doi: 10.31674/book.2022sseg.010

A Study on Impact of COVID- 19 Pandemic on Indian Banking Sector

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ABSTRACT

The banking sector plays a crucial role in the Indian economy. Banks not only provide a flow of finance in the Indian economy but also act as a driver to uplift socio economic development in India. In 2020, the sudden spread of the COVID-19 virus and the imposition of a nationwide lockdown presented numerous challenges in front of all sectors of the Indian economy, including the banking sector. In this paper, the researcher portrays the impact of COVID-19 on the Indian banking sector and demonstrates various measures that have been taken by the Reserve Bank of India (RBI) to counter the adverse impact of COVID-19 on the Indian banking sector. This study is based on secondary data which has been collected from various newspapers, articles, reports, and published research journals available on the internet. According to this report, the RBI and the government should provide more loans and simplify credit conditions in order to increase liquidity in the economy and lessen financial stress among small and medium businesses. The immediate takeaway from the epidemic is that the government should strengthen our economy in order to absorb the impact of future crises of this nature.

Keywords: *COVID-19; Indian Economy; Lockdown; Non-Performing Assets; Loan Moratorium*

JEL code: E43, E58, G21

INTRODUCTION

The Indian economy was already in a precarious state, but the imposition of a nationwide lockdown and the suspension of major economic activities due to COVID-19 weakened it even further (Ali, 2020). This pandemic affected various sectors of the Indian economy. The Indian economy is broadly segregated into three sectors, namely the primary sector (agriculture, farming, fishing, etc.), the secondary sector (manufacturing, processing, etc.) and the tertiary sector (financial services, transportation services, etc.) (Ramakumar & Kanitkar, 2021). All these sectors are supported by banks. Behind every successful economy, there is always a sound banking system. The banking sector is responsible for most of the financial activities going on in the economy, and this sector is working as a supporting hand to all of the industries in terms of financing, credit, transactions, collection, and payment, and it mobilizes deposits and provides credit to various sectors across India. Apart from their traditional work, banks are now facilitating e-commerce, promoting digital transactions and providing forex support to all sectors in the Indian economy. If the banking sector gets impacted by any hindrance, it will also impact other sectors. In this paper, the researcher portrays the impact of COVID-19 on the Indian banking sector and discusses various regulatory measures that have been announced by the RBI so far to ameliorate the economic shock.

LITERATURE REVIEW

In their research paper, Bobade and Alex (2020) emphasised the impact of COVID-19 on the Indian banking sector, as well as RBI policies that have been implemented thus far.

Dev and Sengupta (2020) have written an article about the impact of COVID-19 on the Indian economy along with a detailed analysis of the different sectors that suffered from COVID-19. They highlighted that COVID-19 has had an adverse influence on India's banking sector (particularly public sector banks), and that this sector has been having a hard time dealing with the swelling losses from nonperforming assets (NPAs) on their balance sheets.

Perwej (2020) explained in his article several operational and technical challenges that banks are currently facing due to COVID-19. According to the researcher, banks should focus on utilising new technologies and make their infrastructure agile in order to traverse the obstacles presented by the COVID-19 crisis.

Sharma and Mathur (2021) in their article discussed the impact of the lockdown on Indian banks in the event of moving beyond July 2020. According to researchers, people are now playing it safe as a consequence of the pandemic, and there has been a huge shift toward saving instead of borrowing. It enhanced the amount of money kept in bank accounts.

Chanduji and Thakor (2020) in his article mentioned this pandemic forced Indian banks towards digitizing and optimizing the bank's back-office operations. Researchers revealed that there was a major shift towards precautionary savings and the risk aversion for households. The researcher has also mentioned that in future banks will operate in a financial system that is awash with the liquidity and interest rates are extremely low.

Research objectives

The objectives of this study are

- To understand the impact of COVID-19 on Indian banking sector.
- To discuss the regulatory measures taken by the Reserve Bank India to counter the impact of COVID-19 on the Indian banking sector.

METHODOLOGY

This study is descriptive in nature and it is supported by secondary data. The study objectifies to identify the impact of COVID-19 and the therefore the resultant nationwide lockdown on Indian Banking Sector and to discuss various measures that has taken by RBI to counter its adverse impact. Under the study, data regarding Indian banks concerning the FY 2020-2021, 2021-22 are collected. Data have been collected from various newspapers, articles, reports, published research journal available in internet.

RESULTS AND DISCUSSION

Impact of COVID-19 pandemic on Indian Banking Sector

Banks plays a crucial role in socio-economic development of a country. Every healthy economy is always supported by a sound banking system. Primarily, it collects funds from surplus sector and channelizes them to deficit sector in the form of loans to bridge the gap. Banks also try to reduce regional imbalances. It helps in capital formation and improving standard of living of people by providing loan for purchases of goods and services. Moreover, banks are also facilitating e-commerce, promoting digital transactions, providing forex support to all sectors. So, it is very much required to analyze the impact of COVID-19 pandemic on Indian Banking Sector.

