

Non- banking financial companies growth and development in India (from 2013-18)

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ABSTRACT: NBFCs have played a key role in capital formation. NBFCs have been supplementing the banking sector by bridging the credit differences, i.e., in meeting the increasing financial needs of the corporate sector, delivering credit to the disadvantaged sector and to small local borrowers. NBFCs enjoy a flexible structure than as compared to banks in the organised sector. From time to time, the Central Government as well as Reserve Bank of India have been working towards regulation of NBFCs. The Department of Non-Banking Supervision of RBI has been involved in these activities of regulating as well as supervising the NBFCs.

The present paper focus on "Growth and Development of Non-Banking Financial Companies in India" is an attempt to analyse evolution, growth and development of Non-Banking Financial Companies in India.

Total outstanding borrowing of the NBFC sectors increased as a CAGR of 14.1% during FY13-FY18 which commensurate with the CAGR of 14.45% in the overall credit during the same time period. Overall NBFC sector credit growth has been significantly faster in FY18 than the bank credit growth.

Key Words: Non-Banking Financial Companies Organised Banking Sector, Financial Institutions, and Financial Supermarkets, Reserve Bank of India, Supervision and Regulation.

INTRODUCTION TO NON-BANKING FINANCIAL COMPANIES

Non-banking financial companies (NBFCs) constitute an important segment of the financial system in India. NBFCs are financial intermediaries engaged primarily in the business of accepting deposits and delivering credit. They play an important role in channelizing the scarce financial resources for capital formation. NBFCs supplement the role of the banking sector in meeting the increasing financial needs of the corporate sector, delivering credit to the unorganized sector and to small local borrowers. NBFCs have a more flexible structure than banks. As compared to banks, they can take quick decisions, assume greater risks, tailor-make their services and charges according to the needs of the clients. Their flexible structure helps in broadening the market by providing the saver and investor a bundle of services on a competitive basis. A non-banking financial company has been defined vide clause (b) of Section 45-1 of Chapter IIIB of the Reserve Bank of India Act, 1934, as

(I) a financial institution, which is a company;

(ii) a non-banking institution, which is a company and which has as its principal business the receiving of deposits under any scheme or arrangement or in any other manner or lending in any manner;

(iii) Such other non-banking institutions or class of such institutions, as the bank may with the previous approval of the central government and by notification in the official gazette, specify.

Non-banking financial institutions (NBFIs) comprise a heterogeneous group of financial intermediaries. Those under the regulatory purview of the Reserve Bank consist of all-India financial institutions (AIFIs), non-banking financial companies (NBFCs)¹ and primary dealers (PDs) AIFIs are apex institutions established during the development planning era to provide long-term financing/refinancing to specific sectors such as

(i) Agriculture and rural development;

(ii) Trade;

(iii) Small industries; and

(iv) Housing.

NBFCs are dominated by joint stock companies, catering to niche areas ranging from personal loans to infrastructure financing.



The non-banking finance companies (NBFCs) in the Indian financial system has complemented the banking system and brought about enhanced coherence and diversity in financial intermediation. NBFCs have progressed considerably in terms of operations, heterogeneity, asset quality, regulatory architecture and profitability. NBFCs disbursing credit to the overall commercial sector has increased and gained importance in the preceding few years as banks have faced challenges in lending amid the non-performing assets (NPAs) overhang.

The Financial Stability Board, an international organisation monitoring and making recommendations on the global financial system has deemed lending by NBFCs as “shadow banking” globally. These specialised intermediaries enjoy the benefit of lower transaction costs, financial innovations and regulatory arbitrage. NBFCs play a critical role in emerging market economies by undertaking the following activities: - Reaching out with their services to inaccessible areas - They are substitutes to banks when the banks face strict regulatory constraints - Convenience in transactions on the back of quicker decision making ability, prompt provision and expertise in niche segments

Review of literature

Shollapur M.R in his article in ‘The Indian Journal of Commerce’ has reviewed concept of NBFCs. The NBFCs constituted a significant part of financial system and compliment the service provide by commercial bank in India. The efficiency of financial services and flexibilities helped them build a large body of client including small borrower and bigger corporate establishment. The pace of financial liberalization has an intensified the competition. As a result, there has been a shift towards strategic perspective marketing process of NBFCs. This perspective enable them to predict the future impact of change and help to move out of week area and grab new opportunity through continuous monitoring system.

