Banks' Advances to NBFCs Continues to Grow at a Robust Pace

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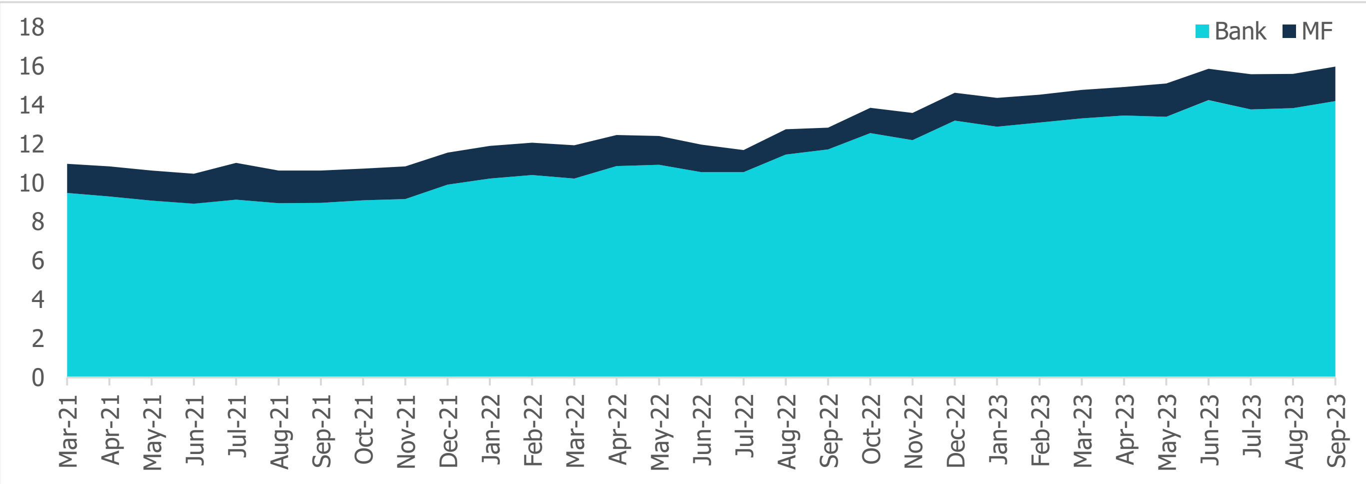
Synopsis

- The credit exposure of banks to Non-Banking Financial Companies (NBFCs) stood at Rs 14.2 lakh crore (pre-HDFC merger number) in September 2023, indicating a 26.3% year-on-year (y-o-y) growth. This expansion is indicative of the robust progress observed in NBFCs during the post-pandemic period. Furthermore, the proportion of NBFC exposure in relation to aggregate credit has risen from 8.9% in September 2022 to 9.4% in September 2023. On a month-on-month (m-o-m) basis, the amount rose by 2.6%.
- Meanwhile, the Mutual Fund (MF) debt exposure to NBFCs, including Commercial Papers (CPs) and Corporate Debt, witnessed an increase of 58.4% to 1.77 lakh crore in September 2023 with CPs remaining around the one lakh crore threshold. Large NBFCs focused on the capital market, while mid-sized and smaller NBFCs continued their reliance on the banking system as their primary source of funding. However, given the general credit risk aversion of MFs, the exposure to NBFCs, particularly those rated below the highest levels, is not expected to witness significant growth. Hence, the aggregate dependence of mid-sized NBFCs on the banking sector for funding is likely to remain high while larger NBFCs will continue to move towards the capital markets.
- Highlighting the relative size of their exposure to NBFCs, MFs' debt exposure to NBFCs touched 12.5% as a percentage of "Banks' advances to NBFCs" in September 2023 from 9.9% in September 2022 and 12.8% in September 2023.

Figure 1: Summary of Banks Loans and MFs NBFC Debt Exposure (Rs. lakh crore)



Source: RBI, SEBI

The data in Figure 1 does not include liquidity made available to NBFCs by banks via the securitisation route (direct assignment & pass-through certificates) and Treasury investments made by banks in the NBFCs' capital market issuances. Liquidity availed by NBFCs including HFCs through the securitisation route was approximately Rs 1.8 lakh crore for the twelve-month period ending September 2023.

