

## Chapter IV

### Non-Banking Financial Institutions

#### Introduction

4.1 All India Financial Institutions (AIFIs), Non-Banking Financial Companies (NBFCs) and Primary Dealers (PDs) form three important segments of the Non-Banking Financial Institutions (NBFIs) sector in India that are regulated and supervised by the Reserve Bank. AIFIs constitute institutional mechanism entrusted with providing sector-specific long-term financing. NBFCs comprising mostly private sector institutions, provide a variety of financial services including equipment leasing, hire purchase, loans, and investments. Primary dealers (PDs) play a crucial role in fostering both the primary and secondary government securities markets. The operational and financial performance of NBFIs sector is presented in this chapter.

#### All India financial institutions (AIFIs)

4.2 Currently, the four AIFIs regulated and supervised by the Reserve Bank are Export-Import Bank of India (EXIM Bank), National Bank for Agriculture and Rural Development (NABARD), National Housing Bank (NHB) and Small Industries Development Bank of India (SIDBI). They play a salutary role in the financial markets through credit extension and refinancing operation activities and cater to the long-term financing needs of the industrial sector.

#### Financial performance

##### Balance sheet of AIFIs

4.3 The consolidated balance sheet of the AIFIs expanded by 9 per cent during 2014-15 reflecting moderation from double-digit expansion in the previous couple of years (Table 4.1). Loans and

advances posted a growth of 11.3 per cent while deposits and borrowings increased by 17 and 9.7 per cent, respectively during 2014-15. AIFIs, during the year, raised short-term funds mainly by floating commercial papers, which are capped under the umbrella limit<sup>1</sup>.

**Table 4.1: Liabilities and assets of AIFIs**

(₹million)

Item	2014	2015	Percentage Variation
<b>Liabilities</b>			
1. Capital	93594 (2.06)	109594 (2.21)	17.1
2. Reserves	520298 (11.45)	566533 (11.44)	8.9
3. Bonds and Debentures	1141801 (25.13)	1059890 (21.41)	-7.2
4. Deposits	1865420 (41.05)	2183064 (44.09)	17.0
5. Borrowings	659456 (14.51)	723318 (14.61)	9.7
6. Other Liabilities	263486 (5.80)	308423 (6.23)	17.0
<b>Total Liabilities or Assets</b>	<b>4544054</b>	<b>4950822</b>	<b>9.0</b>
<b>Assets</b>			
1. Cash and Bank Balances	73364 (1.61)	78213 (1.58)	6.7
2. Investments	243345 (5.36)	256028 (5.17)	5.2
3. Loans and Advances	3911090 (86.07)	4352598 (87.92)	11.3
4. Bills Discounted/ Rediscounted	58385 (1.28)	21067 (0.43)	-64.0
5. Fixed Assets	6253 (0.14)	6586 (0.13)	5.3
6. Other Assets	251617 (5.54)	236330 (4.77)	-6.1

**Notes:** i. Data pertain to four FIs, viz., EXIM Bank, NABARD, NHB and SIDBI. Data for EXIM Bank, NABARD and SIDBI for end March, while end June for NHB.

ii. Figures in parentheses are percentages to total liabilities or assets.

**Source:** Audited OSMOS Returns of EXIM Bank, NABARD and SIDBI for end-March 2014 and 2015, respectively. Audited OSMOS Returns of NHB end June 2014 and 2015, respectively.

<sup>1</sup> AIFIs are allowed to mobilise resources within the overall 'umbrella limit', which is linked to the net owned funds (NOF) of the FI concerned as per its latest audited balance sheet. The umbrella limit is applicable for five instruments viz., term deposits, term money borrowings, certificates of deposits (CDs), commercial papers (CPs) and inter-corporate deposits.

