FIDC

Finance Industry Development Council

Non-Banking Finance Companies (NBFCs) -

Contribution to the Economy & Way Forward

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Chairman
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NBFCs : Overview (As on March 31, 2017)*

- No. of Deposit Taking NBFCs = 179
- No. of Non-Deposit Taking NBFCs
  - -Asset Size < Rs. 500 cr = 11,118
  - -Asset Size >= Rs. 500 cr (NBFC-ND-SI) = 220
- Total No. of NBFCs Registered with RBI = 11,517

* As per RBI's Financial Stability Report dt. June 2017

NBFCs : Overview (As on March 31, 2017)*

As per RBI's Financial Stability Report dt June 2017 *Y-o-Y Growth*

	FY17 (FY16)
Growth in Aggregate Balance Sheet size (Y-O-Y)	= 14.50% (15.50%)
Growth in Share Capital	= 15.20% (4.80%)
Net Profit (%age to total income)	= 14.00% (18.30%)
Growth in Loans and Advances for 2016-17	= 16.40% (16.60%)
Total Investments	= 11.90% (10.80%)
Return on Assets (net Profit as %age of total assets)	= 1.80% (2.10%)
Return on Equity (net profit as %age of equity)	= 6.80% (7.90%)
Gross NPA (as %age of total advances)	= 4.40% (4.60%)
Net NPA (as %age of total advances)	= 2.30% (2.50%)
CRAR (minimum prescribed by RBI is 15%)	= 22.00% (24.30%)
Growth in Total Borrowings for 2016-17	= 15.00% (15.30%)
Leverage Ratio	= 2.80% (2.80%)

NBFCs have performed better than Public Sector Banks

* As per RBI's Financial Stability Report dt. June 2017

NBFCs : Overview (As on March 31, 2017)*

Distribution of Credit given by NBFCs

Industry	- 42.20%
Services	- 30.80%
Retail Sector	- 21.50%
Others	- 5.50%

** As per Economic Survey 2016-17, Volume II dated August 2017, Ministry of finance, Government of India

NBFCs : Overview (As on March 31, 2017)*

NBFCs' Assets

Loans & Advances - 70%
Investments - 17%
Others(*) - 13%

(*) *Cash and Bank balances*
Other Current Assets
Other Assets

** As per Economic Survey 2016-17, Volume II dated August 2017, Ministry of finance, Government of India

NBFCs : Overview (As on March 31, 2017)*

NBFCs' Liabilities

Capital & Reserve - 26.10%
Bank borrowings - 23.10%
Debentures - 21.10%
Commercial papers - 9.50%
Others (*) - 20.20%

(*) *All India FIs*
ECBs
Public Deposits
Pension Funds
Current liabilities & provisions

** As per Economic Survey 2016-17, Volume II dated August 2017, Ministry of finance, Government of India

NBFCs : Overview (As on March 31, 2017)*

NBFCs' Borrowings from Financial System

- Pension Funds are new investors
- Bank Borrowings have declined from last year

SCBs	- 41%
AMC MFs	- 35%
Insurance Cos	- 20%
Pension Fund	- 2%
Others	- 2%

* As per RBI's Financial Stability Report dt. June 2017

NBFCs : Overview (As on March 31, 2017)*

Network of the Indian Financial System

Bilateral exposure
(both payables and receivables)

NBFCs are the 3rd Largest

Scheduled Commercial Banks	- 51%
AMCs MFs	-13%
NBFCs	-12%
All India FIs	- 7%
Insurance cos and HFCs	- 8%
UCBs & Pension fund	- 1%
Others	- 8%

* As per RBI's Financial Stability Report dt. June 2017

Role of NBFCs

Greater Role of NBFCs in the Current Scenario

- The greater role of non-banking sector in resource mobilization, and hence credit intermediation, helped commercial sector, albeit partially, to make up for historically low bank credit outstanding growth. Thus, problems in the banking sector are leading to greater reliance on non-banks for borrowers as well as savers.

- Against asset quality concerns, credit intermediation by public sector banks has retrenched and that by NBFCs and Mutual Fund Funds has increased significantly.

* As per RBI’s Financial Stability Report dt. June 2017

Why NBFCs

- Successful track record of more than 60 years

- Key aspects of financial activity are well regulated (almost at par with banks):
  - Registration with the regulator
  - Minimum size (Net owned Fund)
  - Minimum Capital Adequacy Ratio
  - Prudential Norms on asset classification, income recognition and provisioning
  - Know Your Customer (KYC) & Anti Money Laundering Guidelines
  - Asset Liability Management Guidelines
  - Credit Concentration Norms
  - Maintenance of SLR
  - Code of Fair Business Practices

- Promote Urban Financial Inclusion also (in addition to rural financial inclusion)
- Use modern technology and have developed sound MIS
- Small & Medium NBFCs are having a local/ regional presence (and the large NBFCs through their branches or franchisees) are well versed with the local conditions/requirements

Why NBFCs ? – Contd..