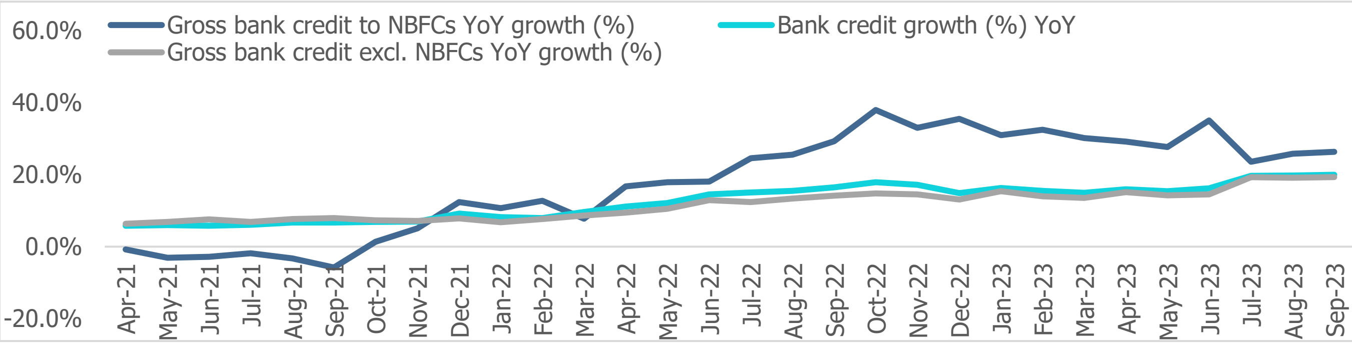
Figure 2: NBFC Debt Sources (Rs lakh crore)

	Feb-2018	Feb-2020	Sep-2023	Ab. Change (%)	
				vs. Feb-2018	vs. Feb-2020
Bank	3.90	8.40	14.20	263.9	69.0
MFs	2.31	1.64	1.77	-23.5	7.7
Total (Bank +MF)	**6.21**	**10.04**	**15.97**	**157.1**	**59.0**

Source: RBI, SEBI

Compared to February 2018 numbers, absolute bank lending to NBFCs has jumped to around 3.5x, meanwhile, MF exposure has reduced by 23.5% over the last five years due to risk aversion by mutual fund managers. Interestingly, MF exposure to NBFCs as a share of Debt Assets Under Management (AuM) has reduced from nearly 20% in the later part of 2018 to around 13%, on the other hand, the share of banks' advances to NBFCs as a share of aggregate advances has doubled from around 4.5% in February 2018 to close to 9.5% in September 2023.

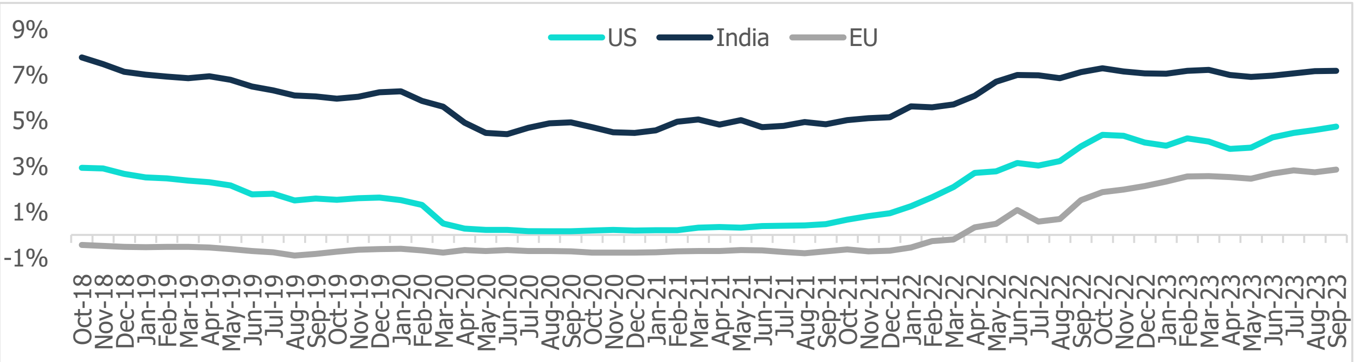
Figure 3: Growth in Bank Credit to NBFCs vis-à-vis overall Bank Credit Growth



Source: RBI

The credit extended by banks to NBFCs has exhibited a consistent upward trend over the last five years and continued its acceleration along with the phased reopening of economies after the Covid-19 pandemic. This growth momentum further accelerated during FY23 and has continued in first half of FY24. Further, after the merger of HDFC Limited with HDFC Bank, the quantum of outstanding exposure of banks to NBFCs had reduced, albeit maintaining the y-o-y growth rate. In September 2023, the quantum of outstanding exposure has reached the pre-merger level. This trend can be primarily ascribed to the expansion in the AuM of NBFCs.