R.M Srivastava & Divya Nigam in their book Management of Indian Financial Institution highlighted that background material for economic growth and financial institution, types of financial institution, recent trend Indian financial market. They put emphasis on the fact that the money market has passed through a phase of substantial adjustment and advancement in recent year.

K.C Shekhar & Lakshmy Shekhar in his book has explained role of indian NBFCs in India has shown rapid development especially in 1990 owing to their high degree of orientation towards consumers and implication of section requirement. The role of NBFCs as effective financial intermediaries arise has been well recognized as they have inherent abilities to take quicker decision, assume risk and customize their services provided by bank and market the components on a conceptual basis.

L M Bhole in his book define the NBFCs perform a diversified range of function and other various financial services to individual, corporate and institutional client. It also play positive role in accessing certain depositor segment and clearing credit requirement of borrowers. It also discusses the major financial market in India. Along with related financial instrument and services i.e. call money, call loan, other short term interest rate instrument and the recent development in money market.

Shashi K. Gupta, Nisha Gupta & Neeti Gupta: in his book define money market is an opportunity for balancing the short term surplus fund of the investor with the short term requirement to borrowers. Another feature of money market is that they are liquid with varying degree. It also define NBFCs play an important role in financial intermediaries because they can take quick decision making assume greater risks and design their product to the need of customer.

OBJECTIVES OF THE STUDY

The main objective of this study is-

1. To examine the growth of NBFCs in India from 2013-18

- Source of financing
- Credit disbursement
- Profitability indicators

RESEARCH METHODOLOGY

Research methodology requires gathering relevant data through journals, newspapers, books, magazines and internet. Also interpret of collected material. The bulletin from RBI, are gathered in order to access the problem related to NBFC.

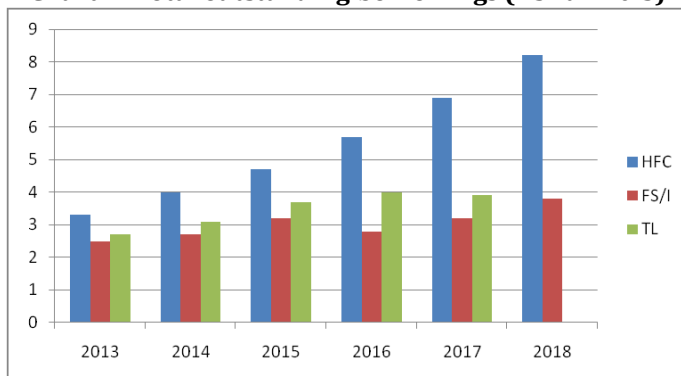
EVOLUTION, GROWTH AND DEVELOPMENT OF NBFCs IN INDIA

Till recently NBFCs and Unincorporated Bodies have been competing and complementing the services of commercial banks all over the world. While, the financial system in a country generally develops through a process of gradual evolution, it has been observed that here is a stage in the evolutionary process wherein the growth of NBFCs is more pronounced than other components of the financial system. Further, they take different forms and sizes depending upon the needs of their clientele. Thus, in the United States of America, the growth of NBFCs was more pronounced during the first three decades of twentieth century and two of the top five commercial lenders are NBFCs and three of the four top providers of consortium finance are non-bank firms at present. In India such marked growth in the non-bank financial sector was noticed in the last three decades. The NBFCs, as a group, have succeeded in broadening the range of financial services rendered to the public during this period. The evolution, growth and proliferation of financial intermediaries are essentially the reflection of the different forms of savings (resource) flows and different types of investment (uses) of such funds – whether for current working capital needs or for capital investments and as between different sectors of the economy. They serve different clientele in their role both as repositories of the community’s savings and as purveyors of funds for investment needs. The nineteenth and early 20th Centuries witnessed rapid urbanization, both in Europe and America. The growth of cities created a tremendous need for mortgage finance. To fill this need, various private groups began to organize building and loan associations (called building societies in England and Canada). However, instalment credit in the USA took off with the beginning of the mass marketing of automobiles around 1915. Automobile companies set up specialized subsidiaries called finance companies to provide instalment credit to car buyers and to finance the inventories of dealers and suppliers. The automobile companies were soon followed by retailers and manufacturers of consumer and producer durables. The idea spread from the United States to many other countries. Raymond W. Goldsmith traces the existence of ‘Chit Funds’ and ‘nidhis’ in India before World War I, that such institutions were more common in Western and Southern India. According to Goldsmith, “Whatever the fragmentary material exists points to the small size of these institutions, which seems to have originated in the mid-nineteenth century, and indicates fairly clearly a rapid decline in their size and importance relative to that of financial institutions of the western type, which developed in India during the 19th century.” Banking Commission (1972) has noticed the rapid progress made by “Finance Corporation” in states like Gujarat and Mysore, (present Karnataka State). These ‘finance corporations’ are petty finance outlets formed under the Partnership Act of India and their capital was always less than Rs.1 lakh. However, literature on non-banking financial sector reveals that the major NBFCs in India are concentrated in six states – West Bengal, Maharashtra, Tamilnadu, Uttar Pradesh, Karnataka and Delhi.

