FIDC NEWS

Finance Industry Development Council

(A Representative Body of Assets and Loan Financing NBFCs)

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COVID LEARNINGS FOR SMALL AND MEDIUM NBFCs

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It is a facile statement to make that the Covid-19 related developments are a black swan event. It has been argued that this is perhaps even worse than the Great Depression of 1929-33 and surely much worse than the 2008 global financial crisis. There is nothing anyone can do about this except to protect oneself and one's business from the ill-effects of the pandemic. The purpose of this write-up is to list down some of the learnings that could benefit NBFCs – especially the small and medium ones.

First, the only ally of an NBFC is the fundamental strength of its business. Businesses that are built on solid fundamentals are more likely to survive – strong ALM, focus on portfolio quality, strength of the collection team would be the deciding factors and not the rate of growth of the book or profits. Conservative business practices would be the best weapon to fight external crises such as the pandemic.

Second, NBFC business is not just an asset-side business, but is very much a liabilities-side business. The bigger issue facing NBFCs today is not asset quality but raising liabilities. With increasing risk aversion on the part of the banks to lend to NBFCs and drying up of money markets, managing liabilities has assumed much greater importance. Let us not forget that an NBFC can possibly survive with a sudden burst of NPAs, but even a small cash flow mismatch can lead to default, rating downgrades and death of the NBFC.

Third, size matters. Even in these times of crises, larger NBFCs have managed to withstand adversities than small entities. Gone are the days when an NBFC could just concentrate on a micro-market and one segment and stay small. Larger the entity, greater is its ability to sustain and grow even in adversity. Perhaps the time has come for NBFC promoters to look at dilution of control and faster growth in the interest of sustainability of business.

Fourth, there is no substitute to high standards of governance. If we see the recent failures in the banking and NBFC space, the failed entities met their fate not due to scale or size or wrong business model etc., but due to poor governance standards. Yes, high governance standard comes at a price, but it is perhaps better to pay that price than suffer business collapse.

So what can NBFCs – especially smaller ones do?

First, to put governance standards in place for a much larger scale of business – in terms of getting good external directors on board, getting knowledgeable consultants to reshape business and making compliance with regulations as a top priority. This will surely bring the profit down in the short run, but will boost respectability and therefore business prospects in the longer run.

Second, keep at least 45-60 days of cash flow needs as liquid securities. This should be seen as an insurance policy against defaulting on any liability repayment obligation. Existence of this would also give a lot of comfort to lenders for them to consider any fresh loan application from the NBFC.

Third, be open to merger/consolidation/external equity infusion if that can help in diversification of risk or quicker growth and sustainability of business. It may be worth remembering that 25% of a Rs. 1000 cr business is greater than 100% of a Rs 100 cr business!

Fourth, there is no short-cut to a long, hard route to a successful business. Conservative lending practices, constant effort to get higher credit ratings, strong focus on governance etc. do not come easy, but there is really no choice. Sticking to fundamental principles is easier said than done, but could be the difference between the business that just survives and the business that makes a mark.

The IL&FS and the Covid events have the potential to separate the men from the boys and it's our choice to belong to either camp.

- K V Srinivasan

MESSAGE FROM CHAIRMAN FIDC MR. RAMESH IYER

As the Unlocking has slowly commenced, we need to interact and discuss not only on these problems, but also the Business opportunities and prospects and newer ways of getting funds, fighting liquidity constraints and Rating downgrades, Eligibility criteria for various GOI schemes, Collections, Recovery, New loans disbursements, demand pickup, economy, staff salary and welfare, work from home, migration and the special technological upgrades required under the "new normal".

RBI should consider infusing liquidity into NBFCs

SS Mundra, former Deputy Governor of the RBI said that the central bank should consider infusing liquidity into NBFCs as they have become cash-starved in the wake of the Covid-19 pandemic.

"I am baffled as to why the RBI has been so reluctant to the NBFC sector. We should be conscious that the sector is very important, particularly to MSMEs. They can look at infusing liquidity in the sector." He also felt that the central bank should not hesitate in extending greater regulatory forbearance if a need arises. [Business Line, Sept.15]

AT A GLANCE

EDITORIAL COMMITTEE

REGULATORY PERIMETER

RBI NOTIFICATIONS & CIRCULARS :

Assignment of Risk Weights on Credit Facilities (Guaranteed Emergency Credit Line) under the Emergency Credit Line Guarantee Scheme: RBI/2019-2020/255; DoR. BP. BC. No. 76/ 21. 06. 201/2019-20; 21.6.2020; Department of Regulation.[All Member Lending Institutions (All Scheduled Commercial Banks including Scheduled RRBs) (NBFCs including HFCs eligible under the captioned scheme) All India Financial Institutions - SIDBI, NHB, NABARD and Exim Bank)]

Loans Sourced by Banks and NBFCs over Digital Lending Platforms: Adherence to Fair Practices Code and Outsourcing Guidelines: RBI/2019-2020/258; DOR (NBFC) (PD) CC. No.112/03.10.001/2019-20; 24.6.2020; Department of Regulation.[All Scheduled Commercial Banks (excluding RRBs) All NBFCs (including HFCs)]

Special liquidity scheme for NBFCs/HFCs: RBI/2020-2021/01; DoR (NBFC) (PD) CC.No. 113/03.10.001/2020-21 0; 1.7.2020; Department of Regulation. [All NBFCs/HFCs]

Credit flow to Micro, Small and Medium Enterprises Sector: RBI/2020-2021/10; FIDD.MSME & NFS.BC.No.3/06.02.31/2020-21; 02.7.2020. [The Chairman/ Managing Director/Chief Executive Officer All Commercial Banks (including Small Finance Banks, Local Area Banks and Regional Rural Banks) All Primary (Urban) Co-operative Banks/State Co-operative Banks / District Central Co-operative Banks All-India Financial Institutions All NBFCs]

Extension of timeline for finalization of audited accounts: RBI/2020-2021/11; DoR (NBFC) (PD) CC. No.114/03.10.001/2020-21; 06.7.2020; Department of Regulation. [All NBFCs]

Exemption from Registration as NBFC – Alternative Investment Fund (AIF): RBI/2020-2021/12; DOR (NBFC). CC. PD. No. 115/ 03. 10.001/2020-21; 10.7.2020; Department of Regulation. [All NBFCs]

Implementation of Section 51A of UAPA, 1967 - Updates to UNSC's 1267/ 1989 ISIL (Da'esh) & Al-Qaida Sanctions List - Addition of one individual: RBI/2020-2021/14; DOR.AML.BC.No.2/14.06.001/2020-21; 18.7.2020; Department of Regulation. [The Chairpersons/ CEOs of all the Regulated Entities]

Implementation of Indian Accounting Standards: RBI/2020-2021/15; DOR(NBFC).CC.PD.No.116/22.10.106/2020-21;24.7.2020; Department of Regulation.[NBFCs and Asset Reconstruction Companies implementing Indian Accounting Standards]

Exemption from Registration as NBFC – Alternative Investment Fund (AIF): RBI/2020-21/12 DOR (NBFC). CC. PD. No. 115/ 03. 10. 001/2020-21; July 10, 2020; [All NBFCs]

Resolution Framework for COVID-19-related Stress: RBI/2020-21/16; DOR.No.BP.BC/3/21.04.048/2020-21; August 6, 2020**.** [All Commercial Banks (including Small Finance Banks, Local Area Banks and Regional Rural Banks); All Primary (Urban) Co-operative Banks/State Co-operative Banks/ District Central Co-operative Banks; All All-India Financial Institutions; All NBFCs (including HFCs]

Offline Retail Payments using Cards / Wallets / Mobile Devices – Pilot: RBI/2020-2021/22; DPSS.CO.PD.No.115/02.14.003/2020-21; 06.8.2020; Department of Payment and Settlement Systems. [The Chairman / Managing Director / Chief Executive Officer Authorised Payment System Operators (Banks and Non-banks)]

Online Dispute Resolution (ODR) System for Digital Payments: RBI/2020-2021/21; DPSS.CO.PD No.116/02.12.004/2020-21; 06.8.2020; Department of Payment and Settlement Systems. [The Chairman / Managing Director / Chief Executive Officer Authorised Payment System Operators and Participants (Banks and Non-banks)]

Opening of Current Accounts by Banks - Need for Discipline: RBI/2020-2021/20; DOR.No.BP.BC/7/21.04.048/2020-21; 06.8.2020; Department of Regulation. [All Scheduled Commercial Banks, All Payments Banks]

Micro, Small and Medium Enterprises (MSME) sector – Restructuring of Advances: RBI/2020-2021/17; DOR.No.BP.BC/4/21.04.048/2020-21; 06.8.2020; Department of Regulation. [All Commercial Banks (including Small Finance Banks, Local Area Banks and Regional Rural Banks) All Primary (Urban) Co-operative Banks/State Co-operative Banks/ District Central Co-operative Banks All All-India Financial Institutions, All NBFCs]

Resolution Framework for COVID-19-related Stress: RBI/2020-2021/16; DOR.No.BP.BC/3/21.04.048/2020-21; 06.8.2020; Department of Regulation.[All Commercial Banks (including Small Finance Banks, Local Area Banks and Regional Rural Banks) All Primary (Urban) Co-operative Banks/State Co-operative Banks/ District Central Co-operative Banks All All-India Financial Institutions All NBFCs (including HFCs)]

Review of Guidelines for Core Investment Companies: RBI/2020-2021/24; DoR (NBFC) (PD) CC. No. 117/ 03. 10. 001/ 2020-21; 13.8.2020; Department of Regulation; [All Core Investment Companies (CICs)]

