Company: Brickwork Ratings

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Present Challenges Being Faced by Non-Banking and Housing Finance Companies

Bangalore, Karnataka, India

Brickwork Ratings (BWR) has taken note of the current liquidity issues being faced by many companies in the NBFC/HFC sector. BWR has a significant portfolio of players in these segments and is interacting with them on a regular basis to understand the position of each company, as also the position of the sector. Based on this, BWR is of the following view:

1. NBFCs and HFCs have played a significant role in credit growth over the last few years. In particular, when the focus of Public Sector Banks (PSBs) shifted to restructuring, resolution, recoveries, controlling provisions and Capital Adequacy, their credit growth came down, and in many cases, turned negative. That space was partially filled by NBFCs and HFCs.

2. These sectors registered a CAGR of 19% and 18% respectively in their AUM over the 3 years period (2015 – 2018), and consequently, their borrowings also went up. While the required CRAR was maintained (Regulatory minimum: 15% for NBFCs and 12% for HFCs), the gearing ratios have increased, and hover between 5x to 8x among major companies. RBI's data as of 31.3.2018 indicates that total amount raised by these sectors (excluding receivables) from the financial system, is Rs. 7,17,000 Crs and Rs. 5,28,400 Crs respectively, and for banks, the combined position represents their highest sectoral exposure.

3. RBI's data also shows that the NBFCs and HFCs have 22% and 26% respectively as Short Term funding, comprising of Commercial Paper (CP), Short Term Loan, ST Deposit and other ST liabilities, and out of this, nearly 50% comprises of CPs. Most of the CPs is invested by Mutual Funds, Insurance Companies, Provident Funds, etc. This means, these companies need to constantly refinance a portion of their debt, and if these refinancing options become scarce, or are expensive, it affects their operations. Since the last week of September 2018, this sector is facing such issues.

4. On the basis of market's perception of the position of each company or group, their share prices also have taken a beating in the range of 30 - 60%. Based on Q2FY19 results (or Q1FY19 figures where Q2 results are not yet published) fundamentals of these companies, as reflected by their asset quality, provisions, provision coverage ratio, NIM or Capital Adequacy, etc., have more or less remained the same as at 31st March 2018. The only change appears to be the market's view on ST ALM mismatches, and the present scarcity of ST funding sources. There also appear to be concerns on some of these companies' exposure to real estate developers – particularly in some geographies.

5. This development is taken note of by the regulators (RBI and NHB), as also by Govt of India, and many steps have been taken, including exhorting banks to continue to fund NBFCs based on standard norms, enlarging refinance windows, providing Partial Credit Guarantees, buying securitized pools, etc. BWR expects that these steps will provide much-needed relief. Since NBFCs have significant portion of their short-term funding made through market instruments, BWR is of the view that continued participation of Mutual Funds, Insurance Companies & Provident Funds in the form of refinance options/fresh investments in these NBFCs would be critical for their successful management of liquidity pressures.

6. For NBFCs/HFCs, all funding – whether LT or ST represents 'Working Capital' facility, and hence the availability of funds, coupled with Capital Adequacy determines the size of their portfolio. In the current scenario, BWR expects that the NBFCs/HFCs will slow down their disbursements, and focus on maintaining liquidity. Consumer retail loans also could decline, to conserve resources. Due to a higher level of securitization and sale of assets, overall AUM will come down. They will also reduce their dependence on CP/ST market, and move towards LT facilities, including revolving facilities from banks. In view of increasing cost of funds, the margins may decline and in turn, could result in lower NIMs in Q3 and Q4 of FY19. Exposure to products like LAP, SME financing and Corporate Loans (mainly to the real estate sector) needs close monitoring by the issuers for any slippages or trends.

7. BWR would keep a continuous watch on the developments, and take appropriate rating action in individual cases, when warranted.

About Brickwork Ratings

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BWR has its corporate office in Bengaluru and a country-wide presence with its offices in Ahmedabad, Chandigarh, Chennai, Hyderabad, Kolkata, Mumbai and New Delhi along with representatives in 150+ locations.

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