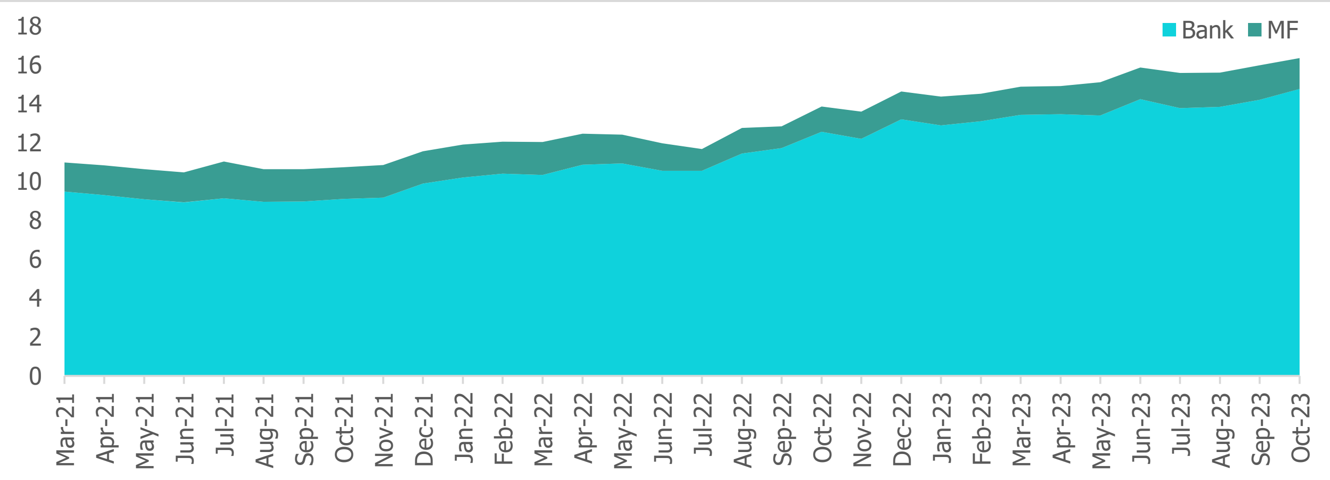
Banks' Loans to NBFCs Moves at Brisk Pace, while MF Exposure is Subdued

December 04, 2023 I BFSI Research

Synopsis

- The credit exposure of banks to Non-Banking Financial Companies (NBFCs) stood at Rs 14.8 lakh crore in October 2023, indicating a 22.1% year-on-year (y-o-y) growth. This expansion is indicative of the robust progress observed in NBFCs during the post-pandemic period. Furthermore, the proportion of NBFC exposure in relation to aggregate credit has risen from 9.4% in October 2022 to 9.6% in October 2023. On a month-on-month (m-o-m) basis, the amount rose by 4.0%. Meanwhile, the Mutual Fund (MF) debt exposure to NBFCs, including Commercial Papers (CPs) and Corporate Debt, witnessed an increase of 21.9% to 1.58 lakh crore in October 2023, while declining sequentially by 10.5% from September 2023.
- Highlighting the relative size of their exposure to NBFCs, MFs' debt exposure to NBFCs remained at 10.7% as a percentage of "Banks' advances to NBFCs" in October 2023 and October 2022, but declined sequentially from 12.5% in September 2023.
- Recently RBI has prescribed an increase in risk weights for advances to AAA-A-rated NBFCs by 25%, while higher risk weights would not be applicable for entities in the BBB+ and below rating categories. This excludes the risk weights for bank loans to HFCs or bank loans backed by PSL loans. The momentum of bank lending to NBFCs which are not covered by the PSL guidelines could likely moderate as this will likely impute higher cost of funds (due to higher risk weights) for entities rated A- and above. Companies rated A- and above form an overwhelming part of the NBFC universe in terms of balance sheet size and exposures. The highly rated NBFCs would drive towards the capital markets. Hence, aggregate dependence of mid and smaller-sized NBFCs on the banking sector for funding is likely to remain high (despite an anticipated increase in lending cost by 25-30 bps) while larger NBFCs will continue to diversify their funding sources. This could lead to a greater than normal increase in securitisation and co-lending partnerships as a liability source for NBFCs (RBI Looks to Reduce Risk Build-up in the Unsecured Lending Segment).