New Definition of Micro, Small and Medium Enterprises – clarifications: RBI/2020-2021/26; FIDD.MSME & NFS. BC. No. 4/ 06.02.31/2020-21; 21.8.2020; Financial Inclusion and Development Department; [The Chairman/Managing Director/Chief Executive Officer All Commercial Banks (including Small Finance Banks, Local Area Banks and Regional Rural Banks) All Primary (Urban) Co-operative Banks/State Co-operative Banks / District Central Co-operative Banks All-India Financial Institutions, All NBFCs]

Implementation of Section 51A of UAPA, 1967: Updates to UNSC's Democratic Republic of Congo List: RBI/2020-2021/25; DOR.AML.BC.No.8/14.06.001/2020-21; 21.8.2020; Department of Regulation; [The Chairpersons/ CEOs of all the Regulated Entities]

Master Directions – Priority Sector Lending (PSL) – Targets and Classification: RBI/FIDD/2020-21/72; Master Directions FIDD. CO.Plan.BC.5/04.09.01/2020-21: Sept. 04, 2020 [All Commercial Banks including Regional Rural Banks, Small Finance Banks, Local Area Banks and Primary (Urban) Co-operative Banks other than Salary Earners' Banks]

Resolution Framework for COVID-19-related Stress – Financial Parameters: RBI/2020-21/34**;** DOR. No. BP. BC/ 13/ 21. 04. 048/ 2020-21 Sept. 7, 2020[All Commercial Banks (including Small Finance Banks, Local Area Banks and Regional Rural Banks); All Primary (Urban) Co-operative Banks/State Co-operative Banks/District Central Co-operative Banks; All All-India Financial Institutions; All NBFCs (including HFCs]

Implementation of Section 51A of UAPA, 1967 - Updates to UNSC's 1267/1989 ISIL (Da'esh) & Al-Qaida Sanctions List - Amendment to 11 entries (10 Individuals and one entry in Entities and Groups): RBI/2020-2021/36; DOR. AML. BC. No. 14/ 14.06.001/2020-21; 11.9.2020; Department of Regulation. [The Chairpersons/CEOs of all the Regulated Entities]

Reserve Bank's agenda for NBFCs/HFCs in respect of Regulation, Supervision and Enforcement for 2020-21

RBI in its Annual Report for the year 2019-20 released on Aug. 25 has listed the Agenda in respect of Regulations, Supervision and Enforcement for F Y 2020-21 in its chapter 3 titled Regulation of Financial Intermediaries. It covers the Agenda for NBFCs and HFCs in respect of RBI's Department of Regulation (DoR). RBI states "A unified DoS has been operationalised in which the supervision of banks, UCBs and NBFCs are undertaken in a holistic manner under one umbrella Department." Report further adds,' A number of measures were taken to sharpen the intensity of on-site examinations while developing a proactive off-site surveillance framework for the SEs taken together.'

The Enforcement Department (EFD) was set up in April 2017 to enforce regulations uniformly across banks. Enforcement in respect of cooperative banks and NBFCs was also brought under the scope of operations of the Department with effect from October

3, 2018. The RBI report lays down goals for year 2020-21. [Source: RBI Annual Report 2019-2020]

RBI announces special liquidity facility of Rs 10,000 cr for Nabard, NHB

The Reserve Bank on Aug. 6 announced an additional special liquidity facility (ASLF) of Rs 10,000 crore equally split between Nabard and the NHB to help small financiers and home loan companies amid COVID-19 difficulties. The liquidity facility will be offered at the policy repo rate, RBI Governor Shaktikanta Das said. Das said ASLF of Rs 5,000 crore will be given to the NHB to "shield the housing sector from liquidity disruptions and augment the flow of finance to the sector through HFCs". Similarly, Rs 5,000 crore will be given to Nabard to "ameliorate the stress being faced by smaller NBFCs and micro-finance institutions in obtaining access to liquidity". [Financial Express/PTI, Aug. 6]

Banks, NBFCs must adhere to fair practices code before outsourcing to digital lending platforms: RBI

With the emergence of various digital platforms in the financial sector claiming to offer hassle free loans, banks and NBFCs are also seen engaging digital platforms to provide loans to their customers. Hence, the RBI in a notification said, "Financial lenders must note that outsourcing of any activity by banks/ NBFCs does not diminish their obligations, as the onus of compliance with regulatory instructions rests solely with them." Banks and NBFCs must follow the instructions laid down by Regulator before engaging digital lending platforms as their agents to source borrowers and/ or to recover dues.

RBI added that violation of these instructions can be viewed serious. "Any violation in this regard by banks and NBFCs (including NBFCs registered to operate on 'digital-only' or on digital and brick-mortar channels of delivery of credit) will be viewed seriously," the regulator added. [ET BFSI, June 30]

RBI Releases Revised Priority Sector Lending Guidelines

RBI's revised Priority Sector Lending [PSL] guidelines will enable better credit penetration to credit deficient areas; increase the lending to small and marginal farmers and weaker sections; boost credit to renewable energy, and health infrastructure. Bank finance to start-ups (up to Rs.50 crore); loans to farmers for installation of solar power plants for solarisation of grid connected agriculture pumps and loans for setting up Compressed Bio Gas (CBG) plants have been included as fresh categories eligible for finance under priority sector. Some of the salient features of revised PSL guidelines are:

To address regional disparities in the flow of priority sector credit, higher weightage have been assigned to incremental priority sector credit in 'identified districts' where priority sector credit flow is comparatively low.

The targets prescribed for "small and marginal farmers" and "weaker sections" are being increased in a phased manner. Higher credit limit has been specified for Farmers Producers Organisations (FPOs)/Farmers Producers Companies (FPCs) undertaking farming with assured marketing of their produce at a pre-determined price. Loan limits for renewable energy have been doubled. For improvement of health infrastructure, credit limit for health infrastructure (including those under 'Ayushman Bharat') has been doubled. [RBI Press release, Sept. 4]

Loan moratorium may have substantial impact on private NBFCs, HFCs: RBI

The loan moratorium could have a significant impact on private NBFCs and HFCs, the RBI has noted in its Financial Stability Report. "The impact of the moratorium on private NBFCs and HFCs can be substantial, with proportion of assets under the moratorium for NBFCs averaged between 39 per cent and 65 per cent based on underlying assets, with approximately 50 per cent of the aggregate assets under moratorium as on April-end," the RBI report released on Friday noted.

Based on the disclosures made by NBFCs and HFCs, the assets under moratorium are dominated by wholesale customers and real-estate developers, although retail portfolios in the micro-loans and auto loan segments have also been affected, the report further said, adding that access of NBFCs and HFCs to capital markets, both debt and equity, is of significant importance to the sector. The RBI also noted that the declining share of market funding for NBFCs is a concern as it has the potential to accentuate liquidity risk for them as well as for the financial system.

"Smaller, mid-sized and AA or lower rated, unrated NBFCs have been shunned by both banks and markets, accentuating the liquidity tensions faced by NBFCs, which was also reflected in the lacklustre response to the Targeted Long-Term Repo Operations 2.0 (TLTRO 2.0)," it said.

System-level stress tests for the NBFC sector's aggregate credit risk for the quarter ending December 2019 were carried out under three scenarios: increase in GNPA by 1 SD, 2 SD and 3 SD, the report further said. It is assessed that the sector's CRAR would decline from 19.4 per cent to 17.2 per cent in the first scenario, to 16.4 per cent in the second scenario, and to 15.2 per cent in the third scenario. [Business Line, July 24]

Resolution Framework for COVID-19-related Stress announced by RBI on Aug.6

The RBI on Aug. 6 permitted a one-time loan restructuring of stressed accounts, conceding a longstanding demand of lenders and the industry. Lenders will get a special window to recast stressed retail and corporate loans without classifying them as non-performing, provided they set aside 10% provisions on such loans.

"The economic fallout on account of the covid-19 pandemic has led to significant financial stress for a number of borrowers across the board. The resultant stress can potentially impact the long-term viability of a large number of firms, otherwise having a good track record under the existing promoters, due to their debt burden becoming disproportionate, relative to their cash flow generation abilities," it said.

Lenders are allowed to extend the tenure of the loan by up to two years, apart from sanctioning additional loans and a repayment moratorium to tide over the crisis. RBI has also extended the deadline for a one-time recast of small business loans by three months to 31 March 2021, provided they were standard as on 1 March.

To avail of the window, RBI said corporate loan accounts should have been standard and not in default for more than 30 days as on 1 March. It added that the accounts should continue to remain standard till the date of invocation or the date on which both the borrower and lenders agree to proceed with a resolution plan.

"The resolution plan may be invoked anytime till 31 December, 2020 and shall have to be implemented within 180 days from the date of invocation," it said. According to RBI, post-implementation, asset classification of an account will be retained as standard, or if the account had slipped into NPA after invocation but before implementation, the asset classification will be restored.

Meanwhile, it will form an expert committee under the chairmanship of KV Kamath, to make recommendations to the RBI on the required financial parameters, along with the sector specific benchmark for this window. [Live Mint, Aug 6]

RBI advised all banks, NBFCs to assess the impact of covid-19 on their balance sheet, asset quality, liquidity, profitability and capital adequacy

RBI Governor Das said the pandemic will result in higher non-performing assets and capital erosion of banks, and stressed on the need to raise capital by both banks and NBFCs. "The economic impact of the pandemic - due to lock-down and anticipated post lock-down compression in economic growth - may result in higher non-performing assets and capital erosion of banks. A recapitalisation plan for PSBs and private banks (PVBs) has, therefore, become necessary. While the NBFC sector as a whole may still look resilient, the redemption pressure on NBFCs and mutual funds need close monitoring," he said.

As such the central bank, Das said, has advised all banks, NBFCs to assess the impact of covid-19 on their balance sheet, asset quality, liquidity, profitability and capital adequacy for the current fiscal.

