Waiting for a fair wind

Mint Road has eased up on loans being given to shadow banks, but risks continue and smooth sailing for unsecured credit is still some time away, reports **RAGHU MOHAN**

Towards the end of February, the Reserve Bank of India (RBI) restored the risk weighting on banks loans to non-banking financial companies (NBFCs; including to microfinance institutions, or MFIs) to 100 — back to its November 2023 position — from 125. It is only a partial relief though.

"Higher risk weighting on unsecured lending continues to be in place while the same on bank funding to NBFCs has been done away with. This is a positive step by RBI," says Rajiv Sabharwal, managing director (MD) and chief executive officer (CEO), Tata Capital.

In effect, the banking regulator has only partly restored the measures it took in November 2023.

Consumer credit exposures of commercial banks and NBFCs (excluding housing, education, vehicle loans and loans secured by gold and gold jewellery) still attract a weighting of 125 per cent.

This tells you how the banking regulator is reading the plot: it wants to support NBFCs with liquidity but is staying firm on its concerns around unsecured credit risk. Over the past few years, unsecured loans have grown at a compounded annual rate of 22-25 per cent, fuelling consumption, but also increasing systemic risk.

The latest move was speculated to be in the works from the day Sanjay Malhotra took charge at Mint Road. It was held that Malhotra's predecessor, Shaktikanta Das, may have gone overboard in pushing up the amount of capital that banks have to set aside on their exposures to their shadow banking cousins. Even as it forced the latter to reduce their reliance on bank lines of credit which had spiked; and broaden their sources of funding. Read together, a view gained ground that NBFCs had been starved of funding and this was affecting demand in the economy.

The Financial Stability Report: December 2024 (FSR: December 2024) has a few nuggets. The nudge to NBFCs to widen their finding sources has paid off. NBFCs were the largest issuers of bonds, with private placement being the preferred mode; volumes stood at ₹2.2 trillion in financial year 2023-24 (FY24), up from the ₹1.85 trillion in the previous year. Some of the bigger players upped their forex borrowings to diversify their sources of funds and contain overall costs. Here, the FSR strikes a cautionary note, "The rise in foreign currency borrowings could pose currency risks to these NBFCs to the extent they are unhedged." And given the concerns on the tariff front with the US, it would not be misplaced if the rupee were to gyrate. On the hedging front, an uptick in forward premia down the line may make the forex option altogether unattractive for NBFCs. Local financial firms have no natural hedge when it comes to forex risks.

Asset quality check

As Pankaj Naik, Director, India Ratings & Research views it, there is a moderation in the asset growth for the NBFCs, which implies that there would be lower requirement of funds on their part.

"One needs to be mindful of the asset quality pressures in the unsecured lending space that is prevalent in the NBFC portfolio. Hence, banks would be cautious in taking incremental exposure to NBFC space even when the risk weights have been normalised," he said.

This may hold true because of another reason. ICRA estimates the overall volume of securitisation of standard assets for Q3FY25 at ₹68,000 crore — largely in line with the volumes witnessed in the previous quarter. The securitisation volumes saw a sharp year-on-year jump of 80 per cent (volumes of ₹38,000 crore) in Q3FY24 as a few large private banks also sold part of their loan portfolio this route. This was the fallout of slack deposit growth with the systemic credit-deposit (CD) ratio inching up to 80 per cent, with some banks at well over 100 per cent.

The rating agency estimates securitisation volumes at ₹1.8 trillion for 9MFY25 against ₹1.4 trillion in the same period of FY24. It is unlikely that banks will support NBFCs all too soon given before matters settle on the CD ratio front apart from the ongoing stress in retail.

Bad loans worry

The FSR: December 2024 calls attention to the sharp rise in write-offs, especially among private banks "which could be partly masking worsening asset quality in this segment and dilution in underwriting standards".

Fresh accretion of bad loans in retail loan portfolios was also dominated by slippages in the unsecured loan book, with 51.9 per cent from unsecured loans as at end of September 2024.

"If anything, we are seeing more consumers seeking structured debt relief. As lenders tighten their collections and consumers struggle with higher EMIs, we have seen a steady increase in enrolments on our platform," says Ritesh Srivastava, founder and CEO of FREED, a retail debt relief platform.

Over 51.9 per cent of new bad loans in retail credit now stem from unsecured loans, reinforcing the need for structured solutions. Srivastava explains, "The challenge is that consumers did not anticipate this sudden squeeze. Easy credit was flowing, and now, with risk weights up and collections tightening, many are feeling the pinch."