Figure 4: Three-Year G Sec Yield Narrows: India, US and EU

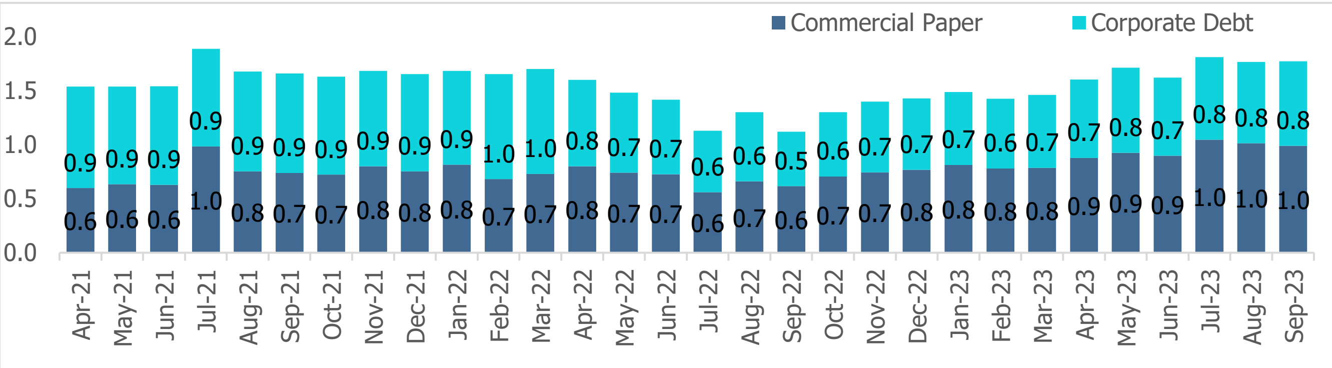


Source: CMIE, St. Louis Fed, Eurostat: Note: Weighted average Yield on Residual Maturity of Government of India Dated Securities in Secondary Market, Market Yield on U.S. Treasury Securities at 3-Year Constant Maturity, Quoted on an Investment Basis, Percent, Monthly, Not Seasonally Adjusted, Spot rate yield curve of AAA-rated euro area central government bonds

Additionally, the higher upswing in global interest rates compared to the Indian market also played a pivotal role. As the above figure shows, the spread between domestic and US and EU g-sec yield has narrowed and when combined with hedging and other costs has reduced the attractiveness of overseas borrowings. This divergence in interest rate movements led to a decline in the utilisation of external commercial borrowings (ECBs) by NBFCs. Meanwhile, the domestic capital market has witnessed some traction. Larger and better-rated NBFCs have been accessing the capital market given that nearly 75% of the issuers in September 2023 have been from the BFSI sector and over 90% of the aggregate issuers have been either AA or AAA-rated entities.

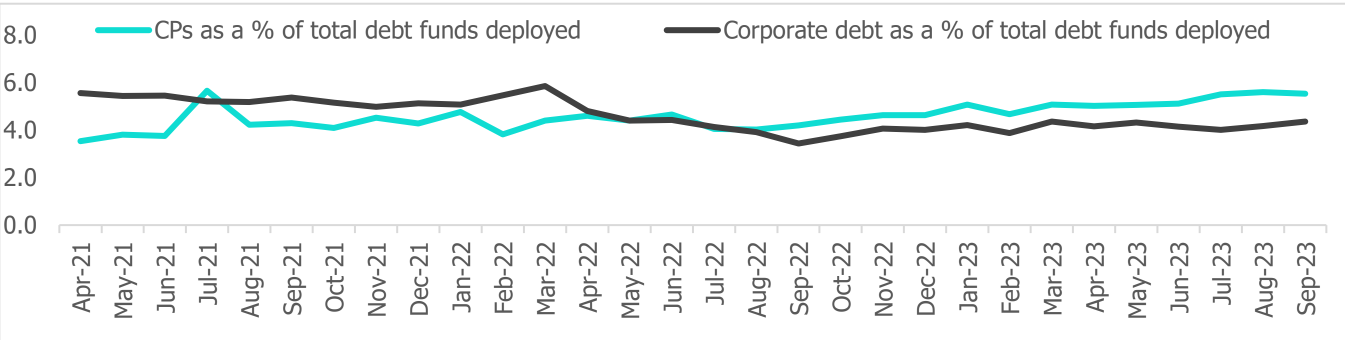
NBFCs are the largest net borrowers of funds from the financial system and banks continue to account for the largest share of the same. Meanwhile, if the funding mix is considered, the share of SCBs would be even higher loan asset sell-down (direct assignments) as a funding source is included in the funding mix. The liability composition of larger NBFCs has started to change a bit as they tap the capital market, while mid-sized and smaller NBFCs unable to access the capital market at cost-effective rates have continued their reliance on the banking system as the primary source of funding.

