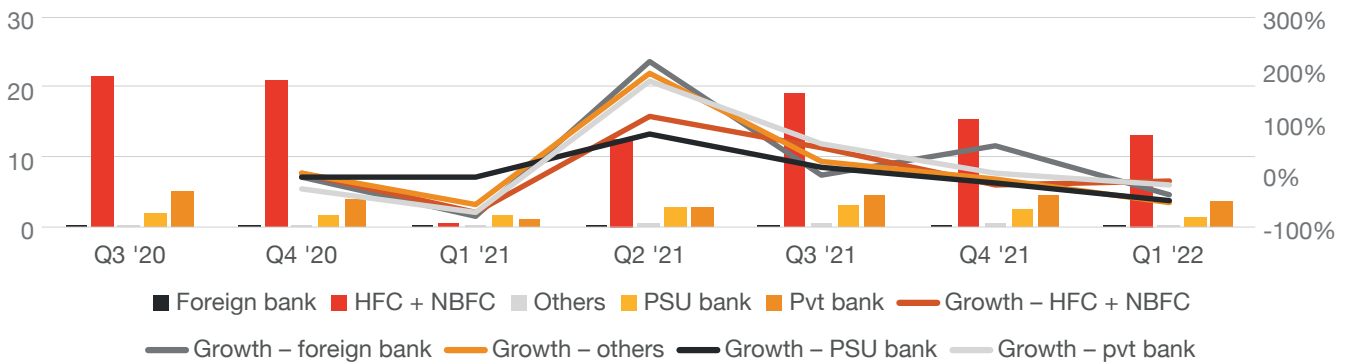
The impact of the first wave led to a decline in demand for loans across all FIs. Foreign banks were the worst hit with approximately 80% decline in the number of loans sourced compared to the pre-COVID months owing to the concentration of portfolios primarily in the urban and semi-urban regions which were worst affected by lockdowns.

PSBs, with a decline of approximately 10% in the total number of loans sourced, fared better than their counterparts during the first wave.

Q2 and Q3 FY21 marked a recovery period for all FIs as the number of cases declined, the vaccination drive gathered speed and customer demand increased. However, only PSBs witnessed a growth of 78% compared to pre-COVID sourcing while demand for loans from private banks, NBFCs and foreign banks remained lower compared to the pre-COVID months.