"Based on the outcome of such stress testing, banks and NBFCs have been advised to work out possible mitigating measures including capital planning, capital raising, and contingency liquidity planning, among others." [Live Mint, July 11]

RBI sets 5 key norms for lenders based on Kamath panel recommendations: Rejig of Covid-hit loans

RBI has specified five key financial parameters that lenders must consider before finalising resolution plans (RP) for eligible borrowers in 26 sectors, ranging from auto to trading, to mitigate the impact of Covid-related stress. The financial parameters relating to leverage, liquidity and debt serviceability are based on the recommendations of the Expert Committee, headed by KV Kamath, on a 'Resolution Framework for Covid-related stress'.

The five financial parameters are:

• Total Outside Liabilities (TOL)/Adjusted Tangible Net Worth (ATNW); • Total Debt/EBITDA; • Current Ratio; • Debt Service Coverage Ratio (DSCR); and • Average DSCR.

Besides auto and trading, the major sectors for which the parameters (ceilings or floors, as the case may be) have been prescribed include aviation, construction, consumer durables/FMCG, corporate retail outlets, gems and jewellery, hotel, restaurants, tourism, power, and real estate.

Under the RBI's framework, only borrowers classified as standard and with arrears of less than 30 days as on March 1, 2020 are eligible for resolution.

Other sectors: Where sector-specific thresholds have not been specified, lending institutions shall make their own internal assessments regarding TOL/ATNW; and Total Debt/EBITDA.

However, the current ratio and the DSCR in all cases shall be 1.0 and above, and ADSCR shall be 1.2 and above.

The central bank said lending institutions are free to consider other financial parameters as well while finalising the resolution plan apart from the mandatory five key ratios and the sector-specific thresholds prescribed.

Graded approach: Given the varying impact of the pandemic on sectors/entities, the RBI said the lending institutions may, at their discretion, adopt a graded approach depending on the severity of the impact on the borrowers, while preparing or implementing the resolution plan. Such an approach may also entail classification of the impact on the borrowers into mild, moderate or severe, as recommended by the Committee. [Business Line, Sept. 7]

RBI releases framework for retail payments systems invites applications

The RBI on Aug. 18 unveiled the framework for setting up umbrella entities for operating pan-India retail payments systems and invited applications [in prescribed form A] from eligible companies by February 26, 2021. As per the framework, the companies with a net worth of over Rs. 500 crore will be eligible to set up an umbrella entity which among other things will be permitted to set up, manage and operate new payment systems in the retail space comprising ATMs, White Label PoS, Aadhaar-based payments and remittance services, said RBI press release.

Among other things, the umbrella entity will be permitted to operate clearing and settlement systems for banks and non-banks; identify and manage relevant risks such as settlement, credit, liquidity and operational; and preserve the integrity of the system. It will also be expected to monitor retail payment system developments and related issues in the country and internationally to avoid shocks, frauds and contagions that may adversely affect the system and/or the economy in general, the RBI said. [Live Mint/PTI, 18 Aug.]

RBI response about RBI buying corporate bonds of NBFCs

With respect to a suggestion for the RBI buying corporate bonds, the governor said the law did not permit the same, at present. However, it is not just the question of law permitting or not. The RBI has provided liquidity support through long-term repo operations and its variants. [Business Standard, July 28]

Targeted Long-Term Repo Operations (TLTROs)

Reserve Bank to conduct auctions of targeted long-term repos of up to three years tenor of appropriate sizes for a total amount of up to Rs.1,00,000 crore at a floating rate linked to the policy repo rate. Liquidity availed by banks under TLTROs should be deployed in investment grade corporate bonds, commercial paper, and non-convertible debentures over and above the outstanding level of their investments in these bonds as on March 27, 2020. [RBI, Monetary Policy Report - April 2020, April 13] ■

[Continued from page-7]

The volatility of investment flows remains a risk for both stock and bond markets.

d. Reform agenda going forward

India lags many of its peers on financial development indicators such as financial sector depth and efficiency. While India's savings-to-Gross Domestic Product (GDP) ratio (30 percent) is in line with that of peers (e.g., Malaysia and Brazil), its credit-to-GDP ratio at 51 percent is much lower101. India has a very particular financial sector structure with numerous but overly fragmented institutions which depend heavily on domestic deposits for funding. The public sector footprint in the financial sector is notably higher than in other emerging markets, which results in high fiscal costs, contingent liabilities, and inefficiencies in credit allocation. To support the country's ambitious long-term growth goals, the large financing gaps in infrastructure (US$1.2 trillion through 2040) as well as in SME and housing finance will need to be closed, requiring stronger capabilities of the financial system.

The recent liquidity and performance issues in the sector, exacerbated by the COVID-19 crisis, present policymakers with a strong reason—and an opportunity—to accelerate efforts towards building a more efficient, stable, and market-oriented financial system.

1) Maintaining financial sector stability is a critical challenge in the light of increased risks.

2) Reforms in the NBFC sector are needed to support its role in channelling credit to the real sector. The government has recognized the important role of NBFCs in serving the needs of niche geographies and sectors and has recently launched several liquidity schemes for NBFCs as part of the COVID-19 economic recovery program. These temporary measures could be institutionalized through sustainable market instruments like a risk sharing facility, Residential Mortgage Backed Securities (RMBS), and a platform (housing) and credit enhancement company (infrastructure) to diversify the funding base and serve the liquidity needs of NBFCs, including smaller ones.* It would also be important to continue strengthening the risk-based regulation and oversight of NBFCs, with the focus on systemically important institutions. Further consolidation in the very fragmented sector should be encouraged through changes in NBFC regulations by the RBI. The funding model for small and medium NBFCs, which cannot access capital markets and depend on refinancing and sale of asset portfolios, leads to cherry picking of NBFC assets by banks, and is not a sustainable model.

3) Deeper capital markets are critical for increasing the availability of long-term finance, especially given the asset-liability mismatches in the banking sector.

4) The role of fintech in accelerating financial inclusion in India has been impressive, but the nexus between fintech and MSMEs has yet to be fully exploited. Fintech lenders have lower origination costs and turnaround time than traditional lenders and could help borrowers, especially MSMEs, restart business activities post lockdown. However, fintech lenders will need to improve their presence at ground level to effectively increase collections from smaller borrowers. Co-origination with banks could be a useful mechanism for fintech NBFCs to scale up lending, given the liquidity constraints they face. Further operationalization and improved coordination of various regulatory sandboxes would increase efficiency and innovation among fintech firms.

5) Last but not the least, it is encouraging that the government seems to be moving to a more selective and strategic public-sector footprint in the financial sector, as witnessed by the consolidation of PSBs and strengthening their corporate governance and oversight.

***The risk-sharing facility will allow NBFCs to diversify funding sources and involve funding, guarantees, etc. for NBFCs to lend to sectors such as MSMEs. The RMBS platform will help HFCs, especially smaller HFCs, to improve liquidity through securitization. The credit enhancement company (CEC) will support de-risking of debt issuances for infrastructure.**

[Abridged version of Chapter-5: India's financial sector: the impact of COVID-19 and the long term policy agenda from World Bank Report titled India Development Update- July 2020; Excerpts relating to NBFC sector] ■

INDIAN ECONOMY IS WITNESSING A V- SHAPED RECOVERY: FINANCE MINISTRY

US economy has contracted by 9.1 per cent, UK, France, Spain, Italy and Germany by 21.7 per cent, 18.9 per cent, 22.1 per cent, 17.7 per cent and 11.3 per cent respectively with the overall Euro area contracting by 15.0 per cent and Japan has contracted by 9.9 percent due to Covid-19. Relative to these advanced nations, India's GDP contraction at 23.9 per cent is slightly higher. The higher contraction has resulted from the stringent lockdown that India enforced in the April-June quarter.

Unlocking witnessing a sharp V-shaped Recovery in India

As countries unlocked in the quarter starting in July, recovery is underway globally. India, too, is witnessing a sharp V-shaped recovery. India's manufacturing purchasing managers' index (PMI), at 52.2, has moved into expansionary zone in August for the first time since the lockdown, presenting much required recovery prospects for the manufacturing sector. The V-shaped pattern of recovery is seen in the following high-frequency indicators: auto sales, tractor sales, fertilizer sales, railway freight traffic, steel consumption and production, cement production, power consumption, e-way bills, GST revenue collection, daily toll collections on highways, retail financial transactions, manufacturing PMI, performance of core industries, capital inflows and exports.

Agriculture is the brightest spot in the revival of growth

Since May, agriculture has persistently been the brightest spot in the revival of growth. Industrial production is showing definite signs of recovery with year-on-year (YoY) growth in eight core industries output showing a smaller contraction in July than in June. Consumption is picking up with passenger vehicle sales rising to their highest level at 1.83 lakh in July as compared to 1.43 lakh in March. Some revival in rural demand is also seen in growing sales of small cars, two-wheelers and sports utility vehicles and fertilizers. Increase in registrations for commercial and agricultural tractors from 52,362 in March to 66,061 in August is further indicative of strengthening rural demand.

Widespread Growth in Economic Activities

Growth in activity since the April-June quarter is further evident in the railway freight traffic of 95.2 million tonnes in July, closing on to its previous year level of 99.7 million tonnes. In the first twenty-days of August, railway freight volume at 60.38 million tonnes has now crossed its previous year level of 56.60 million tonnes. Also creeping up as India unlocks are railway passenger bookings from -7.92 million in April (cancellation of bookings) to 14.62 million in July and domestic aviation passengers from 2.8 lakh in May to 21.1 lakh in July. Steel production at 74.02 lakh tonnes and cement production at 242.47 lakh tonnes in July, as compared to 86.13 lakh tonnes and 280.2 lakh tonnes respectively in the corresponding month of the previous year suggest revival of construction activity.