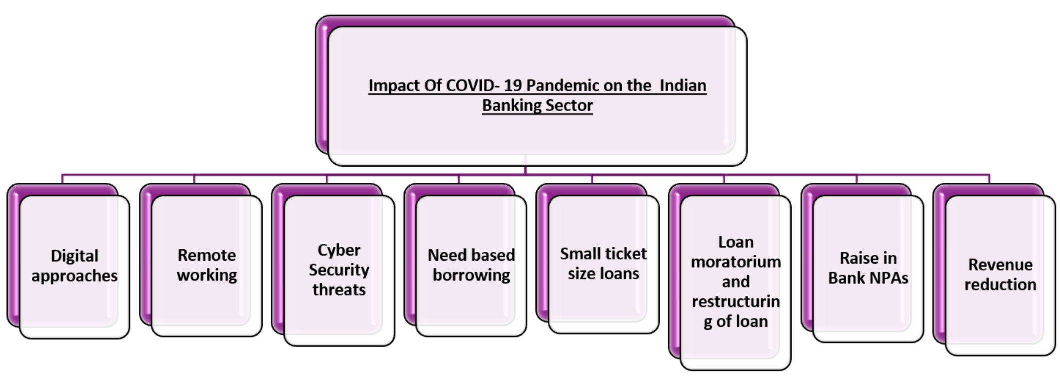


Figure 1: Showing impact of COVID-19 pandemic on Indian Banking Sector

Digital approaches: - During this pandemic bank in India did manage to bring innovation into play, they brought and adopted the age of technology and digitization. This pandemic has accelerated the proliferation of digital transaction as customers mindset shifted to digital payments, online services and other digital solutions. Digitalization has also been very helpful for banks both in terms of maintain contact with their customers and also as organizing their internal ways of working. Though digital solutions are there in India before this pandemic, but this pandemic has created such a scenario that compel banks and their customer to adopt digital banking solutions.

Table 1: Payment system indicators – annual turnover (April-March)

Item	Volume (Lakh)		
	2018-19	2019-20	2020-21
1	2	3	4
A. Settlement Systems			
CCIL Operated Systems	36	36	28
B. Payment Systems			
1. Large Value Credit Transfers – RTGS	1,366	1,507	1,592
Retail Segment			
2. Credit Transfers	1,18,481	2,06,506	3,17,852
2.1 AePS (Fund Transfers)	11	10	11
2.2 APBS	14,949	16,766	14,373
2.3 ECS Cr	54	18	0
2.4 IMPS	17,529	25,792	32,783
2.5 NACH Cr	8,834	11,290	16,450
2.6 NEFT	23,189	27,445	30,928
2.7 UPI	53,915	1,25,186	2,23,307
3. Debit Transfers and Direct Debits	4,914	7,525	10,456
3.1 BHIM Aadhaar Pay	68	91	161
3.2 ECS Dr	9	1	0
3.3 NACH Dr	4,830	7,340	9,630
3.4 NETC (Linked to Bank Account)	6	93	650
4. Card Payments	61,769	72,384	57,841
4.1 Credit Cards	17,626	21,773	17,641
4.2 Debit Cards	44,143	50,611	40,200
5. Prepaid Payment Instruments	46,072	53,318	49,392
6. Paper-based Instruments	11,238	10,414	6,704
Total – Retail Payments (2+3+4+5+6)	2,42,473	3,50,147	4,42,229
Total Payments (1+2+3+4+5+6)	2,43,839	3,51,654	4,43,821
Total Digital Payments (1+2+3+4+5)	2,32,602	3,41,240	4,37,118

Source: RBI, 2021b

Above table shows that within the F.Y. 2020-2021 digital transactions in India have been increased by 28% (i.e., from 3,41,240 lakhs in 2019-2020 to 4,37,118 lakhs in 2020-2021). As customers are becoming quick access to smartphones, internet, banks can easily reach out to their customers and communicate with them digitally. This brings an enormous opportunity for lending institutions like banks to build intuitive customer journeys for interacting with them. Banks can now do the KYC (Know Your Customer), underwriting, and verification process digitally. A lot of services are rendered by banks within the field of lending product design digitally such as click payments, checkout financing (checkout financing refers to loans offered during the merchant's online checkout process), buy now-pay later credit solutions etc. It is expected that this trend would continue in future and this banking sector will witness a rise in the number and size of digital transactions.

There are so many benefits are there in adopting digital approach, like banks are getting benefits in unit cost, customer service, help in improving customer experience significantly, now banks are able to get in their customers at lower cost. The whole digitalization got big boost. Not only banks are getting huge benefits in adopting such ways of working but also customers. Digital banking acts as a touchless approach, there is no such COVID-19 risk in using digital tools for making their transactions. So, for customers it is a secure approach to protect themselves from COVID-19. Ultimately this pandemic will allow banks to push this new way of banking into the future and propel India towards a fintech nation.