- Prevent concentration of credit risk in banks only and complement the banking services

- Provide prompt & tailor made services with least hassles

- Provide a personalized touch – Guidance in insurance matters and help in their hour of need at any time of the day

- Cater to a class of borrowers who :
  - are “unbankable”
  - Do not necessarily have high income
  - are honest & sincere (gauged by the personal touch maintained with them)

Experts' Views on the Role of NBFCs

All the Expert Committees / Task Forces / Working Groups set up by Govt of India OR RBI have fully recognized and highly appreciated the Role of NBFCs in providing need based credit to the "unbanked" segment of the society in rural, semi urban and urban areas

Financial Inclusion – As Defined by RBI

- Financial Inclusion is the process of ensuring access to <u>appropriate financial products and services</u> needed by all sections of the society in general and <u>vulnerable groups</u> such as weaker sections and low income groups in particular at an <u>affordable cost</u> in a <u>fair and transparent manner</u> by <u>mainstream institutional players</u>

How suitable are NBFCs for Promoting Financial Inclusion

	NBFCs
Reliability	High- 20 Yrs of regulations almost at par with banks
Affordablitiy	High- compared to MFIs & local money lenders
Accessibility	High- As they cater to unbankable segment in rural & semi urban areas
Flexibility	High- A balance between flexibility & low delinquencies maintained

NBFCs have all the key characteristics to achieve Financial Inclusion

Innovation and Flexibility

NBFCs have shown great innovation and flexibility commensurate to the needs of the borrowers, within the prescribed regulatory framework

Regulation of NBFCs

Legal Frame Work

The Reserve Bank of India Act, 1934

(As amended by Reserve Bank of India (Amendment) Act, 1997)

- Chapter IIIB : Provisions Relating to Non-Banking Institutions Receiving Deposits and Financial Institutions

- RBI is empowered to regulate

  - Guidelines/Directions Issued By RBI which are dynamic

Definition of NBFC

Sec. 45 I (c) and Sec. 45 I (f)

- Define the activities covered under the definition of NBFCs
- The List of activities include Financing, Acquisition of shares/ stock/ bonds/debentures or securities, hire purchase, collecting monies in lump-sump and otherwise
- Does not include agricultural operations, industrial activities, sale purchase of

  goods, purchase/construction/sale of immovable property
- A company must have any of these activities singly or taken together as its Principal Business to be defined as a NBFC

Definition of Principle Business

RBI Press Release Dt. April 8, 1999

- If 50% or more of a company’s total assets (netted off by intangible assets) are financial assets

and

- If 50% or more of a company’s gross income is from financial assets

then the Principal Business of the company is that of a NBFC

Note : Bank FD is not considered as a financial asset

Classification of NBFCs

Classification

Liabilities Based	- Deposit taking	NBFC – D (Category-A)
	- Non- Deposit taking	NBFC - ND (Category-B)
	- Subsidiary Company	NBFC - ND (Category-C)
Activity Based	- Asset Financing	NBFC - AFC
	- Loans	NBFC – LC
	- Investments	NBFC - IC
	- Infrastructure Financing	NBFC - IFC
	- Micro Financing	NBFC - MFI
	- Factoring	NBFC – FACTORS
	- Infrastructure Debt Fund	IDF – NBFC
	- Core Investment	CIC
Size Based	- Assets of 500 Crores & Above	NBFC - ND - SI (Systemically Imp.)

The Key Issues

Overview

- NBFCs not included in the official agenda on Financial Inclusion
- Focus has been on “regulation” instead of “development” of NBFCs
- Lack of level playing fields with banks & HFCs, specially in taxation matters
- Fund raising is a big challenge, specially for small & medium NBFCs
- Some of the State Govts treat NBFCs as money lenders under the State Money Lenders’ Act despite regulation by the RBI
- Need to assign differential risk weights to assets based on their risk profile
- Need for Formalized arrangement for Regular interaction with RBI and the Ministry of Finance
- “Leasing” needs to be promoted as a tool for capital formation

Funding of NBFCs

- Bank Funding
  - Lack of linkage by banks with NBFCs despite strong recommendations by various Expert Groups
  - Need for liberal Bank Funding at competitive rates
  - “Wholesaler – Retailer” relationship between banks and NBFCs needed

- Deposit acceptance is discouraged by RBI.