Figure 1: Summary of Banks Loans and MFs NBFC Debt Exposure (Rs. lakh crore)



Source: RBI, SEBI

The data in Figure 1 does not include liquidity made available to NBFCs by banks via the securitisation route (direct assignment & pass-through certificates) and Treasury investments made by banks in the NBFCs' capital market issuances. Liquidity availed by NBFCs including HFCs through the securitisation route was approximately Rs 1.8 lakh crore for the twelve-month period ending September 2023.

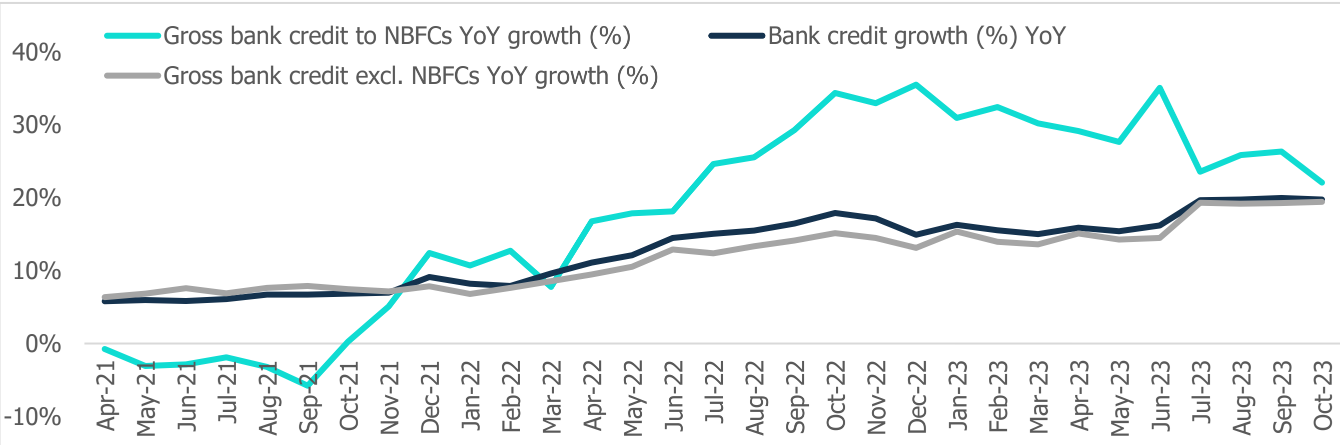
Figure 2: NBFC Debt Sources (Rs lakh crore)

	Feb-2018	Feb-2020	Oct-2023	Ab. Change (%)	
				vs. Feb-2018	vs. Feb-2020
Bank	3.90	8.40	14.76	278.4	75.7
MFs	2.31	1.64	1.58	-31.4	-3.4
Total (Bank +MF)	**6.21**	**10.04**	**16.35**	**163.2**	**62.8**

Source: RBI, SEBI

Compared to February 2018 numbers, absolute bank lending to NBFCs has jumped to around 3.8x, meanwhile, MF exposure has reduced by 31.4% over the last five years due to risk aversion by mutual fund managers. Interestingly, MF exposure to NBFCs as a share of Debt Assets Under Management (AuM) has reduced from nearly 20% in the later part of 2018 to around 11%. On the other hand, the share of banks' advances to NBFCs as a share of aggregate advances has doubled from around 4.5% in February 2018 to close to 9.6% in October 2023.

Figure 3: Growth in Bank Credit to NBFCs vis-à-vis overall Bank Credit Growth



Source: RBI

The credit extended by banks to NBFCs has exhibited a consistent upward trend over the last five years and continued its acceleration along with the phased reopening of economies after the Covid-19 pandemic. This growth momentum further accelerated during FY23 and has continued in first half of FY24. Further, after the merger of HDFC Limited with HDFC Bank, the quantum of outstanding exposure of banks to NBFCs had reduced sequentially, albeit maintaining the y-o-y growth rate. In September 2023, the quantum of outstanding exposure reached the pre-merger level and in October 2023 moved past the same. This trend can be primarily ascribed to the expansion in the AuM of NBFCs.

RBI increases Risk weights on Lending to NBFCs by Banks

RBI has prescribed an increase in risk weights for advances to AAA-A-rated NBFCs by 25%, while higher risk weights would not be applicable for entities in the BBB+ and below rating categories. This excludes the risk weights for bank loans to HFCs or bank loans backed by PSL loans. Further, around 40-50% of the current outstanding would fall in this category meanwhile as the notification is silent on covering the outstanding loans or whether only fresh loans would be subject to these norms.

