Specialised Education NBFCs' Market Share Doubles with Good Asset Quality

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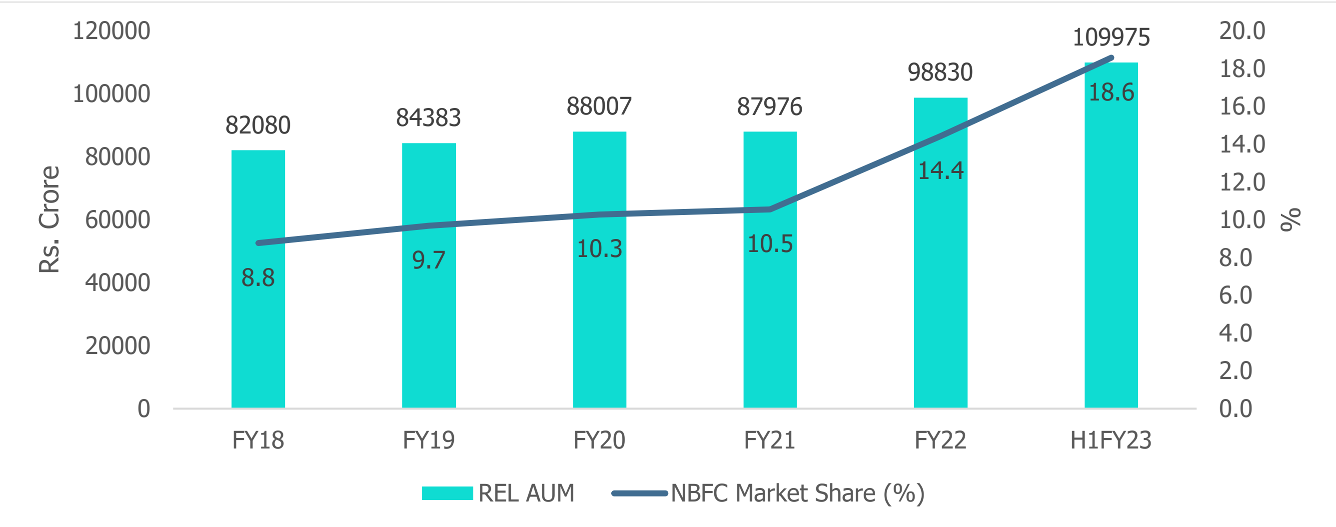
Synopsis

- NBFCs almost doubled their market share in retail education loans (Edu Retail) in the last two years from 9.9% in September 2020 to 18.6% in September 2022; Retail education loan AUM of CARE-rated NBFCs increased from Rs.7,738 crore as on Sep 2020 to Rs 17,877 crore as on September 2022.
- Market share gains of NBFCs came from establishing a strong foothold in overseas student education loans.
- Supported by specialised credit underwriting skills, education loan NBFCs have shown better asset quality parameters as compared to banks, and asset quality has remained stable even during the difficult times of Covid-19. However, a large proportion of outstanding loans has limited seasoning; global macroeconomic uncertainty and volatile job market conditions are major risks to asset quality in the near term on account of the recent large-scale layoff announced by a few MNCs.
- The growth rate is expected to remain strong during FY23 aided by an improved demand scenario for overseas education among Indian students. Though growth rates may moderate in FY24 due to the base effect, evolving changes in the industry, especially on the demand side, are likely to support double-digit AUM growth.

Booming Education Loan Segment for Specialised NBFCs

The overall AUM of the education loan segment stood at Rs.1.10[1] lakh crore as on September 30, 2022, as against Rs.0.88 lakh crore as on September 30, 2020. The education loan segment in India has been primarily dominated by public sector banks. However, over the past five years, specialised NBFCs focussing on overseas education loan segment have seen a steady increase in their market share. Especially during the above-mentioned period, NBFCs have almost doubled their market share.