Source: Equifax

Distribution of new loans sourced based on the type of FIs

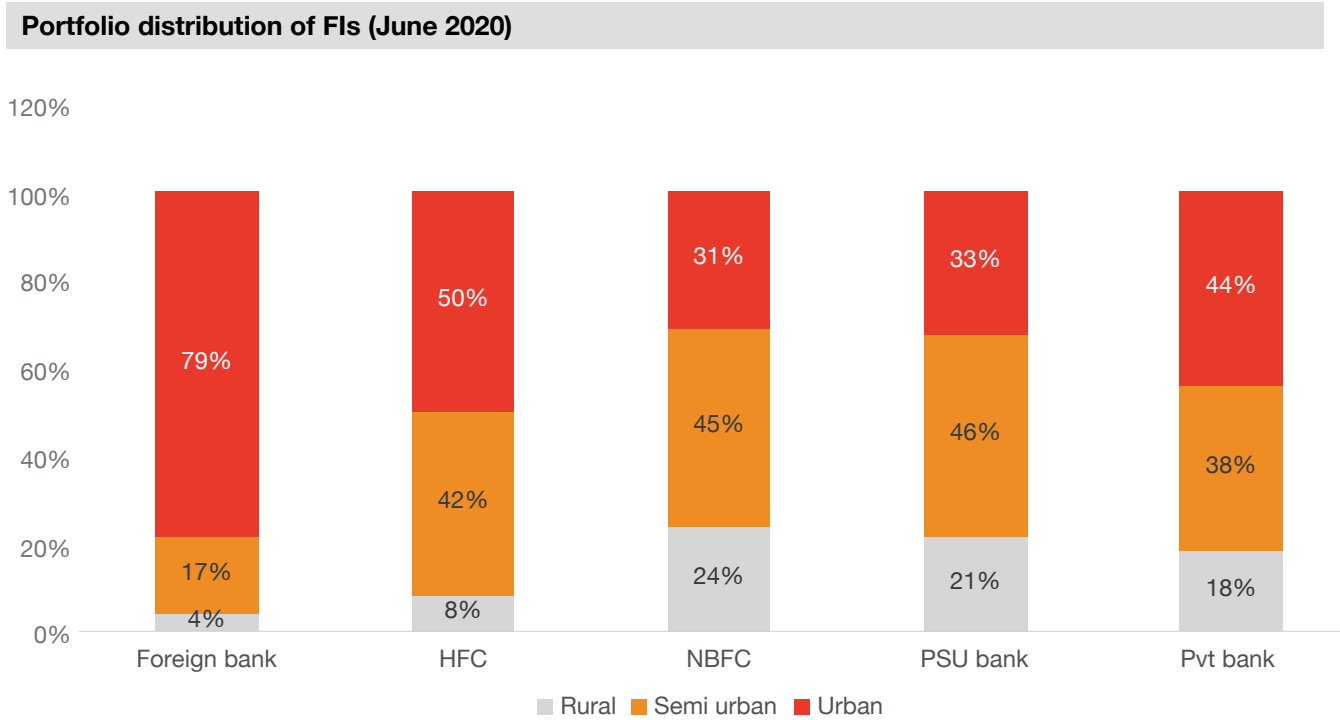


Source: Equifax

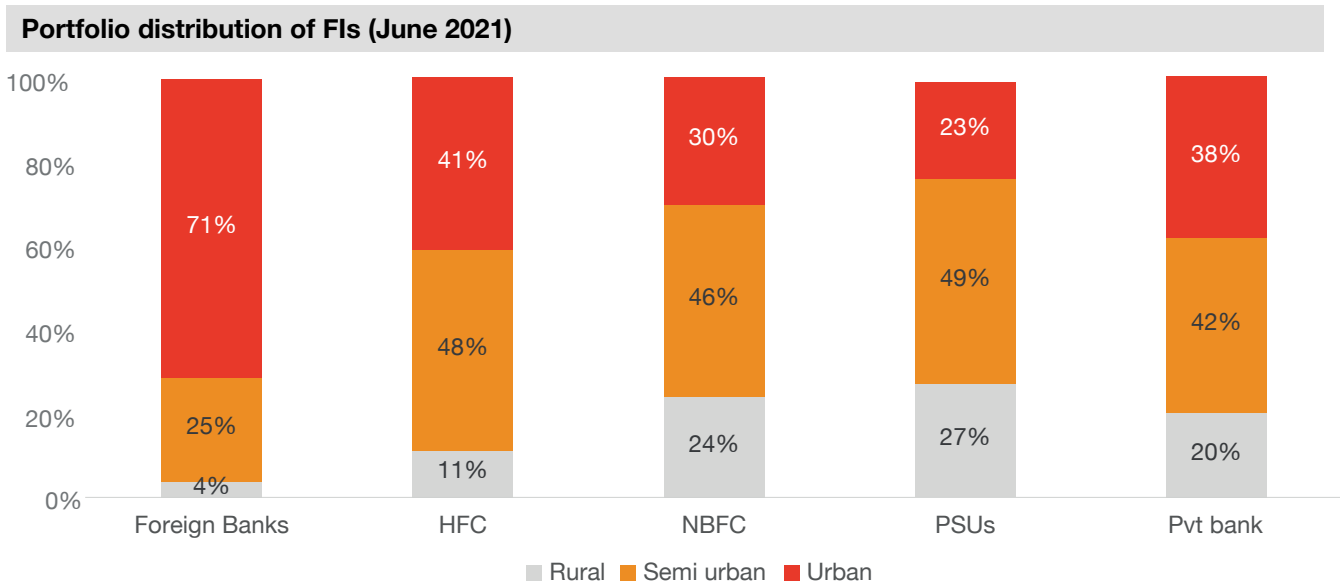
Note: Data for retail lending products considered (auto, business, consumer, housing, personal, property, tractor, two-wheeler and used car loans)

With the onset of the second wave, the total number of loans sourced declined across all FIs in Q1 FY22. Except for PSBs (approximately 50% QoQ decline), the QoQ decline in sourcing in the second wave was lesser compared to the first wave in the wake of localised measures implemented for containing the spread. However, the complete impact of the second wave will become clearer in Q2 FY22 due to demand driven by the festive season.

Portfolio distribution of FIs across geographies



Source: Equifax



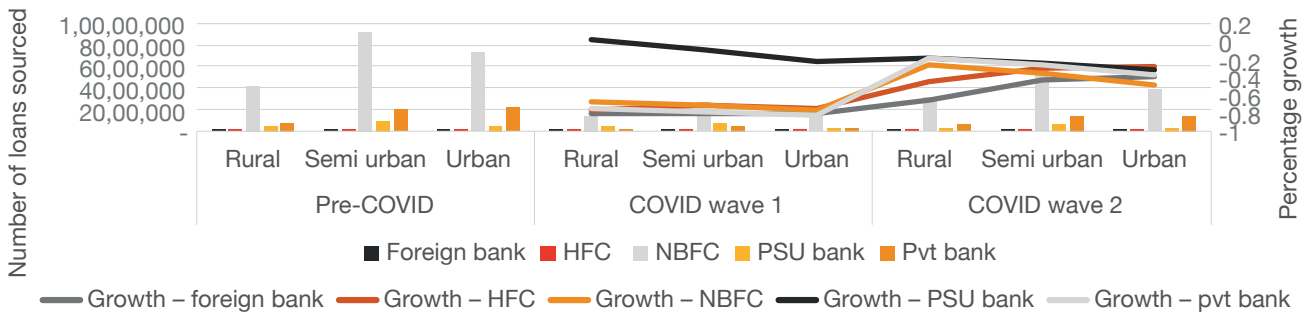
Among FIs, the primary lending focus for foreign banks has been the urban and semi-urban regions. Over the course of the year, they have increased their presence in the semi-urban areas.

The share of loans for HFCs and private banks have diversified into both rural and semi-urban areas.

For NBFCs, their geography-wise share has remained almost the same.

Almost 50% of the loan disbursements for PSBs are in semi-urban areas with a YoY growth of 6% for rural areas.

