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# Future of NBFCs: Tighter norms, coexistence with banks

Five experts discuss the crisis in non-banking finance companies, their impact on the economy and what lies ahead

**What is the new Indiabulls story after the Lakshmi Vilas Bank merger was rejected?**

**Gagan Banga:** Businesses have to evolve and they have to keep evolving every 10-12 years. Indiabulls is an entrepreneurial setup. So version one of Indiabulls' lending business started in 2004 after our IPO where we raised all of ₹52 crore for an enterprise value of ₹250 crore. By 2008, we had built a balance sheet of around ₹15,000 crore. The financial crisis had some learnings for us and we de-grew to about ₹9,500 crore. And, and then over the last 10 years we grew that to ₹1.2 trillion. Now, having done that, which is 12-fold growth over the last 10 years, we have had to recalibrate.

**Your presentation mentions that you are rising from the ashes like the phoenix...**

**Banga:** The single biggest learning is that percentages after a certain size are not relevant, both on the asset and the liability side. You can't have a wholesale financed liability engine and also be doing wholesale loans. We had to recalibrate the business model. We've identified our strengths — distribution, large capital base and technology. When I say we are rising from the ashes like the phoenix, it's on the power of peo-

**If the country wants to do last mile financing at an efficient cost, NBFCs will be required and entrepreneurship will have to be encouraged**

**GAGAN BANGA**  
Vice Chairman & MD  
Indiabulls Housing Finance





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**Banking Annual**

ROUND TABLE



ple capital and equity capital. I am quite sure we will grow 12-fold in the next 10 years, like we did in the last 10 years.

**Is wholesale loan exposure a bigger problem for NBFCs, including housing financiers?**  
**Khushru Jijina:** We started in 2012-13 and because of the group's expertise in real estate, we started with wholesale and residential (lending) and then moved to commercial and non-real estate loans. We had announced our intention to go retail. But, when the Lehman moment happened for NBFCs, we had only a 1 per cent share of retail loans — our timing was wrong. The single largest lesson is that your book needs to be granular. In this last one year, the fact that we could replace our entire commercial papers (CPs) of ₹18,000 crore to ₹600 crore and to zero by November-end, shows that we are going towards granular liabilities.

**Are banks lending to NBFCs?**  
**Jijina:** Yes, but money is not available for growth — what we are getting is liquidity. Because the crisis has moved from one of liquidity to one of confidence now, there is just about enough liquidity for us to survive — to ensure that our existing projects are funded.

**A lot of NBFCs will become more originating and securitising type of balance sheets going forward, and for banks, it will be a big opportunity to use NBFCs' distribution networks**

**V SRINIVASA RANGAN**  
Executive Director, HDFC

**consultant?**  
**Sreedhar Vegesna:** The notion that a financial institution will never fail is a myth. It has happened in the past and it will happen in the future. Even in an extremely regulated environment, you will have situations where somebody will get the risk wrong and in that situation, you have to have an exit approach. And that exit approach in a financial institution cannot be the same as the general economy.

**The real villain of the piece is real estate...**  
**Vegesna:** One of the evolutions that we'll have to see in the marketplace is how do you allow NBFCs to move the liability away from the bundle of the asset and push it back to the bank after two-three years. We don't have the ability to take loans and move them around, which is different in other markets, where they have the ability to take short-term borrowing with short-term lending, and then pass it to somebody who's willing to have a

**What went wrong from your vantage point as a**



**NBFCs with no short-term loans or any governance issue are also suffering the same fate when it comes to liquidity**

**JASPAL BINDRA**  
Chairman, Centrum Group

longer exposure to that lending. These are product evolutions that will have to happen in our market.

**Centrum seems insulated because you're not too much into housing finance?**  
**Jaspal Bindra:** There are enough NBFCs that are pure, granular retail today, with very low leverage. But, I'm speaking on behalf of many others, which have no short-term borrowings or any evidence of corporate governance or any other control failure — and even they are suffering the same fate, when it comes to liquidity. I think the liquidity issue is a confidence failure across the sector. Just because somebody will change their model, I do not see why they will become more attractive and how the confidence will resurface.

**One of the primary reason for the NBFC crisis is weak regulations...**  
**V Srinivasa Rangan:** It started with IL&FS, where there was an asset-liability management (ALM) issue. Risk aversion started building, which also happened because there was no clarity on the distribution of money. Assets and cash flows were all frozen. ALM is very important and to what extent the short-term assets or short-term liabilities can finance the other side of the balance sheet. The asset side is always very illiquid; you can never get the type of liquidity on the

34 | Business Standard | DECEMBER 2019



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## Banking Annual

### R O U N D T A B L E



**Because the crisis has moved from one of liquidity to one of confidence now, there is just about enough liquidity for us to survive**

**KHUSHRU JIJINA**  
MD, Piramal Capital and Housing Finance

**Bindra:** The one thing that hasn't disappeared is the demand for credit. There is an unserved, underserved demand. If I just take the MSMEs (micro, small and medium enterprises), only 10 per cent of them have access to formal credit. Even if I add all the formal credit plus layer it with informal expensive credit, there is still a gap of ₹25 trillion. But, having said that, NBFCs have to change their governance and control standards. NBFCs have to collaborate, and this idea of "I will become a conglomerate and have 25 verticals within my shop" is over.

**Banga:** If the country wants to do last mile financing at an efficient cost without overburdening the customer with very high interest costs, NBFCs will have to be there and entrepreneurship in the financial system will have to be encouraged. The only way to do that is to have a very evolved regulatory system, where no one needs to doubt whether an AQR (asset quality review) is required or not. If an AQR is going to give confidence to the system, do it as of yesterday. But, please make sure that the regulations give good cover to the regulated entities and there is no room to doubt the numbers. This is a simple liquidity crisis, which has got extended to a crisis of confidence.

**Jijina:** There are areas of arbitrage — like funding for land acquisition, which banks are not permitted to do. When corporates see an acquisition opportunity, that is a time for NBFCs to come in. So, there will be niches.

**Rangan:** A lot of NBFCs would become more originating and sort of securitising type of balance sheets and for banks, it will be a big opportunity to use the distribution and underwriting network of NBFCs. It will become more like an asset management business rather than a balance sheet business. ■

**liabilities to match the assets in a very pure sense. You can't have the same set of cash flows coming in from the asset side to finance your liabilities. Diversification is also very important. We (HDFC) haven't been impacted much in this whole scheme of things, largely because our liabilities are quite diversified. We started accepting deposits since the late 1990s, and it has grown into a reasonable percentage of the overall liabilities.**

**Do you agree that the Reserve Bank of India (RBI) and the government were slow in recognising the gravity of the situation?**

**Rangan:** It was largely thought to be a one-institution problem and then became a sort of a credit aversion. The understanding or the acceptance of that was very delayed. I don't know whether liquidity is there in the system and whether liquidity is available to all players and segments.

**What is the way forward for NBFCs?**

**Vegesna:** The way forward is to continue to improve governance. Second is the ability of the regulator to take over where an institution has failed, identify it very quickly and merge it with a bank or another NBFC. The freedom to act needs to come into the regulation. The third is technology. How do you evolve,

**where you have a powerful NBFC which has the reach to customers, married with a technology solution that will revolutionise the way products are dispensed to the customer? That has to be thought through, as the NBFC five years from now will look very different. It will definitely look more like a tech company than just a traditional NBFC.**

**The notion that a financial institution will never fail is a myth. It has happened in the past and it will happen in the future**

**SREEDHAR VEGESNA**  
Partner, PwC India



36 Business Standard DECEMBER 2019