Table 4.2: Financial performance of all India financial institutions

(₹ million)

	2013-14	2014-15	Variation	
			Amount	Percentage
<b>A) Income (a + b)</b>	<b>325765</b>	<b>350113</b>	<b>24348</b>	<b>7.5</b>
a) Interest Income	308887 (94.82)	333694 (95.31)	24807	8.0
b) Non-Interest Income	16878 (5.18)	16419 (4.69)	- 459	- 2.7
<b>B) Expenditure (a + b)</b>	<b>236803</b>	<b>262646</b>	<b>25843</b>	<b>10.9</b>
a) Interest Expenditure	219322 (92.62)	243332 (92.65)	24010	10.9
b) Operating Expenses	17480 (7.38)	19314 (7.35)	1834	10.5
of which Wage Bill	12257	13624	1367	11.1
<b>C) Profit</b>				
Operating Profit (Profit Before Tax)	61330	78339	17009	27.7
Net Profit (Profit After Tax)	41751	52930	11179	26.7

**Note:** (i) Figures in parentheses are percentages to total income/expenditure.  
(ii) Absolute figures rounded-off.

**Source:** 1. Audited OSMOS Returns of EXIM Bank, NABARD and SIDBI for end March 2014 and 2015, respectively.  
2. Audited OSMOS Returns of NHB for end June 2014 and 2015, respectively.

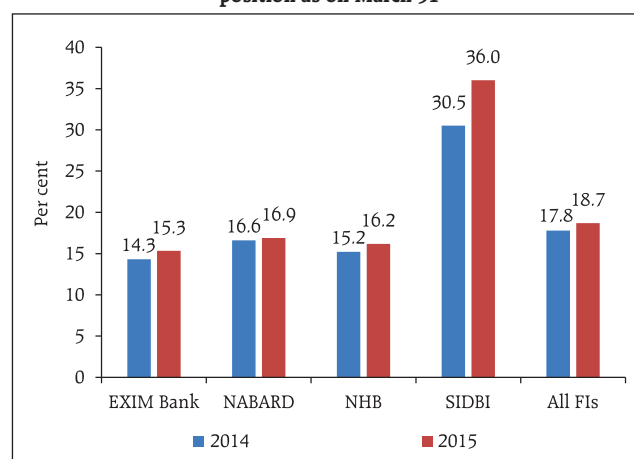
### Financial indicators

4.4 AIFIs posted modest growth in income during 2014-15 owing to low growth in interest income and decline in non-interest income even while income from bill discounting/ rediscounting shrunk substantially (Table 4.2). However, AIFIs fared better on the profitability front as both their operating profit and net profit increased significantly during the year.

4.5 AIFIs maintained capital in excess of the stipulated norm and their capital adequacy position comparatively improved during the year (Chart 4.1).

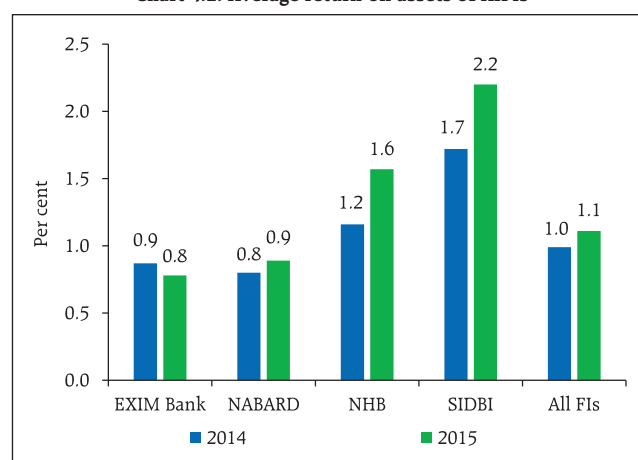
4.6 On the whole, the FIs enjoyed higher returns on their assets during the year barring EXIM Bank whose return on assets was marginally lower (Chart 4.2).

Chart 4.1: Capital to risk (weighted) assets ratio (CRAR) of AIFIs - position as on March 31



Source: RBI supervisory returns.

Chart 4.2: Average return on assets of AIFIs



Note: Data for NHB for end-June.

Source: RBI supervisory returns.

