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NBFCs and HFCs witnessed lower fresh disbursals due to weak demand compounded by risk aversion; collection efficiency improved

This report summarises and analyses the NBFC segment presented in RBI's "Report on Trends and Progress of Banking in India 2019-20" along with financial performance of overall NBFC sector in FY20 and H1FY21. Additionally, we have also analysed Q2FY21 performance of select NBFCs and HFCs.

We have divided our report into two sections:

A) Performance of NBFC sector, and;
B) Performance of Select NBFCs and HFCs

Summary

- *The balance sheet size of NBFCs has decelerated due to moderate growth in loans and advances led by weak demand and risk aversion. NBFCs balance sheet in aggregate is around 18.8% of total SCBs balance sheet. Of the total asset size (Rs.33.9 lakh crore) of NBFCs in FY20, 38.6% is dominated by the government owned NBFCs. As of H1FY21, the balance sheet of NBFC-ND-SI comprises of 86.1% share, while balance 13.9% is accounted by NBFC-D in total balance sheet size of NBFCs.*
- *As on September 30, 2020 out of the total outstanding borrowing of NBFC-ND-SI, around 70% is in the form of debentures and banks, while NBFC-D have around 77.5% of the outstanding borrowings as bank borrowings and debentures. Debentures alone account for approximately 40.0% of the outstanding borrowings of NBFC-ND-SI and 34.4% for NBFC-D. The Industry sector has received the highest credit (53.6%) by NBFC sector, followed by retail segment (23.3%) and services (15.8%). Within the industrial sector, large industries segment has received 46.4% of the credit disbursed to industrial sector.*
- *As on August 31, 2020, the overall percentage of NBFC customers availed the loan moratorium has been comparatively lower than banks, while the loans outstanding under moratorium were higher as compared with banks.*
- *The sample set of NBFCs and HFCs has witnessed lower disbursals and AUM growth in Q2FY21 as compared with Q2FY20 due to a cautious approach towards fresh disbursements and weak demand compounded by risk aversion. The rural focused NBFCs have witnessed an almost normal disbursements and collections (supported by harvest) during Q2FY21.*

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Introduction

During FY20, the NBFC sector faced headwinds in the aftermath of the IL&FS crisis in the form of erosion of confidence among investors, rating downgrades and liquidity stress compounded by the COVID-19 pandemic. On an overall basis, NBFCs were taking corrective actions including reducing business growth, correcting ALM profiles, reducing leverage, etc. Further, in H1FY21, the Reserve Bank of India continued to take sequential regulatory measures to make available sufficient liquidity to the NBFC sector. The consolidated balance sheet of NBFCs gained traction in H1FY21 after witnessing a deceleration in FY20 due to stagnant growth in loans and advances.

RBI classifies NBFCs on the basis of:

1. Liability structure
2. Type of activities undertaken
3. Systematic importance

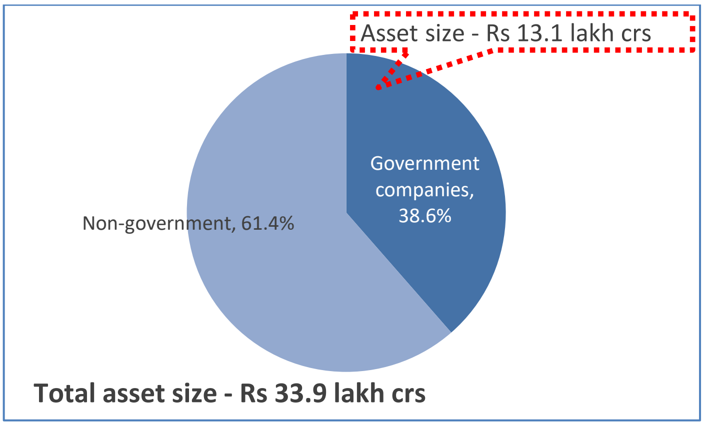
In the first category, NBFCs are further divided into:

- NBFCs-D - Authorised to accept and hold public deposits.
- NBFCs-ND - Non-deposit taking NBFCs which are authorised to accept public deposits but raise debt from market and banks.

Among the NBFCs-ND, those with an asset size of Rs.500 crore or more are classified as systemically important NBFCs (NBFCs-ND-SI). There were 64 NBFCs-D and 292 NBFCs-ND-SI as on July 16, 2020 as compared with 88 and 263 as of March 2019.

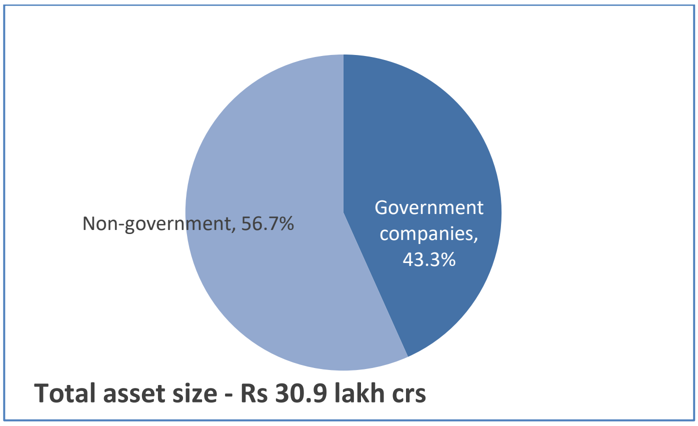
Out of total asset size (Rs.33.9 lakh crore as of March 2020 as compared with Rs.30.9 lakh crore as of March 2019) of NBFC segment, approximately 85.7% is dominated by NBFC-ND-SI. Within NBFC-ND-SI, the government-owned NBFCs hold 43.3% of total assets of NBFC-ND-SI.

Figure 1: Ownership mix of NBFC based on asset size (FY20)



Source: RBI Trends and Progress of Banking in India

Figure 2: Ownership mix of NBFC-ND-SI based on asset size (FY20)



Source: RBI Trends and Progress of Banking in India

NBFCs are also categorised on the basis of activities undertaken as depicted in Figure 3. Based on activities, NBFCs are divided into 11 categories. During FY20 both registration and cancellations were lower at 116 and 298 as compared with FY19 (166 and 1851), when there was a record number of cancellations/surrender of licenses of non-compliant NBFCs.

Figure 3: Classifications of NBFCs by Activity

Type of NBFC	Activity
Investment and Credit Company (ICC)	Lending and investment.
NBFC-Infrastructure Finance Company (NBFC-IFC)	Provision of infrastructure loans.
NBFC-Systemically Important Core Investment Company (CIC-ND-SI)	Investment in equity shares, preference shares, debt or loans in group companies.
NBFC-Infrastructure Debt Fund (NBFC-IDF)	Facilitation of flow of long-term debt into infrastructure projects.
NBFC-Micro Finance Institution (NBFC-MFI)	Credit to economically dis-advantaged groups.
NBFC-Factor	Acquisition of receivables of an assignor or extending loans against the security interest of the receivables at a discount.
NBFC-Non-Operative Financial Holding Company (NBFC-NOFHC)	Facilitation of promoters/ promoter groups in setting up new banks.
Mortgage Guarantee Company (MGC)	Undertaking of mortgage guarantee business.
NBFC-Account Aggregator (NBFC-AA)	Collecting and providing information about a customer's financial assets in a consolidated, organised and retrievable manner to the customer or others as specified by the customer.
NBFC–Peer to Peer Lending Platform (NBFC-P2P)	Providing an online platform to bring lenders and borrowers together to help mobilise funds.
Housing Finance Companies (HFC)	Financing for housing.

Source: RBI Trends and Progress of Banking in India
Note: Investment and Credit Company (NBFC-ICC) is a mix of asset finance companies (AFCs), loan companies (LCs) and investment companies (ICs)

Figure 4: Loan Moratorium availed by customers of NBFC sector (As on August 31, 2020)

	Corporate		MSME		Individual		Others		Total	
	% of total customers	% of total outstanding	% of total customers	% of total outstanding	% of total customers	% of total outstanding	% of total customers	% of total outstanding	% of total customers	% of total outstanding
NBFCs	42.7	37.2	68.8	67.0	23.1	56.5	50.2	33.2	26.6	44.9
SCBs	18.0	30.4	77.2	68.1	43.7	33.9	35.6	39.1	43.8	37.9
System	31.3	34.3	77.5	69.3	42.6	41.0	45.4	42.1	45.6	40.4

Source: RBI Trends and Progress of Banking in India

Figure 5: Loan Moratorium availed by customers of NBFC sector (As on April 30, 2020)

	Corporate		MSME		Individual		Others		Total	
	% of total customers	% of total outstanding	% of total customers	% of total outstanding	% of total customers	% of total outstanding	% of total customers	% of total outstanding	% of total customers	% of total outstanding
NBFCs	39.7	56.2	60.7	61.1	32.5	45.9	37.3	41.4	29.0	49.0
SCBs	24.7	39.1	43.1	65.3	52.1	56.2	45.7	55.7	55.1	50.0
System	30.8	41.9	45.8	65.0	50.4	55.3	45.7	54.6	48.6	50.1

Source: RBI's Financial Stability Report

As on August 31, 2020, the overall percentage of NBFC customers availed the loan moratorium has been comparatively lower than banks, while the loans outstanding under moratorium were higher as compared with banks. Among the sectors MSME segment under NBFCs availed the scheme most. ~69.0% of MSME customers have availed the moratorium as of August 30, 2020 as compared with ~61.0% as of April 30, 2020. Other categories such as individuals, witnessed a reduction in the share of customers 32.5% as of April 30, 2020 to 23.1% as of August 30, 2020, while, the corporate segment has registered a fall in outstanding amount of loans under moratorium between April 2020 and August 2020.