The problem is compounded by the fact that many borrowers may be flitting between banks and NBFCs. The FSR does not throw light on this, but states that 11 per cent of borrowers originating a personal loan under ₹50,000, had an overdue personal loan. Over 60 per cent of them had availed more than three loans during 2024-25 so far. Moreover, nearly three-fifths of customers who have availed personal loans in Q2FY25 had "three live loans at the time of origination".

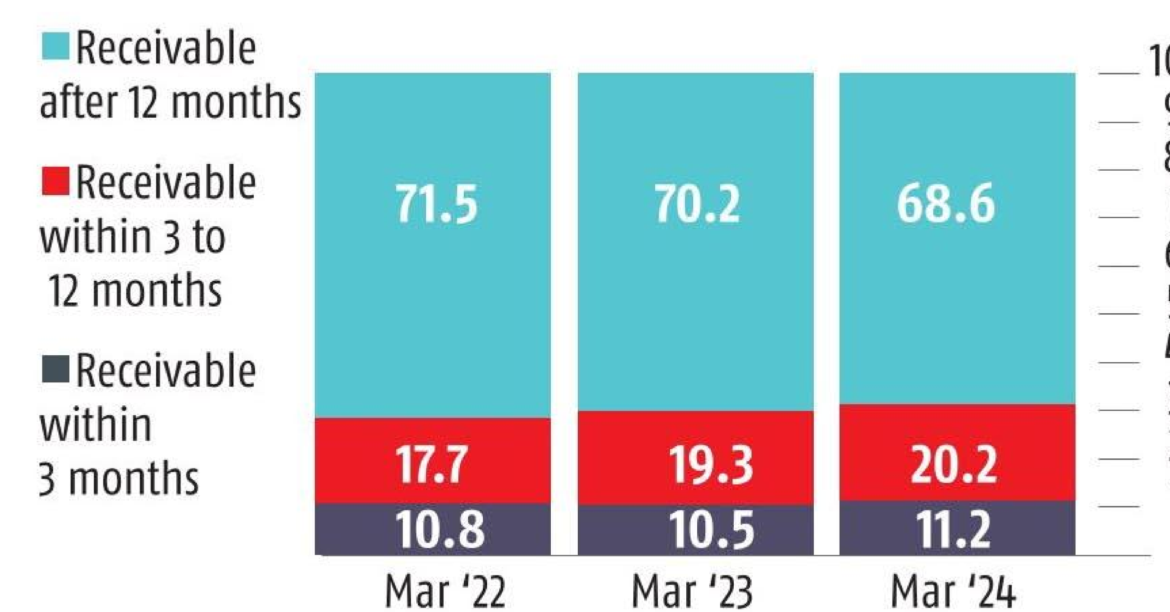
That said, more clarity on the retail book quality can be expected soon.

According to Bhavesh Jain, MD and CEO, TransUnion CIBIL, retaining higher risk weights on unsecured loans combined with the improved frequency of data reporting on fortnightly basis by credit institutions to credit bureaus, is a progressive move by the regulator. Earlier, if a customer has availed a loan from multiple lenders, the reporting of it would be reflected in CIC only after a 30-day period (the change became effective from January 25 this year).

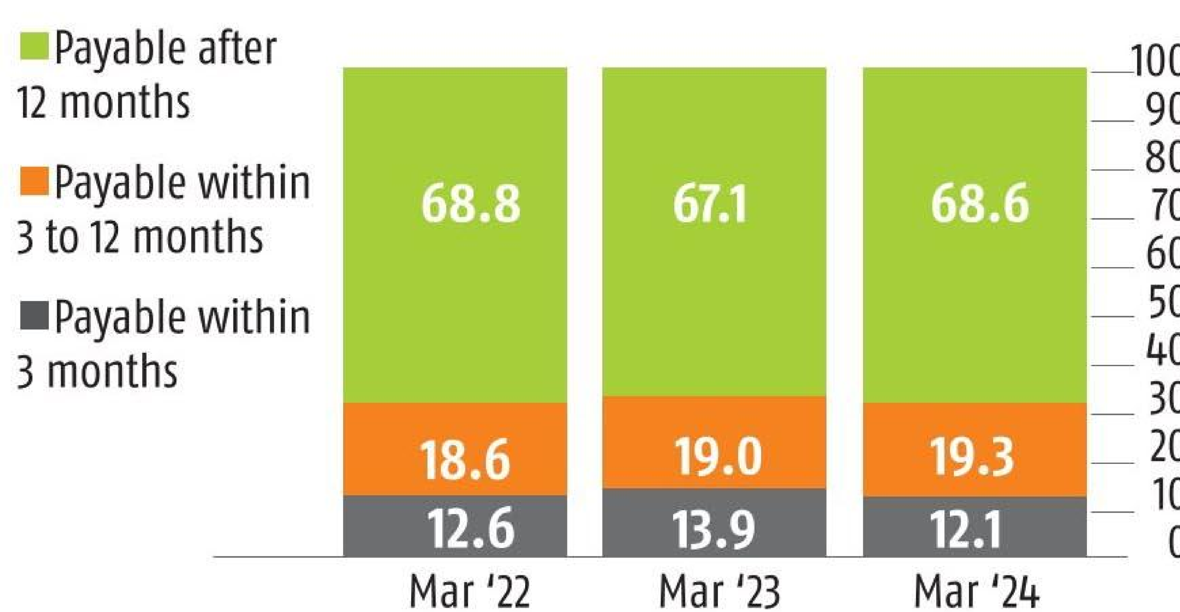
"It will give us a better sense of the stress on the system and lenders will get an early and timely update on the status of the accounts for better portfolio management," Jain said.