4.7 The asset quality of FIs deteriorated marginally and net non-performing advances (NPAs) as percentage to loans increased from 0.19 per cent in 2013-14 to 0.26 per cent in 2014-15 (Chart 4.3). Nevertheless, the stressed asset position of these four FIs remained comparatively better than that of the commercial banks and other NBFCs.

### Non-banking financial companies (NBFCs)

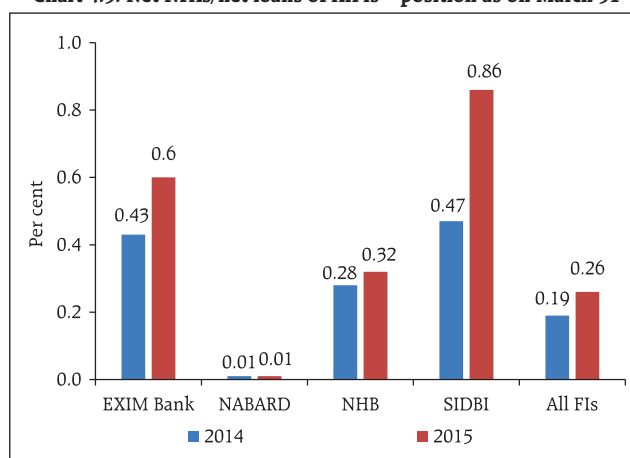
4.8 Based on their liability structure, the NBFCs are classified into two broad categories: (a) Deposit taking NBFCs, and (b) Non-deposit taking NBFCs. As on March 31, 2015, there were 11,842 NBFCs registered with the Reserve Bank; out of which 220 were deposit-taking (NBFCs-D) and 11,622 were non-deposit taking (NBFCs-ND) entities. The two existing residual Non-Banking Finance Companies (RNBCs)<sup>2</sup> are in the process of winding up their businesses.

4.9 The role of NBFC sector in the Indian financial system has become critical in terms of its size, spread and niche areas of operations. Many of the larger NBFCs have grown bigger and become more connected with other financial entities, necessitating periodical review of the regulatory framework for this sector. During the year, the Reserve Bank, with a view to addressing the regulatory gaps, arbitrage and risks associated with NBFCs, initiated a host of measures to strengthen regulation and supervision of NBFCs and harmonise their regulations with those of the banks in a phased manner as also to foster financial stability.

### Deposit-taking NBFCs (NBFCs-D)

4.10 The Reserve Bank, as part of deliberate policy, has been discouraging the NBFCs from engaging in deposit mobilisation activities, with a view to protecting depositors' interests as also fostering financial stability. The regulations for the NBFCs-D have been strengthened so that only the sound and well-functioning entities remain in business.

Chart 4.3: Net NPAs/net loans of AIFIs – position as on March 31



Note: Data for NHB for end-June.

Source: RBI supervisory returns.

## Financial performance

### Balance sheet of deposit-taking NBFCs

4.11 The balance sheet of NBFCs-D expanded by 2.1 per cent during the year (Table 4.3). Loans and advances, which constituted close to three-fourth of

Table 4.3: Consolidated balance sheet of NBFCs-D (as on March 31)

(₹ billion)

Items	2014	2015 P	Percentage Variation
1. Share Capital	33	32	-0.7
2. Reserves and Surplus	274	276	0.9
3. Public Deposits	260	275	5.8
4. Debentures	417	408	-2.1
5. Bank Borrowings	520	551	5.8
6. Borrowings from FIs	16	16	2.6
7. Inter-Corporate Borrowings	1	2	32.7
8. Commercial Paper	93	78	-16.6
9. Borrowings from Government	38	38	-1.0
10. Subordinated Debts	79	78	-2.2
11. Other Borrowings	153	170	11.1
<b>Total Liabilities/Assets</b>	<b>1885</b>	<b>1925</b>	<b>2.1</b>
1. Loans and Advances	1585	1601	1.0
2. Hire Purchase and Lease Assets	46	39	-14.8
3. Investments	58	77	32.8
4. Other Assets	195	205	5.1

P: Provisional.

Note: Absolute figures rounded-off. Percentage variation is based on precise numbers.

Source: Quarterly returns of NBFCs-D.