Section A – Performance of NBFC sector

The analysis has been divided into the following components:

1. Balance sheet analysis
2. Financial performance
3. Sectoral credit deployment of the NBFC sector

1. Balance Sheet Analysis

Composition of liabilities: During the last two years, liabilities of the NBFC sector grew at CAGR of 13.8%, i.e., from Rs.26.2 lakh crore in FY18 to Rs.33.9 lakh crore in FY20. The growth in liabilities slowed to 5.8% (Rs.35.8 lakh crore) in H1FY21. Post the NBFC crisis, the focus shifted from growth to stability, liquidity and concentrated on managing their ALM (asset-liability management). However, larger NBFCs were able to borrow from debt market based on their scale and parentage. Specific measures taken by RBI and Government (e.g. special liquidity scheme for NBFCs/HFCs) enabled these entities to combat liquidity constraints and restricted market access.

On the supply side, sources of funds, especially for small and mid-sized NBFCs, were impacted due to reduced risk appetite of banks for low rated and unrated exposures. On the demand side, the prevailing economic contraction contributed to the subdued credit offtake.

Figure 6: Liabilities of the NBFC sector (Rs. lakh crore)

Particulars	FY18	FY19	FY20	y-o-y growth % FY19	y-o-y growth % FY20	H1FY21	YTD growth % (H1FY21 over FY20)
Share Capital and Reserves	**6.1**	**7.0**	**7.9**	**14.1%**	**13.4%**	**8.8**	**12.0%**
Public Borrowings	**0.3**	**0.4**	**0.5**	**31.7%**	**24.9%**	**0.6**	**11.3%**
Total Borrowings	**18.1**	**21.1**	**16.5**	**-**	**-**	**16.5**	**0.03%**
Secured Borrowings	10.0	11.6	7.1	-	-	7.3	-
Unsecured Borrowings	8.1	9.5	9.4	-	-	9.1	-
Current Liabilities	**1.6**	**2.4**	**9.0**	**-**	**-**	**10.0**	**-**
Total	**26.2**	**30.9**	**33.9**	**17.9%**	**9.8%**	**35.8**	**5.8%**

Source: RBI Trends and Progress of Banking in India

Outstanding Borrowings: The composition of outstanding borrowings of NBFC-ND-SI and NBFC-D has been presented in Figure 7. As of H1FY21, the overall borrowings of NBFCs grew by 7.9% YoY, while NBFC-ND-SI and NBFC-D registered a growth of 8.8% and 1.4% respectively. The share of NBFC-ND-SI marginally improved to 87.9% in overall borrowings (87.1% share in H1FY20).

Figure 7: Composition of outstanding borrowings for NBFCs (Rs. lakh crore, % share)

	NBFC-ND-SI (% of total)					NBFC-D (% of total)					NBFC (% of total)				
	FY18	FY19	FY20	H1FY20	H1FY21	FY18	FY19	FY20	H1FY20	H1FY21	FY18	FY19	FY20	H1FY20	H1FY21
Debentures	50.5%	43.9%	42.2%	43.8%	39.5%	39.1%	36.7%	35.1%	33.7%	34.4%	49.2%	43.0%	41.3%	42.5%	38.9%
Banks	21.8%	27.2%	29.4%	27.0%	29.5%	33.8%	39.3%	42.2%	41.7%	43.1%	23.2%	28.8%	31.0%	28.9%	31.1%
FIs	1.8%	1.9%	3.3%	1.8%	5.2%	1.6%	1.8%	2.7%	1.8%	2.6%	1.8%	1.9%	3.2%	1.8%	4.9%
Commercial Paper	8.1%	7.4%	3.2%	5.5%	3.9%	8.6%	6.7%	2.6%	6.4%	3.0%	8.2%	7.3%	3.1%	5.6%	3.8%
Inter-corporate	3.2%	3.8%	3.5%	4.2%	3.6%	2.5%	2.7%	2.7%	2.8%	2.4%	3.2%	3.6%	3.4%	4.0%	3.4%
Interest accrued	2.3%	1.7%	2.2%	1.9%	2.5%	4.5%	2.5%	2.3%	2.3%	2.2%	2.5%	1.8%	2.2%	1.9%	2.4%
Others	12.4%	14.0%	16.2%	15.9%	15.7%	9.9%	10.2%	12.4%	11.4%	12.3%	12.1%	13.5%	15.7%	15.3%	15.3%
Total (Rs. Lakh crs)	**16.0**	**18.4**	**19.8**	**19.0**	**20.7**	**2.1**	**2.7**	**2.9**	**2.8**	**2.9**	**18.1**	**21.1**	**22.7**	**21.8**	**23.5**

Source: RBI Trends and Progress of Banking in India; Note: others include public deposit

- From the above figure, we can infer that the NBFCs dependence on debentures and CPs reduced, as it has fallen from 57.3% share in FY18 to 48.1% share in FY20 and 42.7% in H1FY21. However, it continues to be their primary source of funding.
- The share of CPs declined for both segments (NBFC-ND-SI and NBFC-D) owing to risk aversion in capital markets and the movement of NBFCs towards longer term-borrowings for better asset-liability management. Similarly, the share of CPs declined in FY20 in the borrowing mix of NBFCs and formed nearly 1/3rd of the total CP issuance.
- Bank borrowings as a share of total borrowings have increased from 23.2% in FY18 to 31.3% in H1FY21. This indicates that banks are compensating for the reduced market access for NBFCs (especially for smaller players) amid the prevailing tight liquidity scenario.

Category-wise classification of outstanding borrowings (NBFC-ND-SI): Figure 8 tabulates category-wise classification of the outstanding borrowings. It can be seen that the Investment and Credit Company, and Infrastructure finance company (providers of infrastructure loans) together have the highest share of outstanding borrowings, which is 90% of the total outstanding borrowing.

Figure 8: Category-wise classification of outstanding borrowings (NBFC-ND-SI)

Category	Amount (Rs Lakh crs)			Amount (Rs Lakh crs)	YTD growth %
	FY19	FY20	y-o-y growth %	H1FY21	(H1FY21 over FY20)
Investment and Credit Company	8.7	8.9	2.6%	8.9	0.0%
Core Investment Company	1.1	1.0	-7.2%	1.2	15.8%
Factoring - NBC	0.0	0.0	-7.5%	0.0	-18.5%
Infrastructure Debt Fund- NBFC	0.2	0.2	18.4%	0.3	11.6%
Infrastructure Finance Company	8.0	9.2	14.7%	9.7	5.8%
NBFC – Micro Finance Institutions	0.4	0.5	17.7%	0.6	14.1%
Total	**18.4**	**19.9**	**7.8%**	**20.7**	**4.0%**

Source: RBI Trends and Progress of Banking in India

Asset Composition: In this section, we look at the composition of the assets, not only for the deposit-taking and non-deposit-taking NBFCs but also for the different categorisation of the NBFCs. Out of the total assets of the NBFC sector (Rs.35.8 lakh crore) in H1FY21, loans and advances account for approximately 70%. Of the total asset size (Rs.33.9 lakh crore) of NBFC segment in FY20, approximately 39.0% is dominated by the government owned NBFCs.

Figure 9: Composition of assets for NBFCs (Rs. lakh crore)

Particulars	FY18	FY19	FY20	y-o-y growth % FY19	y-o-y growth % FY20	H1FY21	YTD growth % (H1FY21 over FY20)
Loans and Advances	19.6	23.2	23.6	18.0%	1.9%	24.6	4.4%
Total Investment	4.2	4.8	5.4	16.1%	12.0%	6.1	13.4%
Cash and Bank	0.8	1.0	1.4	31.0%	39.1%	1.5	8.7%
Current assets	1.3	1.3	2.5	2.3%	86.8%	2.3	-6.2%
Other assets	0.3	0.8	1.0	150.3%	23.0%	1.2	24.9%
Total assets	**26.2**	**31.1**	**33.9**	**18.9%**	**8.9%**	**35.8**	**5.8%**

Source: RBI Trends and Progress of Banking in India

Infrastructure finance companies, predominantly comprises of New Delhi based government companies such as PFC, REC, IRFC, IIFCL etc. The share of Infrastructure finance companies in total assets of NBFCs-NDSI increased in H1FY21, driven by expansion in other assets, mainly investments. PFC and REC gained from liquidity infusion of Rs.90,000 crore for state power distribution utilities (DISCOMs) announced by the Government. As can be seen in the figure below, infrastructure NBFCs has a share of 31.1% in total assets of NBFC sector. PFC and REC together have 21.1% share in total assets of NBFCs as of September 30, 2020.

Figure 10: Composition of assets for select Government owned NBFCs (Rs. lakh crore)

Companies	FY19	FY20	y-o-y Growth %	H1FY21	YTD Growth % (H1FY21 over FY20)
PFC	3.4	3.6	5.9%	3.9	7.5%
REC	3.0	3.5	16.4%	3.7	6.9%
IIFCL	0.4	0.5	19.8%	0.5	-4.9%
IFCI	0.2	0.2	-17.2%	0.2	-6.2%
IRFC	2.1	2.8	33.6%	2.9	5.8%
Total	**9.1**	**10.5**	**15.7%**	**11.2**	**6.0%**

Source: Company Reports; Note: Standalone

Figure 11: Category-wise analysis of loans and advances

Category	Amount (Rs Lakh crs) FY19	Amount (Rs Lakh crs) FY20	y-o-y growth %	Amount (Rs Lakh crs) H1FY21	YTD growth % (H1FY21 over FY20)
NBFC-ND-SI	**19.4**	**19.4**	**0.4%**	**20.5**	**5.5%**
Investment and Credit Company	9.5	9.4	-1.2%	9.7	3.0%
Core Investment Company	0.2	0.1	-29.7%	0.3	120.4%
Factoring - NBC	0.03	0.03	-3.4%	0.03	-18.0%
Infrastructure Debt Fund- NBFC	0.2	0.3	45.5%	0.3	6.2%
Infrastructure Finance Company	8.9	9.0	1.5%	9.6	5.9%
NBFC – Micro Finance Institutions	0.5	0.6	8.2%	0.6	11.0%
NBFC-D	**3.8**	**4.2**	9.7%	**4.1**	-0.9%
Total NBFCs (NBFC-ND-SI + NBFC-D)	**23.2**	**23.6**	**1.9%**	**24.6**	**4.4%**

Source: RBI Trends and Progress of Banking in India

NBFC category-wise breakdown of loans and advances (which comprises around 70% of the total assets of the NBFC sector) has been tabulated in figure 11. Similar to the outstanding borrowings, Investment and Credit Company (ICC), and Infrastructure finance companies (IFCs) are the ones which have the highest quantum of loans and advances amounting to Rs.19.3 lakh crore (78.2% of the total) in H1FY21.