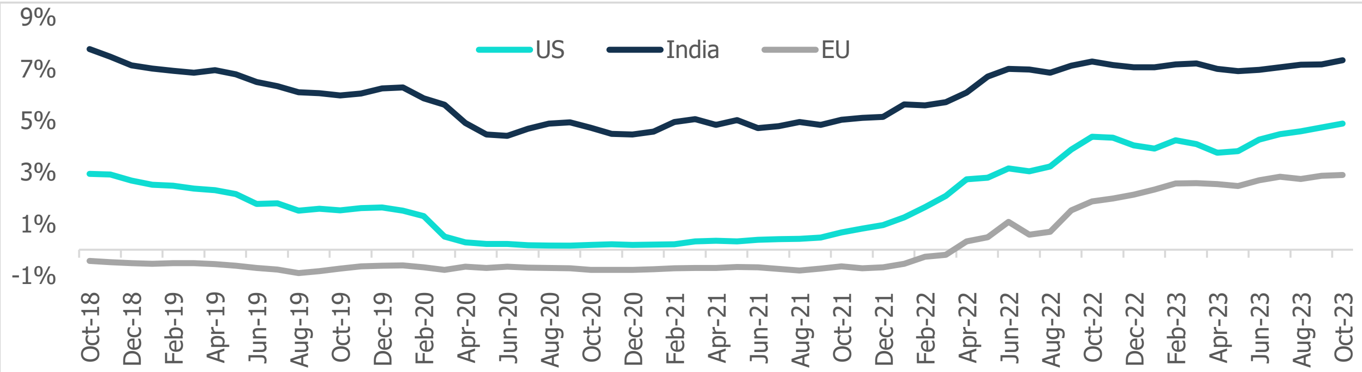
Figure 4: Risk weights for NBFCs

Rating	AAA	AA	A
Current	20%	30%	50%
Revised	45%	55%	75%

Source: RBI, CareEdge

The personal loans as well as advances to NBFCs have been growing strongly and have been the primary drivers of incremental bank credit. We see this as a strong signalling impact to deter growth in the unsecured space while lenders are well-capitalised to manage decrease in CRAR which is anticipated to be around 25-45 bps. Meanwhile, the proportion of bank lending to larger NBFCs could be pared down as they approach the capital market, while aggregate dependence of mid-sized NBFCs on the banking sector for funding is likely to remain high despite an anticipated increase in lending cost by 25-30 bps. This could incentivize securitisation as a liability source for NBFCs.

Figure 5: Three-Year G Sec Yield Narrows: India, US and EU

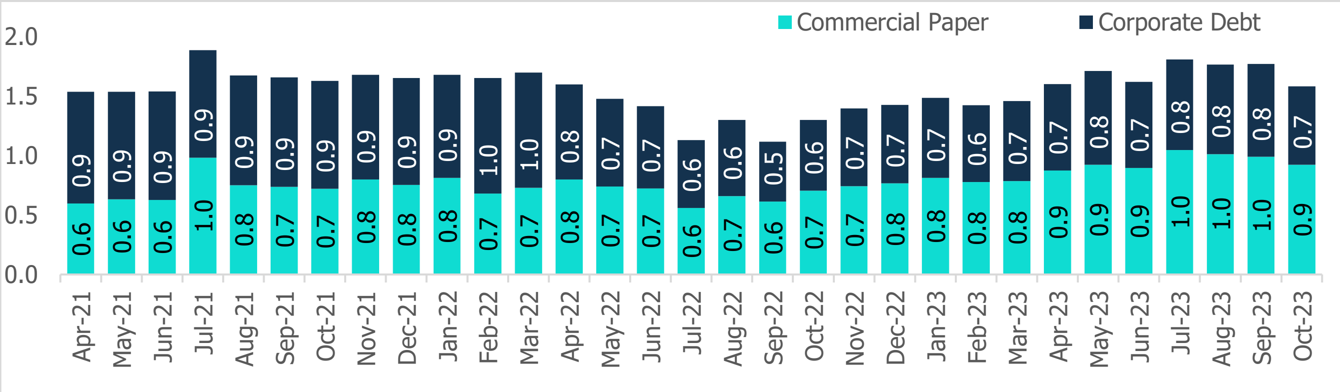


Source: CMIE, St. Louis Fed, Eurostat: Note: Weighted average Yield on Residual Maturity of Government of India Dated Securities in Secondary Market, Market Yield on U.S. Treasury Securities at 3-Year Constant Maturity, Quoted on an Investment Basis, Percent, Monthly, Not Seasonally Adjusted, Spot rate yield curve of AAA-rated euro area central government bonds

