Press Release

NBFC and MFIs' overall funding gap to rise further to Rs.50,000-60,000 Cr

Lack of moratorium availability and banks' weak response to sector TLTRO aggravate liquidity concerns
Refinance from financial institutions or direct refinance from RBI will be the key

24 April, 2020

Further to Acuité Ratings & Research' s previous analysis of NBFC & MFI sector, we believe that the liquidity concerns have aggravated and a quick response is the need of the hour. **The funding gap is estimated to further increase to Rs. 15,000-25,000 Cr.** While RBI has provided a 3 month moratorium framework for borrowers of banks and NBFCs for March-May period, it is increasingly clear that all banks are not likely to grant such a moratorium for their NBFC or MFI exposures. Further, a 50% response in the first tranche of bids for RBI's TLTRO 2.0 indicates that banks are hesitant to take fresh exposures to the sector, particularly to small and mid-sized NBFCs including MFIs, at this juncture. **Thus, the refinance window of Rs. 50,000 Cr through government financial institutions such as SIDBI assumes significant relevance.**

In the opinion of Acuité Ratings, the lack of backup or alternative funding lines will have serious implications for the sustainability of the NBFC sector over the next 3 months as collections from the borrowers are likely to be limited in the April-May period. **Says Suman Chowdhury, Chief Analytical Officer, Acuité Ratings & Research *"We had undertaken an analysis of the top 11 retail NBFCs in India and estimated the funding gap for this group in Q1FY21 at Rs. 10,000-20,000 Cr with the expectation of moratorium availability from banks. Without the moratorium or partial moratorium from banks, the funding gap will increase further to Rs. 15,000-25,000 Cr. Clearly, the gap for the aggregate sector including MFIs in Q1 will be much higher at around Rs. 50,000 -60,000 Cr based on broad estimates."***

Although RBI announced TLTRO 2.0 for an amount of Rs. 50,000 Cr where at least 50% has to be specifically deployed in debt instruments of mid and small NBFC/MFIs, the initial response has been muted, reflecting the credit aversion in the banking sector. Against the auction amount of Rs. 25,000 Cr in the first tranche of TLTRO 2.0, only 14 bids for Rs 12,850 Cr has been received. Therefore, fresh funding or refinancing to the NBFC sector from TLTRO 2.0 is unlikely to exceed Rs. 10,000 Cr unless there is a significant change in the banks' response in the second tranche.

Acuité, therefore believes that the other part of the RBI stimulus provided for the sector i.e. the refinance window of Rs. 50,000 Cr through government financial institutions such as SIDBI will be critical. SIDBI, which has been allotted Rs. 15,000 Cr, has already announced schemes to provide liquidity support by extending short term loans to NBFCs and MFIs. While the refinance facility will be available to small and mid-sized lenders in the sector who provide loans to MSMEs, they need to be rated in the investment grade with a minimum networth of Rs. 20 Cr and with capital adequacy above the mandatory levels. This may provide some short term relief to the sector and enable some of the players to sustain their operations for another 3 months. However, if collections don't revive rapidly for the NBFCs and MFIs in particular within this period, the liquidity challenges may continue and will necessitate longer term funding.

Adds Mr. Chowdhury *"With limited response of the banks to TLTROs specifically for NBFCs and the refinance line from SIDBI to be primarily deployed for smaller NBFC/MFIs, Acuité foresees a significant liquidity challenge for the mid-rung NBFCs with AUMs in the range of Rs.5000-50,000 Cr. While large NBFCs with over Rs. 50,000 Cr AUMs may still continue to get fresh funds through TLTRO and even directly from banks and other domestic investors, there is a risk of a liquidity crisis in the mid segment of the NBFC sector if these players are not able to access alternative funding sources."*

It is understandable that banks and investors will have concerns on the asset quality and profitability of the sector over the next few quarters, given the impact of the slowdown aggravated by the Covid lockdown. Nevertheless, a lack of liquidity support in such a lockdown scenario may have longer term implications for the sustainability of the mid-size NBFC players who are now systemically important. In order to prevent any solvency crisis in the sector, RBI may consider a direct medium term financing window for the sector with appropriate terms and conditions or can consider a much higher refinancing line for financial institutions like SIDBI. Additionally, the government may explore providing a first loss guarantee up to a defined level for additional exposures of banks through TLTRO to address the credit concerns, as has been provided for securitisations transactions in the previous year.

About Acuité Ratings & Research Limited:

Acuité Ratings & Research Limited *(Erstwhile SMERA Ratings Limited)* is a full-service Credit Rating Agency registered with the Securities and Exchange Board of India (SEBI). The company received RBI Accreditation as an External Credit Assessment Institution (ECAI), for Bank Loan Ratings under BASEL-II norms in the year 2012. Since then, it has assigned more than 8,000 credit ratings to various securities, debt instruments and bank facilities of entities spread across the country and across a wide cross section of industries. It has its Registered and Head Office in BKC, Mumbai.

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