The overall growth of loans and advances contracted in FY20 to 1.9% as compared with 18.1% in FY19. Also, the growth has moderated to 4.4% in H1FY21 as compared with a growth of 4.6% in H1FY20 (*discussed in detail in section 3*). There was a sharp reduction in credit growth to all sectors except retail (refer figure 19). Agriculture, Industry and Services sectors witnessed a significant decline, while the retail sector registered a slower growth in FY20 as compared with FY19. ICC and IFC segments together registered an YTD growth of 4.5% as compared with a growth of 0.1% in FY20 (y-o-y). Loans and advances growth of NBFC-MFI segment improved in H1FY21 (YTD) as compared with FY20.

Figure 12: Composition of loans & advances for select Government owned NBFCs (Rs. lakh crore)

Companies	FY19	FY20	y-o-y Growth %	H1FY21	YTD Growth % (H1FY21 over FY20)
PFC	3.0	3.3	10.2%	3.6	7.8%
REC	2.7	3.1	15.6%	3.4	8.0%
IIFCL	0.4	0.3	-4.3%	0.3	1.8%
IFCI	0.1	0.1	-21.5%	0.1	-9.3%
IRFC	1.3	1.6	18.4%	1.6	3.3%
Total	**7.5**	**8.4**	**12.3%**	**9.0**	**6.6%**

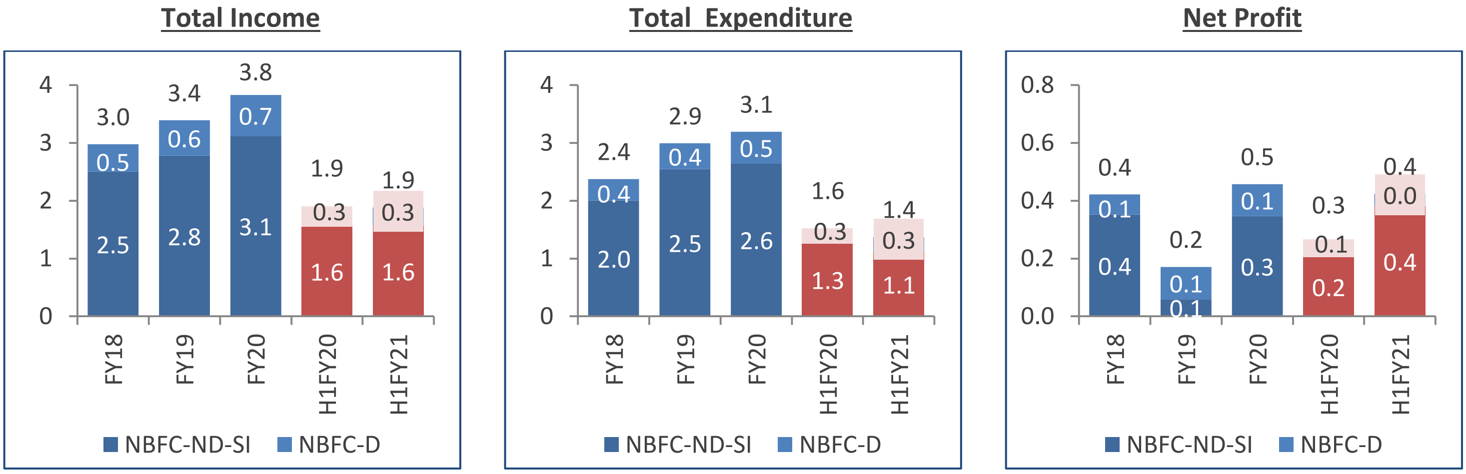
Source: Company Reports; Note: Standalone; loans and advances of IRFC includes lease receivables

As can be seen in the above figure, select government owned NBFCs has a share of 36.6% in total loans and advances of NBFC sector, while, PFC and REC together dominates the loans and advances with a share of 28.3% as of September 30, 2020.

2. Financial performance

This section looks at the annual and half-yearly performance of the NBFC-ND-SI and NBFC-D companies for the financial years, FY18, FY19, FY20, H1FY20 and H1FY21. Key financial indicators of the profit and loss account like total income, total expenditure and net profit after tax have been presented.

Figure 13: Comparison of Financial Performance between NBFC-ND-SI and NBFC-D companies (Rs. lakh crore)



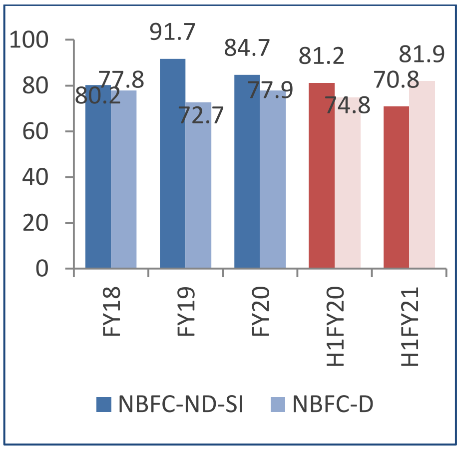
Source: RBI Trends and Progress of Banking in India

The above figure shows that the total income grew strongly at 13.9% y-o-y in FY19, but the growth slowed down to 12.9% y-o-y in FY20 due to slower loan disbursals and rate cuts. NBFC sector registered a net profit growth of 167.3% in FY20 as compared with a de growth of 59.4% in FY19 (low base).

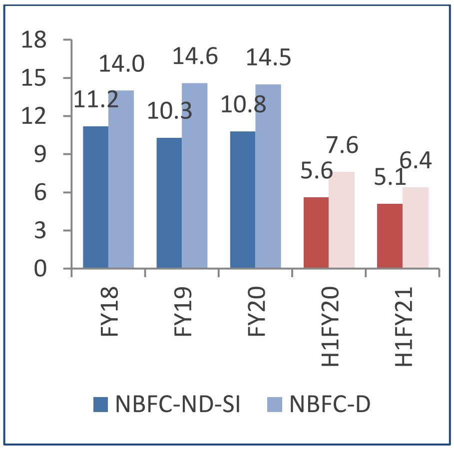
Key Financial Ratios: A comparison of financial ratios for FY18, FY19, FY20, H1FY20 and H1FY21 is given in Figure 14. Although we have seen that NBFC-ND-SI comprise around 83.0% share in total income of the NBFC sector, the income and net profit measured as percentage of total asset is higher for the NBFC-D set of companies (it accounts for around 23% share in net profit of NBFCs). The total cost to income ratio of the NBFC-ND-SI declined from 80.2% in FY18 to 70.8% in H1FY21 indicating a fall in operating expenditure of this segment. On contrary, the total cost to income ratio of the NBFC-D increased from 77.8% in FY18 to 81.9% in H1FY21.

Figure 14: Key financial ratios (as percentage of total assets)

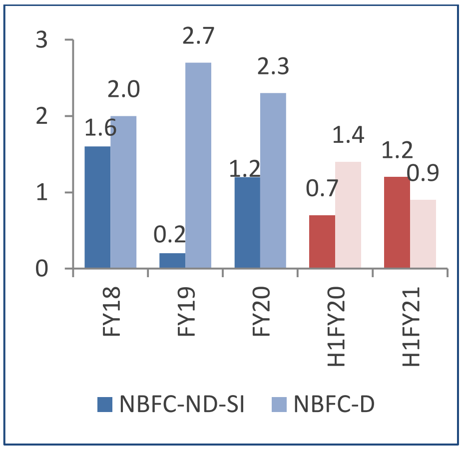
Cost to income ratio (%)



Income to total assets (%)



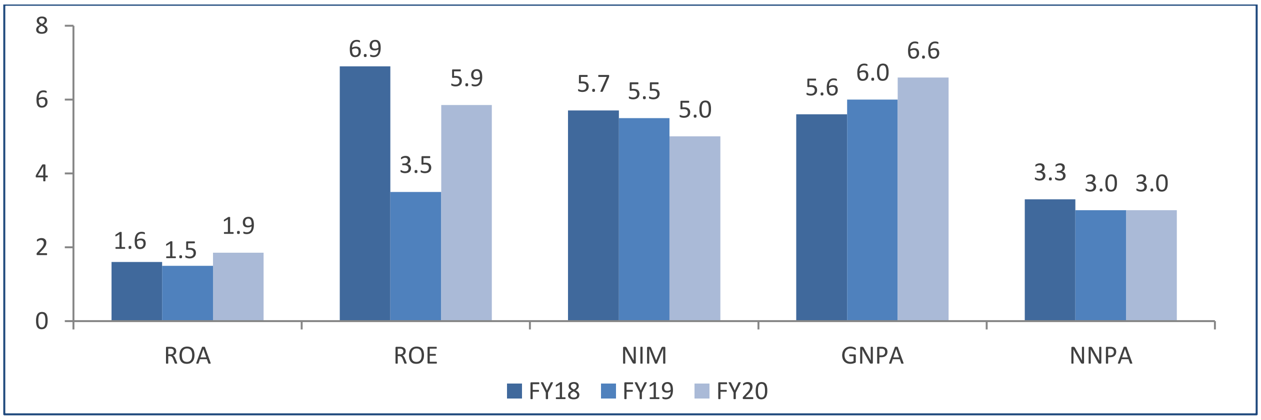
Net profit to total assets (%)



Source: RBI Trends and Progress of Banking in India

- The cost to income ratio has been higher for NBFC-ND-SI during the last three financial years and came down significantly in the first half of FY21 owing to lower operational costs.
- The total income as a percentage to total assets declined from 11.2% in FY18 to 10.8% in FY20 and further declined to 5.1% in H1FY21.
- The balance sheet of NBFC-ND-SI category witnessed a fall in FY20, while NBFC-D continued to grow at a healthy pace, While in H1FY21, balance sheet growth of NBFC-ND-SI gained traction due to pick up in loans and advances and base effect.