Indications of early resumption of economic normalcy

Power consumption is quickly reverting to the last year's baseline, reaching 97 per cent of corresponding previous year levels and crossing pre-COVID (February) levels in August, 2020. Sustained impetus in E-way bills generated is reflected in their value at Rs. 13.8 lakh crore in August, reaching 97.2 per cent of corresponding month of the previous year. E-way bills are a strong and leading indicator of revenue collections, supply chain corrections and logistics growth, and thus their significant growth augurs well for early resumption of economic normalcy.

External Sector buoyancy

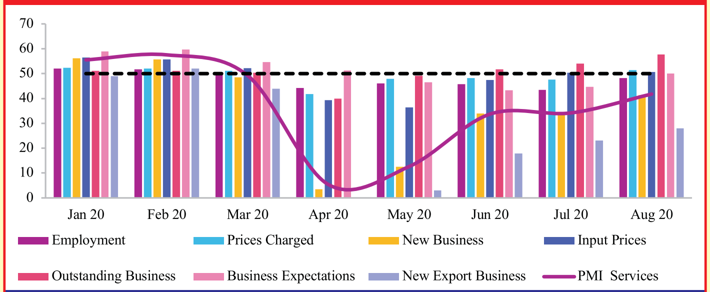
On the back of robust FDI and FPI inflows and savings from tepid imports, forex reserves, as on August 21, have risen to an all-time high of USD 537.5 billion. These are capable of financing more than 13 months of imports, should the need arise from a surge in real sector activity. India's external sector remains resilient. Merchandise exports witnessed broad-based rebound in the last three months, inching closer to pre-Covid levels in July. Exports were recovering faster than imports.

Retail & UPI payment transactions rebounded sharply

Retail payment transactions via NPCI platforms rebounded sharply in June and July, after the dip during the lockdown months of April and May, signaling a larger shift towards online payments amid the pandemic. UPI payment transactions hit an all-time high of Rs. 2.9 lakh crore in value and 149 crore in volume terms in July.

PMI services index marginally improved in August to 41.8 over 34.2 in July though still in contractionary zone. Movement of other high frequency indicators of services sector activity also suggest modest resumption of economic activity. (Chart-1)

Chart-1 PMI Services Performance



Source: IHS Markit

Upbeat corporate bond market, credit spreads narrow down

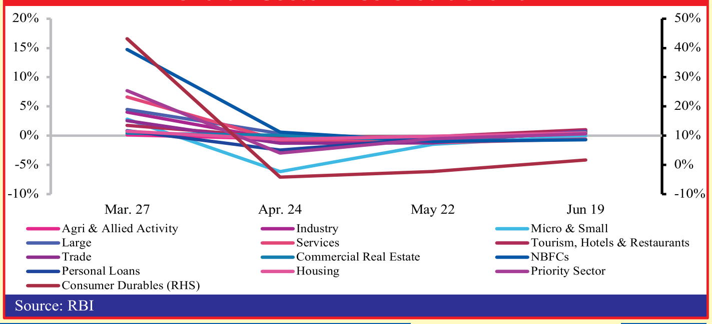
Borrowings costs on corporate bonds have significantly eased to fifteen year lows after record global and domestic stimulus measures to mitigate COVID-19's financial fallout. Renewed interest has emerged in this market with 91 maiden corporate bond issuers so far this year. These developments bode well for deepening of the corporate bond market and providing more choices for investors. At the same time, this optimism is also driven by the current liquidity flush into emerging bond markets. With illiquidity premia dissipating under the impact of Operation Twist and TLTRO 1.0, spreads of 3-year AAA-rated corporate bonds over similar tenor government securities have also declined from 246 basis points at end-April to 55 basis points in end-August.

While overall credit growth continues to remain muted, credit for agriculture, large industry and Micro & Small Enterprises (MSE) improve, services credit growth robust

Credit off-take from banks was muted during FY 2019-20, growing at 6.1 per cent y-o-y in a sharp loss of pace from 13.3 per cent a year ago. Bank credit growth continued to moderate in the first five months of this year at 5.5 per cent as on 14th August 2020 mirroring weak credit demand and increased risk aversion in the banking system. Further, regional lockdowns and the consequent slowing of economic cycle have added to weak credit off-take.

However, sector-wise credit has improved month-on-month in June compared to April and May, particularly for agriculture and allied-activities, large industries and MSEs. Credit to services sector continued to grow at a robust 10.7 per cent YoY in June inching closer to previous year levels with month-on-month recovery seen in real estate, NBFCs, trade and tourism. Personal loans and housing loans in particular, also picked up in June, auguring well for consumption sentiment. (Chart-2)

Chart-2 Sector wise Credit Growth



Source: RBI

Improving monetary policy transmission, increasing Commercial Paper (CP) issuances for NBFCs

Strong liquidity interventions via LAF route by RBI have enabled improved monetary policy transmission. Interest rates on instruments like the 3-month Treasury bill, CP and certificates of deposit have fully priced in the reduction in the policy rate and are, in fact, trading below it in the secondary market. Commercial paper issuances in FY 2020-21 are at an all-time high. Effective weighted average yield of CPs has decreased from 5.39 per cent in April to 3.99 per cent in July. Oil and gas and NBFC sector dominated the CP issuance market with more than 50 per cent share. Market financing conditions for NBFCs, which had become challenging, have largely stabilised in the wake of targeted policy measures (Chart-3). CPs yield of NBFCs has softened to reach 3.80 per cent as on July 31, 2020.

Chart-3 CPs raised by NBFC Sector in FY2021 (Rs. crore)

Month	Financial institutions	HFC	NBFC	MFI	Total
April	7275	4400	4275	-	15950
May	1000	6950	22033	-	29983
June	6000	5000	17963	5	28968
July	2650	1775	19406	10	23841
Aug	16925	18125	63677	15	98742

Source: CCIL

Policy matrix towards a calibrated reconstruction of the economy

The world after COVID-19 will be different with structural changes in production, consumption and work patterns. As India emerges from this crisis, it will be critical to re-orient the country's policy matrix towards a calibrated reconstruction of the economy and building resilience for an uncertain future. Some areas that may require specific attention include agrarian supply chains, factor markets, infrastructure, ICT, start-ups, financial inclusion, skilling and health care. Progress in these areas will sustainably boost economic growth in years to come:

- **Enhancing resilience of India's agriculture, building efficient and sustainable agrarian supply chains.**
- **Deepening structural reforms in factor market and boosting infrastructure to reignite manufacturing.**
- **Leveraging ICT and startups for reconstructing a resilient and innovative services sector.**
- **Strengthening an AtmaNirbhar's Bharat position in global value chains**
- **Harnessing digital finance to unleash the true potential of financial inclusion:**

The digital payment infrastructure created as part of JAM trinity has enabled a timely and targeted fiscal relief response to the pandemic. Going forward, wide-spread deployment of online and offline digital payment acceptance infrastructure, particularly in remote areas, is key to unleashing the true potential of financial inclusion in an increasingly digitized post-covid world. In a world witnessing a paradigm shift in consumer behavior, expanding the digital retail space may emerge as a critical nudge to gradually regain the pre-COVID-19 consumption momentum. [Extracts from Monthly Economic Report [Aug.], Department of Economic Affairs, Ministry of Finance, GoI, Released on Sept. 4.Sub-heading are added to facilitate readers]

SEBI MOVES

Hearty Congratulations

Ajay Tyagi

Will continue as Chairman, Securities and Exchange Board of India till Feb.28, 2022

Ease information disclosure norms for privately placed NCDs: FIDC

Finance companies have sought an amendment to the SEBI regulations, seeking easier disclosure requirements pertaining to the furnishing of audited financial figures of the last three years for private placement of debentures. At present, SEBI norms require the stand-alone financial information (such as P&L statement and balance sheet) for the last three years as well as auditor qualifications, from the issuer seeking to issue listed non-convertible debentures (NCDs).

FIDC, in a communication to the SEBI chairman, said: "We respectfully submit that the said regulations be amended for private placement of NCDs. These NCDs are directed towards sophisticated investors, who will be able to make a distinction between issuers based on intensive disclosures required for such issuances."

The listing regulations impose significant governance and disclosure requirements on entities seeking to issue listed NCDs. [Business Standard, Aug. 27]

SEBI amends insider trading norms; entities to maintain database on UPSI

SEBI has amended insider trading norms, wherein listed entities will have to maintain a structured digital database containing nature of unpublished price-sensitive information.

The amendments include providing for maintaining a structured digital database containing nature of unpublished price-sensitive information (UPSI), the names of persons who have shared the information, automation of the process of filing disclosures to stock exchanges, and restriction on trading window.

The database should also contain the names of such persons with whom information is shared under the new insider trading norm along with the PAN or any other identifier authorised by law where PAN is not available, as per the notification. [Business Standard, July 21]

SEBI eases default recognition norms for Covid-related debt restructuring

SEBI has extended the relaxation given for default recognition on account of restructuring of debt, till December 31. It had directed credit rating agencies not to assign default grade to entities that undergo restructuring solely due to Covid-related stress, earlier in March. [Business Standard, Aug. 31]

SEBI eases rules to raise funds via preferential issues tweaks takeover code

The market regulator on June 25 changed the pricing norms for preferential allotment of shares to make it easier for the corporate sector to raise funds in the wake of covid-19-related financial hardships. It also amended the takeover code.

Under SEBI's new option, approved on Thursday, higher of the 12-week average and two-week average prices will be considered to fix the allotment price. This relaxation is applicable till the end of the year and the shares allotted through this route would be locked-in for three years. The 12-week pricing covers almost the entire lockdown period during which the stock prices were extremely volatile and adhering to 26-week pricing had become impossible. [Live Mint, June 25]

SEBI for continued rating of errant cos

SEBI is not in favour of a demand from credit rating agencies (CRA) to let them withdraw ratings of uncooperative companies that fail to provide required information, two people aware of the matter said. The regulator wants the ratings to continue, since withdrawing them would leave investors with even less information, the people said, requesting anonymity.