Sources of Financing

This section examines the salient indicators of NBFCs with regard to the borrowings and their key ratios which help to understand the growth in the financing activity. Chart 1 exhibits the total outstanding borrowings (long term borrowings, short term borrowings and current maturity of long term borrowings) of the sample NBFCs under study. The total outstanding borrowings of all three categories are Rs. 16.5 lakh crs in FY18 having increased from Rs. 8.5 lakh crs in FY13

Chart 1: Total outstanding borrowings (Rs. lakh crs)



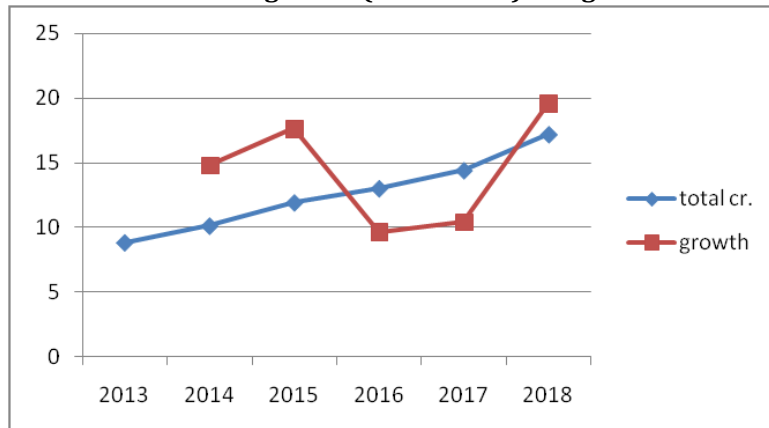
Source: CARE rating

Out of the total borrowings, the highest contribution to the tune of 49.4% is of the Housing Finance Companies (HFC) segment. The reliance on higher borrowings and a CAGR of 19.7% during FY13-FY18 is on the back of a commensurate increase in the credit extended by HFCs. - The borrowings of HFCs have witnessed a sustained double-digit growth on an average of 20.0% during the previous five years. - The share of HFC's borrowings in total borrowing portfolio has increased from 38.8% in FY13 to 49.4% in FY18. Despite the growth in outstanding borrowings in each category, the share of financial services/investment companies (FS-I) and term lending institutions (TL) segments' borrowings in overall NBFC sector borrowing has witnessed a decline over the years under study compared with the share of HFCs. The share of borrowings for the FS-I segment declined from 29.5% in FY13 to a low of 22.9% in FY17, following which it again gained reaching 23.1% in FY18. The share of borrowings for TL segment has witnessed increase during FY13-FY16 to scale 31.9% after which it declined by almost 4% in FY17 and subsequently declined in FY18 to stand at 27.3%. The CAGR growth of borrowings in case of FS-I and TLs is at 8.6% and 11% respectively during FY13 - FY18.

Credit Disbursement

This section deals with the asset side of the balance sheet focusing on the credit granted by the NBFCs to the varied sectors to fund their requirements. The NBFC sector has traditionally funded both the industrial and the retail segments. The RBI study states that while industry has received about 2/3rd of the total credit by these companies, there has been a significant jump in the share of retail credit from 3.4% in FY15 to 17.7% in FY17. Chart 2 shows that total credit disbursed by these sample companies under study and the growth in the total credit across the time period.

