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Non-Bank Finance Companies & Housing Finance Companies

Restructured book could double in FY2022 as aftermath of second wave of Covid-19 pandemic

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CREDIT OUTLOOK: NEGATIVE

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Restructured book of non-bank finance entities expected to double to 3.1-3.3% from 1.6% in March 2022

NBFCs to witness higher restructuring compared to HFCs, considering their target borrowing segments

The restructured book of non-bank finance entities (NBFCs + HFCs)[1] is expected to double to 3.1-3.3% in March 2022 from 1.6% in March 2021. The restructured book for NBFCs is expected to be 4.1-4.3% as of March 2022 (up from 2.2% in March 2021) while the same is expected to be 2.0-2.2% for HFCs (up from 1.0% in March 2021). The second wave of Covid-19 infections has impacted the budding recovery in non-bank collections witnessed in Q3 FY2021 and Q4 FY2021, impacting the cash flow of the underlying borrowers and thereby further prolonging the recovery process. In view of the Covid-19-induced stress, the Reserve Bank of India (RBI) allowed lenders to restructure their credit while maintaining the standard asset tag in FY2021; via circulars issued in May and June 2021, the RBI included loans to small businesses, which are a key target segment for non-bank finance entities, and extended the micro, small and medium enterprise (MSME) restructuring window to September 2021.

NBFCs and small-sized entities witnessed higher restructuring in FY2021: NBFCs had a higher restructured book outstanding as of March 2021 vis-à-vis HFCs because of the nature of their exposures. For HFCs, security is in the form of mortgage while NBFC exposures are either unsecured or are backed by varied asset classes like vehicles, mortgages, plant and machinery, inventory, receivables, etc. The target borrower segment also plays a key role as a high share of restructuring was observed in smaller entities (assets under management (AUM) of less than Rs. 50 billion). Borrowers catered by these entities would have a relatively higher risk profile, also characterised by higher yields, which exposes them to increased vulnerabilities in a downcycle or a stressed scenario.

Entities with higher share of personal and SME credit witnessed higher restructuring: Vehicle, SME and personal loans which accounted for the bulk of the NBFC credit, faced with asset quality related pressures during the last fiscal. Entities with a sizeable share of new and heavy & medium commercial vehicles witnessed higher restructuring while the same was modest for other segments like cars, two-wheelers and tractors, etc. Stress was also observed in unsecured exposures, i.e. personal and SME loans, because of the subdued risk profile of the target borrowers, thus leading to higher restructuring in these segments.

Relaxation in restructuring criteria expected to provide relief: The borrower eligibility criteria has been relaxed as the requirement is only a standard asset tag as of March 2021 under the *Resolution Framework for Covid-19-related Stress 2.0 (RF2.0)* vis-à-vis up to 30 days past due (dpd) as per the *Resolution Framework for Covid-19-related Stress 1.0 (RF1.0)*. The RBI has further enhanced the exposure limit eligible for restructuring to Rs. 500 million from Rs. 250 million, which augurs well for non-bank finance entities as they can now offer restructuring to a broader borrower base.

[1] *NBFCs – Non-banking financial companies; HFCs – Housing finance companies; excluding public sector entities and infrastructure finance companies*

ABOUT ICRA

ICRA Limited (formerly Investment Information and Credit Rating Agency of India Limited) was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

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- Assist the regulators in promoting transparency in the financial markets;
- Provide intermediaries with a tool to improve efficiency in the funds raising process.

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