Regulations require CRAs to keep every credit instrument rated all through its lifetime. They can be withdrawn only if a bank issues a no-objection certificate, 75% of bond issuers agree, or if the instrument/loan has been assigned a 'D' or default rating.

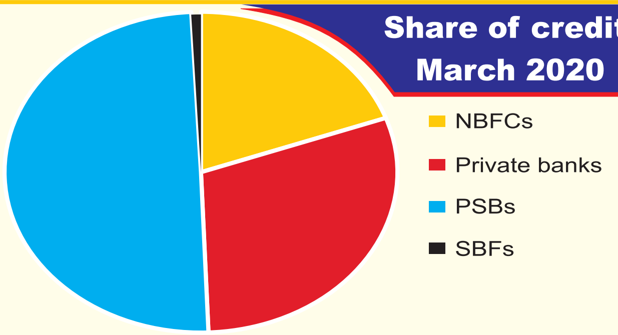
Rating agencies last week wrote to SEBI and RBI that they wish to stop rating credit instruments and bank loans of un-cooperative issuers. They argued that rating without complete information renders the entire exercise futile. However, SEBI does not seem to think that way. [Live Mint, July 10]

INDIA'S FINANCIAL SECTOR: THE IMPACT OF COVID-19 AND THE LONG TERM POLICY AGENDA: WORLD BANK

Summary: Multiple reforms in recent years have improved India's financial sector oversight and financial inclusion, but more needs to be done to cope with the current headwinds and improve the depth and efficiency of financial intermediation. The impact of the COVID-19 pandemic risks exacerbating long-standing structural issues such as slowing credit growth, liquidity shortages in the NBFC sector, and a high level of NPLs. The authorities' anti-crisis response in recent months focused on injecting liquidity into the financial system through policy rate cuts and special liquidity and credit support windows to MSMEs and NBFCs, among others. Borrowers were also provided temporary relief through a loan moratorium and suspension of insolvency procedures, while lenders benefit from regulatory forbearance. While these extraordinary steps help mitigate the immediate crisis impact, preparations should be made to cope with increased NPLs and potential solvency issues for banks and NBFCs after the measures expire.

a. Impact of COVID-19 and immediate policy response

Share of credit, March 2020



Source : RBI
Notes : Data for NBFCs are for September 2019.
SFBs - small finance banks

The Indian financial sector had been in a tumultuous period since late 2018. Onset of the COVID-19 pandemic, the default of NBFCs, cooperative bank (PMC), the resolution of a private bank (Yes Bank), and overhang of legacy NPLs across commercial banks—all in the context of an economic slowdown—had been contributing to slowing credit growth and decreasing market confidence.

Credit growth has slowed down in recent years. Since 2017, it decelerated sharply from historical averages, mainly due to a slowdown in activity of the PSBs. Credit growth in the NBFC segment also declined after 2018 due to liquidity issues, leading to a credit crunch for MSMEs and other sectors dependent on NBFC financing.

Bank NPLs remain high despite recent resolution efforts, and NBFC NPLs increased. Meanwhile, NBFC NPLs have increased from 4.5 percent in 2015-16 to 6.4 percent in March 2020. The NBFC liquidity crisis in the past eighteen months has given rise to a "triple balance sheet" problem, with banks, NBFCs, and the corporate sector (especially real estate firms) trapped in a vicious cycle of deteriorating asset quality and liquidity shortages.

The large PSB sector requires significant fiscal outlays and has been outperformed by private banks

The NBFC sector provided an alternate channel of credit for the real sector, especially MSMEs, in recent years but faced funding challenges. The default of several large NBFCs in 2018 led to capital market funding drying up, even for NBFCs which were not in distress. Since NBFCs relied heavily on short-term funding to finance long term assets, the sudden withdrawal of liquidity was especially problematic. Although banks have stepped in to provide funding to NBFCs (in large part responding to incentives from the government and the RBI), it came at a cost to NBFCs, of more onerous funding terms for securitized loans, such as banks' requirements for higher collateralization levels and high quality of securitized assets.

While India's equity market has been growing rapidly, the corporate bond market is underdeveloped and contributes to the lack of diversity in funding sources.

b. Impact of COVID-19 and immediate policy response

Since the onset of the COVID-19 crisis in India in March 2020, the authorities have taken a wide range of actions to mitigate the impact on financial institutions and borrowers.

The government announced additional measures to support MSMEs and NBFC liquidity, as part of the economic recovery program announced in May 2020. These measures mostly comprised liquidity facilities from the RBI and lenders, with partial or full guarantee by the government. The government has initiated the implementation of these facilities. Banks and NBFCs have started sanctioning credit to beneficiaries under these facilities, with a few initial roadblocks (low initial disbursement to MSMEs and concerns over end use of additional credit). The liquidity measures announced so far have low immediate fiscal outlays but substantial calls on the guarantees included in these measures could result in additional fiscal costs over the medium term.

The measures by the government and the RBI have mitigated immediate liquidity concerns, but their impact on credit growth remains to be seen. Credit growth remains low at 6.2 percent for the fortnight ended June 19, 2020 compared to 12.3 percent during the same period last year. Commercial banks have lately kept very high liquid balances with the RBI, in the region of Rupees 6-7 trillion (around US$80-93 billion) which are substantially in excess of the required minimum reserves. This is for two key reasons. Firstly, financial institutions and other creditors have turned highly risk-averse towards funding economic activities given the uncertainty about the current environment. Secondly, the financial sector still has not fully embraced innovations in financial technologies that could accelerate credit and payment delivery to MSMEs.

The measures by the government and the RBI have mitigated immediate liquidity concerns, but their impact on credit growth remains to be seen.

c. Emerging risks post lockdown

The banking sector is facing increased, long-term asset quality and profitability pressures given the negative economic outlook.

NBFC and MFI balance sheets are stressed on both the liabilities and asset sides. The NBFC sector is facing exacerbated liquidity risks as the volatility in financing from both banks and capital markets has increased since the onset of the COVID-19 pandemic. Debt moratoriums provided by NBFCs to their borrowers may not be uniformly counter-balanced by moratoriums on their own borrowings (banks can provide moratorium to NBFCs on a case by case basis) or direct access to RBI liquidity windows. An attempt to improve NBFC liquidity through TLRTO 2.0, a targeted repo operation to channel liquidity to NBFCs through banks, was only partially successful as banks availed only 25 percent of the total amount100 . While the various liquidity facilities have partially eased funding for NBFCs in the past two months, the spread remains high. On the asset side, the capacity of borrowers (mostly real estate, MSME, retail) to repay after the moratorium is uncertain. Likewise, the expected increase in loan delinquencies and slippages in repayment rate for the MFI sector due to a collapse in clients' revenues could threaten the viability of many institutions.

Small private banks and NBFCs could be more severely impacted than larger banks.

Banks' and NBFCs' capital adequacy could come under stress as asset quality deteriorates and profitability declines. The CRAR for banks was 14.8 percent as of the end of March 2020, as compared to the regulatory minimum of 10.9 percent. For NBFCs, CRAR stood at 19.6 percent as of the same date, down from 22.1 percent in March 2018 but was still above the regulatory minimum of 15 percent. It should be kept in mind, however, that aggregate capital buffers may mask weaknesses in some financial institutions. While insolvency of an individual bank, NBFC, or MFI is not likely to lead to a systemic crisis, it could still have a lasting impact on market confidence for the entire sector, as seen in the case of large NBFC failures in recent years.

[Continued on page-4]

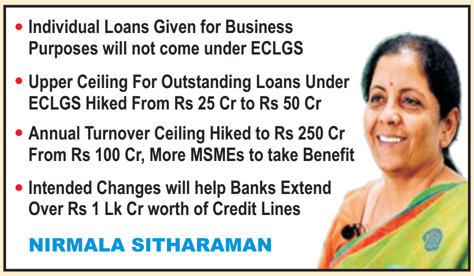
BOOST TO THE ECONOMY FROM TOP

PM Narendra Modi during his interaction with industry leaders of banking and NBFC sectors asked them to pass on benefit of the Centre's relief package down to the consumers.

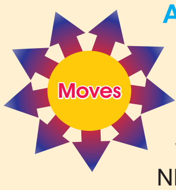
Following his interaction with industry leaders and stakeholders, Prime Minister Narendra Modi had said in a tweet, "Had an extensive interaction with stakeholders from banks and NBFCs to deliberate on the roadmap for economic growth, helping entrepreneurs and a range of other aspects." The small entrepreneurs, SHGs, farmers should be motivated to use institutional credit to meet their credit needs and grow.

Progress of initiatives such as the emergency credit line for MSME, additional KCC cards (Kisan Credit Cards), liquidity window for NBFC and Money Flow Index (MFI) was also reviewed. While it was noted that significant progress has been made with respect to most schemes, banks need to be proactive and actively engage with intended beneficiaries to ensure that the credit support reaches them in a timely manner during this time of crisis.

PM urged chief executives of both public sector and private sector banks to do some heavy lifting to support the economy during the ongoing Covid-19 pandemic to enable its quick revival in the days to come. [PMO/PIB, July 29]



The Finance Minister appreciated the efforts of banks and NBFCs during the lockdown in effective implementation of the Pradhan Mantri Garib Kalyan Yojana and the Aatmnirbhar Bharat related measures. The Finance Minister also exhorted the **lenders to proactively respond to needs of companies and businesses, as well as those of individual borrowers, and to spearhead the efforts for rebuilding businesses** desperate for help owing to COVID-19 related distress. [PIB Delhi, 3 Sept.]