Figure 15: Key profitability and asset quality indicators of the NBFC sector (%)



Source: RBI Trends and Progress of Banking in India

- As per RBI's trends and progress report, the improvement in ROA and ROE of NBFCs in FY20 was due to a base effect (IL&FS event) and lower provisions as companies have already provided in FY19.
- Interestingly, while NBFCs have ROA of 1.9% in FY20, while SCBs (Scheduled Commercial Banks) had ROA of 0.2% in the same period. Similarly SCBs had NIM of 2.9% in FY20 thus, indicating higher profitability of NBFCs.
- The GNPA ratio increased to 6.6% in FY20 from 6.0% in FY19 which is partly due to increase in slippages (from 0.30% in FY19 to 0.52% in FY20), while the NNPA ratio stood stable. Recovery and write offs ratio of NBFCs increased from 0.08% and 0.07% in FY19 to 0.10% and 0.13% in FY20 respectively.

Asset quality of the overall NBFC sector has also been considered below:

1. Classification of NBFC loan book (Figure 16)
2. Category-wise analysis of NPA ratio (Figure 17)

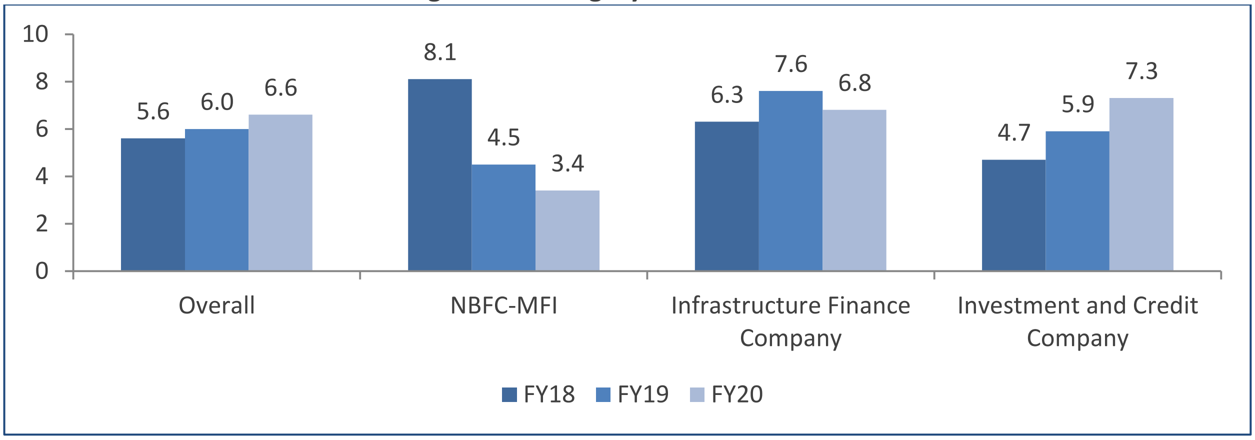
Figure 16: Classification of NBFC loan book (%)

Classification of NBFC Assets	% of total assets			
	FY18	FY19	FY20	H1FY21
Standard Assets	94.7	94.0	93.5	93.3
Sub Standard Assets	3.0	3.5	3.6	3.2
Doubtful assets	2.1	2.0	2.4	2.9
Loss assets	0.2	0.5	0.5	0.6

Source: RBI Trends and Progress of Banking in India

In the above classification of assets, it can be observed that ~3.5% of the total assets of the NBFC sector in H1FY21 is classified as either doubtful or loss assets as per NPA regulations. As the loan book size contracted (refer figure 11); the quality of loan book also declined in FY20 and further in H1FY21. In FY20, the proportion of standard assets has declined as slippages to sub-standard category increased. In figure 17, we have analysed NBFC category-wise NPA ratio for FY18, FY19 and FY20.

Figure 17: Category-wise GNPA ratio



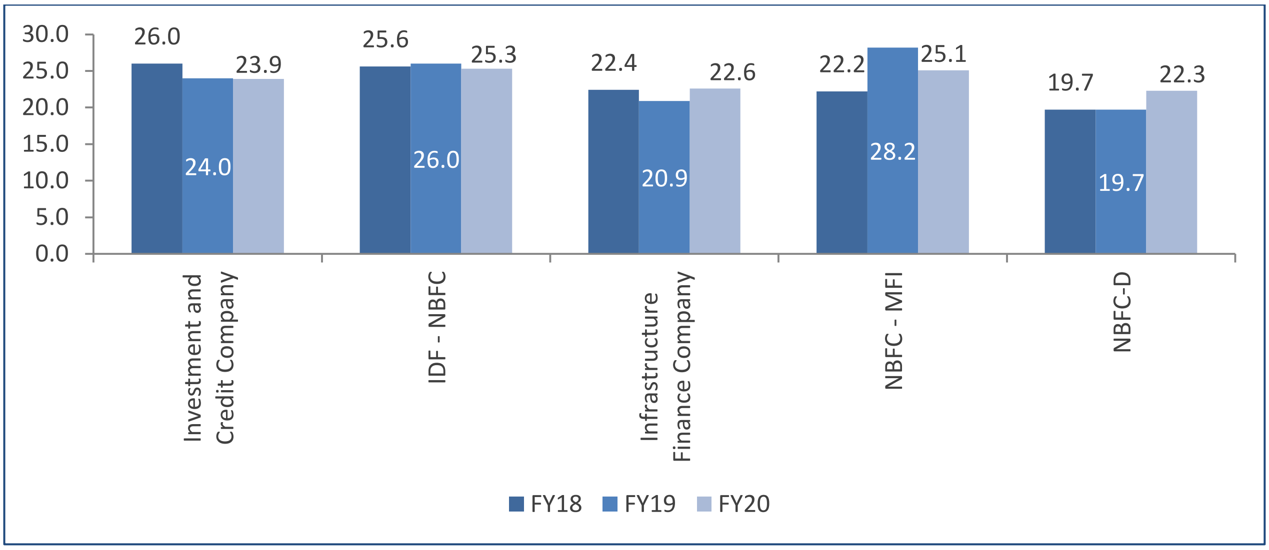
Source: RBI Trends and Progress of Banking in India

- As seen in figure 11, the infrastructure finance company, and investment and credit company accounts for 78.2% of the total outstanding loans and advances, as a result the non-performing assets in these two segments are driving the overall NPA ratio higher for the NBFC sector.

- As per RBI's trends and progress report, infrastructure finance companies reported an improvement in the GNPA ratio as a result of resolution in stressed thermal assets of PFC/REC. The GNPA ratio of NBFCs-ND-SI deteriorated in FY20 on account of worsening asset quality of NBFCs-ICC. The NBFC-MFI segment registered further improvement in asset quality driven by healthy quality of MFI loan portfolio.

Capital Adequacy Requirements:

Figure 18: CRAR for different categories of NBFC sector (%)



Source: RBI Trends and Progress of Banking in India

- The stipulated norm of the CRAR for the NBFC sector is 15%. It can be observed in Figure 18 given above that the CRAR of all categories of NBFC has been above the stipulated norm.
- As seen earlier, the overall loans and advances grew at a moderate rate during H1FY21 as compared to H1FY20 on account of which the CRAR was higher for Investment and Credit Company, Infrastructure Finance Company and NBFC-D. The CRAR of NBFC-MFI deteriorated due to the capital erosion as on March 2020.
- On the other hand, CRAR of NBFC-D increased on account of equity infusion which strengthens their balance sheets.

3. Credit deployment by the NBFC sector:

- As can be seen in figure below, the industry sector (53.6% share in FY20) accounts for the largest proportion of the credit deployed followed by retail segment (23.3%), service sector (15.8%) and balance 7.4% accounts for other non-food credit and agriculture & allied activities. However, only retail portion is growing amongst all the segments.
- Additionally, within the industrial sector, the large industries have received 46.4% (Rs.5.87 lakh crore) of the credit disbursed to this segment (Rs.12.65 lakh crore) in FY20. During FY20, industrial sector credit was impacted by the stress in thermal power projects (includes infrastructure projects), slowdown in construction activities (so lower demand for funds), fall in manufacturing sector output and disruptions caused by COVID-19.
- In service sector, the commercial real estate (CRE) segment received Rs.1.29 lakh crore of credit in FY20, which is 34.7% of the total credit disbursed to the service sector. Credit to CRE segment, which constitutes for around one third of the credit extended by NBFCs to services sector has declined sharply due to disruptions caused by pandemic.

- Retail loan segment grew by 21.6% y-o-y in FY20, led by increase in credit disbursed to vehicle and auto loan which accounts for 43.4% of the total credit disbursed to retail segment. However, several NBFCs remained ahead of the curve in retail sector by diversifying into other areas of vehicles financing like used vehicles, two-wheelers in place of commercial vehicles which helped in arresting the fall in credit to retail sector.
- There was a contraction in credit to agriculture, mainly due to the shift in lending by NBFC-MFI to industry.

