

Why the RBI's measures for NBFCs may not ease the sector's pain

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Banks have been lending only to good quality NBFCs; they may continue to be wary of risky assets

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Aside from lowering repo rate and reducing risk weights for consumer credit to boost lending, the RBI also undertook two measures to ease the ongoing pain in the NBFC sector. In a bid to free up banks' capital, the RBI raised the permissible bank's exposure limit to single NBFC to 20 per cent of Tier I capital from 15 per cent earlier. It has also allowed bank lending to NBFCs for further on-lending to agriculture, micro and small enterprises and housing—to be counted as priority sector lending.

Currently, all domestic and foreign banks with at least 20 branches are required to lend a minimum of 40 per cent of their total loans (Adjusted Net Bank Credit (ANBC) or credit equivalent amount of off-balance sheet exposure (whichever is

higher)) to the priority sector (agriculture, micro enterprises, weaker sections etc). By counting a portion of the lending done by banks to NBFCs on lending to some of these segment as priority, the RBI hopes to induce banks to lend more to NBFCs.

While the RBI's measures can help ease flow of credit to NBFCs, it will only aid few NBFCs.

Going by the data put out by RBI, after growing by 27 per cent YoY in FY18, bank lending to NBFCs grew by a higher 29 per cent in FY19. As of June, the growth has been even higher at 37 per cent; yet the noise around the troubles of NBFC sector, has only grown louder.

This is because large NBFCs with sound backing and quality loan book have been able to raise funds from banks (maybe at a higher cost), over the past year, despite sectoral challenges. The problem lies with funding NBFCs with high exposure to stressed segments such as real estate (developer segment), infrastructure and LAP.

Hence the key issue of channelling funds to cash-strapped NBFCs and improving the risk perception, will not be addressed by the RBI's Wednesday measures. Banks will continue to lend to good quality businesses and the RBI's measures are unlikely to induce them to take on riskier assets. The growing concern of unresolved liquidity issue with many NBFCs, will likely persist.

SBI focusses on high quality NBFC

Banks' preference to quality assets and loan book over the past year, has seen credit flow to select NBFCs—the various regulatory tweaks hence benefitting only few players.

SBI's latest June quarter report, that shows the break-up of its NBFC book, gives an indication of how banks have been wary of risks within the sector. Of SBI's exposure to housing finance companies, 70 per cent are those that are either

backed by large private sector institutions or by PSUs. Only 30 per cent are 'other private' players.

Of SBI's exposure to other NBFCs other than housing finance, 46 per cent pertain to central and state government and those backed by PSUs, 36 per cent are backed by large private sector institutions; only 18 per cent are other private NBFC players.

SBI has stated that it has been paring down its exposures in the 'private others' category of NBFC and growth has been driven by government sector or PSU backed NBFCs.

If the largest lender's loan book composition is any indication, it would appear that much of the measures taken over the past year have aided select government/PSU backed or large NBFCs.

Several measures

Aside from conducting significant amount of OMOs or open market operations—buying of government securities—the RBI has also been undertaking other regulatory measures over the past year to ease liquidity conditions for NBFCs. RBI allowed banks to reckon government securities held by them up to an amount equal to their incremental outstanding credit to NBFCs and HFCs, as liquid assets under LCR. It also allowed banks to offer partial credit enhancement (PCE) to bonds issued by some of the NBFCs.

In February, it allowed rated exposures of banks to all NBFCs, to be risk-weighted as per the ratings assigned by rating agencies, rather than the blanket 100 per cent weight applicable earlier.

Pursuant to the Budget announcement of one-time partial credit guarantee to PSU Banks for high-rated assets of financially sound NBFCs, the RBI had announced additional liquidity facility to banks for purchase of assets from and on-lending to non-banking financial companies and housing finance companies.

NBFC **RBI and other central banks**

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