

NBFC loans to MSMEs may get dearer

ANUPREKSHA JAIN

Mumbai, 27 May

Loans to micro, small, and medium enterprises (MSMEs) may get dearer as non-banking financial companies (NBFCs) are likely to make higher provisions for loans extended under credit guarantee scheme following the Reserve Bank of India's (RBI) digital lending norms released earlier this month, according to NBFC officials. Most loans to MSMEs are covered under credit guarantee schemes.

According to the latest RBI guidelines, regulated entities (RE) cannot enter into default loss guarantee (DLG) arrangements on the loans covered by the credit

guarantee schemes. Currently, zero risk weight is applicable to these loans which are sanctioned under credit guarantee schemes.

A DLG is a contractual arrangement between the regulated entity and another entity, under which the latter guarantees to compensate the regulated entity for the loss due to default up to a certain percentage of the loan portfolio of the RE.

Loan service providers (LSPs) provide DLGs to non-banking companies for loans covered under credit guarantee schemes to compensate if a loan turns into a bad loan. Post these restrictions, NBFCs will have to bear loss on their own as LSPs cannot provide loss guarantee to these NBFCs, of-

LATEST RBI NORMS STATED THAT REGULATED ENTITIES CANNOT ENTER INTO DEFAULT LOSS GUARANTEE ARRANGEMENTS ON THE LOANS COVERED BY CREDIT GUARANTEE SCHEMES

officials said. DLG, in most cases, is fixed at five per cent.

"If a rate for loans given under the credit guarantee scheme was 12 per cent, it will be 15 per cent now because we (an NBFC) have to undertake the loss if it converts into a bad loan. We have to make provisions and the result will be an increase in the lending rates," said a senior official with a NBFC.

Credit guarantee scheme was

launched to strengthen the credit delivery system and to ensure credit flow to the MSME sector and other underserved sectors. Credit Guarantee Funds Trust for Micro and Small Enterprises provides credit guarantees to banks and NBFCs, reducing lending risks for micro and small enterprises. Loans under credit guarantee schemes usually have competitive interest. It enables financial institutions to lend to high-risk businesses, making loans more accessible for MSMEs.

"MSME loans will become expensive by the amount we are losing up on DLGs or may be higher than this. There has been a push from the government side to increase lending towards MSMEs,

therefore, everyone is focused right now on MSME lending but it is a sensitive segment. Now we are not getting any DLGs, we have to cover them under guarantee schemes, leading to higher provisions," said another NBFC official.

Analysts said this could cause some challenges to financial institutions as higher provisioning will impact their net profits.

As on March 31 2024, MSMEs received 8.9 per cent of the total NBFC credit, up from 7.9 per cent in 2023 and 6.5 per cent in 2022. In total credit extended by banks and NBFCs to MSMEs, NBFCs expanded their share to 11.7 per cent in FY24, with those engaged in services cornering a larger share, the RBI noted.