Figure 19: Sectoral deployment of NBFC credit

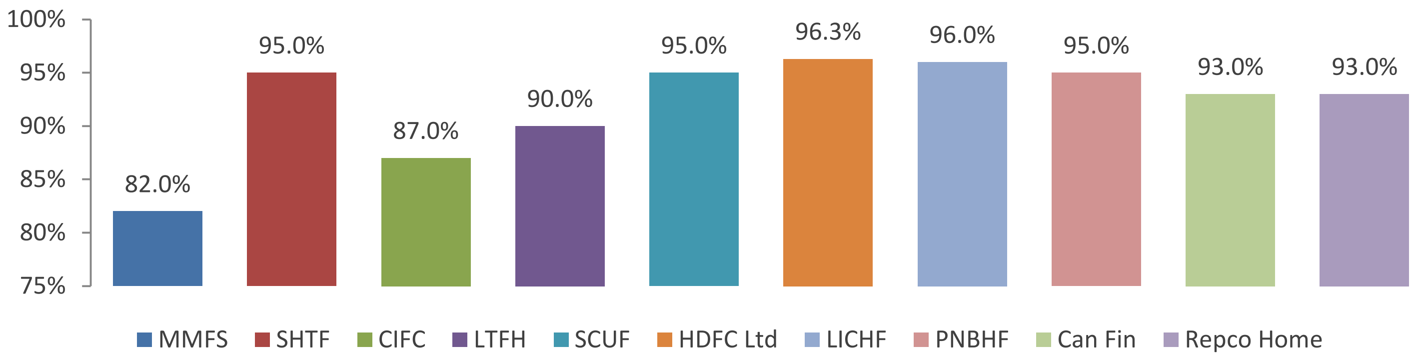
Particulars	Amount (Rs. Lakh cr)		y-o-y growth (%)	% share of total (FY19)	% share of total (FY20)
	FY19	FY20			
Gross Advances	**23.2**	**23.6**	**1.9%**	-	-
Non-food Credit	**23.2**	**23.6**	**1.9%**	-	-
Agriculture & Allied Activities	**0.7**	**0.6**	**-13.0%**	**3.1%**	**2.6%**
Industry	**12.7**	**12.7**	**-0.3%**	**54.8%**	**53.6%**
Micro and Small	*0.4*	*0.8*	*80.7%*	*1.8%*	*3.2%*
Medium	*0.2*	*0.2*	*-5.8%*	*0.8%*	*0.7%*
Large	*7.1*	*5.9*	*-17.1%*	*30.6%*	*24.9%*
Others	*5.0*	*5.9*	*16.9%*	*21.6%*	*24.8%*
Services	**3.9**	**3.7**	**-3.3%**	**16.6%**	**15.8%**
Commercial real estate	*1.5*	*1.3*	*-14.8%*	*6.5%*	*5.5%*
Trade	*0.3*	*0.4*	*26.9%*	*1.3%*	*1.6%*
Retail	**4.5**	**5.5**	**21.6%**	**19.5%**	**23.3%**
Housing loans	*0.2*	*0.2*	*37.1%*	*0.7%*	*0.9%*
Vehicle/auto loans	*2.0*	*2.4*	*18.2%*	*8.7%*	*10.1%*
Consumer durables	*0.1*	*0.1*	*-0.4%*	*0.2%*	*0.2%*
Other Non-food credit	**1.4**	**1.1**	**-19.9%**	**5.9%**	**4.7%**

Source: RBI Trends and Progress of Banking in India

Section B – Performance of select NBFCs and HFCs

In this section we have analysed Q2FY21 performance of Non-Banking Financial Companies (NBFCs) and Housing Finance Companies (HFCs). In this study we have considered 15 NBFCs (list given in Annexure) which constitutes ~65 of total NBFC assets and 9 HFCs (list given in Annexure) which constitute ~91 of total HFCs assets.

Figure 20: Average collection efficiency is >92% in September 2020



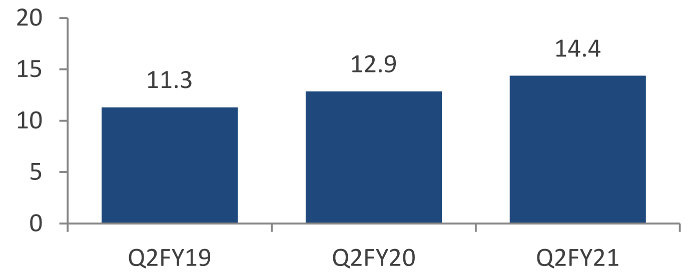
Source: Company reports; Note: HDFC Ltd – Individual loan

Banks' outstanding to NBFCs registered a highest growth of 46.3% in absolute terms from September 2018 (Rs.5.5 lakh crore) to September 2020 (Rs.8.0 lakh crore). The overall composition of NBFCs in bank credit increased from 6.9% in September 2018 to 8.7% in September 2020 and remained stable on m-o-m basis (8.7% in August 2020). However, growth in bank credit to NBFCs has registered a downward trend, due to the base effect and risk aversion in banking system due to the COVID-19 pandemic. Also, NBFCs were not in need of funds as disbursements were muted.

NBFCs: Business Update

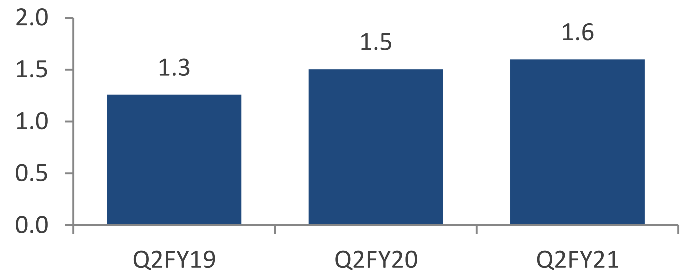
Despite slower rundown due to moratorium to a significant part of their borrowers, the loan growth for the NBFCs on y-o-y basis came at 11.8% in Q2FY21 as compared with 13.6% in Q2FY20 due to weak demand on the back of nationwide lockdown and the resultant risk aversion. Out of 15 companies, 4 companies have clocked a loan growth of more than 10% YoY, 3 companies witnessed a negative growth and rest 8 companies registered a marginal growth during Q2FY21. The growth in AUM of gold financier was driven by sharp rise in gold prices and increase in loan to value ratio (LTV) from 55% to 61% in Q2FY21. As a part of Atmanirbhar package for discoms, PFC and REC together have sanctioned Rs.1.18 lakh crore of which Rs. 31,000 crore has been disbursed. Loan growth was aided by disbursement under Atmanirbhar package for both these companies. Disbursements were muted during Q2FY21 which registered a growth of 6.3% YoY as compared with ~20% YoY in Q2FY20 mainly due to risk aversion. All NBFCs witnessed a decline in overall disbursement growth except Muthoot Finance, which registered a sharp increase during Q2FY21 led by gold price momentum. Disbursement in vehicle/infrastructure of L&T Finance was up to ~75% of YoY levels during Q2FY21 in the quarter and tractor disbursements increased by ~60% YoY.

Figure 21: Loan (Rs lakh crore)



Source: Company reports, CARE Ratings Calculation; Note: Loan excluding Max Financial, SREI infra and IFCI Ltd.

Figure 22: Disbursements (Rs lakh crore)

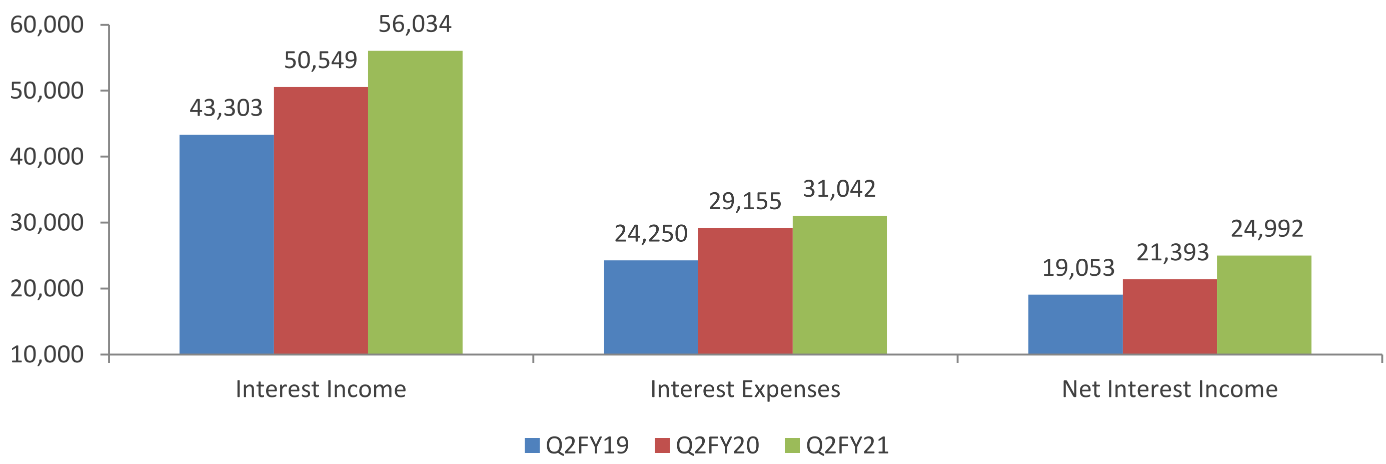


Source: Company reports, CARE Ratings Calculation; Note: Disbursements exclude Bajaj Finserv, Edelweiss, Max Financial, Shriram Transport, SREI infra and IFCI Ltd.

Despite of lower YoY growth in loan book of NBFCs, NII growth came at 16.8% in Q2FY21 as compared with 12.3% in Q2FY20. This can be ascribed to:

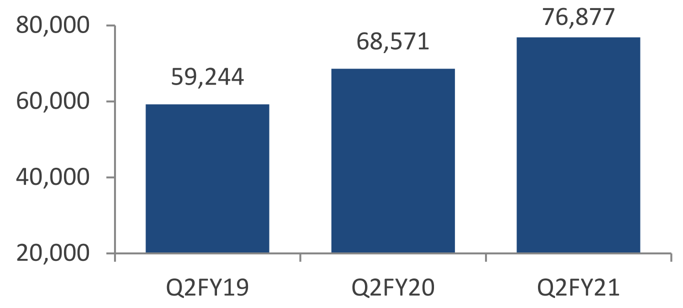
- The interest income increasing by 10.9% in Q2FY21 as compared with 16.7% in Q2FY20, despite the moratorium. The interest income growth can also be attributed to decrease in gross NPAs (Excluding Bajaj Finserv, Max Financial, Edelweiss Financial, Aditya Birla Capital, SREI Infra and IFCI) from Rs.76,660 crores in Q2FY20 to Rs.67,474 crores in Q2FY21.
- The borrowing cost for NBFCs declined in Q2FY21 as compared with Q1FY21 and Q2FY20. Since March 2020, the weighted average yields have fallen by ~235 bps (primary market). Both corporate bonds and commercial papers saw their average secondary market yields decline in September 2020. Corporate bond yields (weighted average yields) at 6.74% in September 2020 was ~15 bps lower than in September 2019. Additional liquidity available has enabled many NBFCs to negotiation better interest rates.