Remote working: - This pandemic and lockdown has been created a troublesome situation for banking sectors. Multiple business continuity challenges have been arisen in fort of banking sectors to provide services, obey compliance functions, and maintaining social distancing norms. Banks are taken care of their branches', customers, employees and that they need to make sure that linkage has not broken during this point.

Banks have tried to open all their branches' and rendered services as per RBI mandate during this tough time. Banks has devised new ways of working like remote working, internet banking to continue its operations and deliver satisfactory level of services to their customers. It has been seen that productivity of workers has gone up in remote working platform and feedback from customers is also stated the same. This remote working saves 2 to 3 hour every day in unproductive travel time for some employees. It has helped them to extend their productivity and operational efficiency. At the same time due to this platform and pandemic situation so many contractual bank employees had lost their job also. As per the data published by the All-India Bank Employee Association (AIBEA) 1.5 lakhs bank employees (frontline workers) have been tested positive. And more than 1300 bank employees have lost their life due to COVID-19 (Chanduji & Thakor, 2020).

Cyber Security threats: - Financial institutions are always favorite among cyber criminals. During this difficult time with the increasing needs of remote working and more uses of digital approach by banks and their customers, there is a growing concern for cybercrimes. It has been observed that now days malware attacks have becoming more and more frequent. The banking frauds in India have increased during this pandemic situation.

Table 2: Fraud cases - bank group-wise

(Amount in ₹ crore)						
Bank Group/Institution	2018-19		2019-20		2020-21	
	Number of Frauds	Amount Involved	Number of Frauds	Amount Involved	Number of Frauds	Amount Involved
1	2	3	4	5	6	7
Public Sector Banks	3,704	64,207	4,410	1,48,224	2,903	81,901
	(54.5)	(89.8)	(50.7)	(79.9)	(39.4)	(59.2)
Private Sector Banks	2,149	5,809	3,065	34,211	3,710	46,335
	(31.6)	(8.1)	(35.2)	(18.4)	(50.4)	(33.5)
Foreign Banks	762	955	1026	972	521	3,315
	(11.2)	(1.3)	(11.8)	(0.5)	(7.1)	(2.4)
Financial Institutions	28	553	15	2,048	25	6,839
	(0.4)	(0.8)	(0.2)	(1.1)	(0.3)	(4.9)
Small Finance Banks	115	8	147	11	114	30
	(1.7)	(0.0)	(1.7)	(0.0)	(1.6)	(0.0)
Payments Banks	39	2	38	2	88	2
	(0.6)	(0.0)	(0.4)	(0.0)	(1.2)	(0.0)
Local Area Banks	1	0.02	2	0.43	2	0
	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)
Total	6,798	71,534	8,703	1,85,468	7,363	138,422
	(100.0)	(100.0)	(100.0)	(100.0)	(100.0)	(100.0)
Note: Figures in parentheses represent shares in total (in per cent).						