<sup>2</sup> RNBCs in the process of winding up are: Peerless General Finance and Investment Ltd. and Sahara India Financial Corporation Ltd. (SIFCL).

their assets, rose marginally whereas investment activities of NBFCs-D witnessed a sharp rise during the year. On the liability side, the expansion was mainly in terms of public deposits, and bank borrowings. Borrowings from banks still constituted the largest source of funding for NBFCs-D. Mobilisation of funds through debentures, which constituted the second biggest source of funding, declined during the year. Borrowing through commercial papers also declined sharply during the year.

### Financial indicators

4.12 As compared to the previous year, growth in profitability declined during 2014-15 which *inter alia* may be attributed to increased interest payment burden and higher operating expenses (Chart 4.4).

### Asset quality of NBFCs-D

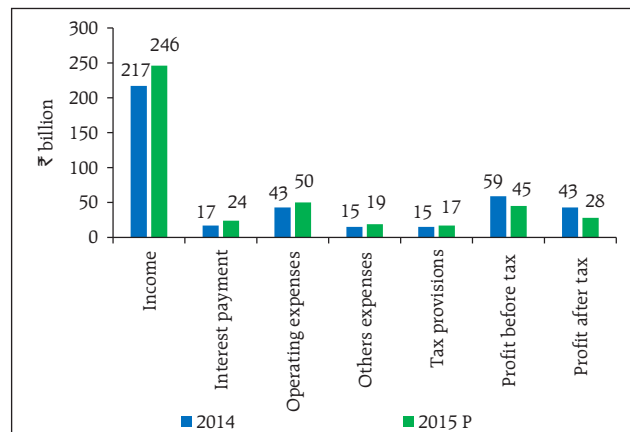
4.13 Asset quality of NBFCs-D deteriorated as both gross and net NPAs increased during 2014-15 (Chart 4.5). Category-wise, deterioration in asset quality was more in respect of the Asset Finance Companies (AFCs) as compared to the Loan Companies (LCs)<sup>3</sup>.

### Non-deposit taking systemically important NBFCs (NBFCs-ND-SI)

#### Financial performance

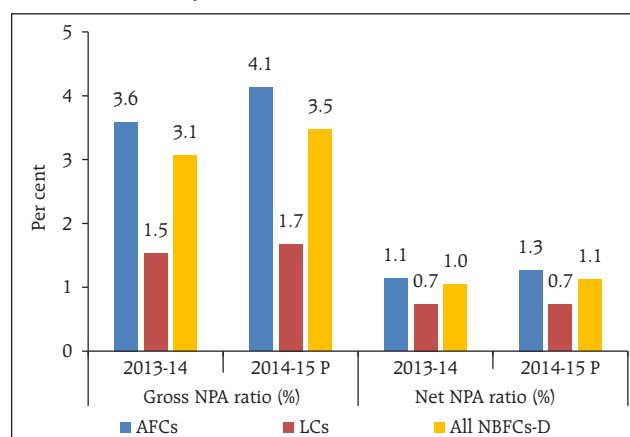
4.14 Non-deposit taking NBFCs with an asset size of ₹1 billion or more were being classified as systemically important NBFCs (NBFCs-ND-SI) till November 2014. Since then, an upward revision in the asset size criterion for classifying NBFCs-ND-SI<sup>4</sup> has been effected, which now stands at ₹5 billion. During 2014-15, the balance sheet of NBFCs-ND-SI expanded significantly on the back of marked growth in disbursement of loans and advances on the asset side and sharp rise in borrowings on the liability side (Table 4.4).

Chart 4.4: Select financial parameters of NBFCs-D – position as on March 31



Source: RBI supervisory returns.

Chart 4.5: Gross NPA and net NPA of NBFCs-D



Source: RBI supervisory returns.

