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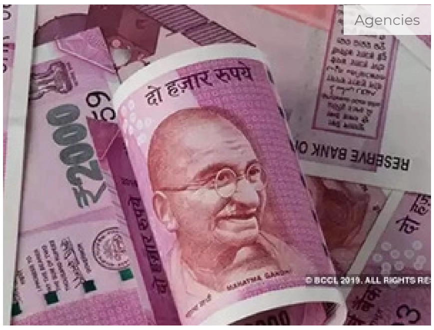
Bank lending to NBFCs surges, smaller companies face higher costs

By Saloni Shukla, ET Bureau Last Updated: Jul 14, 2022, 01:24 AM IST

Synopsis
Data shows that bank loans to non-bank lenders touched Rs 11 lakh crore in May 2022, having expanded by Rs 1.87 lakh crore in 12 months in absolute terms. This is at a time when mutual funds continued to reduce their exposure to NBFCs. During the same period, mutual fund debt exposure to non-bank lenders dropped 3.4% to Rs 1.5 lakh crore.



A huge quantum of borrowings to be raised by large NBFCs would lead to a further increase in the banks' exposure to the sector, and small NBFCs thus could face crowding out, the report said.

Non-bank finance companies (NBFCs) are increasingly turning to banks to meet their funding requirement with the latest data from the Reserve Bank of India (RBI) indicating a 21% year-on-year jump in bank loans to non-bank lenders. Borrowing is shifting to the banking system amid a sharp pullout of funds from debt mutual funds and rising funding costs in capital markets, experts said.

“The borrowings of NBFCs could get skewed to banks in FY23, given the hardening of rates in the capital markets,” said Pankaj Naik, director at credit rating agency India Ratings. “Small NBFCs could witness a sharp increase in their funding costs as the sector moves towards banks for meeting its funding requirements,” he said. “A large quantum of borrowings to be raised by large NBFCs would lead to a further increase in the banks’ exposure to the sector, and small NBFCs thus could face crowding out.”

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Mutual funds have been steadily reducing their exposure to nonbank financiers after having burnt their fingers post the collapse of Infrastructure Leasing and Financial Services (IL&FS) in August 2018. While non-banks faced a turbulent liquidity crisis in the subsequent months, data collated by CareEdge shows that growth in bank credit to NBFCs witnessed a healthy growth of 11.2% in 2021-22 and has continued its upward trajectory, reporting a growth of 17.4% in April 2022 and 20.6% in May 2022.

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At the same time, investments in corporate debt of NBFCs dropped by 18.1% on year to `74,000 crore in May 2022. The percentage share of NBFCs to total corporate debt too declined to 4.4% in May 2022 from 5.4% in May 2021.

Analysts pointed out that despite the sharp rise in bank funding, a significant uptick in repo rate could lead to a compression in NBFCs' net interest margins ranging from 35-50 basis points, reflecting a rise of 90-100 bps in incremental funding costs. Most NBFCs have 28% to 63% of borrowings from banks.

"Sharp rise in repo led to a similar rise in repo-linked borrowing rate even as there may be a time lag in raising marginal cost lending rates," said M B Mahesh of Kotak Institutional Equities. "While these benchmarks go up, the impact will likely be visible on NBFCs' borrowing cost only post the reset date," he said.

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