Comparative analysis of loans sourced by FIs across the COVID-19 waves



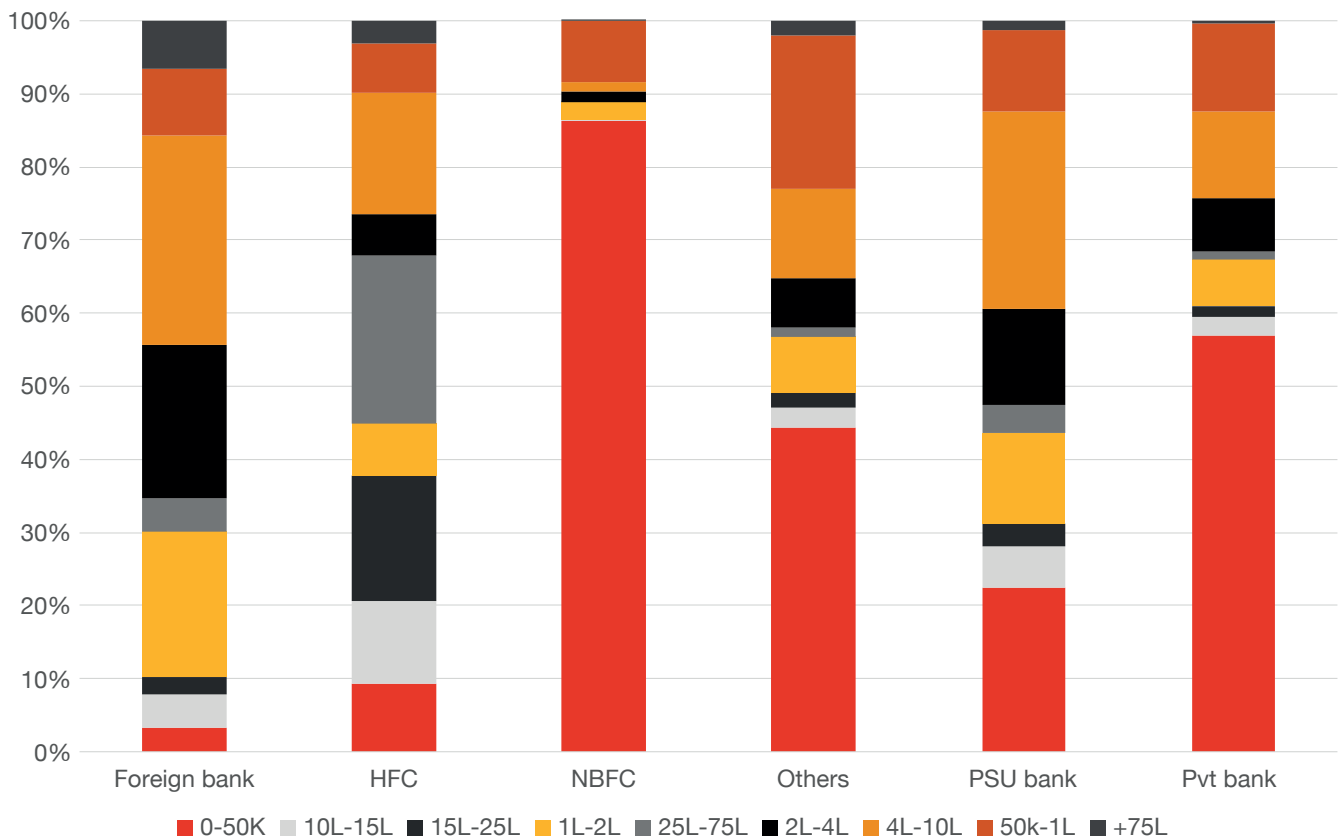
Source: Equifax

Note: Data for retail lending products considered (auto, business, consumer, housing, personal, property, tractor, two-wheeler and used car loans)

Sourcing for all FIs except PSBs fared better during the second wave compared to the first due to a more robust digital infrastructure and higher consumer demand. While the first wave witnessed a decline of approximately 70% for all FIs across rural, semi-urban and urban areas except PSBs, the second wave had a varied impact on lending recovery. Compared to the pre-COVID period, disbursements remained lowest for foreign banks with the rural portfolio being the worst hit owing to the larger impact of the second wave felt across rural areas. Disbursements by NBFCs, PSBs and private banks fell by approximately 30–40% compared to pre-COVID levels. Urban areas were impacted the most owing to a higher number of cases, localised lockdowns and a drastic slowdown in economic activities.



Distribution of loan ticket sizes across different FIs (as on June 2021)