All NBFCs can now provide MSMEs loans against dues via TReDS

The Cabinet on Wednesday allowed all NBFCs to provide discount loans to MSMEs against dues from government departments, through the TReDS platform. So far only a selected NBFCs and banks were on the platform and could give the discount loans to MSMEs. Cash flow and liquidity have been a major concern for MSMEs amid the pandemic. Union Information and Broadcasting Minister Prakash Javadekar said that the decision has been taken to improve the liquidity flow to the MSMEs. He noted that MSMEs get their dues on the bills generated from government departments and agencies after 90 days which creates liquidity issues and the latest move has been aimed towards easing the liquidity flow during such delay. [IANS, Aug. 19]

Eligibility of Commercial Vehicles under ECLGS

National Credit Guarantee Trustee Company has on July 2 clarified that all eligible borrowers (business enterprises / MSMEs constituted as proprietorship, Partnership, Registered company, Limited Liability partnerships, Trusts and Society or any other legal entity and including individuals in the case of loans covered under MUDRA scheme) who have availed loans against vehicles (including construction equipment vehicles, taxis etc,) which are registered for commercial purposes are eligible for assistance under Emergency Credit Line Guarantee Scheme (ECLGS). This was done by it in response to questions raised about eligibility of commercial vehicles under the scheme, stated Durgesh Pandey, CEO, NCGTC in a circular dated July 2.

Single e-compliance window soon: MCA initiates discussions with RBI, SEBI, DPIIT on transfer of data

The corporate affairs ministry [MCA] has initiated discussions with various regulators on the possibility of creating a single platform or compliance forms with common data sources, the official said.

MCA initiates discussions with RBI, SEBI, Department for Promotion of Industry and Internal Trade [DPIIT] on transfer of data. The government is looking to develop a single online compliance framework for India Inc to enable companies to comply with different regulatory requirements at one go, an official privy to the development said. "The idea is to reduce compliance burden," a senior government official told ET.

Companies at present have to make multiple filings. Different regulators have different requirements and formats for submission of data. Once the common platform is in place, companies can file all their data in one place and regulators can get their data from one source, experts said. [ET Bureau, Aug. 21]

Vehicle scrappage policy could come by September end: Nitin Gadkari

The much-awaited vehicle scrappage policy is in its final stages of approval and will be rolled out within a month, road transport and highways minister Nitin Gadkari said on Saturday. "The vehicle scrapping policy is very important for the revival of the auto industry. I assure you that the scrappage policy is in its last stages of approval and it will come within a month. It may even come within this month-end," Gadkari said. [Live Mint, Sept. 5]

I-T Dept asks banks to refund any fees levied on UPI transactions from January 2020

Income Tax Department on Aug. 30 came hard on banks for collecting charges from specified businesses providing payment facility through RuPay debit card or BHIM UPI. Banks have been asked to refund charges and also cautioned that such collection would attract a penalty. [Business Line, Aug. 30]

NABARD launches credit guarantee programme for NBFC-MFIs

The National Bank for Agriculture and Rural Development (NABARD) introduced a dedicated debt and credit guarantee product to guarantee unhindered flow of credit in rural areas hit by the COVID-19 pandemic.

NABARD has launched "Structured Finance and Partial Guarantee Programme" to NBFC-MFIs-entails offering partial guarantee on pooled loans extended to small and mid-sized micro finance institutions (MFIs), a release said.

"The partially guaranteed loan facility will catalyse much-needed financing to millions of households, agricultural and business markets to sustain in the post COVID-19 environment," NABARD Chairman Mr G R Chintala said. [IBEF: August 25]

Professionals like doctors, lawyers brought under govt's credit guarantee scheme for MSMEs

Professionals including doctors and lawyers who have taken loan for their business needs will now be eligible for credit under the special credit guarantee scheme for medium and small enterprises. The government on Saturday expanded the scope of the scheme to include "individual loans given for business purposes" within the ambit of Emergency Credit Line Guarantee Scheme.

Upper ceiling of the loans outstanding under the scheme announced by finance minister Nirmala Sitharaman as part of the Atam Nirbhar Bharat package is being raised to Rs 50 crore from Rs 25 crore now. Annual turnover ceiling has been raised to Rs 250 crore from Rs 100 crore in line with new definition of MSMEs. [Economic Times, Aug. 1]

An Accounting Breather

The government has revised the Indian accounting standards to reflect the true and accurate impact of Covid-19 on companies' financials and align them with the International Financial Reporting Standards. The revisions will give investors a better picture of the economic impact of the pandemic on a company, experts said. The Ministry of Corporate Affairs has amended the Indian accounting standards relating to presentation of financial statements, business combinations and changes in accounting estimates, among others. The most significant change relates to Ind AS-116, which sets out the principles for recognition, measurement and disclosures relating to commercial lease in financial statements. [BloombergQuint, Aug. 5]

Banks and FIDC oppose Finance Ministry move to decriminalise cheque-bounce offence

Fear of criminal action is a strong deterrent for willful defaulters: Banks have added their voice to the increasing chorus of stakeholders opposing the Finance Ministry's proposal to decriminalise the offence of cheque return under Section 138 of the Negotiable Instruments (NI) Act, 1881. Banks, under the aegis of the Indian Banks' Association, have represented to the Finance Ministry that this provision in the NI Act should continue.

Bankers say they resort to legal action under Section 138 (relating to dishonour of cheque) only in cases where borrowers willfully default on loans. The fear of criminal action, including imprisonment for up to two years or fine, which may be twice the amount of the cheque, or both, acts as a deterrent to such borrowers.

Enforcement of contract: FIDC, a representative body of asset and loan financing NBFCs has also opposed the proposal to do away with Section 138. Mahesh Thakkar, Director General, FIDC, cautioned that decriminalising the offence under Section 138 of the NI Act would lead to further deterioration in enforcement of contract, especially in terms of honouring acknowledged debt and liability.

He emphasised that small and medium enterprises, apart from NBFCs, will be the worst sufferers and the marketplace will be relegated to cash and carry transactions, with cheques losing their value as a means to secure transactions. [Business Line, July 21]

Auction Buyer liable to clear power arrears

The liability to pay electricity dues of the previous owner falls on the auction purchaser if the terms of the sale recites "as is where is, what is there is and without any recourse basis", according to the Security Interest (Enforcement) Rules. This interpretation was given to the phrase by the Supreme Court last week while setting aside the judgment of the high court in Telangana Power Distribution Co vs Srigdhaa Beverages. A unit of a mineral water bottling company was sold through auction by invoking the Securitisation Act ("Sarfaesi") as the owner could not repay a loan given by Syndicate Bank. The distribution company demanded the dues of the defaulting company from the new buyer, leading to the litigation. The terms of the sale deed and the licensing clauses contained several legal terms which were interpreted by the high court and the Supreme Court in different ways, ultimately in favour of the supply company. [Business Standard, June 7]

Court stays out of credit ratings

The credit rating of a company is usually rendered after taking into account all positive or negative factors and it is an opinion rendered by experts in the field. A court will not interfere unless the opinion is "perverse, arbitrary and mala fide". A court cannot also stop the rating agency from disclosing or publishing it. So stated the Delhi High Court in its judgment in the case, Jindal Power Ltd vs ICRA Ltd. JPL filed a suit requesting the court to quash its downgrading from BBB+ (stable outlook) to BBB (negative outlook) by Icra, which is a rating agency following the SEBI (Credit Rating Agencies) Regulations. Both parties had signed an agreement in 2016 on rating and there was no dispute for the past few years. However after the economic stress and the Covid pandemic, several issues were raised by the rating agency. Rejecting the stand of JPL, the court observed that "the evidentiary value of opinion of an expert has to be decided on the basis of the credibility of the expert and the relevant facts supporting the opinion. The emphasis has to be on the data on the basis of which opinion is formed. Further, if the opinion is intelligible, convincing, and based on reasoning, no decree declaring the said opinion as null and void, unenforceable and ineffective can be passed". [Business Standard, Sept. 3]

Caution in stopping arbitration

Civil courts have the power to stop a party to an agreement from invoking arbitration, but it should be exercised sparingly. The Calcutta High Court stated so while rejecting a prayer for such an anti-arbitration injunction in its judgment, Balasore Alloys Ltd vs Medima LLC. The Odisha company, which exports ferro alloys to the US firm, fell out over two agreements. The first one stated that any dispute will be arbitrated in India according to the domestic law, while a related contract signed later mentioned the International Chamber of Commerce (ICC) in London as the forum that would follow the British law. Balasore moved the high court seeking an anti-arbitration injunction, restraining the US firm from going forward with its intent to approach ICC. Rejecting the prayer, the court stated that the mere existence of multiple proceedings in multiple forums is not sufficient reason to render an arbitration agreement inoperative. It added that the burden of proof to show that a forum is not convenient or that the proceedings launched before a neutral foreign forum is "vexatious or oppressive" is upon the party which alleges so. [Business Standard, Aug. 20]

Finance Minister reviews on Sept.3 preparedness for implementation of loan resolution framework for COVID-19 related stress with Heads of Scheduled Commercial Banks & NBFCs

Supreme Court grants relief to borrowers, extends loan repayment moratorium till September 28

The Supreme Court on Sept. 10 virtually extended the loan moratorium period till September 28, granting relief to borrowers, by extending the interim order asking banks not to declare as NPAs accounts that are unable to make repayments. "Accounts not declared NPA as on August 31 shall not be declared NPA till further orders," the apex court bench led by Justice Ashok Bhushan had declared in its interim order last week. [ET online, Sept. 10]

Misrepresentation charge in arbitration

The question was whether an arbitration clause could be acted upon when one party alleges that it entered into the agreement by fraudulent inducements by the other. This problem arose in the case, Avitel Post Studioz Ltd vs HSBC Pi Holding (Mauritius), in which the latter alleged that it had extended a loan to the Avitel group on misrepresentation of facts and fraud. The group included Avitel India, Avitel Mauritius and Avitel Dubai. They represented to HSBC that it had a project with BBC, but it turned out to be untrue. HSBC invoked the arbitration clause, which named Singapore as the venue applying the law there. The award of the tribunal went against the Avitel group, leading to a slew of litigation in the Bombay High Court and in district courts. The Supreme Court allowed those suits to continue while observing that "a reading of the foreign final award in this case would show that a strong prima facie case has indeed been made out as the award holds the BBC transaction as a basis on which the contract was entered into and the USD 60 million paid by HSBC, would clearly fall within fraudulent inducement to enter into a contract under Section 17 of the Contract Act. Such a contract would be voidable at the instance of HSBC." [Business Standard, Sept. 3]

IMAGINING NBFC SECTOR IN THE POST PANDEMIC WORLD

At ETBFSI Converge, the heads of top NBFCs discussed the future of the sector and what role does re-invention of business models play in the survival of the industry in a post pandemic world. At another ETBFSI Converge, the tech heads of leading Indian NBFCs shared their idea of how to make our NBFCs world-class.

