Role of NBFC in the overall Credit Growth in the Market

Prologue

- NBFCs have given credit to important industries like real estate, infrastructure, and MSMEs, which have recently played a significant role in accelerating economic growth.
- The overall amount of credit provided by NBFCs is increasing, with the total outstanding balance reaching Rs. 31.5 lakh crore.
- NBFCs play a crucial role in the Indian financial system, especially in providing credit to sectors that are not served by traditional banks. They cater to the needs of small businesses, low-income households, and other underserved markets, filling the gap left by banks.

Financial Access and Supportive Government Schemes

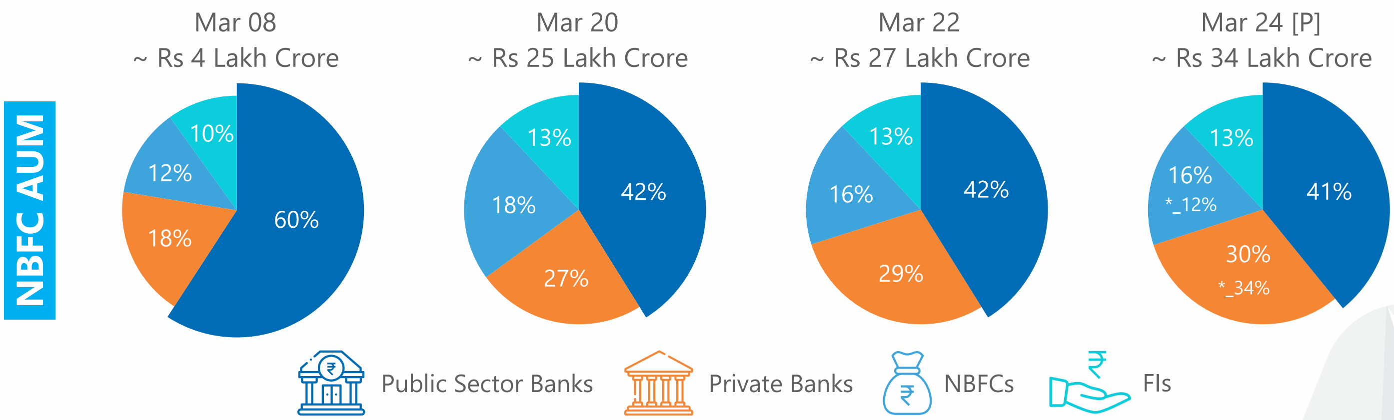
NBFCs have gradually become important mechanisms to fuel growth and entrepreneurship due to the launch of government-backed schemes including Pradhan Mantri Jan-Dhan Yojana which has contributed to a significant increase in the number of bank accounts. These NBFCs have also been key in being able to mitigate and manage the spread of risks during times of financial duress and have increasingly become recognized as complementary services to banks.

- They provide credit to borrowers who may not be able to obtain credit from banks, such as small businesses and low-income households.
- They offer a wider range of lending products than banks, such as leasing, hire-purchase, and mortgage loans.
- They are more willing to lend to borrowers in newer and emerging sectors, such as the renewable energy and technology sectors.
- They provide credit at competitive interest rates, which can help to boost economic growth

NBFCs do play a critical role in participating in the development of an economy by providing a fillip to transportation, employment generation, wealth creation, bank credit in rural segments and to support financially weaker sections of the society. NBFCs have evolved given the extensive changes in the regulatory framework for NBFCs in India which have moved from simplified regulations to stringent and extensive regulations as well as towards rationalization per the currently revised NBFC regulatory framework.

Market Share of NBFCs in Overall Credit

NBFCs had steadily increased their market share till recent years, with AUM accounting for as much as 18% of the overall credit pie in March 2019, up from 12% in March 2008. Several challenges over the past three fiscals lowered their share to 16% in fiscal 2022, with banks making bigger growth strides. However, NBFC growth is expected to pick up from here on, which should help sustain their ~16% AUM share.