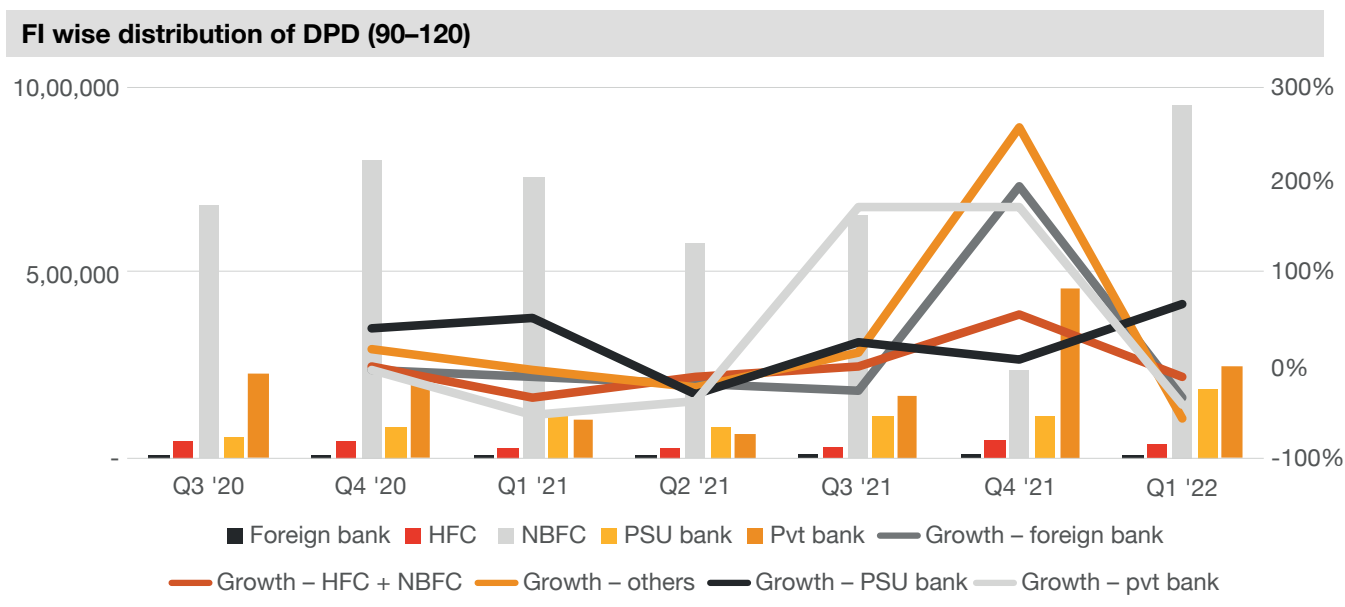
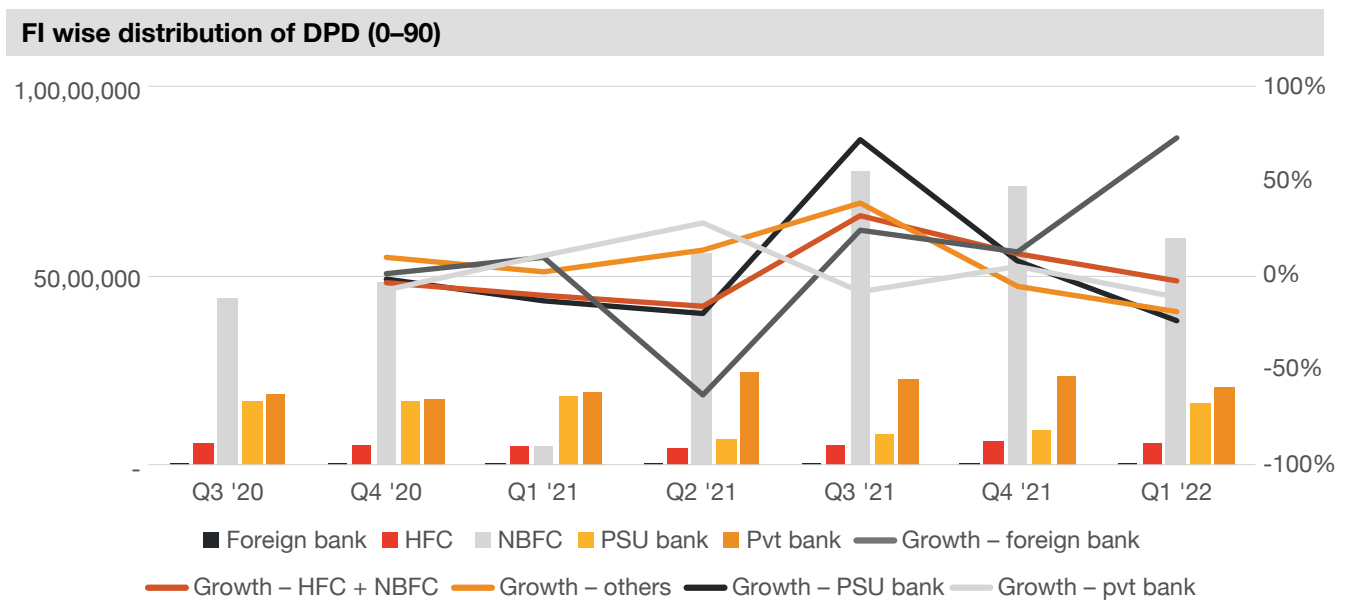


Source: Equifax

Note: Data for retail lending products considered (auto, business, consumer, housing, personal, property, tractor, two-wheeler and used car loans)

Both the waves led to a shift in the borrowing behaviour pattern with a transition towards need-based low ticket sized loans for purposes like medical emergencies, health insurance purchase and rental deposits. The rise of new-age lending platforms and FinTech players further accelerated the rise of small-ticket loans.

Owing to the high growth in low ticket sized personal loans, a majority of the loans sourced across FIs in Q1 FY22 have ticket sizes below INR 10 lakh. While approximately 85% of the loans disbursed by NBFCs have ticket sizes below INR 50K, approximately 70% of the loans sourced by private banks were below INR 1 lakh. Ticket sizes for a majority of the loans disbursed by PSBs ranged from INR 2–10 lakh.