Chart 2- Total outstanding credit (Rs. lakh crs) and growth in credit (%)

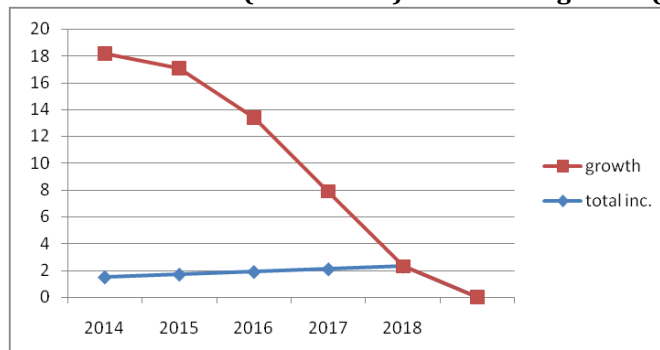


Source: CARE rating

Profitability indicators

This section covers few profitability indicators of the NBFC sector as a whole which will give an understanding of the performance of this sector during FY13 to FY18. Chart summarise the total income during the last 5 years and the growth in the income during this period. It is observed that, barring FY16, the total income under study has witnessed rapid and double digit growth in income. The total income of these companies has grown at CAGR(compound annual growth rate) of 12.2% during FY13 to FY18.

Chart 2 Total income (Rs. lakh crs) and income growth (%)

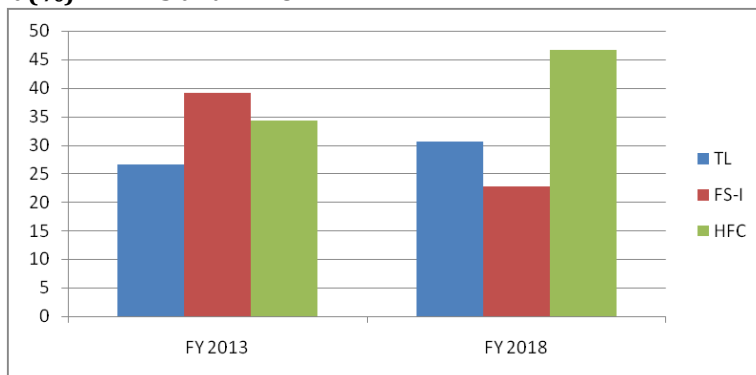


Source CARE rating

Recent RBI frameworks for NBFCs

To address the liquidity crunch faced by some segments of the NBFC sector, primarily on account of asset liability mismatches, the RBI has come up with regulatory relaxations to ease the challenges of the sector. – Banks are permitted to raise their exposure to a single NBFC (non-infrastructure financing NBFC) from 10% to 15% until the end of the year. - Till Dec 31, 2018, the government securities equivalent to the incremental credit disbursed by the banks to NBFCs after October 19 will be eligible for Liquidity Coverage Ratio (LCR) requirements. This is in addition to the 13% carve out from Statutory Liquidity Ratio (SLR) norms permitted for use against LCR requirements. - To provide partial credit enhancement (PCE) to bonds issued by systematically important non-deposit taking financial companies (NBFCs) registered with RBI and HFCs registered with National Housing Bank.

Share of total credit (%) in FY13 and FY18



Source: care ratings

Chart exhibits the share of Credit of each of the three categories of NBFCs and juxtaposes with the share of credit (outstanding loans and advances) for FY13 and FY18. The credit share covered in the following chart is the quantum of the outstanding credit of the NBFCs as at the end of the year. The objective of the following chart is to find out which category of the NBFC sector has the highest share total credit and how has it changed between FY13 and FY18.

CONCLUSION

- The total outstanding borrowings of the NBFC sectors under study, which is the primary source of funding has increased at a CAGR of 14.1% during FY13-FY18 which has been at a commensurate pace with the CAGR of 14.4% in the overall credit during the same time period.
- The overall NBFC sector credit growth has been significantly faster in FY18 than the bank credit growth

NBFCs in India have become prominent in a wide range of activities like hire purchase finance, equipment lease finance, loans, and investments. NBFCs have greater reach and flexibility in tapping resources. In desperate times, NBFCs could survive owing to their aggressive character and customised services. NBFCs are doing more fee-based business than fund-based. They are focussing now on retail sector-housing finance, personal loans and marketing of insurance. The strong NBFCs have successfully emerged as 'financial institutions' in a short span of time and are in the process of converting themselves into 'financial supermarket' – a one-stop financial shop. The growth trend of NBFCs in India is still catching momentum. Their role in the economy cannot be neglected and RBI should also make certain policies which should help them to flourish along with care for its investors.

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