Extension of COVID-19 Loan Moratorium - Know the Implications

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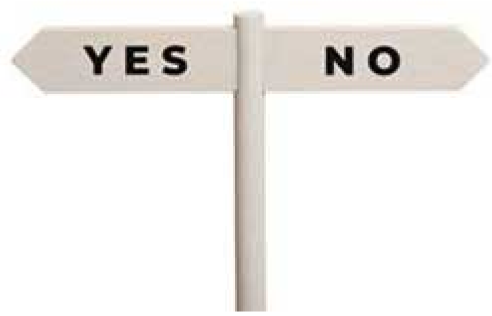

- Shobhit Agarwal -

Due to the COVID-19 and subsequent lockdowns across the country, the RBI allowed banks and other lending institutions a three-month loan moratorium on EMIs from March to May 2020. This was later extended by an additional three months up to August 31, 2020.

The moratorium certainly helped borrowers, be they homebuyers or real estate developers, reeling under monetary pressure brought on by the pandemic. Additionally, RBI also maintained that banks should not term late payment as defaults. However, the banking regulator left it to the discretion of lenders to decide on whether to grant or withhold the moratorium, and for how long, depending on individual borrower profiles.

Reportedly, the RBI is again mulling the possibility of extending this moratorium period. Whether it does so or not, borrowers must consider the pros and cons of availing of this facility if it is approved. Should they further defer their EMIs or stretch themselves and continue servicing their loans as per schedule?

No blanket advice can be given for this dilemma - as always, the devil lies in the detail. It is important to remember that this is no 'free lunch' and that there is fine print to consider. To some homebuyers, the loan moratorium is a temporary respite and provides additional time to sort out their finances. To others, it adds to the monthly financial burden since the EMI amount would increase once the benefit period is over.

Benefits of the loan moratorium

Several borrowers, including developers, have already availed of the benefit of EMI moratorium for six months, with the possibility of a further extension. For developers, a one-time loan restructuring could have been a better option, but a further extension of the loan moratorium would certainly be welcome.

Previously, the RBI had also converted the accumulated interest for the moratorium period into a term loan. This means that the borrower would not have to immediately repay the accumulated interest on the loan once the moratorium ends.

For developers - it gives them more time to sort out their finances. Residential sales across cities are gradually reviving with the lockdown being lifted. With the festive season approaching, housing sales activity is likely to gather momentum. Therefore, an extension will give developers the time to collect funds via sales and later service their loans via these funds once the moratorium period ends. The fact that non-payment of EMIs will not result in falling into banks' bad books is an added relief.
For individual borrowers - it will help both salaried and self-employed borrowers facing difficulties with servicing their car, home and personal loans due to the unique exigencies of the pandemic. It is an opportunity to regain financial clarity. Individual borrowers are also safe from unfavourable action by banks due to non-payment of EMIs, which would otherwise adversely impact their credit score. The RBI has ensured that availing of this moratorium will not be considered a default for the said period.

A word of caution for home loan borrowers

Over the past couple of months, some banks have reset their MCLR rates for borrowers who have availed the moratorium benefits. As a result, many borrowers are now receiving notifications regarding the resetting of their loan tenure, which has been reduced by a few months depending on the amount borrowed.

Their monthly EMI amount will eventually increase with the lowering/resetting of the loan tenure once the loan moratorium period is over. This can significantly upset financial planning in future. Since many individuals lost their jobs or took pay cuts due to COVID-19, they may find it even more difficult to repay these increased EMIs.

Increased EMIs may lead to defaults by some existing home loan borrowers, especially those in a job crisis or other business uncertainties. Also, while the six-month moratorium did provide relief in a time of uncertainty, home loan borrowers will now need to tread with greater caution if the RBI extends the moratorium.

Borrowers who want to consider restructuring their loans with their respective banks will need to check the fine print. It is important to establish the exact amount of their monthly EMIs once the moratorium period ends. They must also consider the possibility that the uncertainty continues, and that they may be unable to service their loans once the extension period expires.

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