Source: Equifax
 Note: Data for retail lending products considered (auto, business, consumer, housing, personal, property, tractor, two-wheeler and used car loans)

The number of cases in the softer delinquency buckets witnessed a growth in Q2 FY21 across all FIs (highest being for foreign banks) except private banks after the first wave. This was primarily due to the end of the moratorium period in August 2020 and an estimated 121 million job losses which affected the repayment behaviour of borrowers and reduced the collections efficiency owing to restricted movements across the country. Post a recovery period of almost two quarters, the number of delinquent cases further grew in Q1 FY22 owing to the impact of the second wave on borrowers' economic activity.

Owing to the impact of the first wave, a high number of accounts slipped into the 90-120 DPD bucket in Q3 FY21, with the highest QoQ growth in delinquencies recorded for NBFCs, private banks and foreign banks. This was primarily due to the liquidity crunch faced by mid- and low-income high-risk borrowers, who form a majority of the non-traditional customer base of the NBFCs, in the wake of the pandemic.

03 Key drivers of change

The retail lending scenario has evolved with the onset and continuation of the pandemic, and incumbents are now facing increased competition from new-age NBFCs. New players, equipped with end-to-end digital processing capabilities and ensuring a quicker turnaround time, are reaching out to prime borrowers, the key target segment of traditional lenders. Retail lenders need to identify key drivers of change and adopt it in their ways of doing business for sustainable competitive advantage.

3.1 Digitisation in retail lending

The first and second waves have provided impetus to both financial organisations and regulators to digitise existing lending journeys with the aim of bringing operational efficiencies to a larger customer base. As per the PwC-Equifax Survey conducted in May 2021,¹³ in the wake of the first wave, 29% credit managers and executives highlighted digital transformation as a core focus area while 25% were focusing on customer experience. Initiatives taken by both FIs and regulators corroborate the identified focus areas.

Initiatives by FIs

- **Digitisation in customer acquisition:** Lenders, big and small, have adopted redefined KYC norms enabled through E2E video-KYC process, virtual sales assistance and contactless process for completing the customer-borrowing journey and machine learning (ML) based banking analysis to build a digital lending infrastructure in the pandemic. Players in the space of providing video-KYC tools have witnessed exponential growth owing to the focus on digitisation across the lending landscape. Additionally, new players are making headways into the Indian lending market with unique use cases like virtual property valuations and analytics for further reducing manual intervention across the entire lending journey.
- **Mobile first:** With the total number of smartphone users in India is poised to reach 83 crore by 2022,¹⁴ India will be giving stiff competition to China for the position of the country with the highest number of smartphone users. Customers are now accustomed to executing complex tasks and transactions using their mobile devices and expect to be able to utilise a full range of banking services using such channels. Lenders must not add mobile only as an additional channel, but also focus on tailoring customer journeys and aligning expectations during the product-creation process as well. Capabilities need to be developed for identifying customers' preferred mode of communicating with the FI responding to their needs via their preferred channel. In 2020, FinTech NBFCs accounted for 45%¹⁵ of all personal loans disbursed. This shows how comfortable the current crop of loan seekers are when it comes to availing digital financial services as the solutions/apps are tailor-made and the customer journeys are intuitive.

¹³ <https://www.pwc.in/assets/pdfs/consulting/financial-services/mapping-the-indian-retail-lending-landscape.pdf>

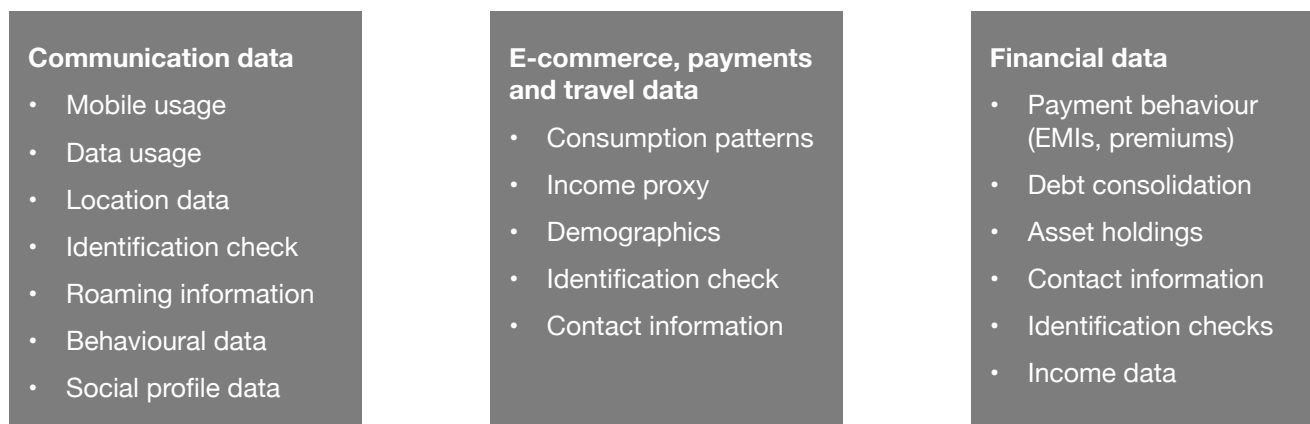
¹⁴ <https://www.iamai.in/KnowledgeCentre>