Chart 1: Trend in Education loan outstanding and movement of market share



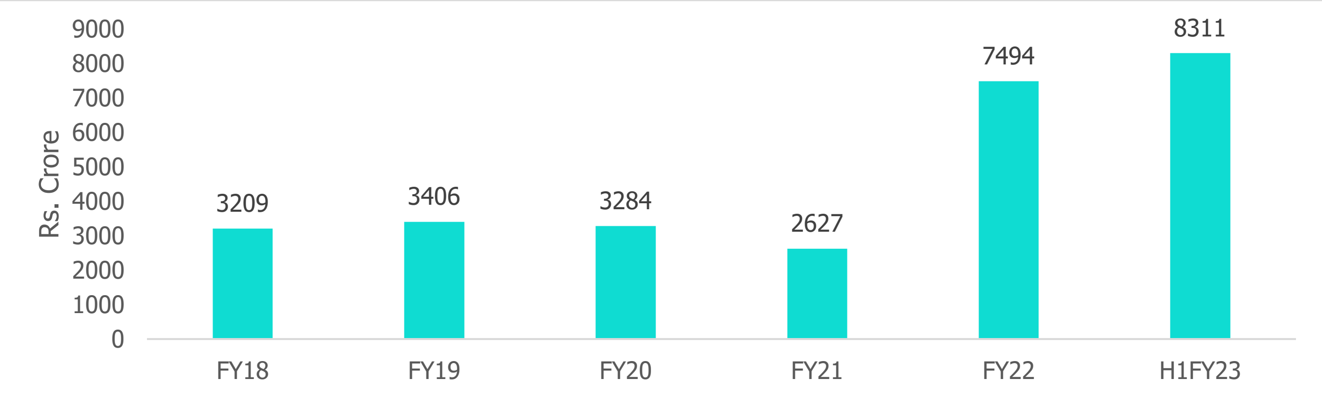
Source: RBI Report: Sectoral Deployment of Credit

Education loan NBFCs have shown good growth in disbursements over the years (chart 2). The NBFCs have focused on building expertise in the segment with well-defined sourcing channels including educational consultants, digital

[1] CareEdge Estimates based on RBI Report on sectoral deployment and data from CARE Rated NBFCs

marketing, direct walk-in at branches, DSAs including career counsellors, and marketing promotion in various colleges and student forums. The disbursements witnessed moderation during FY21 on account of the travel restrictions in place in various countries across the globe on account of Covid-19 with students also opting for deferment of the courses. With the severity of Covid-19 subsiding and the easing of travel restrictions post the second wave of Covid-19 the NBFCs have witnessed a sharp increase in disbursements from Q2FY22 aided by robust demand for the overseas education segment.

Chart 2: Trend of Disbursement of Specialised Education Loan Financing NBFCs

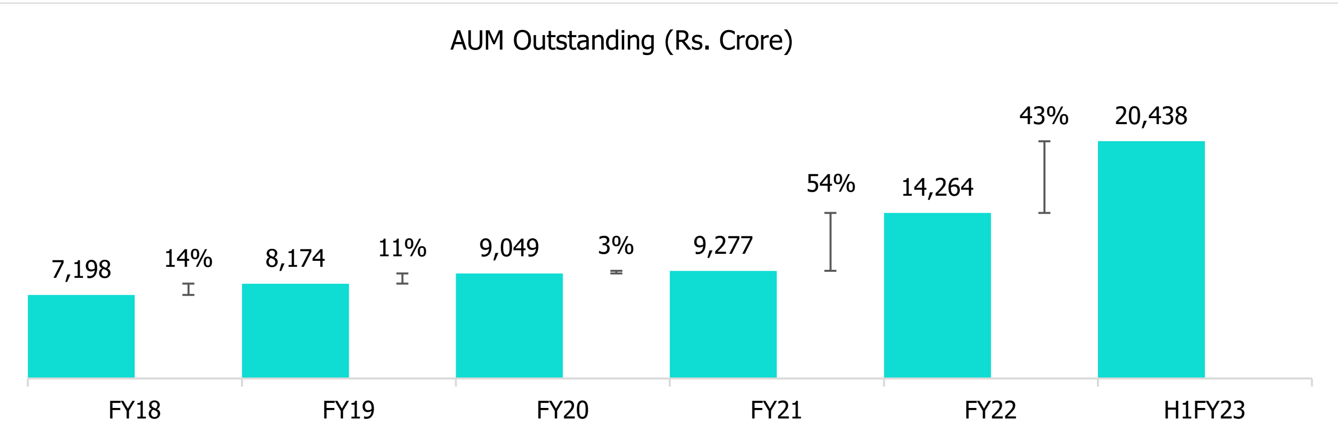


Source: Company (Care Rated Entities forming 87% of outstanding AUM of NBFCs as on September 30, 2022)