As the above figure shows, the spread between domestic and US and EU g-sec yield has narrowed and when combined with hedging and other costs has reduced the attractiveness of overseas borrowings. Additionally, the higher upswing in global interest rates compared to the Indian market also played a pivotal role. This divergence in interest rate movements led to a decline in the utilisation of external commercial borrowings (ECBs) by NBFCs. Meanwhile, the domestic capital market has witnessed some traction. Larger and better-rated NBFCs have been accessing the capital market given that most of the issuers are from the BFSI sector and over 90% of the aggregate issuers have been either AA or AAA-rated entities.

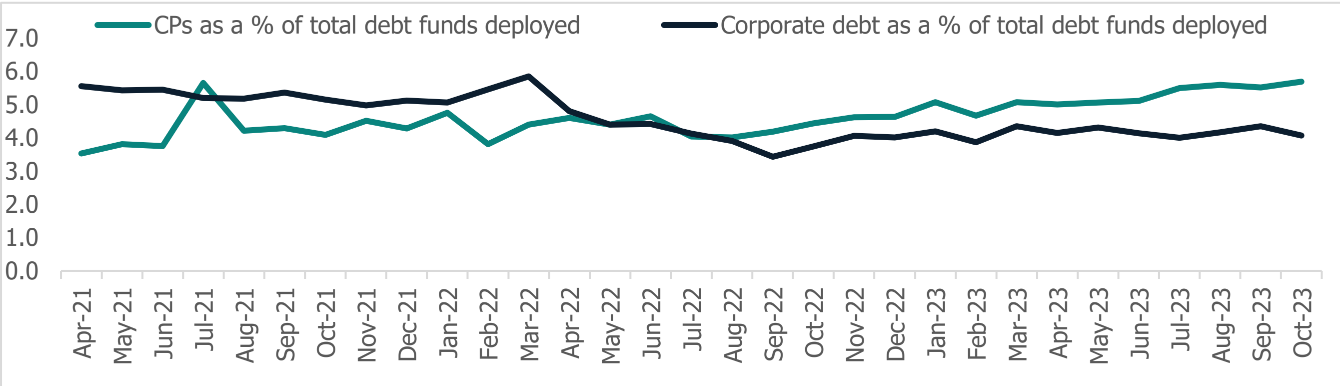
Investment in corporate debt of NBFCs rose by 11.1% y-o-y to Rs.0.66 lakh crore in October 2023 but declined sequentially by over 15%. Meanwhile, the share of total corporate debt to NBFCs expanded to 4.1% in October 2023 from 3.7% in October 2022. The outstanding investments in CPs of NBFCs fell below the Rs one lakh crore mark, declining by 6.7% sequentially but increasing by 31% y-o-y to Rs.0.92 lakh crore in October 2023. CPs (less than 90 days) rose by 27.6% y-o-y to Rs.0.64 lakh crore in October 2023, CPs (90 days to 182 days) increased by 55.7% to Rs.0.22 lakh crore, and CPs (more than 6 months) declined by 6.7% to Rs.0.05 lakh crore in the reporting period.

Figure 6: Total Debt Funds Deployed in NBFCs via CPs and Corporate Debt (Rs lakh crore)