¹⁵ <https://www.sidbi.in/files/announcements/Fintech-Pulse-Vol-II.pdf>

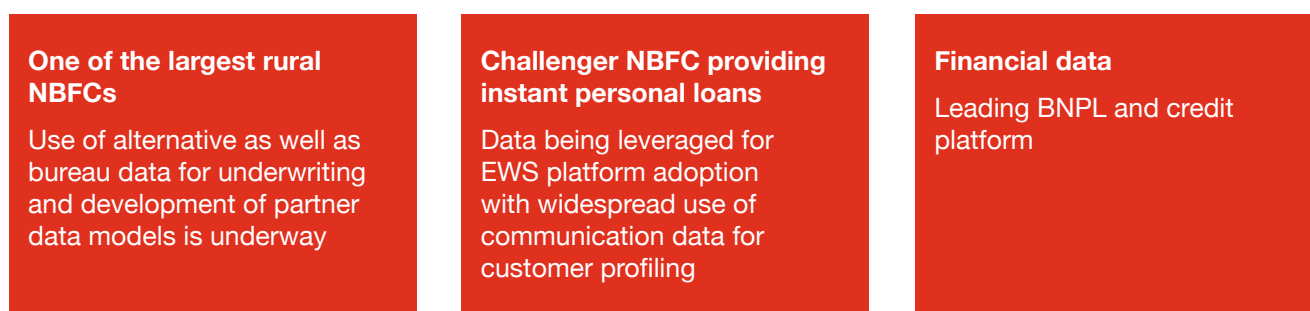
Underwriting transformation

A dramatic increase in the low ticket size unsecured lending across FIs post the COVID waves has meant a transition away from the traditional underwriting data sources through primarily two main modes of operations:

- **Data transformation leveraging advanced analytics:** Refining the existing data models for advanced use cases like E2E customer lifecycle management and supply chain management or credit default prediction while leveraging extensively emerging technologies like ML to increase the accuracy and predictive capability of analytical models.
- **FinTech partnerships:** Strategic partnerships with niche FinTech players providing access to alternative data sources like assets related data of consumers and online transaction data of consumers.