AUM growth of Specialised NBFCs Exceed Overall Edu Retail Industry Growth

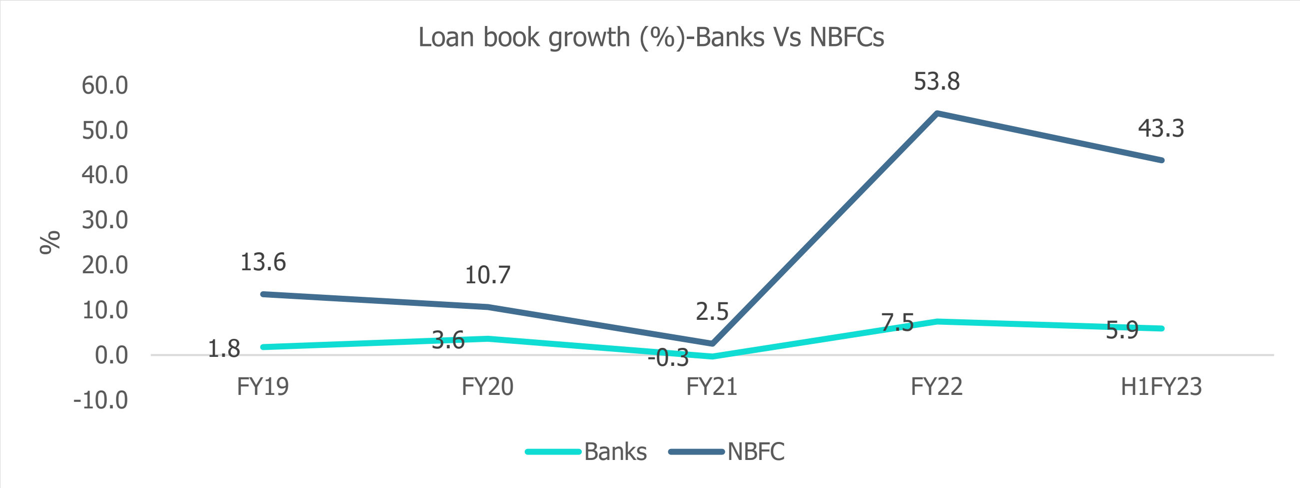
With healthy increase in disbursements, the AUM for NBFCs has witnessed 26.3% CAGR during FY18 to H1FY23 as against 7.2% CAGR witnessed in the overall retail education loan book and the same has led to an increase in market share of NBFCs in education loan segment from 9.9% as on September 30, 2020, to 18.6% as on September 30, 2022.

