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Market Watch

Fitch says liquidity pressures faced by non-banking financial sector to continue

BY PTI | DEC 03, 2019, 10.45 PM IST

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Liquidity pressures faced by the non-banking financial sector following the IL&FS failure are likely to continue though funding costs have come off the peak, [Fitch Ratings](#) said on Friday.

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"We view wholesale and [housing finance companies \(HFCs\)](#) as more vulnerable -- given their higher leverage, weaker asset-and-liability maturity (ALM) profiles and higher concentration risks. Large retail finance companies with well-managed [ALM](#) profiles should continue to access bank and capital markets funding. Further, funding diversification in the offshore markets by larger issuers would benefit their funding profiles," it said in its outlook for emerging market finance and leasing companies.

Indian finance and leasing companies are likely to grow at a slower pace in 2020 than in prior years, amid weaker economic growth and liquidity constraints, it said.

Fitch said its 2020 sector outlook is underpinned by challenging operating environments, lower growth prospects, and rising funding pressure. "Liquidity pressures faced by the sector following the IL&FS failure are likely to continue, though funding costs have come off the peak."

Increasing competition to offset lower growth may weigh on profitability and test risk appetite.

"This is likely to have an impact on loan growth, including business loans and commercial vehicle (CV) loans. The slowdown in automotive sales has had a particular impact on auto-loan growth and is likely to continue, while the acute slowdown in real estate may have a prolonged impact on construction financing as new disbursements have halted," it said.

Companies focused on small-ticket consumer loans continue to grow above the industry rate, owing to the lower credit penetration and higher exposure to rural sectors where credit competition with banks is lower.

Certain asset classes (new CV loans, metro and tier-I housing loans, and large-ticket loans against property) could see weakening margins due to rising competition from banks, while funding costs are likely to stay high as market rates should remain volatile -- given the liquidity strain, Fitch said.

HFCs with thinner margins are more vulnerable to losses if asset-quality pressures increase due to rising real estate delinquencies. The economic slowdown, coupled with deterioration in corporate and SME (small and medium enterprise) earnings, will affect asset quality for CV loans and loan against properties.

"The weaker growth outlook should ease pressure on capitalisation. However, weakening asset quality for companies exposed to the construction sector may pressure capitalisation. Access to new capital is likely to be challenging as the market appetite for equity investments in these companies remains subdued," it said.

Indian finance and leasing companies cater to a diversified retail market, including consumers and SME segments, which may have a moderate impact on asset quality. However, granular portfolios, high-yield profiles and matched asset tenors provide an adequate buffer against system-wide liquidity and asset-quality shocks, it added.

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