Securitisation will fund small finance banks, NBFCs growth: Moody's

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MUMBAI: Securitisation will continue to be instrumental for the eight micro finance institutions turned small Indian finance banks, as it will take time for them to develop a retail deposit franchise, says a report by rating firm Moody's.

The non bank finance companies and MFIs will continue to fund through securitization at the same time as the sector grows.

In India, the Reserve Bank of India in September 2015 granted approval to 10 entities -- including eight microfinance institutions (MFIs) -- to operate as small finance banks.

With the aim of promoting financial inclusion to under-served segment, these small finance banks will accept deposits and extend credit to marginal farmers and small business units. Their mandate overlaps with the target market of MFIs.

Securitization is a way by which NBFCs fund themselves. "However, in India, in times of financial stress - as occurred during the micro-finance crisis in Andhra Pradesh in October 2010 (see box) - securitization markets remained open as a funding source for NBFCs-micro-finance institutions," the report said.

"The number of bank branches per 100,000 population in rural and semi-urban areas is still less than half of that in urban and metro areas13, we expect that both NBFCs that focus on micro-finance (NBFC-MFIs) and small finance banks will co-exist," the report said.

Securitization will continue to be instrumental for these small finance banks, as it will take time for them to develop a retail deposit franchise. NBFC-MFIs will continue to fund through securitization as the sector grows.

Also banks are required to lend 40% of credit towards priority sector, and this prompt banks to invest in pass through certificate (PTC) securitizations issued by NBFCs; banks that cannot satisfy RBI targets for lending to priority sectors of the economy can meet the requirements by investing in securitizations issued by NBFCs where the underlying assets are loans to priority sectors, the report stated.

PSL targets apply across a wide range of asset classes, including commercial vehicles, micro-finance receivables and loans against properties.

Most private sector banks find it difficult to meet their entire PSL target organically, because the requirements generally demand the disbursement of loans to borrowers across a wide geographical spread - including rural and semi-rural locations - which entails having intensive origination and collection infrastructure throughout these areas.