Figure 5: Total Debt Funds Deployed in NBFCs via CPs and Corporate Debt (Rs lakh crore)



Investment in corporate debt of NBFCs rose by 55.1% y-o-y to Rs.0.78 lakh crore in September 2023. Meanwhile, the share of total corporate debt to NBFCs expanded to 4.4% in September 2023 from 3.4% in September 2022. Meanwhile, the outstanding investments in CPs of NBFCs remained around the Rs one lakh crore mark, increasing by 61% y-o-y to Rs.0.99 lakh crore in September 2023 but declined by 2.2% sequentially from August 2023. CPs (less than 90 days) rose by 54.6% y-o-y to Rs.0.67 lakh crore in September 2023, CPs (90 days to 182 days) increased by 76.8% to Rs.0.24 lakh crore, and CPs (more than 6 months) increased by over 77.6% to Rs.0.08 lakh crore in the reporting period.

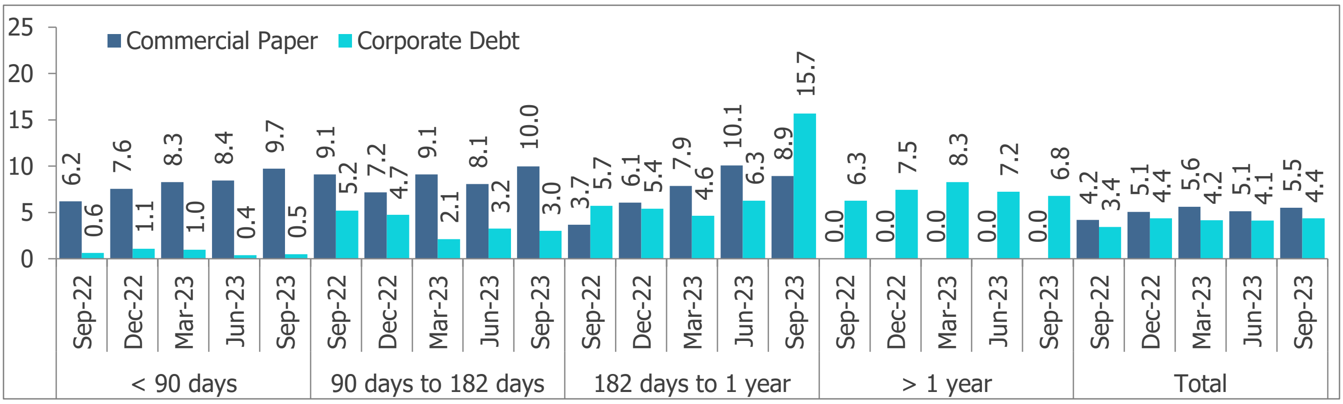
Figure 6: Total Debt Funds Deployed in NBFCs via CPs and Corporate Debt (%)



Source: SEBI

The percentage share of funds deployed by MFs in CPs as a percentage of banks' exposure to the NBFCs stood at 7.0% in September 2023, increasing by around 150 bps y-o-y. The proportion of CPs (less than 90 days) deployed in NBFCs as a percentage of aggregate funds deployed for less than 90 days reached 9.7% in September 2023 as compared to 6.2% over a year ago period, the percentage of CPs (90 days to 182 days) rose to 9.98% from 9.1% over a year ago, and CPs (greater than six months) percentage grew to 8.9% in September 2023 as compared to 3.7% over a year-ago period.

Figure 7: Trend in Proportion of CPs & CD Deployed in NBFCs as a % of Debt Funds by Duration



Source: SEBI

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