Substituting human intervention with tech: Sachin Pillai, MD & CEO,Hinduja Leyland Finance

According to Sachin Pillai the business model remains the same in terms of the customer segment, asset classes and the network. However, the way of approaching business has changed amidst pandemic. He asserted, "It was our belief that the customer section we focus on which is self employed will somewhat lag behind in following the changing trends. Fortunately, we were surprised to witness 10 times more usage of our customer service apps and other digital platforms." He strongly feels that the customers are becoming more aware and trying their best to change their approach. To an extent possible the company is looking forward towards substituting human intervention with tech.

Shift to Digital was an external challenge: TT Srinivasaraghavan, MD, Sundaram Finance

He strongly believes that 're-inventing business models' is a wrong buzz phrase that is thrown around often times. NBFC sector constitutes a lot of risk, and everybody in his/her own ways is trying to deal with that perspective. "Technology has been the major new element to take the centre stage. Retail business is a touch and feels business, it requires physical contact. Unfortunately due to the pandemic, that has come to a standstill. Adapting to technology was not an internal challenge but an external one. We were comfortable with going digital but getting our customers to sign up for digital portals or apps was a big change, fortunately we did well", he added.

"People cannot go digital overnight": George Alexander Muthoot, MD, Muthoot Finance

Mr. Muthoot majorly speaks about the Gold Loan sector because it constitutes 90% of their business. "Biggest Issue with the Gold Loan sector is that it is a touch and feels business. The branches had to open and our customers had to visit to conduct business activities. The months of March and April posed the biggest challenge for us." He added: "Many of our customers are small customers. We could not ask them to go digital or become techno savvy overnight. However, we asked our staff to go and get their bank accounts mapped to their loan accounts. After that the usage got somewhat better."

"Change Has to Happen": Hemant Kanoria, Chairman, SREI Infrastructure Finance

Mr. Kanoria says that the Infrastructure Financing sphere has been focusing more on the equipment financing side since the last 4-5 years. After the 2018 episode of IL&FS, companies focusing on equipment financing and project financing space were majorly affected. We had to work closely with banks to see how we can share the risks and if there was a need to reduce our portfolio. According to Kanoria, every NBFC has been re-engineering and redesigning its way of conducting business in order to survive the disruptions caused by the pandemic.

Growth has been the biggest challenge: Dr Kshama Fernandez, MD & CEO, Northern Arc Capital

In terms of re-inventing the business model, Dr Kshama Fernandez, MD & CEO, Northern Arc Capital, that the biggest challenge she faced was connectivity. Northern Arc for the last couple of years have been spending a large amount of time and capital on developing a digital interface for the employees.

"When the whole lockdown happened, we were able to switch instantaneously from a physical working environment to working remotely from our homes. We are majorly focusing on maintaining the confidence we have built in the underline sectors. The biggest challenge has been growth that is what we are trying to grapple with. Being digitally ready to face the new state of our world has been the saving grace for us," Fernandez added. [Abridged version, ETBFSI, September 11]

HOW TO MAKE OUR NBFCs WORLD-CLASS-WHAT TECH HEAD OF NBFCs THINK

At the ETBFSI Converge, the tech heads of leading Indian NBFCs share their idea of how to make our NBFCs world-class.

Embark upon leveraging AI and ML at every piece of the value chain: By successfully tapping into the hinterlands of the country with the help of advanced technologies, NBFCs have emerged as a reliable alternative to banks. The NBFCs are aggressively partnering with fintech startups to make the most of the new-age technologies — artificial intelligence and machine learning, among others — to build products for the 'digital customers'. However, there it's a long way for Indian NBFCs when compared to their international peers, and for that NBFCs would have to embark upon leveraging AI and ML at every piece of the value chain.

Every area will need AI/ML and algorithm machines: While discussing what lies ahead of our NBFC sector, Ekhlaque Bari, EVP & CTO, Fullerton India, said, "Risk management is going to be the most important part that will be touched by AI/ML but not the only part. Every area will need AI/ML and algorithm machines. I believe Artificial Intelligence and Machine Learning will play a huge part going forward." Bari says that we have plenty of ideas but the slow execution has made a difference. "AI, facial recognition, risk management, and underwriting are some aspects where other countries have done better than India. China uses facial recognition to detect fraud and to arrive at an underwriting score. Some countries have deployed voice bot. Bari further added that the customer is still the king and will always be. Things have to be made more convenient for the customers."

Designing the right product to deliver: For Durgaprasad Swaminathan, SVP & CIO at Cholamandalam Finance the initial experience is the big differentiator. "Are we designing the right product to deliver? Are we making it easier for us to identify the customer from an identity perspective and financial credit worthiness perspective?" he asked. He added that NBFCs need to make it easier for the customer to identify the product.

Regulators need to be forward-looking: Ramesh Narayanaswamy, Group CTO, Aditya Birla Capital feels that the regulators have to take a huge step forward in allowing both customers and organisations to do thing. "I feel that we need more regulatory assistance. Regulators need to be a little forward-looking." This will give the overall system in the country much robustness. We have to come up with holistic products and solutions; understand the customer a bit more because ultimately it's going to be all about the power of one as every customer is going to be unique. And this can be achieved only through automation, having proxies and through data." He says that for Indian NBFCs, the biggest challenge is scale. "The challenge in India is that you have to do it at a larger scale even if we have the required technology. In other countries there is no problem of scale and they have all the latest technologies. This means that the technology cost will be significantly more in India." [ETBFSI, Sept.11]

IMF: Small- and mid-sized biz bankruptcies may triple

The International Monetary Fund warned that the rate of bankruptcy for small- and medium-sized businesses may triple this year in the absence of sufficient government support, threatening to stall the economic recovery and cause financial instability. A staff analysis of 17 countries suggests that bankruptcies for the firms could surge to 12 per cent, from 4 per cent before the pandemic, the IMF said in a report on July 16. Italy would see the biggest increase due to a large drop in aggregate demand and high share of production in contact-intensive industries. Across the Group of 20, relief from taxes and social security contributions, grants and interest rate subsidies have been an important salve, the IMF said. [Bloomberg/Business Standard, July 17]

Collection efficiency improving in NBFC sector, hopes of near normalisation by Diwali: Report

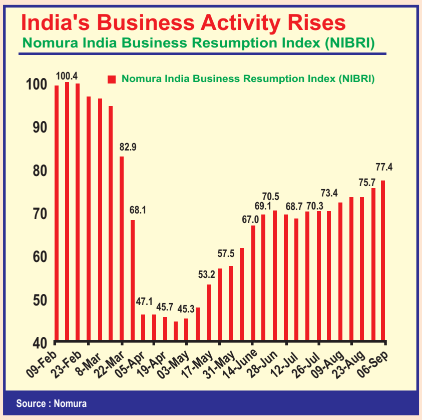
NBFCs have ramped-up their collection infrastructure aggressively and growth is visible across product segments, a report by Motilal Oswal said. The brokerage said the report was prepared following its annual general investor conference, which saw participation from 15 NBFCs. "With improving macros across most business segments, there was increased optimism on collection efficiency as well as on growth across product segments. In retail lending, at least 15-20 per cent improvement was seen in collections over the last two months. "Overall collection efficiency was at 70-75 per cent for micro loans, at 80-90 per cent for vehicle finance, and at 85-90 per cent for affordable housing across financiers in August 2020," the report said. [BFSI News/PTI, Sept. 10]

"It has been a pleasant surprise in collections post-moratorium," says TT Srinivasaraghavan, Managing Director, Sundaram Finance. While segments such as hospitality and bus transportation have been badly affected, recoveries have been quite encouraging in several others, though varying from region to region. "We have all hues in this," he adds. [Business Line, Sept. 29]

PRSF Scheme to promote Energy Efficiency Projects: SIDBI

The objective of the PRSF Scheme is to promote Energy Efficiency Projects in India implemented through performance contracting route (ESCO route) by way of SIDBI extending credit guarantee of upto 75% of the loan amount for such ESCO projects. Out of USD 37 million, USD 28.5 m (Approx Rs 215 Cr) worth guarantee amount is currently available under PRSF Scheme.