MATURITY PROFILES OF RECEIVABLES AND PAYABLES OF NBFCs

Loans and advances (share in %)



Borrowings (share in %)



Note: Data are provisional.

Source: Supervisory Returns, RBI

CREDIT SNAPSHOT

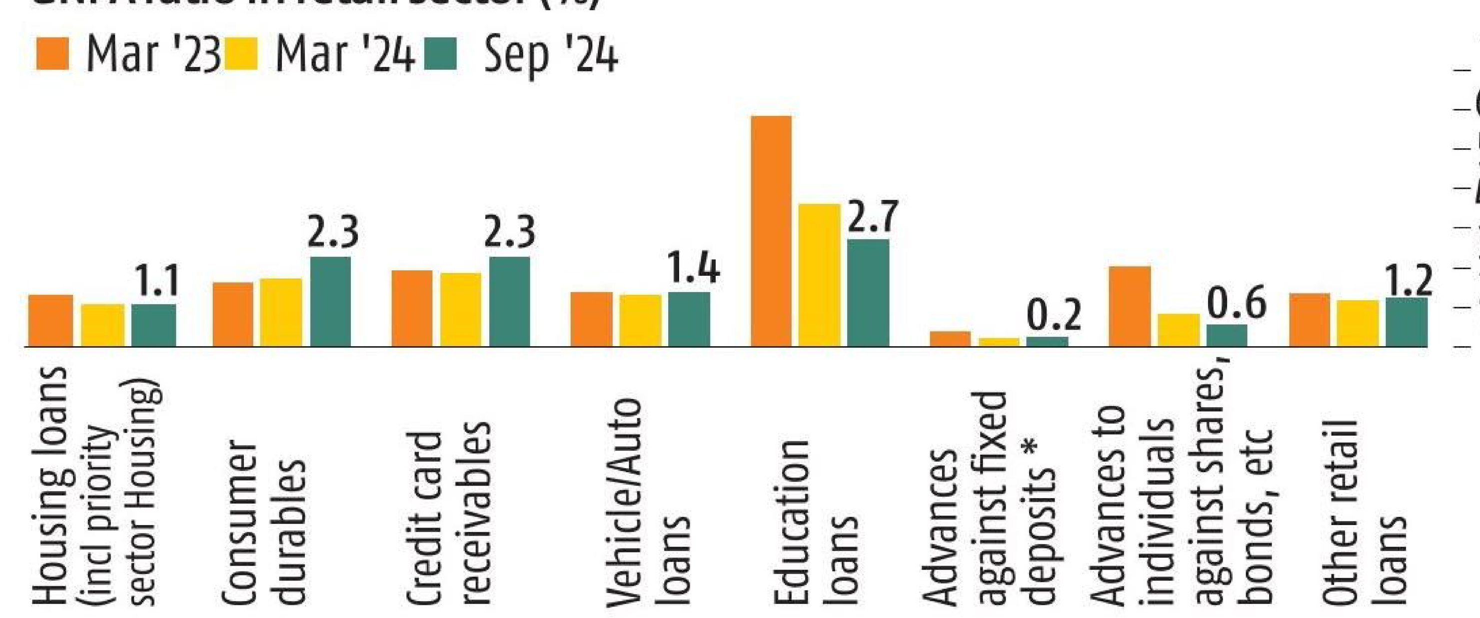
Growth in origination volumes (accounts)

Product	Qtr ended Sept 2023 (%)	Qtr ended Sept 2024 (%)
Home loan	3	-10
Loan against property	16	3
Auto loan	12	-3
Two-wheeler loan	19	4
Personal loan	32	11
Credit card	9	-24
Consumer durables loan	2	-6

Source: TransUnion Cibil

ASSET CHECK

GNPA ratio in retail sector (%)



*Including FCNR (B), etc.

Source: Off-site returns (domestic operations), RBI.