Figure 23: Net Interest Income (NII) (Rs Crore)



Source: Company Reports, CARE Ratings calculation

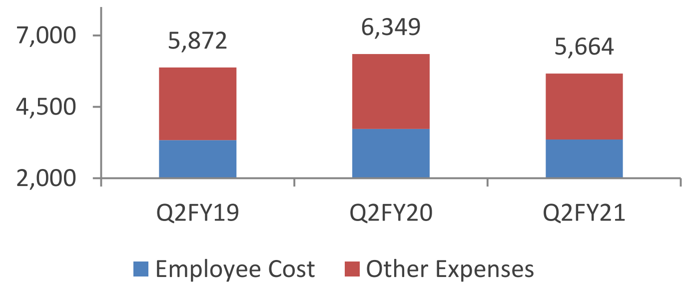
Figure 24: Total Income (Rs Crore)



Source: Company Reports, CARE Ratings calculation

- Total income growth of NBFCs slowed down to 12.1% in Q2FY21 vis-à-vis 15.7% for the same period in the previous year; due to the slow growth in interest income (Figure 23) compared with the previous year (interest income accounts for around 73.0% share of the total income).
- Other income which accounts for the balance 27.0% share of total income increased by 15.7% growth in Q2FY21 as compared with 13.1% growth in Q2FY20.

Figure 25: Operating Expenses (Rs Crore)



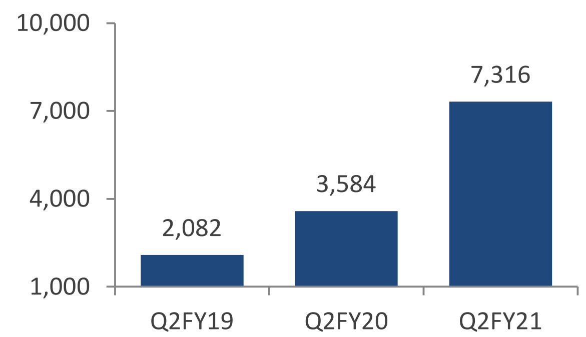
Source: Company Reports, CARE Ratings calculation

- The employee cost which accounts for 59.2% of total opex of NBFCs registered a de growth of 10.0% in Q2FY21 as compared with growth of 11.6% in Q2FY20. The operating expenses have also registered a de growth of 10.8% vs. a growth of 8.1% in Q2FY20. The other expenses declined by 11.8% in Q2FY21 as against a growth of 3.5% in Q2FY20. The employee cost for SREI Infra, Bajaj Finserv, Mahindra & Mahindra Finance, Shriram City Union, Max Financial, PFC and REC declined by more than 15% YoY during Q2FY21largely due to drop in staff count.

Operating expenses for Bajaj Finserv declined led by its insurance subsidiaries employee cost and infrastructure cost. The company took initiative and negotiated for the rents and shifted to digitalization which had resulted in lower infrastructure cost and shift of annual increments to quarterly increments has resulted in reduction of Employee cost during Q2FY21.

Provisions and Contingencies

Figure 26: Provisions more than doubled (Rs Crore)



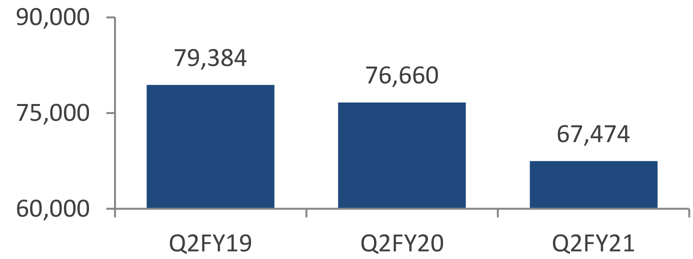
Source: Company Reports, CARE Ratings calculation

- During Q2FY21 total provisions increased by 104% YoY as compared with an increase of 72.2% in Q2FY20, as additional provisions made by NBFCs as a prudent measure. (*COVID -19 specific provision as a % of loan book is given in annexure*)
- Bajaj Finserv's provisions increased by 196.6% YoY during Q2FY21, as company had made additional COVID related provisions of Rs.1,370 crore.
- L&T Finance Holdings had made additional COVID related provisions during Q2FY21 of Rs.512 crore, taking the total additional provisions at Rs.1757 crore which is ~2% of the standard book.
- Shriram City Union Finance had made COVID-19 related provisioning of Rs.101 crore in Q2FY21, taking the total provisions of Rs.701 crore for COVID-19.

- Shriram Transport Finance had made Rs.401 crore of provisions in Q2FY21, Rs.300 crore for accounts which would have been NPA if Supreme Court order was not in place and rest is additional cautious provisioning for COVID-19.
- Provisions of Cholamandalam Investment & Finance registered a sharp increase of 233.8% YoY as Management's prudent measure. The company made additional provisions of Rs.250 crore taking total provisions to ~2.6% of book.
- In the coming quarter's provisions of NBFCs are expected to remain elevated on account of recognition of stressed assets owing to COVID-19 and its disruptions affecting the business which could impact its financial performance.

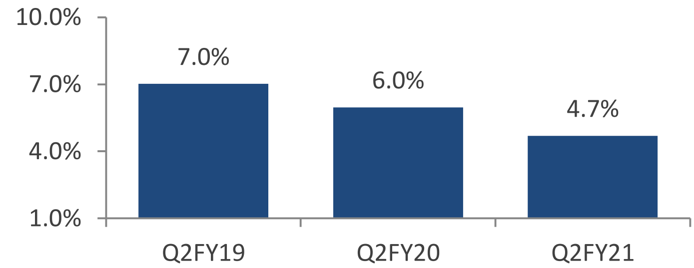
Asset Quality

Figure 27: GNPAs improved (Rs Crore)



Source: Company Reports, CARE Ratings calculation; Note- GNPAs excluding Bajaj Finserv, Max Financial, Edelweiss Financial, Aditya Birla Capital, SREI Infra and IFCI

Figure 28: GNPA ratio



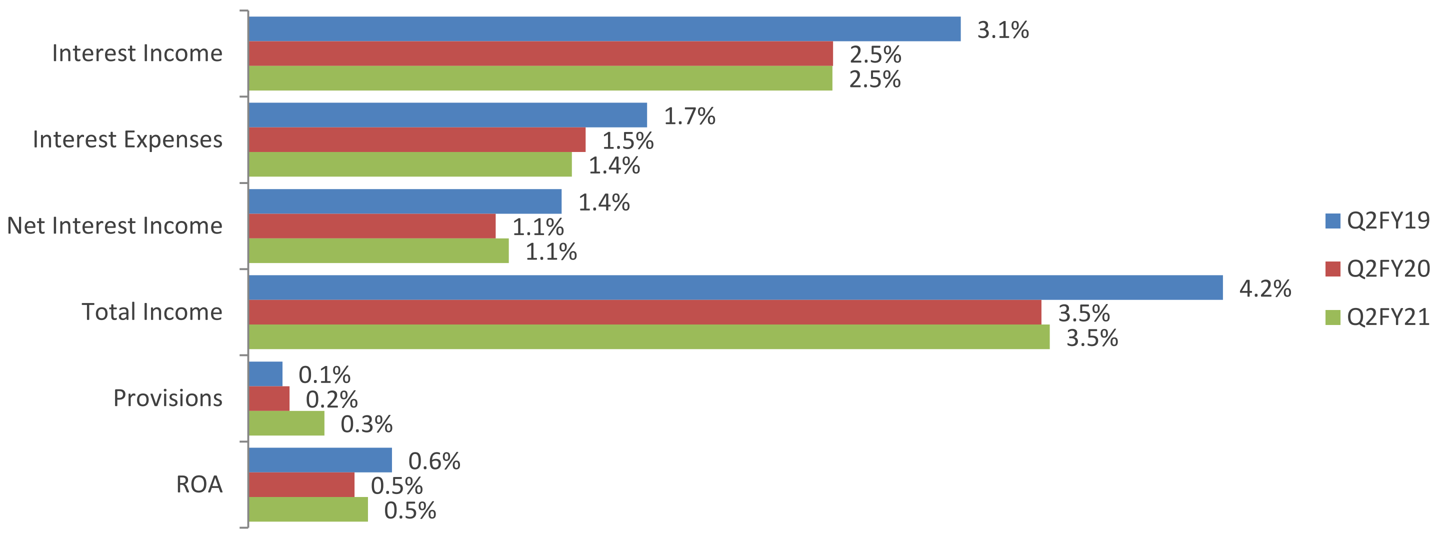
Source: Company Reports, CARE Ratings calculation; Note- GNPAs excluding Bajaj Finserv, Max Financial, Edelweiss Financial, Aditya Birla Capital, SREI Infra and IFCI.

NBFCs witnessed a significant improvement in gross NPAs during Q2FY21 as compared with Q2FY20 due to regulatory dispensation which has halted the NPA recognition since March 1, 2020 onwards. On September 3, 2020, the Supreme Court had ordered that accounts which were not declared NPA till August 31, 2020 shall not be declared as NPA till further orders. In absolute terms GNPAs declined from Rs.76,660 crore in Q2FY20 to Rs.67,474 crore in Q2FY21. The GNPA ratio also witnessed a sharp fall in Q2FY21 to ~4.7% as compared with ~6.0% in Q2FY20 and ~7.0% in Q2FY19 respectively.

Profitability

The profitability of NBFCs stood largely stable due to the slow growth in their advances in Q2FY21. The NBFCs recorded return on assets (ROA) from 0.46% in Q2FY20 to 0.52% in Q2FY21 as profitability impacted majorly on account of an increase in their provisions despite significant reduction in operating costs. The moderation in interest income comes on account of the slow growth in the advances of the NBFCs. As a result, the NBFCs have been able to conserve their NIMs and ROA at levels similar to that in Q2FY20. Most NBFCs made additional COVID related provisions as a prudent measure. Hence there was an increase in the provisions of NBFCs in Q2FY21. The ROA chain indicates that the growth in the loan of NBFCs has led to a rise in their interest income; their interest expense as a percentage of total assets has declined marginally and there was a fall in the cost of borrowing of some NBFCs.