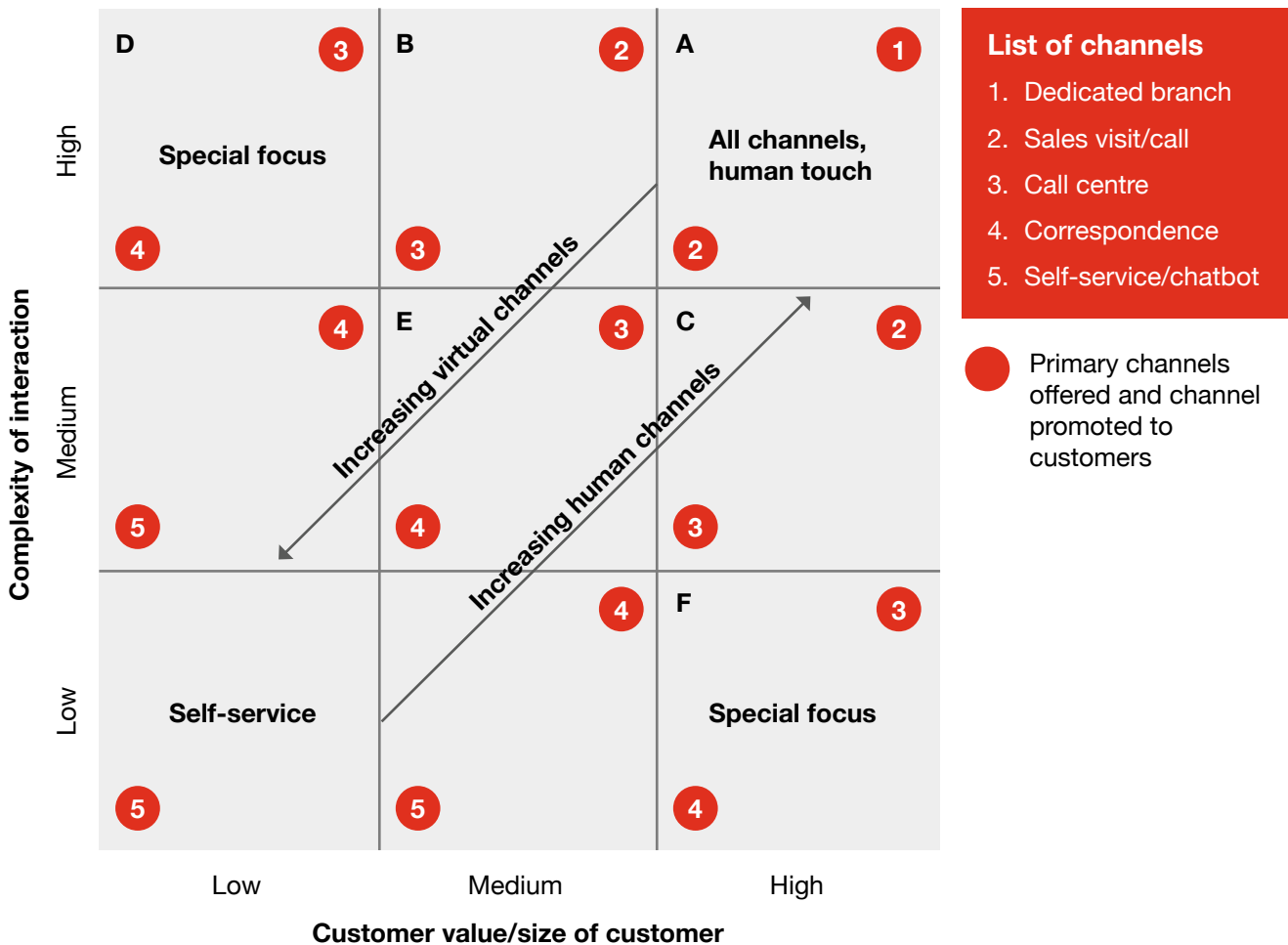


Illustrative data models used by financial players



- **Contactless collections:** During the first and second waves, reduction in collections efficiency due to restricted personnel movement and limited availability of physical collections channels were the key challenges faced by small lenders. This has led to a conscious push towards digital payments for collections and technology initiatives like hyper-personalised AI-driven virtual chatbots for driving contactless collections and reducing the turnaround time (TAT) and process cost. Use of technology is enabling players to automate collections, support customer queries, manage outbound collections calls and assist customers in making digital payments for collections.
- **Virtual servicing:** The pandemic has accelerated the growth of contextualised remote servicing for borrowers to reduce the overall time for customer query resolution. FIs are looking to leverage customer data analytics and extensive product and customer driven segmentation to provide services in the most effective way.

Channel segmentation for optimisation of interaction time along borrowers' journey



Source: PwC analysis

Key regulator and Government driven interventions

- Know Your Customer Guidelines, 2020:** The RBI introduced the Video based Customer Identification Process (V-CIP) on 10 May 2021, an alternative method of customer identification with facial recognition and customer due diligence by an authorised official of the Regulated Entity (RE). The central bank also amended its 2016 Master Direction on Know Your Customer (KYC) on 9 January 2020 as well as introduced Digital KYC. All REs will have to mandatorily conduct e-KYC if online verification is not possible. However, only banks are allowed to capture video KYC. Other NBFCs will have to adhere to the traditional methods of KYC as stated in the 2016 circular.
- Payment ecosystem:** The regulator has laid the foundations for creating a framework around FinTechs and also created a separate FinTech department which will help in regulating the sector. Currently, the sector remains largely unregulated. The framework would also help in addressing the challenges in the current ecosystem. These developments would help in creating a legal and regulatory structure within which FinTechs/digital lending institutions can operate and thrive.
- Federated consent architecture:** A joint public-private initiative for streamlining data governance by providing users control over their data and allowing seamless sharing which can thereby be leveraged by players for a smooth and intelligent lending journey for borrowers. The account aggregator (AA) framework is one such initiative which will democratise credit by enabling individuals to access, aggregate and share financial data within the network of FIs which are a part of the AA framework.

3.2 Embedded financing

As per the PwC-Equifax Survey 2021, the most preferred alternative for business growth was product and service innovation with 29% of the respondents choosing the same. This is reflected in the changing landscape of lending product variants with multiple FIs transitioning towards **embedded lending for diversifying their sourcing channels. Lenders are offering financial products** embedded into the interconnected ecosystem through partnerships with players in sectors like education and healthcare to offer specific need-based products.

In order to truly capitalise on the strengths of embedded lending, FIs need to internally look at their capabilities, existing product lines and value chain, and identify areas where collaborating with ecosystem players can create more value than building or buying. Some of these systems and capabilities are too costly for a lending focused organisation to build and maintain.

BNPL, a key embedded lending model, is gaining traction in the post pandemic lending landscape. It provides targeted offerings for millennials and younger customers aimed at breaking down bulk cash outflows into low-cost EMIs through bite-sized credit. BNPL products are becoming popular in India with the growth of e-commerce as well as internet and smartphone penetration. Market leaders expect BNPL products to scale up further with BNPL payments in the country expected to grow by 72.7% annually to reach USD 6,327.2 million in 2021.¹⁶ The growing popularity of the low-cost product has also pushed large private sector players to foray into the space.

In light of the gaining popularity of embedded lending, the Government is also providing impetus to application programming interfaces (APIs) driven lending through the AA framework. AA can provide consent-based access to a customer's banking history to digital lenders, thus enabling a differentiated lending experience, especially for MSMEs and new-to-credit borrowers who lack access to formal credit. The marketplaces and aggregator models, easily accessible through new-age FinTech platforms and apps as per their need for different customer segments, are expected to lead to the opening up of an entirely new paradigm of embedded lending in the retail lending landscape.