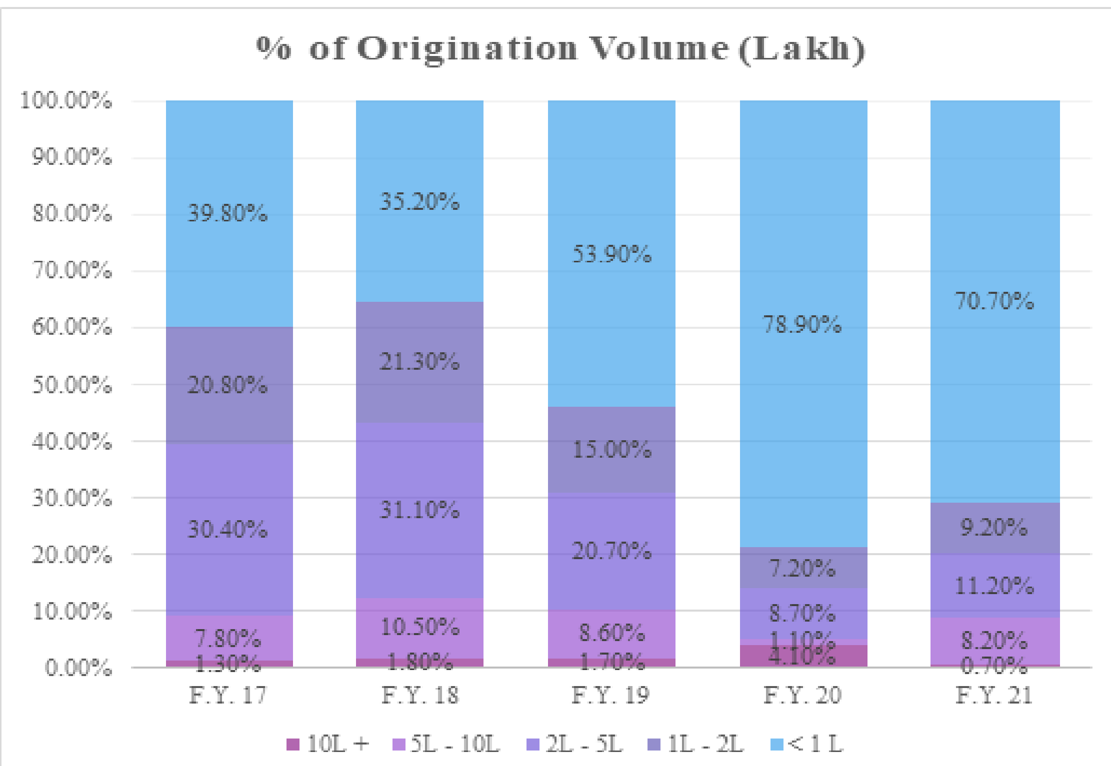
Source: RBI, 2021b

According to RBI's annual report for 2019-20, the amount involved in banking frauds has grown 2.5 times from Rs. 71,534 crores to Rs 1,85,468 lakh crores in 2019-20 compared with Rs 71,500 crore in 2018-19 (Ali, 2020) and grown 1.93 times in 2020-21 compared to 2018-19. If there is a privacy breach or breach in security in a bank, it basically leads to the information of the customers being sold or purchased on the dark web by other cybercriminals. Ultimately these types of privacy breach led to loss of data and earnings for a banking institution, disruptions in their operations, loss of reputation of that bank along with loss of their both actual and potential customers.

At this present situation cybersecurity and access management has played a vital role. This has been used by banks to protect banking confidential data, customers data, reduce or eliminate loss, and meet the regulatory compliance requirements. Now banks have implemented more security practices like data encryption, automated scanning and monitoring processes, security audit to further safeguard their customer interest, current remote working, digital way of doing businesses in the future.

Need based borrowing: - Before this pandemic people are wont to borrow money to fulfill their desire of travel, dining, experiences, luxury purchases, and other indulgences. During this pandemic situation peoples are afraid of the chance of job loss, salary reductions, economic uncertainty at the same time so many people have already experienced their salary reduction and ultimately their disposable has gone down (RBI, 2020). Now, people take loan out of necessity like education, medical emergencies, and other essentials. Now, people exercise caution about their borrowing. Presently customers are taking need-based borrowing than Want-based borrowing.

Small ticket size loans: - It has been observed that due to economic distress triggered by the corona virus pandemic, now customers are taking small ticket sized loan (loan below Rs. 1,00,000 in value), for emergencies or for financing their immediate requirements. At the present scenario it has been observed that there is lower appetite for traditional unsecured and larger ticket sized loans. Now it is become very difficult for the first-time borrowers with no credit history to obtain larger ticket sized loans from banks. As now banks have critically analyzed that what amount should be given to customers so that it would be not over levered to customers (RBI, 2021a).



Source: RBI, 2021c

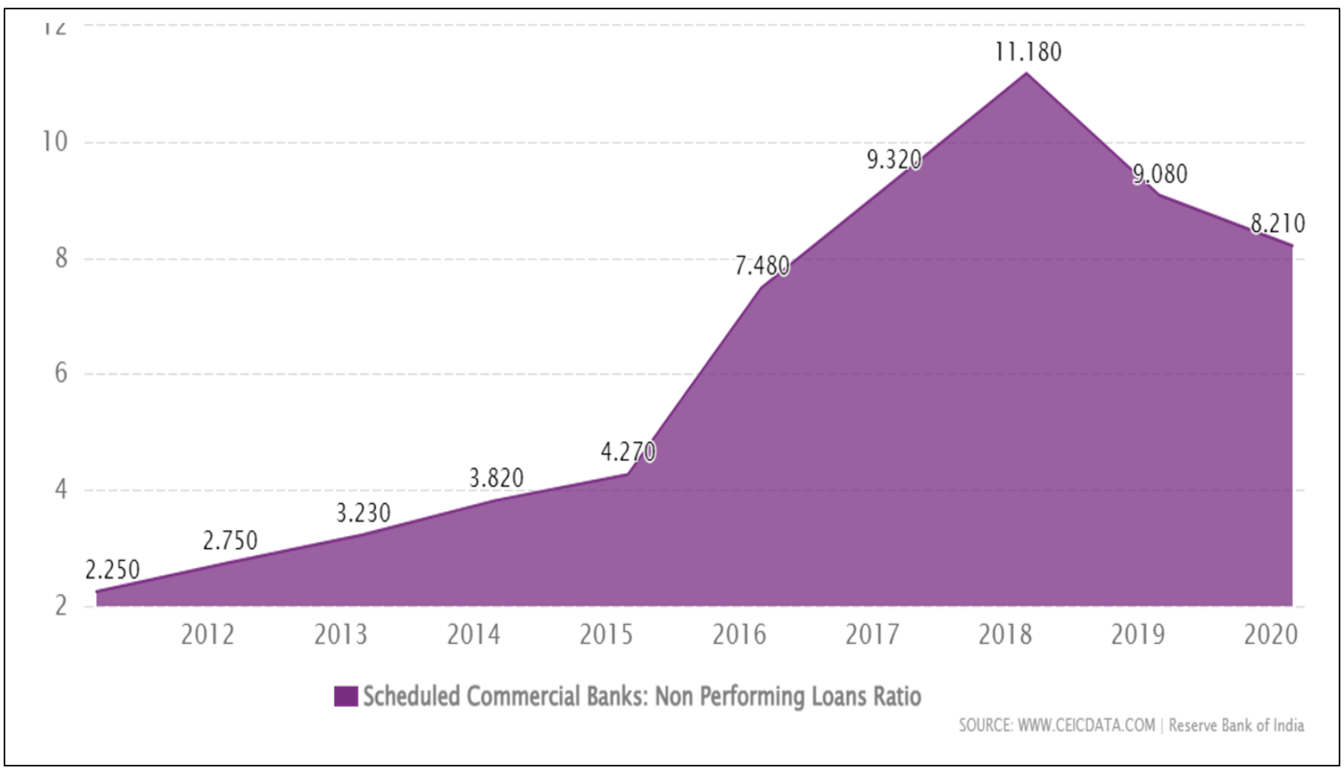
Figure 2: Personal loan originations - ticket size