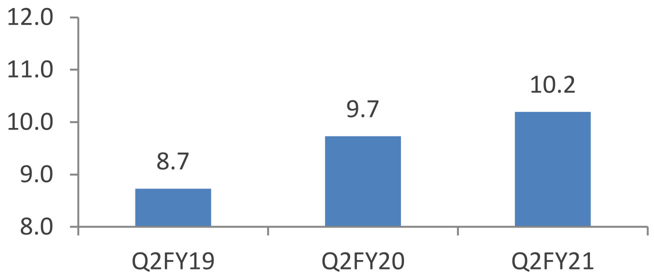
Figure 29: Q2FY21 - ROA Chain



Source: Company Reports, CARE Ratings Calculation

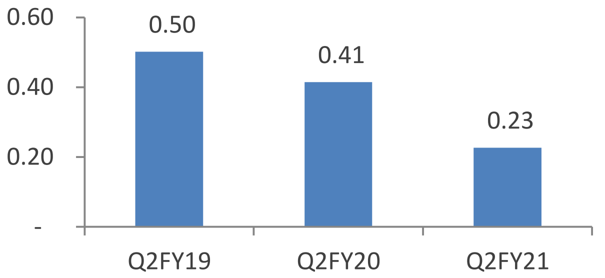
<u>HFCs</u>: Business Update

Figure 30: Loan book (Rs lakh crore)



Source: Company reports, CARE Ratings Calculation; Note: Loan/AUM excluding Aavas Financiers.

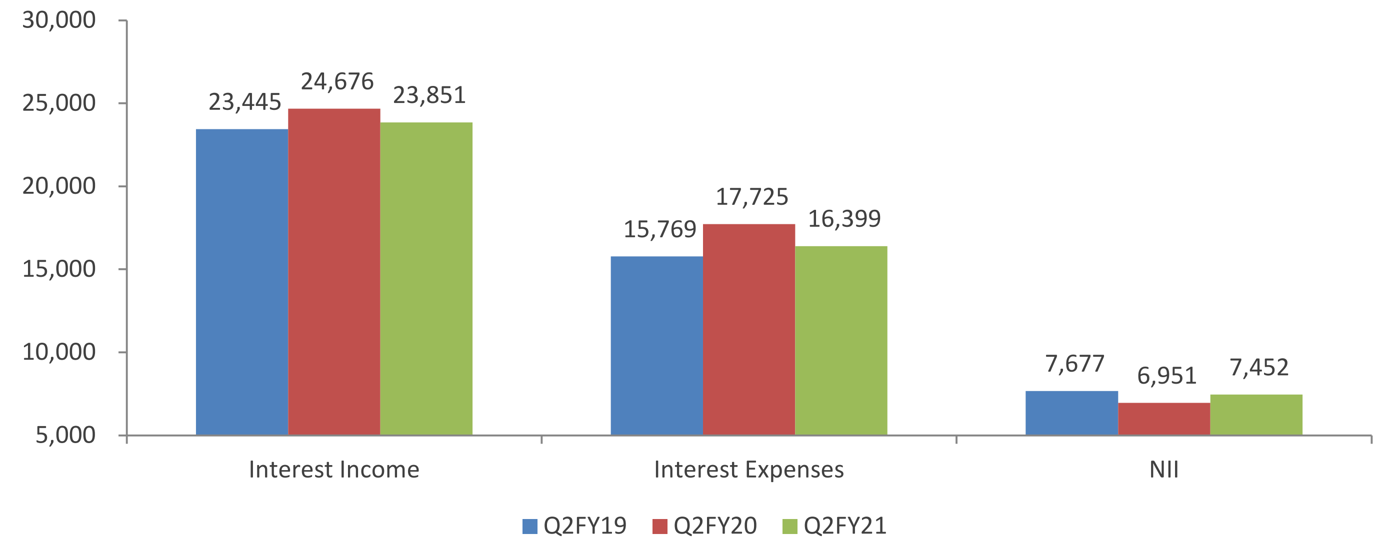
Figure 31: Disbursements (Rs lakh crore)



Source: Company reports, CARE Ratings Calculation; Note: Disbursements excluding HDFC Ltd, Indiabulls Housing Finance and Aavas Financiers.

As per RBI's bank sectoral deployment of credit, housing loan growth registered a growth of 11.0% YoY during the quarter ended September 2020 as compared with 18.0% YoY growth during quarter ended September 2019. The Loan growth for sample HFCs moderated to 4.8% YoY in Q2FY21 as compared with 11.4% in Q2FY20 due to weak economic conditions and risk aversion. The disbursements growth witnessed a sharp decline of 45.3% YoY in Q2FY21 as compared with a decline in Q2FY20 at 17.4% YoY due to extended lockdown and weak macroeconomic environment. For HDFC Ltd, loan growth was driven by disbursement in individual loan book (which is ~75% of overall loan book) during Q2FY21. The individual loan disbursements were ~95% of pre covid levels.

Figure 32: Net Interest Income (NII) (Rs Crore)

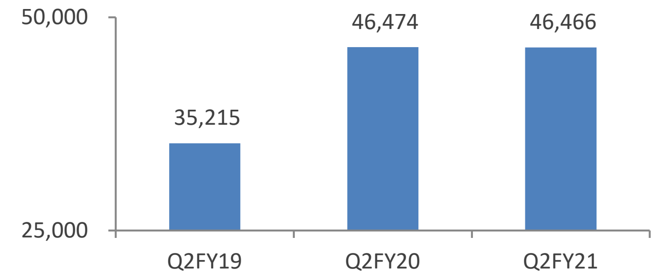


Source: Company Reports, CARE Ratings calculation

Despite of lower growth in Loan book, NII growth increased by 7.2% in Q2FY21 as compared with a growth of -9.5% in Q2FY20. This can be ascribed to:

1) The interest income growth declined by 3.3% in Q2FY21 as compared with a growth of 5.2% in Q2FY20, due to muted disbursements during the quarter. While, the interest expenses growth declined by 7.5% in Q2FY21 as compared with a growth of 12.4% in Q2FY20, led by lower cost of funds.
2) The borrowing cost for HFCs declined in Q2FY21 as compared with Q1FY21 and Q2FY20. Since March 2020, the weighted average yields have fallen by ~166 bps (primary market). Both corporate bonds and commercial papers witnessed a decline in their average yields (secondary market) in September 2020. Corporate bond yields (weighted average yields) at 6.74% in September 2020 was ~15 bps lower than in September 2019.

Figure 33: Total Income (Rs Crore)



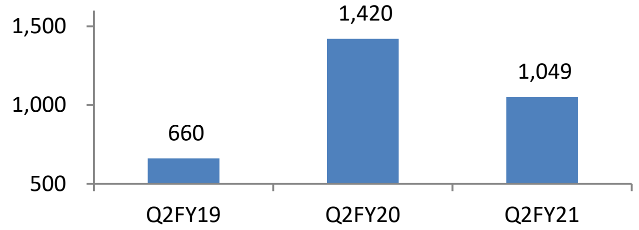
Source: Company Reports, CARE Ratings calculation

- Total income growth of HFCs was marginally lower in Q2FY21 as compared with Q2FY20; due to the slow growth in interest income (Figure 32). (Interest income accounts for around 51.0% share of the total income).
- Other income which accounts for the balance 49.0% share of total income increased by 3.7% growth in Q2FY21 as compared with 85.2% growth in Q2FY20.

Operating Expenses

The employee cost of HFCs registered a de growth of 25.7% in Q2FY21 largely due to lower staff count (de growth of 23.4% in Q2FY20). The other expenses declined by 22.8% in Q2FY21 as against a de growth of 51.9% in Q2FY20. However, the operating expenses have also registered a de growth of 24.7% vs. a de growth of 36.7% in Q2FY20 driven by lower employee and non-employee cost. LIC Housing Finance reported a higher growth in its operating expenses in Q2FY21 due to CSR expenses.

Figure 34: Provisions and Contingencies (Rs Crore)

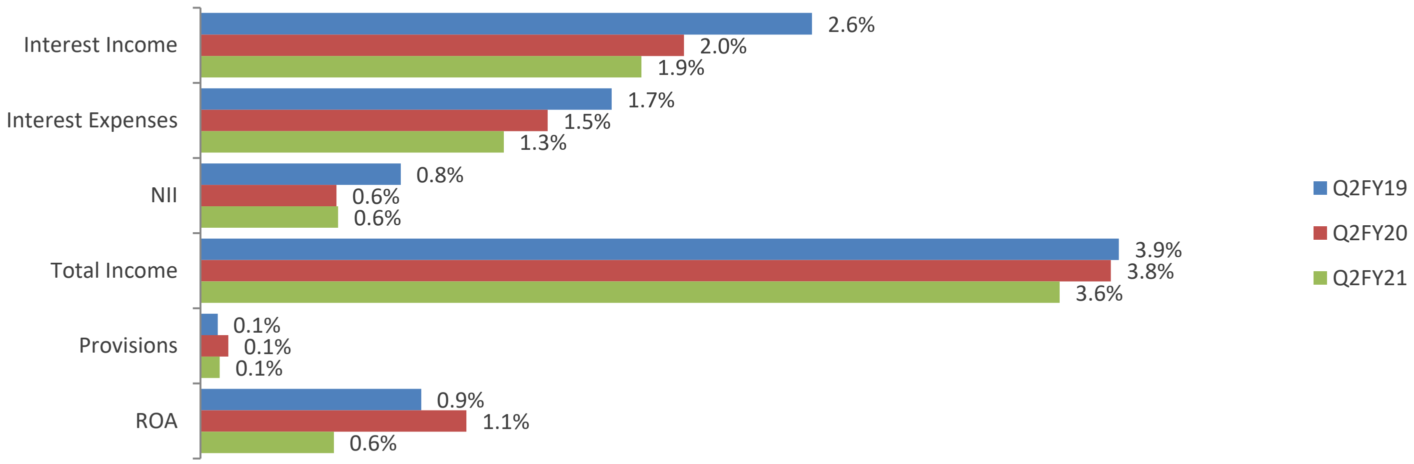


Source: Company Reports, CARE Ratings calculation

During Q2FY21 total provisions for HFCs declined by 26.2% YoY as compared with an increase of 115.3% (due to ECL provisioning under IND-AS) in Q2FY20. There was an increase in provisions during Q1FY21 (Provisions of Rs.2,036 crore in Q1FY21); hence the incremental COVID related provisions were lower in Q2FY21.