- Securitization Guidelines issued by RBI have restricted securitization of receivables
  - it needs to be ‘Originator – friendly’

- Priority Sector status accorded to bank lending to NBFCs for on-lending to priority sector has been withdrawn.
- Urgent need for a refinancing window specially for small and medium NBFCs
  - MUDRA can play an important role

Imprudent Taxation of NBFCs

- Income Tax Act - Deduction allowed to banks, FIs & HFCs, for non-recognition of income on NPAs and provisions made against NPAs (u/s 36(i)(vii) of Income Tax Act) @ 7 to 10% – NBFCs allowed 5% only*
- Income on NPAs is accounted on receipt basis u/s 43D of Income Tax Act by Banks and FIs - denied to NBFCs only
- Exemption from TDS requirements on EMIs denied to NBFCs only
- TDS on lease rentals entails deduction of TDS from the principal component also
- GST rate on Lease Rentals of an asset give on lease = GST rate on the normal sale of that asset – No incentive to Leasing
- GST on Sale of Repossessed Assets is unjustified
- Denial of depreciation benefits to the lessor in-spite of CBDT circular
- Low rate of depreciation (@15%) on Construction and Mining Equipment - need to increase it to at least 30% (at par with CVs)

**Union Budget 2016-17*

Recovery Avenues for NBFCs

- Union Budget 2015-16 granted coverage under the SARFAESI Act, but with the following riders:
  - Only NBFCs with asset base of 500 cr and above, have been given coverage
  - Sections on Enforcement of Security Interest applicable only in cases where the ticket size of the loan is 1.0 cr and above

- NBFCs do not have access to Debt Recovery Tribunals

- Indirect means - Criminal complaints for Cheque bouncing u/s 138 of The Negotiable Instruments Act : Time consuming and not very effective

- Filing Application for appointing "Receiver" under the Arbitration Act – Sale of the asset cannot be done till the arbitration proceedings end

Recent Developments

World Bank Group

(Through IFC)

Collaborates with FIDC to conduct Training Programs for NBFCs on

- Commercial Credit Reporting
- Movable Asset Financing

NABARD
Initiates Refinancing of NBFCs

- *NBFCs with Credit Rating AA- and above refinanced by NABARD*

- *NBFCs with lower Credit Rating to be refinanced by NAB SAMRUDDHI (Subsidiary of NABARD)*

Hon’ble Prime Minister

Shri Narendra Modi

in his address to the nation on December 30th 2016 announced coverage of NBFCs under the Credit Guarantee Scheme (CGTMSE) for MSME Lending

Following the PMs address, NBFCs are engaged in regular discussion for MSME Financing, with:

- Ministry of MSME

(through Secretary and Additional Secretary)

- SIDBI
- CGTMSE
- MUDRA

Recent Developments

- FDI Norms have been further relaxed – entry level fixed at 2 cr and additional capital requirements done away with

- NBFCs with asset base of 500 cr & above given coverage under the SARFAESI Act

- Demonetization had adversely impacted collections & disbursements in Q3 & Q4 of FY 2016-17

- Insolvency and Bankruptcy Code, 2016 is a game changing law :
  - Recognizes business failures and provides an exit route
  - Acceptance of Insolvency application against the defaulting debtor by NCLT stays all other legal proceedings under any other law
  - Time bound resolution plan
  - If resolution is not feasible, liquidation in a time bound manner
  - Clearly lays down priority in which various creditors, claimants will be repaid
  - Creditors dues and Employee wages get higher priority over Govt dues

- Impressive growth, better asset quality (low NPA levels), adequate CRAR have put NBFCs as a Bright Spot in the economy

Way Forward

Future Scenario

- Relaxation in norms likely to attract lot of FDI
- RBI may create only 2 categories of NBFCs – CIC and Non CIC
- Indian Finance Code (IFC) by FSLRC proposes “activity” & not ‘entity” based regulation
- Huge potential for financing SMEs/MSMEs by NBFCs
- Leasing as a tool for capital formation and lending to low capital SMEs needs to be promoted : World Bank has shown interest
- New Players like P2P Lenders may change the rules of the game
- Financial Technology (Fintech) shall play a transformational role
- “Intangible” Asset based lending holds immense promise and potential

NBFCs Role in the PM's Vision of New India

- *Driving Financial Inclusion for more than 70 yrs*
- *Innovation and Flexibility - making them more acceptable and accessible*
- *Promoting & Encouraging Entrepreneurship*
- *Likely to play a key role in MSME Financing*
- *Enhanced Reliability due to :*

  - Regulation history of 20 yrs
  - Regulatory Framework "Harmonised" with Banks and other Fis
  - Better Asset Quality – Lower level of NPAs
  - Impressive & sustained Growth

Thank You