Table 4.4: Consolidated balance sheet of NBFCs-ND-SI-position as on March 31

Item	₹ billion		
	2014	2015 P	Variation (Per cent)
1	2	3	4
1. Share Capital	638	685	7.4
2. Reserves and Surplus	2311	2613	13.1
3. Total Borrowings	8669	10177	17.4
4. Current Liabilities and Provisions	608	691	13.6
<b>Total Liabilities/ Total Assets</b>	<b>12226</b>	<b>14166</b>	<b>15.9</b>
1. Loans and Advances	8273	9555	15.5
2. Hire Purchase Assets	895	985	10.1
3. Investments	1888	2267	20.1
4. Other Assets	1170	1359	16.2

P: Provisional.

Note: Data presented here pertain to 418 entities, which have consistently reported data for end March 2014 and 2015 respectively and accounted for more than 95 per cent of the total assets of the NBFCs-ND-SI sector.

Source: Monthly returns of NBFCs-ND-SI (₹1 billion and above).

<sup>3</sup> Asset finance company (AFC): AFC is a non-bank financial company, carrying on the principal business of financing of physical assets. Investment company. Loan company (LC): LC is non-bank financial company, carrying on the principal business of providing loans or advances for any activity other than its own but does not include AFC.

<sup>4</sup> For the sake of comparability, however, in the present analysis, old definition of NBFCs-ND-SI has been considered.

4.15 Loans and advances extended by NBFCs-ND-SI posted significant growth at 15.5 per cent during 2014-15, in contrast to the slowdown in commercial bank's non-food credit during the same period (Chart 4.6). Strong growth in credit extended by the NBFC - Infrastructure finance companies (IFCs), microfinance companies and loan companies contributed to sturdy growth in the loan portfolio of NBFCs-ND-SI. Among the sectors, infrastructure, medium and large-scale industries, and the transport sectors contributed to strong growth in credit off-take of the NBFCs-ND-SI.

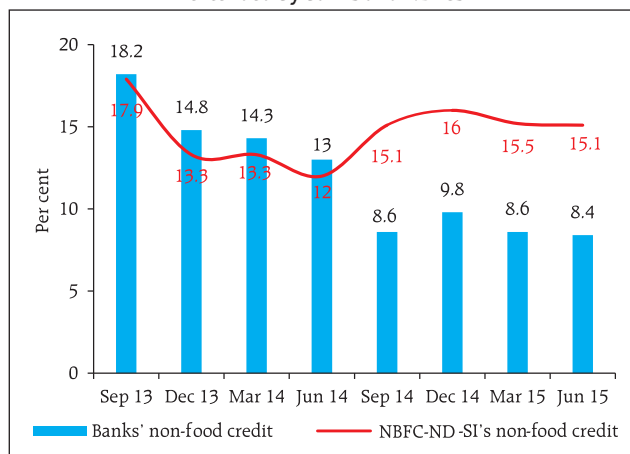
4.16 During 2014-15, NBFCs-ND-SI raised funds mainly through debentures and commercial papers. Borrowings from banks, which earlier constituted the main source of funding, has been progressively reduced. A notable feature is the rising exposure of mutual funds to the financial instruments floated mainly by the NBFC-IFCs, LCs and NBFC-Micro Finance Institutions (NBFC-MFIs).

#### Financial indicators

4.17 Profitability of the NBFCs-ND-SI improved significantly as at end-March 2015 (Chart 4.7). Net profit as a ratio to total income remained in double-digits and higher than last year's level.

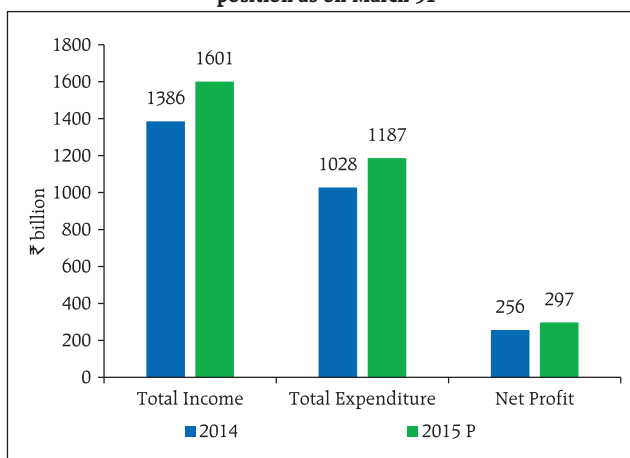
4.18 Nevertheless, asset quality of systemically important NBFCs continued to deteriorate and the NPA ratio rose marginally compared to the previous year (Chart 4.8). Amongst the NBFCs-ND-SI, LCs accounted for the major chunk of NPAs followed by NBFC-IFCs and AFCs as at end-March 2015. The asset quality of the NBFC-MFIs witnessed some improvement *albeit* it still remained at an elevated level.

