Loans to developers could cause trouble for NBFCs, HFCs

By: FE Bureau | Updated: December 24, 2018 7:37 AM

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While a systemic contagion is unlikely, a few non-banking financial companies (NBFCs) and home finance companies (HFCs) that have exposure to weak property developers could be in trouble. The real estate sector shows few signs of recovering in the near term as sales have been sluggish and inventories remain high. Asset prices have not corrected meaningfully and consequently there are few buyers who can afford to buy homes. Banks are better off because they have relatively more exposures by way of lease rental discounting and a relatively small exposure to what are called core developer loans.

These core loans are more risky. While these grew at 18% between 2014-15 and 2017-18, the NBFCs added exposures at a very modest pace but clocked in a growth of what could be a suicidal 46%. Indeed, for non-banks and HFCs the share of developer loans to total credit jumped from 6.2% in 2014-15 to 10.7% in 2017-18. While the lenders in the top rung do not have anything to worry about, intermediaries that are stuck with big exposures to poor quality assets could be adversely impacted.