Chart 3: Growth in AUM-Education loans-NBFCs



Source: Company, CareEdge Ratings

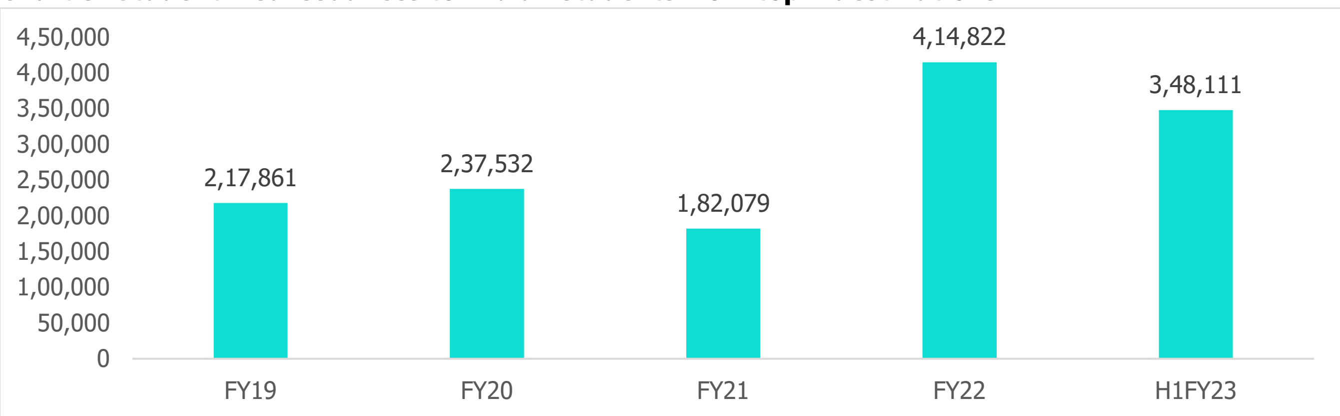
Chart 4: Trend in Loan Book Growth



Source: Company, CareEdge Ratings

Higher loan book growth of NBFCs as compared to banks is primarily driven by the robust demand for the overseas education segment among Indian students. NBFCs have carved out a niche in the overseas education loan segment supported by specialised credit underwriting skills; whereas Banks had primarily concentrated on catering to the domestic education segment with 66% of loans outstanding of banks being qualified as priority sector (loans to individuals for educational purposes, including vocational courses, not exceeding Rs 20 lakh). Disbursements of NBFCs have significantly picked up post Covid-19 although some portion was on account of the pent-up demand in FY22 and the depreciation of INR in the subsequent period. However, there is a significant increase in demand for pursuing overseas education among Indian students which offer a wider variety of courses, research options and skill-based training for students compared to the domestic education system and also attracted by better post-study career prospects available. Countries like the USA, Canada, the UK, Australia, and, New Zealand are the major destinations preferred by Indian students and the same can be witnessed with an increasing number of visa issuances to Indian students.

Chart 5: Student Visa issuances to Indian students from top 4 destinations



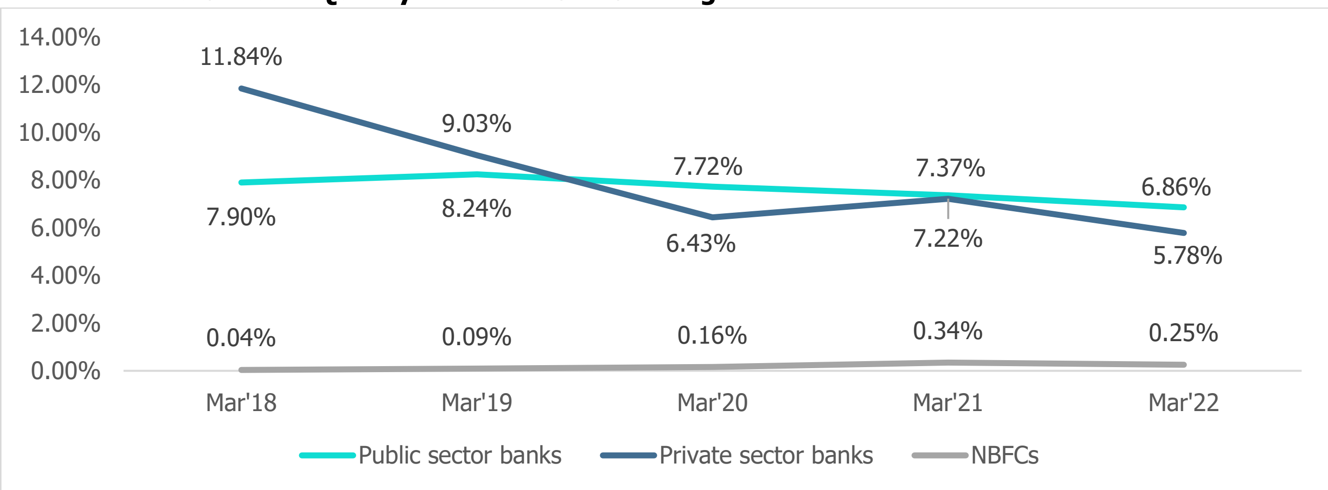
Source: Immigration statistics from USA, Canada, UK and Australia

The rise in overseas education demand is also aided by the increased availability of funding supported by specialised NBFCs adopting a student-led approach in risk underwriting enabling companies to estimate future employability and earnings potential, which includes an overall academic screening of students rather than traditional collateral-based lending adopted by banks thus leading to expansion in the pool of students eligible for funding. Further, during the past two years, few structural changes are evolving in the foreign education market such as the inflow of foreign students from China witnessing a decline on account of the development of the domestic higher education system leading to higher availability of seats within China, and hence lower appeal for overseas education among Chinese students. Geopolitical tensions post outbreak of Covid-19 has also led to decline in issuance of visa to Chinese students. Owing to the above factors, the share of seats available to Indian students has witnessed an increase.