**Chart 4.6: Comparative growth (y-o-y) in credit extended by banks and NBFCs**



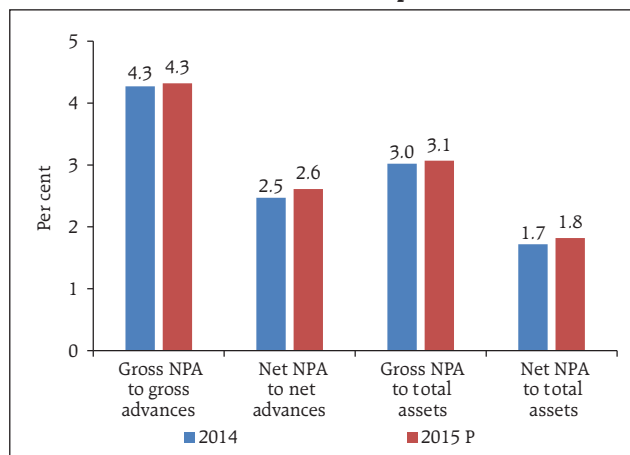
**Note:** Data pertains to NBFCs-ND-SI with asset size of ₹1 billion and above.  
**Source:** RBI.

**Chart 4.7: Financial performance of NBFCs-ND-SI - position as on March 31**



P: Provisional.  
**Source:** RBI supervisory returns.

**Chart 4.8: NPA ratios of NBFCs-ND-SI - position as on March 31**



P: Provisional.  
**Source:** RBI supervisory returns.

4.19 NPAs of the NBFCs-ND-SI sector were primarily concentrated in infrastructure sector, transport operator segment, and medium and large scale industries. However, the systemically important NBFCs remained well-capitalised. The capital adequacy ratio of these entities remained far above the mandated level of 15 per cent.

### Primary dealers (PDs)

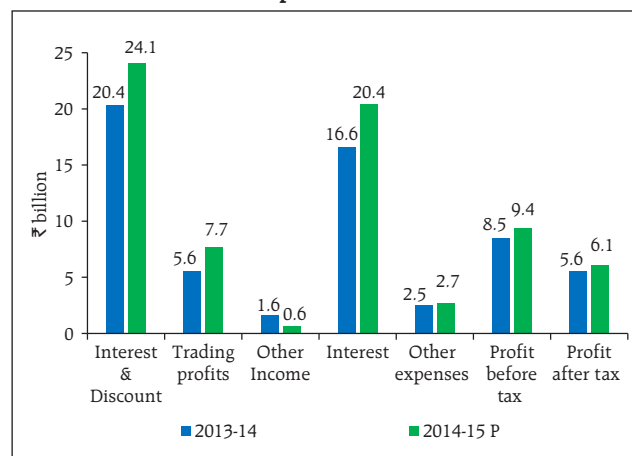
4.20 As on March 31, 2015, 20 Primary Dealers (PDs) were operating in Indian financial market. Of these, 13 were bank-PDs while seven were standalone PDs. All the PDs achieved a higher success ratio (bids accepted to bidding commitment) than the previous year and this remained way above the mandated ratio of 40 per cent during 2014-15. In the auctions of dated securities, the share of the PDs (bids accepted to the securities issued) increased marginally during 2014-15 to 51.8 per cent. Devolvement pressure on the PDs remained comparatively lower during the year. Partial devolvement on the PDs took place on two instances involving ₹52.7 billion during 2014-15 as compared to 12 instances for ₹174.5 billion during 2013-14.