Figure 2 indicates that there was almost 2 times growth in volume of small ticket size loan from 2017 to 2020. And during the FY 2020, small tickets loans were 78.9 % of personal loans disbursed, followed by 8.2% drop in FY 2021 due to 2nd wave of COVID-19.

Loan moratorium and restructuring of loan: - During this pandemic situation so many customers have lost their job, experienced salary reduction etc. Now, financially affected customers trapped in the economic crisis due to this pandemic. In 2020 during the first wave COVID-19, RBI had announced a loan moratorium and restructuring scheme. Due to the second wave of Covid-19, on 5th May 2021, RBI has announced a resolution framework 2.0 for many borrowers including individual and MSME borrowers. Now, banks are providing loan restructuring and loan moratorium facility to their financial distress individual and MSME customers.

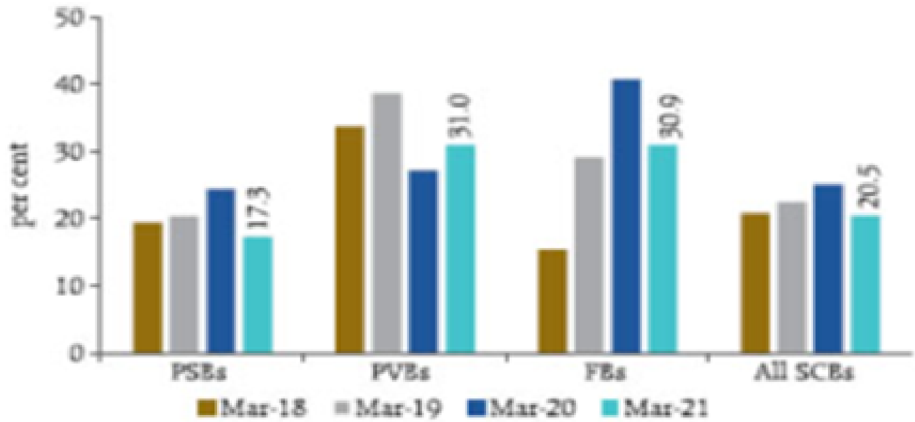
Loan restructuring is a process where borrowers facing financial distress, they can modification of the loan terms and conditions with the lender to avoid default. When borrowers face financial distress, they can opt these facilities. Loan restructuring permits customers to extend their loan tenure with or without changes in the rate of interest. This facility offers to borrowers by considerably bringing down their EMI burden. it negatively impacts the borrowing capacity of customers for that extended period until the restructured loan is cleared. At the same time with the introduction of these Scheme, banks can now able to avoid these loan accounts from being declared as NPA, it basically provides a positive impact to their financial statements (RBI, 2021d).

Raise in Bank NPAs: - India had a bad history of NPAs, due to waves of COVID-19 Indian banking system has been reeling under the pressure of NPAs. Though RBI has been very active during his pandemic and has taken several numbers of actions to shield national economy from the destruction of the pandemic but still India has been experiencing deterioration in economic activity due to the pandemic and enhanced bank NPA stresses. If the principal and/or interest amount of a loan and advance is overdue for a period of 90 days, it is termed as Non-Performing Asset (NPA).