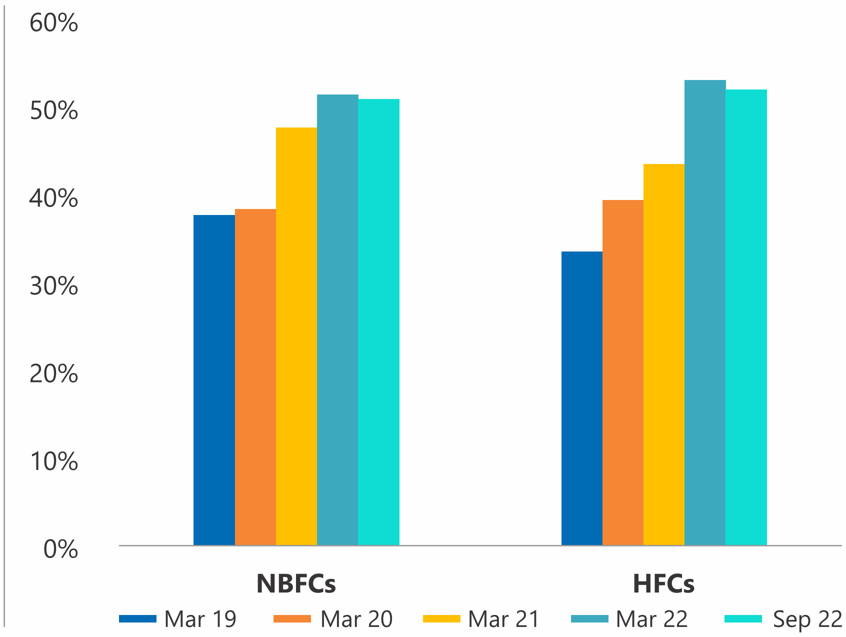


Increase in NBFCs' AUM from just Rs 3.6 lakh crore in March 2008 to almost Rs 27 lakh crore in March 2022, and expected to increase further, indicates the importance of the sector to overall credit delivery in the economy.

Stronger Balance Sheets, Better Asset Quality Underpin Growth

NBFCs are stronger and more resilient today, and better positioned in almost all operationally critical parameters. On the capital front, NBFCs have raised almost Rs 70,000 crore of equity in the past 3.5 years, which has materially improved gearing. The subdued business landscape in the past three fiscals also contributed to the better gearing.

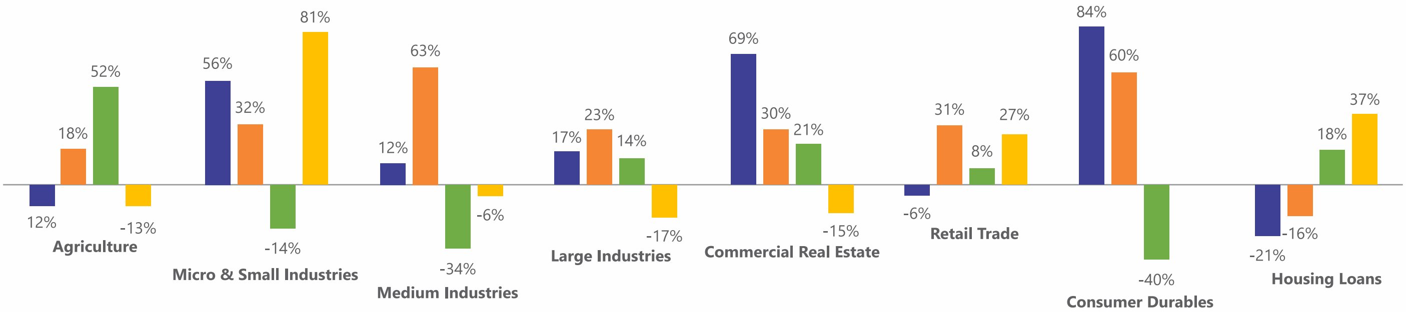
Provisioning levels also increased in the past couple of years, as NBFCs created management overlays to provide for uncertainty pertaining to the pandemic. Overall, the sector has stronger balance sheets.