Better Asset Quality Parameters of Education Loan NBFCs compared to Banks

Traditionally, the Banking sector has witnessed high gross NPA levels in the education loan segment. With the education loan book forming a small portion of the overall loan portfolio of the bank, the underwriting approach is generic with a focus on collateral-based lending. Most banks offer a scheme for an education loan as per the Indian Banks' Association (IBA) model education loan scheme to students pursuing higher studies. Banks primarily lend smaller ticket size loans compared to NBFCs with ticket size less than Rs 20 lakh being eligible to be classified under priority sector lending and loans with upto Rs 4 lakh being lent without any collateral. Owing to the relatively lower ticket size of education loans, the absence of specialized underwriting teams, limited monitoring/ tracking systems, NPAs in education loans are relatively high for banks. On the other hand, despite majority of loans being unsecured in nature, NBFCs have been able to maintain healthy asset quality in comparison to the banks on account of niche expertise of specialized NBFCs in loan underwriting and follow-up thereafter.

Chart 6: Trend of Asset Quality in Education Loan Segment



Source: RBI Report: Sectoral Deployment of Credit; Banks: GNPA %; NBFCs: Gross Stage 3%.

NBFCs have developed strong domain expertise, providing tailor-made solutions and competitive products with an efficient domain-specific technology platform for loan processing and dynamic credit underwriting. Further, periodic monitoring of the delinquency performance of the portfolio on various parameters like co-borrower income, CIBIL bands, etc is done.

Further, the NBFCs also map the country-wise course category, course discipline, GRE score band, average monthly salary levels for a particular course, etc. This enables to NBFCs to understand the income potential and demand in the job market for its existing and potential students. Thus, the NBFCs are able to re-align and review their credit and underwriting parameters as and when required.

Majority of the student's financing (almost 98%) by NBFCs are extended towards post-graduation courses. It is worthwhile to note employability of postgraduate students are relatively better than undergraduate students and they have shorter tenure of course. Hence, better asset quality is expected. Within master's courses, majority of funding is extended to Science, Technology, Engineering, Management (STEM) which have high employment opportunities. While credit underwriting factors in income of the parents and sanction loans with longer tenure typically 10 years, due to the relatively higher potential income level of students, prepayments are high in overseas education loans. The prepayment rates of overseas education loan range from 20%-30% per annum, post completion of the scheduled course. The same results in effective tenure of fewer than 6 years. Further with loans being co-guaranteed by parents, the NBFCs are better placed to collect the scheduled EMIs.

Apart from the robust credit appraisal mechanism, regular contact with students is maintained by NBFCs with students required to pay at least partial interest during the study period as compared to banks which offer moratorium period of up to one year post course completion. Regular interactions with students are maintained by NBFCs through direct contact by way of email/blog services for any support services that the students may require. NBFCs also offers other support services to students such as travel, forex requirement and any other support services thereby providing other income by way of cross-selling opportunities. Well-defined risk management practices and continuous touch base with students have resulted in maintenance of good asset quality over the years.

Outlook

Albeit moderation of growth during FY21 on account of Covid-19, the aggregate AUM of education loan financing NBFCs have witnessed steady growth over the years leading to steady increase in market share in the segment. Growth rate has witnessed a significant increase during FY22 and H1FY23 aided by a robust demand scenario for the overseas education segment among Indian students. The trend is expected to be continued as witnessed by healthy loan application logins witnessed among NBFCs and continued high visa issuances to Indian students. CareEdge Estimates aggregate AUM of education loan financing NBFCs to be above ~Rs.25,500 crore as on March 31, 2023, with AUM growth of around 80% during FY23 and CAGR of 28.8% over the last five years.

On the asset quality front, with the strong domain expertise, the education loan financing NBFCs have been able to identify and lend to customers based on the industry trends for job opportunities and earning potential, leading to lower delinquencies, same has resulted in better asset quality with Gross Stage 3 assets (%) less than 0.5% during past five fiscal years ended March 31, 2022. CareEdge expects NBFCs to maintain asset quality in Edu Retail at a comfortable level in the near term considering a low amount of restructured loan portfolio outstanding and the relatively better customer profile majorly comprising of students STEM courses and Masters' courses which inherently exhibits stable income profile and better repayment behaviour. While the long-term outlook for the education loan market remains robust, in the near-term asset quality concerns exist on account of global macroeconomic uncertainty and volatile job market conditions including the recent large-scale layoffs given the low seasoning of the portfolio.

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