Source: https://www.ceicdata.com/en

Figure 3: GNPA ratio of public and private sector banks



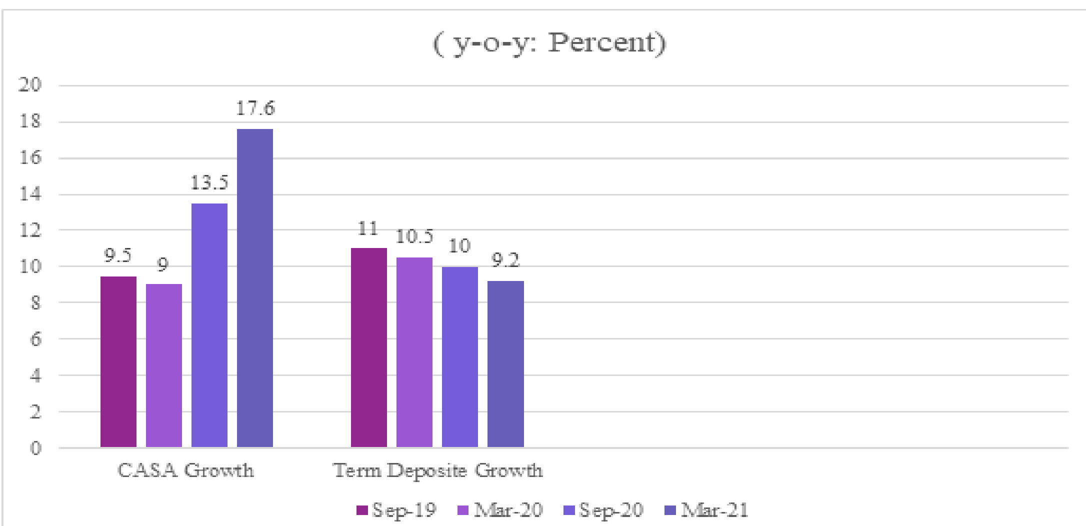
Source: RBI, 2021d

Figure 4: Write off to GPA

Figure 3 indicates that after reaching the peak in FY 2018 (11.18%), GNPA ratio started declining. In September 2019 it had been 9.08% and 8.21% in September, 2020. According to a RTI response this fall has been seen due to write off more NPAs in FY 2019 and 2020 (shown in figure 4) and recovery of huge NPAs accounts (Rs.1,31,894 crore worth of NPAs in FY 2020-21) through various debt recovery channels.

The second wave of COVID-19 has worsened stressed assets in Indian banking system, adding more pressure on the financial stability. As per the 23rd issue of the Financial Stability Report (FSR) NPAs of the banking sector were projected to increase to 13.5 % of advances by September 2021, from 7.5 % in September 2020, under the baseline scenario. At the same time as per the same report Macro stress tests indicate that the gross non-performing asset (GNPA) ratio of Scheduled Commercial Banks may raise from 7.48 % in March 2021 to 9.80 % by March 2022 under the baseline scenario (RBI, 2021b).

Revenue reduction: - The COVID-19 pandemic has halted the wheel of the economy. During this pandemic situation peoples are scared of the possibility of job loss, salary reductions, economic uncertainty, at the same time so many people have already experienced their salary reduction and ultimately their disposable income has gone down. During this situation banks loans showed downward trend and now people are taking mainly need based loan and they preferred to deposit rather to borrow with the expectation of securing their future. During FY 2020-21, Current account and savings account (CASA) deposits grew rapidly (shown in figure 5). On the other hand, the banks have become liable to pay them interest against those deposits that indicates it will increase banks interest expenses.



Source: RBI, 2021d

Figure 5: CASA growth in CASA and Time deposit

As RBI had announced a loan moratorium and restructuring scheme i.e., resolution framework 2.0. These scheme helps customers to reduce their financial stress but at the same time these cause decline in revenue of banks. Due to this situation cross border transactions have gone down; loan capabilities of individual and small business customers have gone down and NPA stress has also been increasing that why banks interest income declining continuously and impacting banks financial health. It also increases stressed assets. Apart from this bank now offering more insurance products to their customers because now people prefer health and life insurance product than regular typical bank products.

RBI regulatory measures to counteract the impact of COVID 19 on the Indian banking sector:

During this COVID- 19 pandemic situation RBI has announced slew of regulatory measures as a part of a calibrated strategy for overcoming from these pandemic disruptions by several provisions, cutting down repo rate and easing of asset classification norms. RBI has declared relaxation in repayment of debt and improving access to working capital management. At the same time RBI has also focused on reduction of financial stress to the individual borrowers, business holders, so that they can continue their business during the unprecedented COVID-19 crisis.