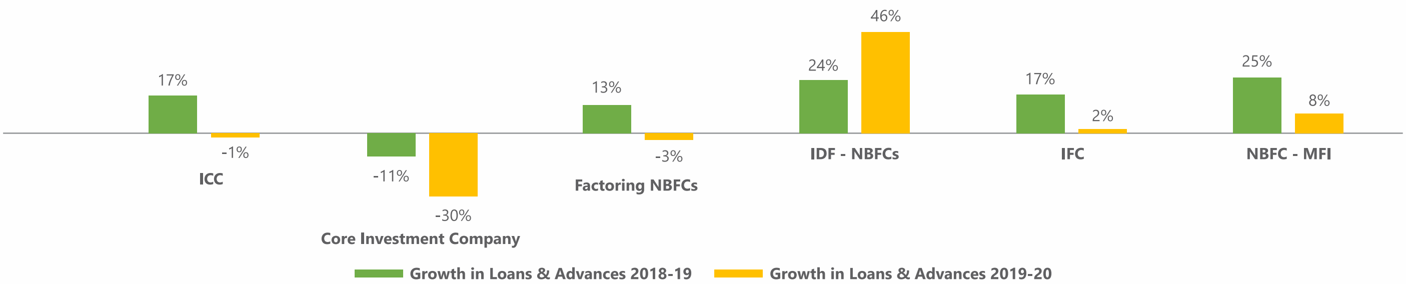
Between March 2021 and March 2022, there was a marginal increase for a few asset segments amid lingering concerns regarding the restructured book. Asset quality metrics have improved across segments in the first half of this fiscal based on the numbers as on September 30, 2022.

The fundamentals are expected to hold with improvement in the macroenvironment. At the same time, restructured books have reduced considerably over the past year, with most segments now holding negligible outstanding restructured portfolios.

Sectoral Credit Growth : Key Sub Sectors



Growth in Loans & Advances



Some of the key sectoral credit growth across key sub-sectors is for MFIs which have clocked 80% growth in 2019-20 and housing loans which have registered 37% growth in the same timeframe. Similarly, growth in loans and advances for NBFC-IDFs and NBFC-MFIs have registered strong growth at 46% and 8% respectively for 2019-20 period and similarly also demonstrated an upward growth trend in 2018-19.

Competition From Banks And Rising Interest Rates

While NBFCs are relatively well placed today as compared with the past few years, competition from banks and the rising interest rate scenario pose challenges. Competition from banks has intensified, especially in the traditional segments. The banking system has also gone through its fair share of cycles.

Grappling with asset quality concerns, inadequate provisioning and weak capital buffers in 2018, the banking sector now has manageable non-performing assets (NPAs) with a healthy provision coverage ratio (PCR) and comfortable capital buffers; and is well placed to tap growth opportunities. In fact, banks have outpaced NBFCs in growth since March 2020. While the gap has narrowed this fiscal, NBFCs continue to lag.

NBFCs have faced funding-access challenges in the past few years, especially in debt capital markets. Banks, though, have provided significant support to them, with bank credit to NBFCs touching an all-time high of Rs 11.7 lakh crore as of

September 30, 2022. Consequently, the share of bank funding in the overall resource profile of NBFCs increased to 36% in September 2022 from 27% four years ago, nearly mirroring the drop in share of non convertible debentures (NCDs).

For deposit-taking NBFCs, fixed deposits (FDs) were a big focus area, especially as bank FD rates were low. While debt capital market issuances have been subdued over the last year or so given the rising interest rate environment, there has been some uptick in the last quarter or so.

Another funding route that has helped NBFCs is securitisation, including through direct assignment. Here, too, banks account for the bulk of pool purchases, providing indirect funding to the NBFC sector.

Outlook

Non-Banking Financial Companies (NBFCs) play a significant role in the overall credit growth in the market. They provide credit to a wide range of borrowers, including individuals, small and medium enterprises (SMEs), and large corporations. NBFCs are also a major source of credit for the housing and infrastructure sectors.

In the Indian context, NBFCs have been a key driver of credit growth in recent years. In the financial year 2022-23 (April-March), NBFCs' credit grew by 16.7%, compared to 10.7% growth in bank credit. This was led by strong growth in the lending to the housing and retail sectors.

Since NBFCs work in connection with the government and the private sector on operations, they significantly raise the living conditions of the general community. Due to its reputation for supporting industry, fostering the development of infrastructure, and even serving as the foundation for the average person's finances, the banking sector will always be of utmost importance in the business world.

However, in recent times NBFC sector has played a crucial role, and its presence in a country only serves to strengthen the economy.

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NBFCs offer a wider range of lending products than banks, such as leasing, hire-purchase, and mortgage loans.

NBFCs are more willing to lend to borrowers in newer and emerging sectors, such as the renewable energy and technology sectors.

NBFCs provide credit at competitive interest rates, which can help to boost economic growth.

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