Source: SEBI

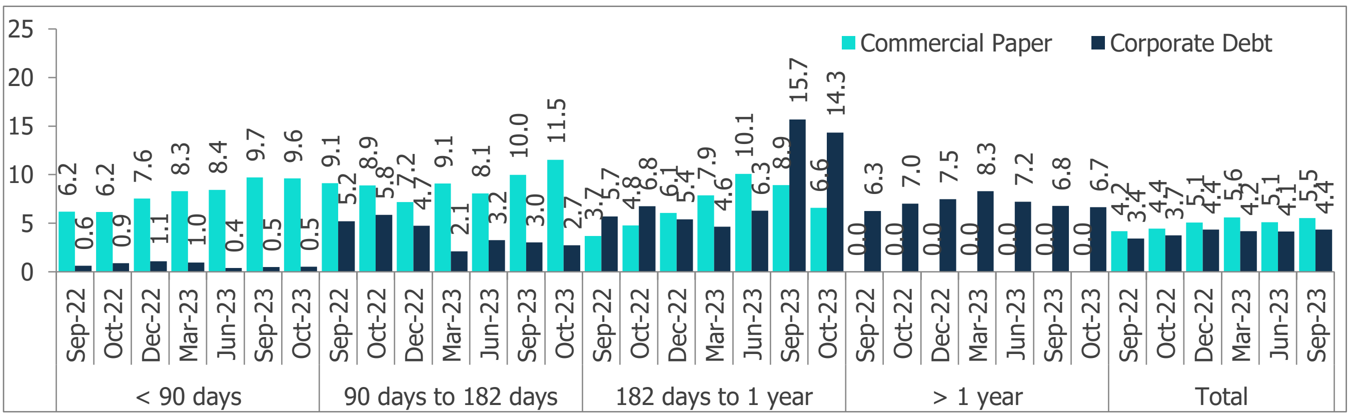
Figure 7: Total Debt Funds Deployed in NBFCs via CPs and Corporate Debt (%)



Source: SEBI

The percentage share of funds deployed by MFs in CPs as a percentage of banks' exposure to the NBFCs stood at 6.3% in October 2023, increasing by around 40 bps y-o-y. The proportion of CPs (less than 90 days) deployed in NBFCs as a percentage of aggregate funds deployed for less than 90 days reached 9.6% in October 2023 as compared to 6.2% over a year ago period, the percentage of CPs (90 days to 182 days) rose to 11.5% from 8.9% over a year ago, and CPs (greater than six months) percentage grew to 6.6% in October 2023 as compared to 4.8% over a year-ago period.

Figure 8: Trend in Proportion of CPs & CD Deployed in NBFCs as a % of Debt Funds by Duration



Source: SEBI

Contact

Sanjay Agarwal	Senior Director	sanjay.agarwal@careedge.in	+91 - 22 - 6754 3582 / +91-81080 07676
Saurabh Bhalerao	Associate Director – BFSI Research	saurabh.bhalerao@careedge.in	+91 - 22 - 6754 3519 / +91-90049 52514
Mradul Mishra	Media Relations	mradul.mishra@careedge.in	+91 - 22 - 6754 3596

CARE Ratings Limited
Corporate Office: 4th Floor, Godrej Coliseum, Somaiya Hospital Road, Off Eastern Express Highway, Sion (East), Mumbai - 400 022
Phone : +91 - 22 - 6754 3456 I CIN: L67190MH1993PLC071691

Connect :

Locations: Ahmedabad I Andheri-Mumbai I Bengaluru I Chennai I Coimbatore I Hyderabad I Kolkata I New Delhi I Pune

About Us:

CareEdge is a knowledge-based analytical group offering services in Credit Ratings, Analytics, Consulting and Sustainability. Established in 1993, the parent company CARE Ratings Ltd (CareEdge Ratings) is India's second-largest rating agency, with a credible track record of rating companies across diverse sectors and holding leadership positions in high-growth sectors such as BFSI and Infra. The wholly-owned subsidiaries of CareEdge Ratings are (I) CARE Analytics & Advisory Private Ltd previously known as CARE Risk Solutions Pvt Ltd, and (II) CARE ESG Ratings Ltd, previously known as CARE Advisory Research and Training Ltd. CareEdge Ratings' other international subsidiary entities include CARE Ratings Africa (Private) Limited in Mauritius, CARE Ratings South Africa (Pvt) Ltd, and CARE Ratings Nepal Limited.

Disclaimer:

This report is prepared by CARE Ratings Limited (CareEdge Ratings). CareEdge Ratings has taken utmost care to ensure accuracy and objectivity while developing this report based on information available in public domain. However, neither the accuracy nor completeness of information contained in this report is guaranteed. CareEdge Ratings is not responsible for any errors or omissions in analysis / inferences / views or for results obtained from the use of information contained in this report and especially states that CareEdge Ratings has no financial liability whatsoever to the user of this report.

Celebrating 30 Years