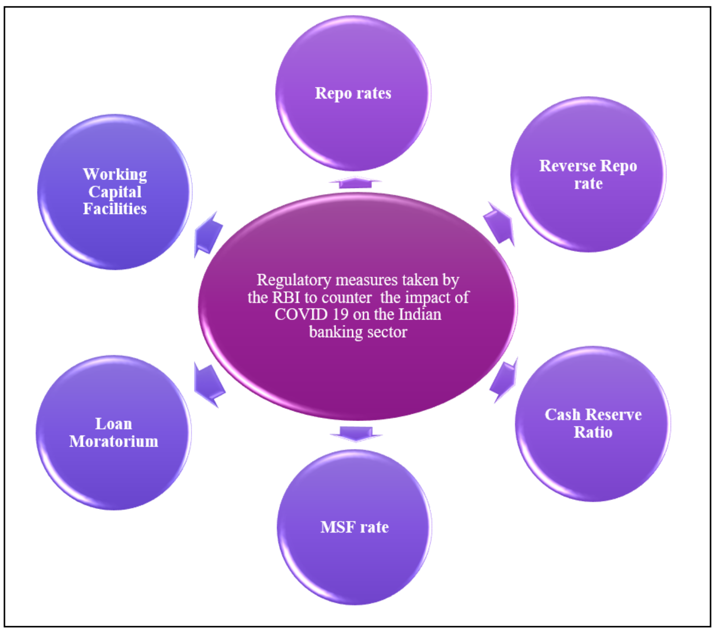


Figure 6: Showing various regulatory measures taken by the RBI to counteract the impact of COVID 19 on the Indian banking sector

Repo rates: - The rate at which the RBI lends money to banks termed as Repo rate. RBI changing its key lending rates according to changing macroeconomic factors. 22nd May 2020, it was a remarkable day, on that day RBI organized a pre-term Monetary Policy Committee meeting and decided to cut repo rate by a record 40 basis points (shown in figure 7). The repo rate or key lending rate was cut down to a fifteen-years low of 4.00%. This modification impacts all sectors of the economy.

RBI uses this rate as to signal monetary policy. The RBI has slashed down the key lending rate/ repo rate by a total of 115 basis points since March 2020 to accelerate economic growth and to adhere the economy to combat with this COVID-19 pandemic crisis (RBI, 2021b). It was the steepest cut since October 2004. Due to reduction of repo rate, banks get the benefit of reduction in the cost of funds and allow them to provide credit at lower interest rate. It will increase the demand for loans due to lower interest rates that means it will help customers to get the credit, business loan at lower cost which eventually pave the way for economic development. In 2021, RBI kept the repo rate unchanged at 4.00%.

Source: CEICDATA.COM https://www.ceicdata.com/en

Figure 7: Repo rate (%)

Reverse Repo rate: - like repo rate, RBI also uses reverse repo as an instrument to control money supply in the economy and stimulate various aspects of economic growth. The rate at which Reserve Bank of India borrows money from the commercial banks termed as reverse repo rate. It is the rate at which commercial banks put their excess money in RBI. During 2020, RBI slash down the reverse repo rate by 40 basis points to 3.35% from 3.75% (shown in figure 8), as the RBI ramped up measures to relieve stress on an economy ravaged by the COVID-19 pandemic. As RBI reduced reverse repo rate, now banks tend to invest their money in other areas in the market and it prompts banks to make more funds/ loan available for the various productive sectors of the economy. It increases the cash flow/ liquidity in the market. In 2021, RBI kept the reverse repo rate unchanged at 3.35% (RBI, 2021e).

Source: CEICDATA.COM https://www.ceicdata.com/en

Figure 8: Reverse Repo rate (%)

Cash Reserve Ratio: -During 2020, in the view of COVID-19 crisis, RBI cuts down CRR to 3% (it is the percentage of total deposit that banks are required to maintain with the RBI). It helps banks to reduce their lending rates and aid monetary transmission in economy. This reduction had made by RBI to provide comfort to banks on their liquidity requirements.

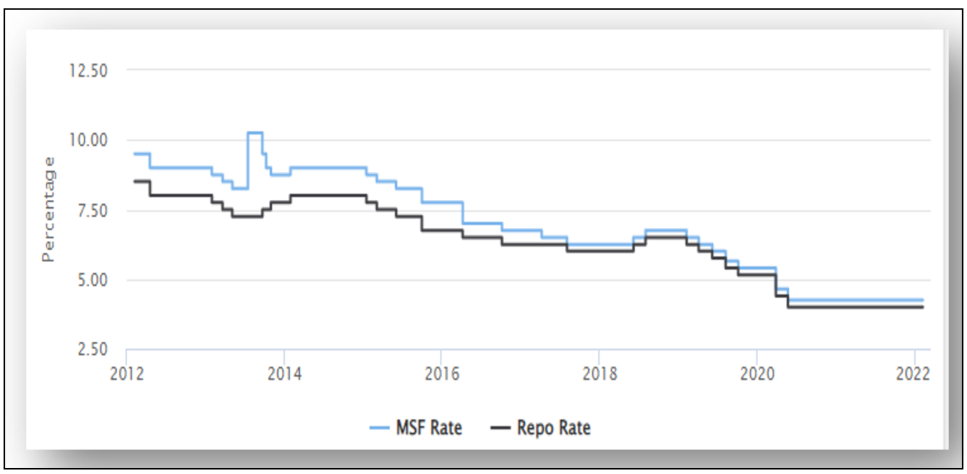
In line with strengthening signs of economic recovery, the RBI has forecast that real GDP, hit by the COVID-19 in 2020-21, is expected to grow by 10.5 per cent in 2021-22 and RBI has scaled back the CRR to 4% in two phases to remove unwinding surplus liquidity from the system (shown in figure 9). As per an estimate by SBI's economic research wing, the restoration of CRR to 4% will drain Rs 1.50