3.3 Ecosystem buildout

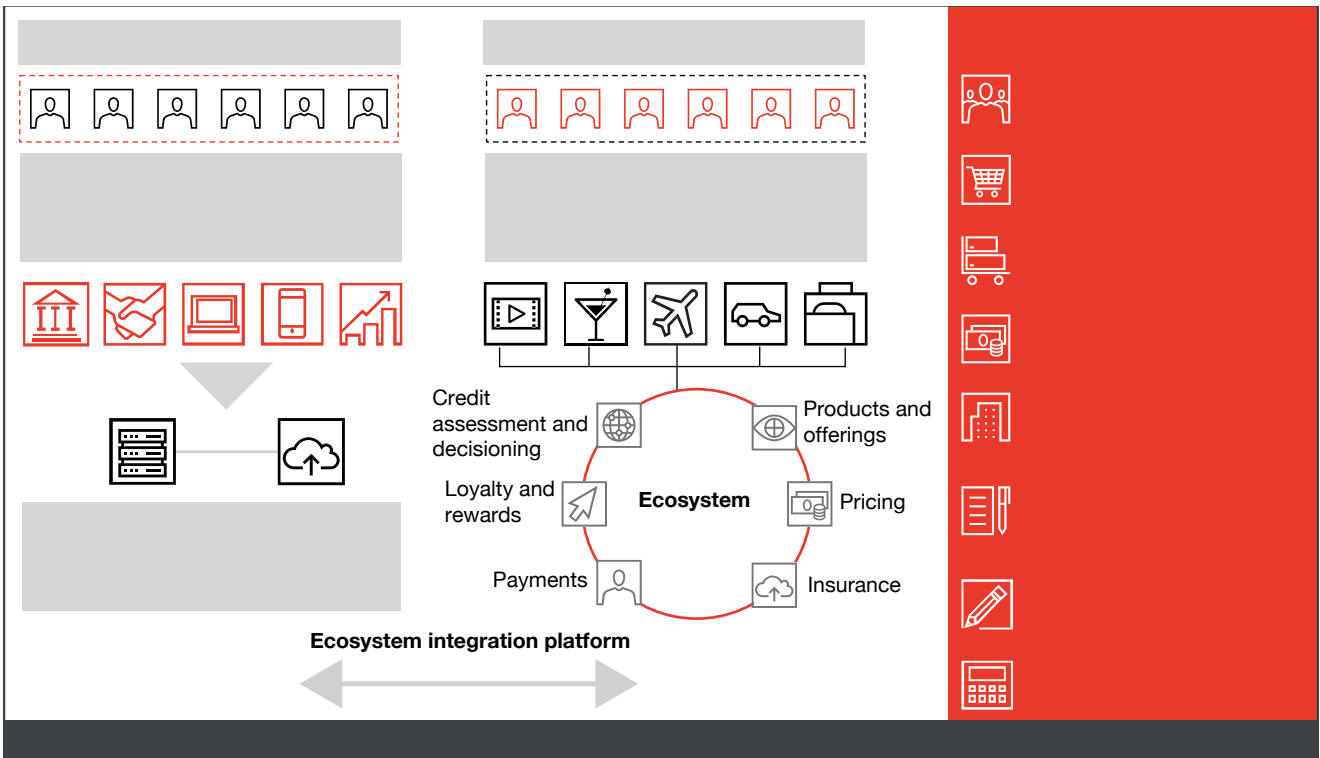
In a highly competitive landscape of approximately 10,000 NBFCs and banks, FIs have recognised the need for providing collaborative ecosystem-driven lending avenues and leveraging the network effects of players in the ecosystem for higher penetration of lending products. Ecosystem-driven lending can be enabled by two key mechanisms:

1. strategic partnerships with players in the lending ecosystem, e.g. HFCs partnering with FinTechs for providing alternative data for underwriting
2. embedding NBFC financing in the overall ecosystem for the product offerings, e.g. providing rental deposit financing in collaboration with players providing rent agreement registration services.

Ecosystem players across lending products, namely payment partners, direct sales agents, property aggregators/brokers, real estate agents, builders, and acquisition and collections facilitators provide access to unique data-driven insights into FIs that can be leveraged for higher penetration, robust underwriting models and improved customer servicing for both existing and prospective borrowers.

¹⁶ <https://www.pwc.in/assets/pdfs/consulting/financial-services/mapping-the-indian-retail-lending-landscape.pdf>

Financial ecosystem



Source: PwC analysis



04 Conclusion

The COVID-19 pandemic has brought about unprecedented business challenges, with significant macroeconomic impact on organisations in India and worldwide. FIs have been reeling under the impact of the pandemic for the past few quarters, with full repercussions likely to be felt in the coming years as well. Sourcing, which was severely impacted during the first wave, showed signs of recovery in the subsequent quarters. FIs embracing digital adoption in the lending processes was one of the key contributing factors for the increased sourcing numbers. This development has changed the way lenders looked at the traditional ways of banking and compelled them to be agile and adopt digital processes, with newer business models and technologies being adopted more than ever before. The rapid use of digital solutions and digital transformation of businesses has helped lenders to operate effectively in the new normal. However, it is also important for institutions to be wary of the various security threats that accompany digitalisation and constantly assess and track the risks that they carry.

With the accelerated pace of vaccination and better preparedness among citizens and corporates, India now has a better chance of efficiently handling future waves of the pandemic. The third wave, though sizeable in terms of the number of cases, might not disrupt economic activity fully. Since economic activities have now resumed at nearly pre-COVID levels, lenders need to prioritise identifying and arresting of portfolio vulnerabilities at an early stage while filling the enormous credit gap. Moratoriums given to the customers can possibly impact their repayment behaviour, and this is where customer connect and engagement becomes imperative.

With customers adopting digital channels and digital banking rapidly, lenders must innovate and create solutions that fit into the customer context. Customers are no longer only looking for financial products, and lenders must find ways to customise and fit offerings as a part of the overall ecosystem which addresses larger customer problems. FIs need to focus on serving customers through their channels of choice and with relevant products and value-added services. While digital channels would be key going forward, FIs need to correctly identify how to achieve the human touch and personalisation while serving through contactless channels.



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