

Cash supply to impact asset classes

FALAKNAAZ SYED

Mumbai

DEMONETISATION disrupted the cash ecosystem in which some of the niche Non-Banking Finance Companies (NBFCs) operate. While the third quarter ended December 16 results was a mixed bag for NBFCs (even though they were better than anticipated), the real impact from demonetisation would be seen in the results of the fourth quarter ended March 31, said analysts. Adding to the pressure are the new norms for NBFCs from the central bank that prescribe a limit of Rs 20,000 for transactions in cash and will reduce their ability to accept partial or full loan repayment in cash thus reducing their leeway on the collections front.

"It (demonetisation impact) was more pronounced on niche NBFCs (small business loans, small fleet commercial vehicle operators and microfinance companies) with some headwinds on loans against property. Housing finance companies, unsecured loans to the urban/salaried segment and wholesale lending companies were least affected on asset quality though growth has taken a knock," said M.B. Mahesh, analyst at Kotak Institutional Equities in a research report.

Overall delinquencies, especially in the softer buckets, are expected to increase in the near term as demonetisation impacted collections across asset classes. The extent of impact in each asset class, however, was varied. Post the withdrawal of Rs 500 and Rs 1,000 notes on November 8, people were short of legal tender notes. This resulted in a dip in collection efficiency across lenders.

ICRA has recently revised the portfolio growth outlook for FY2017 to 17-19 per cent vis-a-vis the previous estimate of 19-22 per cent as retail credit off-take got impacted post demonetisation.

TARGET SEGMENT

"The key target segment of NBFCs – the self-employed – is likely to have been impacted more, as a sizeable share of

their business is based on cash transactions, which were affected by the shortage in currency following demonetisation. The extent of recovery in the borrower businesses and income levels and their ability to contribute margins for asset purchase and business funding, would be key drivers of growth in the near to medium term. The NBFC business has been affected by the moderation in disbursements with limited cash availability (especially microfinance and gold backed lending). The NBFCs are also expected to focus more on collections than on incremental business," said Rohit Inamdar, senior vice-president and group head financial sector ratings at ICRA. The performance of the affected asset classes going ahead will depend primarily on the pace of restoration of currency supply in the system and the degree of impact of demonetisation on the borrower business volumes and cash-flows, said Inamdar.

As on September 30, 2016, the total managed retail credit (including off balance sheet book) of NBFCs stood at around Rs 5.4 lakh crore and grew y-o-y by about 20 per cent in the first half of the current financial year as against 19.9 per cent in FY2016 and 14.8 per cent in FY2015. The total NBFC retail credit including SME credit stood at about Rs 6 lakh crore as on September 30, 2016 and grew y-o-y by about 22 per cent in H1FY2017.

"Some moderation in business growth, higher competitive pressures, fall in operating efficiencies because of increased focus on collections and, higher credit cost would partly offset the benefit of lower cost of funding. NBFC net profitability (return on average managed asset) is expected to be in the range of about 1.6-1.8 per cent for FY2017," said ICRA.

CASH COLLECTIONS

NBFCs in auto and business finance are not engaged in cash disbursements but are largely involved in cash collections. Shriram Transport Finance and Shriram City Union Finance had high-

lighted that over 60 per cent of their collections are in cash.

"Some NBFCs chase delinquent borrowers and collect cash as partial settlement thus improving their recoveries. As such, the above restrictions on accepting cash (which will likely get implemented with immediate effect) will affect collection efficiency of NBFCs in a month during which recovery efforts are at a peak. Rural finance companies like Mahindra Finance have large bets on collections in 4QFY17 as cash shortage had affected NPLs in past quarters as well," said Kotak Institutional Equities.

DISRUPTION

"We believe that this revision will disrupt NBFCs operating in the cash ecosystem even as the experience during demonetisation of managing such transitions was impressive. We await further clarity before revising our forecasts and price targets," said Mahesh.

"While collection trends are improving, we believe overdue asset pool could continue to rise. Rise in overdue assets have likely been sharper at MFIs versus NBFCs due to political factors. Part of this could potentially slip into NPA in the next few quarters. We believe GNPA and credit costs could surprise negatively in the next few quarters," said Jefferies India.

Moody's Investors Service in a report said that NBFCs in India will demonstrate broadly stable asset quality, but delinquencies will likely rise over the next 1-2 quarters, as demonetisation adversely affects collections across asset classes. "While the 90+ days delinquency rate in the commercial vehicle (CV) loan segment largely stabilised in the first half of the fiscal year ending March 31, 2017, such delinquencies should build up in the near term due to the adverse impact of demonetisation and tighter recognition norms for non-performing assets (NPAs)," said Alka Anbarasu, Moody's vice president and senior analyst.

NBFC have been affected by moderation in disbursements with limited cash availability. NBFCs are expected to focus on collections than on incremental business.