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NBFC

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RBI's Covid-19 measures positive but half-hearted

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RBI has announced key relief measures for NBFCs today, viz. targeted long-term repo operations (TLTRO) 2.0, special refinance facilities for All India Financial Institutions (AIFIs), and a one-year extension for real estate loans. Though the measures are welcome, we think banks will conservatively deploy monies only in NBFCs that offer comfort on credit and on commercial viability. Given the likelihood of selective deployment, we believe the regulator should step in to assume the burden of credit risk.

Banks will be selective in TLTRO 2.0: Based on our interactions with treasury officials of various PSU banks, we expect lively bidding for TLTRO 2.0. Banks will most likely deploy at least 50% of these funds (a) towards NBFCs rated between BBB- and AA- and (b) only in cases where it makes commercial sense. We see a strong likelihood of banks charging 600-700bps over repo rate to NBFCs and MFIs. Further, deployment will likely be limited to entities with longstanding relationships and strong credit comfort.

Similar conservative approach likely in AIFI refinancing: AIFIs such as NABARD, SIDBI and NHB have been permitted special refinance facilities of Rs 250bn, Rs 150bn and Rs 100bn respectively. We believe this additional funding would have a salutary effect on the refinancing liabilities of NBFCs, MFIs and HFCs. At the same time, AIFIs will be highly cautious while assessing credit risk and will price in their risk for on-lending operations.

Breather on asset recognition/real estate loans: RBI announced that NBFCs will not have to treat moratorium accounts as impaired accounts under Ind-AS. We believe this will allow lenders to create additional provision buffers against these exposures, which can be later used for any delinquencies. NBFCs have also been permitted to extend commercial real estate loans by a year from the date of commencement of commercial operations (DCCO). This should provide relief to NBFCs as well as the real estate sector.

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Key RBI measures

Targeted long-term repo operations 2.0

In order to channel liquidity to small and midsized corporates, including non-banking financial companies (NBFC) and micro finance institutions (MFI), that have been impacted by Covid-19 disruptions, RBI has decided to conduct a second round of targeted long-term repo operations at the policy repo rate for tenors up to three years – these operations will be for a total amount of up to Rs 500bn to begin with, in tranches of appropriate sizes.

The funds availed under TLTRO 2.0 are to be deployed in investment-grade bonds, commercial paper (CP) and non-convertible debentures (NCD) of NBFCs. At least 50% of the total funds availed shall be apportioned as below:

- 10% in securities/instruments issued by MFIs,
- 15% in securities/instruments issued by NBFCs with asset size of Rs 5bn and below, and
- 25% in securities/instruments issued by NBFCs with asset size between Rs 5bn and Rs 50bn.

Investments made under this facility will be classified as held-to-maturity (HTM) even in excess of 25% of the total investment permitted in the HTM portfolio. Exposures under TLTRO 2.0 will not be reckoned under the large exposure framework (LEF). Funds availed of would have to be deployed within 30 working days from the date of the operation.

Our view: Based on our interactions with treasury officials of various PSU banks, we expect lively bidding for TLTRO 2.0. Banks will most likely deploy at least 50% of these funds (a) towards NBFCs rated between BBB- and AA- and (b) only in cases where it makes commercial sense. We see a strong likelihood of banks charging 600-700bps over repo rate to NBFCs and MFIs. Further, deployment will likely be limited to entities with longstanding relationships and strong credit comfort.

Refinancing facilities for All India Financial Institutions

AIFIs such as the National Bank for Agriculture and Rural Development (NABARD), the Small Industries Development Bank of India (SIDBI) and the National Housing Bank (NHB) are facing difficulties in raising resources from the market.

Accordingly, RBI has decided to provide special refinance facilities for a total amount of Rs 500bn to NABARD, SIDBI and NHB to enable them to meet sectoral credit needs. This will comprise Rs 250bn to NABARD for refinancing regional rural banks, cooperative banks and MFIs; Rs 150bn to SIDBI for on-lending/refinancing; and Rs 100bn to NHB for supporting housing finance companies (HFC). Advances under this facility will be charged at the RBI's policy repo rate prevailing at the time of disbursal.

Our view: We believe this additional funding would have a salutary effect on the refinancing liabilities of NBFCs, MFIs and HFCs. However, AIFIs will be cautious while assessing credit risk and will price in their risk for on-lending operations.

Breather on asset quality recognition

In respect of all accounts for which lending institutions decide to grant moratorium or deferment, and which were standard as on 1 Mar 2020, the 90-day NPA norm shall exclude the moratorium period, i.e., there would be an asset classification standstill for such accounts from 1 March to 31 May 2020.

NBFCs, which are required to comply with Indian Accounting Standards (IndAS), may be steered by the guidelines duly approved by their boards and as per advisories of the Institute of Chartered Accountants of India (ICAI) in recognition of impairments. In other words, NBFCs have flexibility under the prescribed accounting standards to consider such relief to their borrowers.

Our view: NBFCs will be able to create additional provision buffers against these exposures, which can later be used for any delinquencies.

Extension of resolution timeline

For large accounts under default, an additional 20% provision has to be made if resolution is not completed within 210 days. Recognising the challenges to resolution of stressed assets in the current volatile environment, the central bank has decided that the period for the resolution plan shall be extended by 90 days.

Our view: This measure will benefit large NBFCs/HFCs and prove helpful in creating provisioning buffers for large accounts.

Extension of NBFC loans to commercial real estate projects

In line with banks, NBFCs have now been permitted to extend the DCCO by a year in respect of loans to commercial real estate projects delayed for reasons beyond the control of promoters, without treating the same as restructuring– this is over and above the one-year extension permitted in the normal course.

Our view: We believe this will provide relief to NBFCs as well as the real estate sector.

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BUY – Expected return >+15%

ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

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