Scheduled Commercial Bank or NBFCs with average net worth of INR 500 million during last 3 years, with at least BBB credit rating and active in lending business for a minimum period of 3 years out of which 2 years with profitably and RBI specified minimum CRAR are eligible to participate. For complete details on PRSF Scheme and Project eligibility visit http://prsf.sidbi.in/. [SIDBI Circular]



India's economy is slowly recovering, shows Nomura India Business Resumption Index

After a brief plateauing in July, the pace at which economic activity is normalising rose in August and the uptrend continued into early September despite mounting Covid-19 infections. Nomura's India Business Resumption Index, which tracks business activity on a weekly basis, rose to 77.4 for the week ended Sept. 6 from 75.7 at August-end and 70.3 at July-end. [BloombergQuint, Sept. 7]

NBFCs to FM: Ease loan rejig eligibility rules for small cos

NBFCs have petitioned the finance minister to relax norms and allow restructuring for all standard loan accounts and not just those which are without any overdue for more than 30 days. According to the lenders, micro and small enterprises have uneven cashflows and were facing challenges even before the Covid-19 pandemic.

On September 3, representatives of the NBFC sector met with the finance minister to discuss the one-time restructuring of debt and progress in disbursing loans under the emergency credit line guarantee scheme (ECLGS) and partial credit guarantee scheme. In the meeting, it was decided that all lenders will have a board-approved restructuring policy for their stressed customers by September 10. Following this, they will commence the process of restructuring loans of eligible customers by September 15.

The government conceded to the NBFC request to extend the ECLGS to individuals carrying on any business activity. The finance ministry pointed out that the current performance of NBFCs in terms of sanction and disbursement of ECLGS loans is slow and they must accelerate disbursals and target to achieve maximum coverage by the end of September. The scheme is set to end on October 31, or until the disbursement of Rs 3 lakh crore. [TNN, Sept. 08]

Periscope

India's 'Regulatory Cholesterol' Still Obstructs Ease Of Doing Business

Businesses have to deal with a combined 1,536 acts, 69,233 compliances and make almost 7,000 filings in the country, an analysis by TeamLease, a staffing, regulatory and compliance management firm, showed. States with larger economies such as Gujarat and Maharashtra have more than 3,000 compliance requirements each. The web of regulations comes as every authority applies its own set of norms to businesses, according to Rishi Agarwal, chief executive at Avantis Regtech, a subsidiary of TeamLease that collated the data, told BloombergQuint. This results in a number of redundant and overlapping legislation that hamper ease of doing business, he said. "Every ministry sees only their leg of the elephant. With this data analysis, we aim to show the entire elephant."

India's rank has jumped 71 places with reforms like the goods and services tax, the Insolvency and Bankruptcy Code and easier compliance to start a business. Still, significant challenges remain, particularly in areas like enforcing contracts and registering property. [BQ Desk @bloombergquint, Jul 12]

Tech giant Google is foraying into the digital lending space

It is set to become a $1-trillion opportunity in the next five years, according to sources. Its digital payments app GPay is forming partnerships with fintech firms and has already onboarded ZestMoney to offer credit to consumers, signalling a larger interest to tap the financial services market in the country. Bengaluru-based ZestMoney is now integrated on GPay's digital store's Spot platform to offer credit to customers. This feature will allow customers to avail credit with ZestMoney from GPay directly. "Google has indirectly entered the digital lending space," said a person familiar with the matter. [Business Standard, July 27]

FIDC In Action

FIDC seeks a separate fund for smaller NBFCs

Small and mid-sized non-bank lenders are seeking a creation of separate fund. In a letter written to the finance minister, FIDC, an association of NBFCs has sought a creation of separate fund where small and mid-sized will be able to borrow from institutions like SIDBI and NABARD.

FIDC has said NBFCs irrespective of their ratings, P&L accounts shall be made eligible to borrow from this fund as term loans for a period of 3-5 years. FIDC also wants banks to be advised for showing some relaxations towards NBFCs financials and create a sectoral cap for the small and mid-sized NBFCs. FIDC said in the letter, "The Banks/FIs usually look at certain profitability ratios such as Interest Coverage Ratio, Credit Loss ratio and Profitability ratios etc. while granting new facilities to NBFCs. These ratios play an important role in approval of new facilities.

It added, "These profitability ratios are usually complied in normal economic conditions. We are living in abnormal times now, hence, it would be in fitness of the situation to relax the profitability ratios and covenants - for the financial years 2019-20 and 2020-21. It would be easier on part of the Banks/FIs to relax conditions for the current year, if the same is backed by a regulatory advice." [ETBFSI July 17]

Government, RBI need to ensure that cash-flushed banks lend to NBFCs: FIDC

NBFCs have been going through a liquidity crisis over the past two years and the Covid-19 pandemic has only worsened the situation. Mahesh Thakkar, the Director General of FIDC is of the view that Centre and the RBI should intervene and ensure that well-capitalised banks lend towards the small and medium NBFCs which largely cater to MSMEs and small businesses.

Speaking to IANS, Thakkar said that although noting that skepticism towards lending to NBFCs still exists among the banks, it has, somewhat eased in the past few months since the government's liquidity measures and sovereign guarantee schemes. "Problem is that the banks are sitting with huge funds... and where to lend is the problem," he said. [IANS July 11]

NBFC loan sanctions fell 15% in Q4 FY20: FIDC

Data released by the FIDC on Thursday revealed that sanctions by NBFCs amounted to Rs.2,56,330.05 crore in the quarter ended March 31, 2020 as against Rs. 3,02,654.69 crore in the same period a year ago. "We must remember that in the fourth quarter of 2018-19 also there was a 31 per cent annual reduction in sanctions in the aftermath of IL&FS and so this reduction of 15 per cent is in spite of the base effect of low volumes and therefore, is actually very sharp," said Mahesh Thakkar, Director General, FIDC. He added that most industrialised States such as Delhi, Maharashtra and Tamil Nadu showed a decline, while in Gujarat there was a flat trend. Barring bank guarantees, personal and education loans, property loans and home credit finance, sanctions in most other categories declined in the quarter. According to the data, secured business loan sanctions fell by 52 per cent in the fourth quarter of last fiscal, while housing loans fell by 31 per cent. Personal auto loan sanctions fell by 32 per cent in the January to March quarter and two-wheeler loans declined by 18 per cent. Sanctions for used car loans also declined by 14 per cent in the period and those for used tractors fell by 19 per cent. Sanctions for agri loans, too, were down by 60 per cent in the period. Consumer loans fell by six per cent and gold loans declined by 22 per cent in the fourth quarter last fiscal. [Business Line, July 9]

Allow acceptance of Form 60 as an alternative, where the customers do not have PAN under ECLGS

FIDC also took up with NCGTC's CEO Durgesh Pandey on August 18 stating that the "NCTGC requires PAN as mandatory information to be provided by MLIs while uploading borrower details on NCGTC portal. This requirement would amount to exclusion of those individuals who do not have PAN." These individual drivers-cum owners financed by many lenders usually do not have incomes requiring them to file income tax return. Therefore, in those cases, these customers may not obtain Permanent Account Number (PAN). This requirement would amount to exclusion of those individuals who do not have PAN but furnish Form 60 to the lending institutions. Mr. Thakkar therefore appealed for allowing acceptance of Form 60 as an alternative document, where the customers do not have PAN.

In view of the provision in the Operational Guidelines of the ECLGS it is required that the annual turnover of the borrower in FY 2019-20 should not exceed Rs. 250 crore. It further states that if the accounts for FY 2019-20 have not been audited/ finalized, the MLI may rely on borrower's declaration on turnover. The portal also requires MLIs to input exact turnover of the borrower while uploading borrower data. FIDC therefore requested NCGTC to allow declaration from the borrower stating that the turnover does not breach the limit prescribed in the Operational Guidelines of the Scheme. The NCGTC portal may accordingly be suitably modified.

FIDC seeks exemption of NBFCs from restriction on opening of current accounts

FIDC has urged the RBI to exempt NBFCs from the restriction imposed on opening of current accounts by banks. In a bid to curb multiple operating accounts for loans and maintaining credit discipline, the RBI has taken additional measures wherein banks have been directed not to open current accounts for customers already availing credit in the form of cash or overdraft (OD)

In its letter to RBI, the FIDC has said that NBFCs borrow from banks mostly as term loans and the percentage of borrowing as cash credit is low. An NBFC may operate its main collection or disbursement account with a bank from which it does not have a cash credit facility but only a term loan, for reasons of better service levels or branch strength in the geographical area served by the NBFC.

"Unlike manufacturing industry which borrows term loans for specific projects (and therefore direct disbursement to suppliers is possible), NBFCs create a loan portfolio and then avail of term loans for refinancing their existing loan portfolio. Direct disbursement to "suppliers" is not possible in such a scenario," it said.

The FIDC noted that there are existing regulations governing borrowing and end use of funds by NBFCs which are practical and provide a strong framework of governance and control. "All banks seek NOCs from existing banks while opening current accounts of NBFCs. We therefore request you to please exempt NBFCs from this regulation on restriction of opening of current accounts and on the stipulation of remitting term loans to 'suppliers'," said the letter from Mahesh Thakkar, Director General of FIDC. [IANS, August 21]

ECLGS: NBFC body seeks addition to list of individuals seeking assistance

FIDC a representative body of NBFCs has written to Finance Minister Nirmala Sitharaman seeking inclusion of all individuals who have taken loans for purchase of vehicles for commercial purposes for assistance under the Emergency Credit Line Guarantee Scheme (ECLGS). [ET Auto.com, July 6]

Put NBFCs at par with banks for increase in LTV ratio for gold loans: FIDC

RBI has recently permitted banks in India to increase the permissible loan-to-value ratio (LTV) for loans against the pledge of gold ornaments and jewellery for non-agricultural purposes from 75 per cent to 90 per cent and the relaxation is applicable for a limited time up to March 31, 2021. But gold loan NBFCs have been kept out of the purview of the relaxation. FIDC letter said, "We request that the RBI extend the mitigation benefit to the customers of all the gold loan focused RBI Registered NBFCs too." [IANS, August 21]

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[Courtesy: Business Standard]

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