Profitability

Figure 35: Q2FY21 - ROA Chain

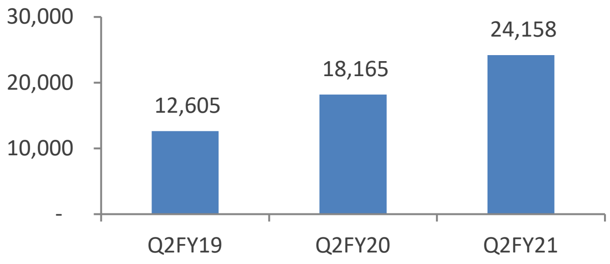


Source: Company Reports, CARE Ratings Calculation

The profitability of HFCs declined due to the slow growth in their disbursement in Q2FY21. The HFCs recorded a fall in return on total assets (ROA) of 1.1% in Q2FY20 and 0.6% in Q2FY21 majorly on account of muted growth in Net Interest Income. The moderation in interest income comes on account of the slow growth in the disbursements of the NBFCs. Most HFCs made additional COVID related provisions as a prudent measure in Q1FY21. Hence there was a marginal fall in the incremental provisions of HFCs in Q2FY21. The ROA chain indicates that the growth in the loan of HFCs has led to a decline in interest income; their interest expense as a percentage of total assets have also declined and a fall in the cost of borrowing of some HFCs.

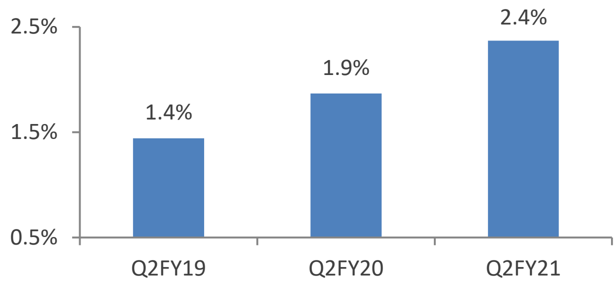
Asset Quality

Figure 36: GNPAs (Rs Crore)



Source: Company Reports, CARE Ratings calculation; Note- GNPAs excluding Aavas Financiers

Figure 37: GNPA ratio



Source: Company Reports, CARE Ratings calculation; Note- GNPAs excluding Aavas Financiers

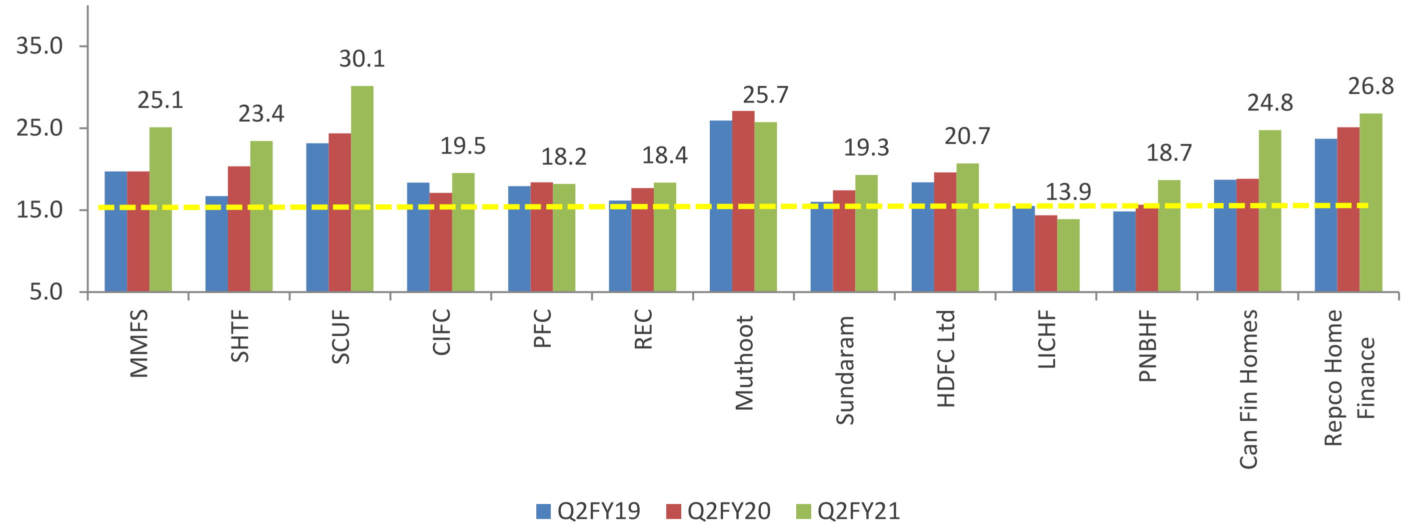
HFCs witnessed deterioration in gross NPAs during Q2FY21 as compared with Q2FY20 despite of regulatory dispensation. In absolute terms GNPAs increased from Rs.18,165 crore in Q2FY20 to Rs.24,158 crore in Q2FY21. The GNPA ratio also witnessed a sharp increase in Q2FY21 to ~2.4% as compared with ~1.9% in Q2FY20 and ~1.4% in Q2FY19 respectively.

HDFC Ltd.'s overall collection efficiency for individual loans was 96.3% in September. The collection efficiency for non-moratorium customers stood at 99.5%. The non-performing loans would have been only 2 bps higher at 1.83% of the loan portfolio if Supreme Court order on asset classification were not considered; with individual NPLs at 0.88% and non-individuals NPLs at 4.19%. For LIC Housing Finance 3-4 big ticket developer loans are in final stages of resolution which should improve the NPA movement in Q3FY21. Its Individual stage 3 assets stood at 1.7% and project stage 3 assets stood at 16.5%.

Capital Adequacy Ratio (CRAR) under Basel III for NBFCs and HFCs

NBFCs in Figure 38 had a strong capital position during Q2FY21. RBI requires NBFCs to maintain a minimum level of CRAR or Capital to Risk Assets Ratio of 15%. NBFCs had requested RBI to consider a one-time measure to allow NBFCs to draw down from their Reserves and adjust towards additional ECL provision requirement. It will enable the NBFCs to shore up their balance sheet strength by reporting a more fortified ECL provision cover against their likely increase in delinquent loans and remain eligible to access equity/debt capital when COVID situation improves. The aggregate Debt/Equity ratio of sample NBFCs improved marginally at 4.0x as of September 2020 as compared with 4.3x as of March 2020.

Figure 38: CRAR position of select NBFCs and HFCs (%)



Source: Company Reports

Conclusion

- As on August 31, 2020, the overall percentage of NBFC customers who have availed the loan moratorium has been comparatively lower than banks, while the loans outstanding under moratorium were higher as compared with banks.
- The combined sample set of NBFCs and HFCs have witnessed a lower disbursals and AUM growth in Q2FY21 as compared with Q2FY20 due to cautious approach towards fresh disbursements and weak demand compounded by risk aversion. During Q2FY21, the rural focused NBFCs have witnessed an almost normal disbursements and collections supported by harvest.
- The funding challenges for NBFCs and HFCs could mount again (especially for smaller NBFCs), on the back of Covid-19 related disruptions, leading to tighter liquidity concerns. The liquidity covers of NBFCs and HFCs will be dependent on collections and the ability to raise resources during these challenging times. Amidst this challenging time, banks overall exposure to NBFCs have been increasing, while the share of CPs and corporate debt deployed together in NBFCs witnessed a declining trend during November 2019 to November 2020. While this has seen minor reversal lately, the long term trend is to be seen.
- As the economic recovery is gaining the traction, the gradual pickup in disbursements is expected in the second half of FY21. For most of large NBFCs collection efficiency has improved and may improve further.
- It will be important to monitor the collection trends and restructuring under the COVID-19 stress resolution framework for NBFCs and HFCs.

Annexure

Annexure 1: Select NBFCs/HFCs which have made specific COVID-19 provisions in Q2FY21 -

NBFCs/HFC	Covid Provisions (Rs Crore)	Covid Provisions as a % of their loan book
Bajaj Finserv Ltd	900.0	0.7%
L&T Finance Holdings Ltd	483.0	0.5%
Mahindra & Mahindra Financial Services Ltd	433.0	0.7%
Shriram Transport Finance Company Ltd	416.7	0.4%
Shriram City Union Finance Ltd	101.0	0.4%
HDFC Ltd	1,200.0	0.2%

Note: Company reports; loan book as on September 30, 2020

Annexure 2: List of NBFCs

1	Bajaj Finserv Ltd
2	L&T Finance Holdings Ltd
3	Mahindra & Mahindra Financial Services Ltd
4	Shriram Transport Finance Company Ltd
5	Shriram City Union Finance Ltd
6	Max Financial Services Ltd
7	Edelweiss Financial Services
8	Cholamandalam Investment and Finance Company Ltd
9	Power Finance Corporation Ltd
10	REC Ltd
11	Aditya Birla Capital Ltd
12	Muthoot Finance Ltd
13	Sundaram Finance Ltd
14	SREI Infrastructure Finance Ltd
15	IFCI Ltd

Note: Consolidated priority

Annexure 3: List of HFCs

1	HDFC Ltd
2	LIC Housing Finance
3	Indiabulls Housing Finance
4	PNB Housing Finance
5	Housing Urban Development Corporation Ltd
6	Can Fin Homes
7	GIC Housing Finance
8	Repco Home Finance
9	Aavas Financiers

Note: Consolidated priority

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