### Financial performance of standalone primary dealers (PDs)

4.21 All the seven standalone PDs posted profit during 2014-15. Profitability increased due to softening of yields during the year. (Chart 4.9).

4.22 Standalone PDs held more risk-weighted assets during the year (Chart 4.10). The capital adequacy position of the PDs declined during the year to 39.6 per cent from 48.7 per cent as at end of March 2014. However, their capital adequacy position was well above the regulatory stipulation of 15 per cent. The PDs were able to meet all their primary and secondary market regulatory requirements during the period.

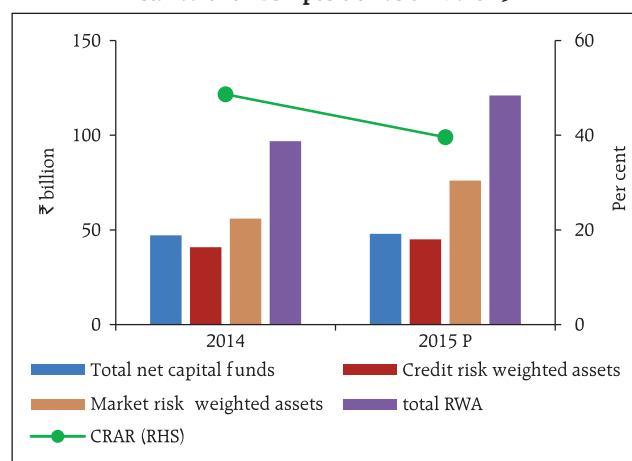
Chart 4.9: Financial performance of standalone PDs



P: Provisional.

Source: RBI supervisory returns.

Chart 4.10: Capital and risk weighted asset position of standalone PDs – position as on March 31



Source: RBI Supervisory Returns.

### Overall assessment

4.23 The dynamics of the NBFCs sector is reflective of its evolving role in niche areas of specialised services. Operationally, the sector remained relatively stronger *vis-à-vis* the commercial banks in terms of capital adequacy and profitability. There has also been certain amount of consolidation in the NBFCs space, with some larger-sized NBFCs having grown bigger and becoming well-connected with other financial entities, which has financial stability implications. Asset quality of the entire NBFIs sector also suffered deterioration in recent years.

4.24 In order to address the issue of recovery of bad loans, bigger NBFCs, with an asset size of ₹5 billion and above, have been proposed to be brought under the SARFAESI Act, 2002<sup>5</sup>. With a view to address the regulatory gaps and arbitrage owing to differentiated regulation for the NBFCs *vis-à-vis* commercial banks and risks associated with NBFCs, the Reserve Bank has revised regulatory framework. The revised regulatory framework, put in place in November 2014, aimed at addressing gaps in regulations of NBFCs and harmonising regulation with that of the commercial banks. Some of the important changes *inter alia* include raising of net owned funds (NOF) for the NBFCs to ₹10 million by March 2016

and ₹20 million by March 2017, rating requirement for all unrated deposit-taking AFCs by March 31, 2016 for being eligible for acceptance of public deposits, fixing of threshold of ₹5 billion for all the NBFCs-ND for being considered systemically important, and harmonisation of the asset classification norms for NBFCs-ND-SI and NBFCs-D in line with that of banks, in a phased manner. The entire regulatory framework was revised with a view to transforming over time to an activity-based regulation of NBFCs while ensuring that NBFCs having low risk profiles would be lightly regulated.

4.25 Notwithstanding such interventions, bringing the credit intermediation activities of a number of small entities, organised and unorganised, which operate as shadow banking entities outside regulatory oversight, within the regulatory jurisdiction remains a challenge. The Reserve Bank has been, from time to time, through its outreach, sensitisation programmes and public notices, sensitising public not to fall prey to such entities. To deal with delinquent and unauthorised entities, State Level Coordination Committee (SLCC) was reconstituted in May 2014 with active state level intervention to facilitate regular sharing of market intelligence and effective coordinated timely action.

<sup>5</sup> Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002.