Banks say risk-weight cut on loans to NBFCs will support credit flow to sector

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Though the Reserve Bank of India recently took steps to enhance credit flow from banks to non-banking finance companies (NBFCs), Bankers say there are no liquidity issues in lending to these companies. They emphasise that paring risk weights for this segment, whereby relatively less capital will be required to make loans, will encourage banks to step up lending.

NBFCs, including housing finance companies (HFCs), have felt the impact of default by IL&FS and some of its arms. It has raised the spectre of NBFCs not being able to roll-over the debt raised from mutual funds and banks.

Further, the recent credit rating downgrade of, Supertech Ltd, by Brickwork Ratings has raised concerns about developer loans possibly turning sour.

"RBI needs to reduce the risk weight for banks on their NBFC lending. Lower risk weight means lower capital requirements. That will push banks to lend to NBFCs. Banks are facing a problem of capital not liquidity," said a top banker.

That the financial system, including banks, are comfortable on the liquidity front is underscored by the last auction (on October 19) of five government securities aggregating a notified amount of ₹11,000 crore. The RBI received bids aggregating ₹39,380 crore.

Further, in the fixed rate reverse repo operation conducted on October 17 (for two days) and on October 19 (overnight), Banks parked surplus liquidity aggregating ₹12,829 crore and ₹10,375 crore, respectively, with the central bank.

Risk weight assigned to assets (loans/ investments), which is prescribed by the RBI, and the capital required to make the loans/investments are directly co-related. If a class of loans carries higher risk weight then banks will need to set aside more capital to give such loans.

For example, if the risk weight on NBFCs rated 'A' and 'BBB' are 50 per cent and 100 per cent, respectively, then for a ₹100 crore loan made by a bank to each of these companies, the capital it will need to set aside will be ₹4.5 crore and ₹9 crore, respectively.

At a time when interest rates on money market instruments such as commercial papers have gone up for NBFCs due to increased risk perception, bankers say they are game to step up lending to these companies. But a cut in the risk weight on such assets will give them added comfort to do so.

Last Friday, the RBI activated additional funding lines for NBFCs, including HFCs, by temporarily relaxing regulatory prescriptions so that banks can take higher exposure to them and also draw more liquidity under the so-called ‘liquidity coverage ratio’.

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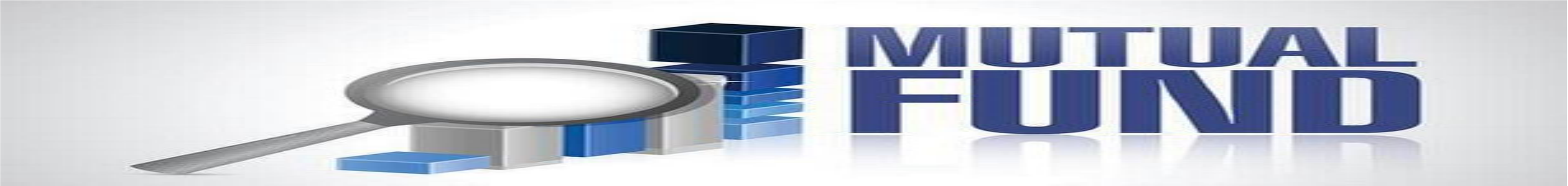

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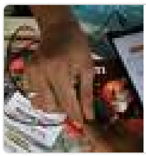

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