lakh crore (approx.) of liquidity from the system, but due to the adverse effect of the lockdowns imposed by different state governments to fight with the second wave of COVID, the RBI has lowered the growth forecast for FY22 to 9.5 per cent from the previous 10.5 per cent (RBI, 2021a).

Source: CEICDATA.COM https://www.ceicdata.com/en

Figure 9: CRR (%)

MSF rate: - MSF stands for Marginal Standing Facility, it is one types of Liquidity Adjustment Facility provided by the RBI to banks, when banks liquidity totally dries up then banks can borrow funds from the RBI overnight, up to 1% of its NDTL (Net demand and term liabilities) at a higher rate than repo rate. MSF rate refers to the rate at which banks avail MSF facility from RBI. That means MSF rate is more expensive than repo rate. In March 2020 RBI reduced MSF rate 40 basis point (from 4.65% to 4.25%) to increase liquidity and strengthen the Indian economy (shown in figure 10).



Source: CEICDATA.COM https://www.ceicdata.com/en

Figure 10: MSF rate (in %)

Loan Moratorium: - With an aim to support borrowers who were reeling under the monetary impact of the first wave of the Coronavirus in India, Reserve Bank of India (RBI) governor permitted banks in India to offer a loan moratorium of 3 months on term loans, outstanding as on 1st march, 2020. It was really a massive relief for the middle class. Later, the RBI allowed the loan moratorium as part of a restructuring scheme, where the loan moratorium could be extended up to a total period of two years.

Loan moratorium period can be described as a legally authorized period of time during which borrowers can differs their loan installments. This period is also termed as EMI holiday. Generally, it is offered to assist borrowers who is facing temporary financial difficulties to pay installments. Usually, if loan repayment is deferred by the borrower, the borrower's credit history and risk classification of the loan can be negatively affected. But in case of loan moratorium facility, the borrower's credit rating will not be impacted in any way for that particular loan. In, 2021 again RBI permits loan moratorium to support borrowers with the motive to reduce the financial stress of Individuals and Small Businesses (RBI, 2021a).

Working Capital Facilities: - During this pandemic all banks are permitted by RBI to allow three months deferment of interest payment in respect of working capital facility in the mode of Cash Credit and Overdraft. RBI also permitted all banks to reassess the working capital cycle (mainly in the form of elongation in working capital cycle) and revise working capital limit for the borrowers. The above-mentioned steps have taken by RBI as a measure to minimize financial stress of borrowers (The Economic Times, 2021).

CONCLUSION

The outbreak of the coronavirus has severely impacted every sector across the planet in recent years. This outbreak has created such a disturbing situation that it has caused an unprecedented shock to the Indian economy. Banking operations have been affected by this ongoing pandemic. It presents several challenges ahead for the Indian banking sector. Moreover, this pandemic has highlighted deficiencies within the Indian banking system. Banks should now focus on utilizing new technologies in their operations and make their infrastructure agile to manage these challenges. Ultimately, use of technology would scale back the dependency on hand operated entries and manual operations within banks. Now, banks have got to create such an environment in order for the health of their employees and customers to be protected. During this difficult period, banks must also reskill their employees on new processes and new ways of working. People are now playing it safe as a consequence of the pandemic, and there has been a huge shift toward saving instead of borrowing. It enhanced the amount of money kept in bank accounts. During this pandemic, people are playing it safe. They have started saving their earnings and keeping them in their bank accounts for uncertain situations. It enhanced the amount of money kept in bank accounts and a downward trend in loans has been observed. As a result, a liquidity crisis has been observed during this hard time. However, RBI has announced Resolution Framework 1 and Resolution Framework 2.0 to combat this situation. But still, the government and RBI need to do many things in the near future to beat the negative impact of COVID-19. The RBI and the government should provide more loans and relax loan criteria to provide more liquidity in the economy and reduce the financial stress of all small and medium enterprises. The immediate learning from the pandemic is that the government should make our economy stronger to soak up the impact of this type of crisis in the future.

ACKNOWLEDGMENT

The completion of this article could not have been possible without the motivation and support of respected professor Dr. Ashish Kumar Sana, Dr. Biswajit Paul, Dr. Bappaditya Biswas and Rohan Prasad Gupta . A debt of gratitude is also owed to Prof. Dr. Sandeep Poddar and the entire editorial team for giving the opportunity to contribute this research article for the esteemed edited volume.

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