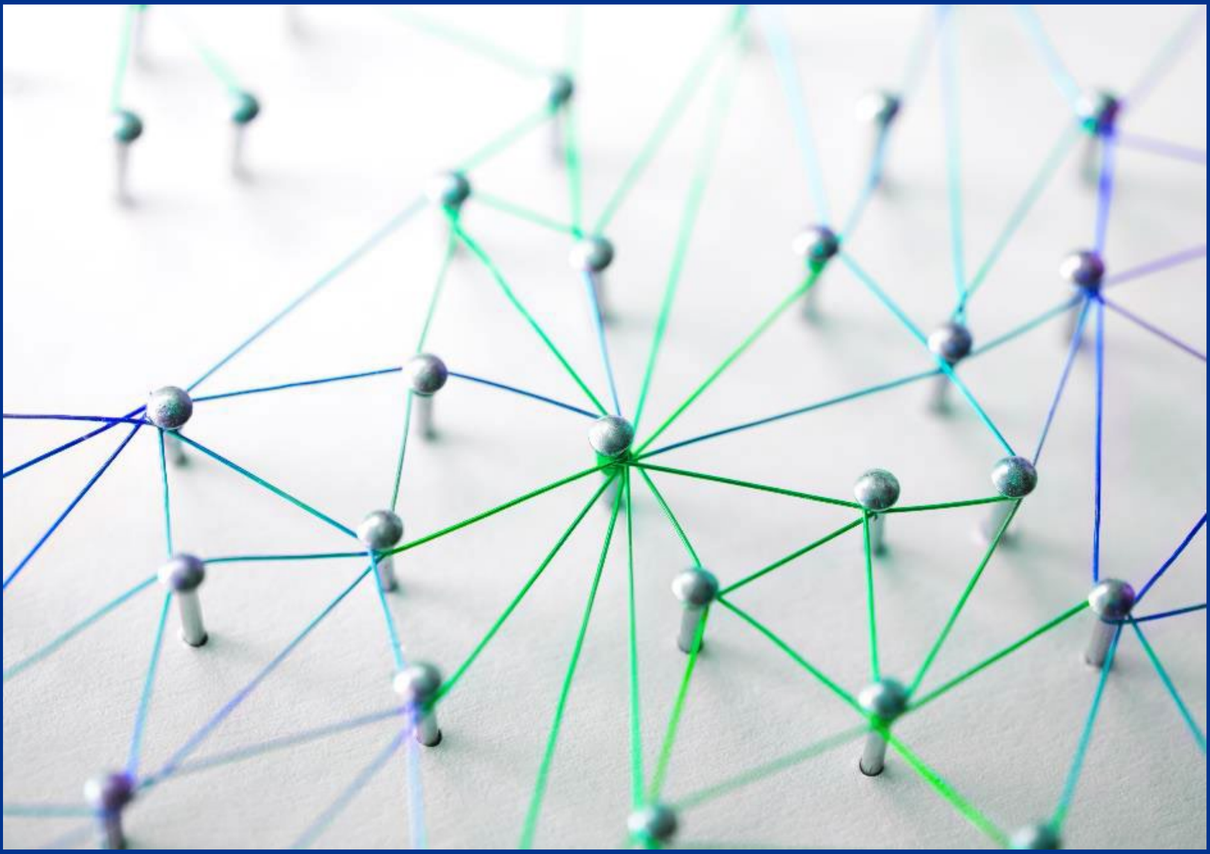
Role of NBFCs and HFCs in driving sustainable GDP growth in India



November 2022

Foreword

Financial institutions play a major role in ensuring economic stability and delivering government supportive measures to households and businesses at time of crises, including the recent outbreak of COVID-19 pandemic. While the world has largely emerged out of the pandemic, the economic and political aftershocks of an on-going geopolitical conflict has stalled countries' post-pandemic recoveries and accelerated the normalisation of monetary and fiscal policies after years of unprecedented stimulus measures. Inflation in the U.S. has spiralled to its highest in the last four decades[1], while Europe is embarking on a dark and hostile winter owing to an energy crisis that came through following Russia's invasion into Ukraine. Meanwhile, a stronger U.S. dollar amid tightening macroeconomic conditions has led to massive outflows of capital in emerging markets.

A major silver lining, amid the growing darkness around the world, has been the stronger-than-expected economic recovery in India, which is set to end 2022 as Asia's fastest growing economy. The country's calibrated approach in tackling the pandemic, especially restraining the temptations of big stimulus measures, unlike its developed peers, has put her on a strong footing to tackle the ensuing economic and financial challenges. Although India is not completely immune to the global economic turmoil and other uncertainties, including the situation in Russia and trajectory of the virus, her strong economic barebones will continue to help her sail through the upcoming challenges and drive the momentum into 2023.

The economic recovery in India has been reinforced by a revival in investment sentiment and healthy consumer spending, which has put the country on the heels of a new credit cycle following years of tepid growth. While the banks were hindered by high levels of bad debt, non-banking financial companies (NBFCs) were hit by severe liquidity challenges following the collapse of a few major players in the market. The introduction of supportive measures, such as Emergency Credit Line Guarantee Scheme (ECLGS), and increased capital spending by the government have helped the financial firms recover from the pandemic struggles and expand their balance sheets. The recovery bodes well for the country, especially at a time when the government is aiming to push its affordable housing initiatives as well as create a favorable economic situation for micro, small and medium enterprises (MSMEs) to reap benefits from the disruption in global supply chains.

In this report, KPMG in India and Confederation of Indian Industry (CII) highlight the pivotal role that NBFCs, including housing finance and asset finance companies, play in the country's credit infrastructure, especially in delivering last-mile connectivity to the vast unorganized sector that lacks access to bank credit. From enabling housing and vehicle loans to several aspirational buyers to meeting the working capital needs of small businesses, NBFCs have grown significantly over the past decade by harnessing digital solutions, flexible underwriting practices and leveraging data analytics for personalized products and offerings. With the country's 'Atmanirbhar Bharat' aspirations and USD5 trillion target by 2025, NBFCs have a major role in filling the gaps in our lending landscape. The report also explores how regulation, Environmental, Social, and Governance (ESG) and emerging technological trends, such as peer-to-peer lending, are shaping the industry.

Mr Chandrajit Banerjee
Director General, CII
Confederation of Indian Industry (CII)

Sanjay Doshi
Partner and Head-FS Advisory
KPMG in India

Table of contents

Overall credit market

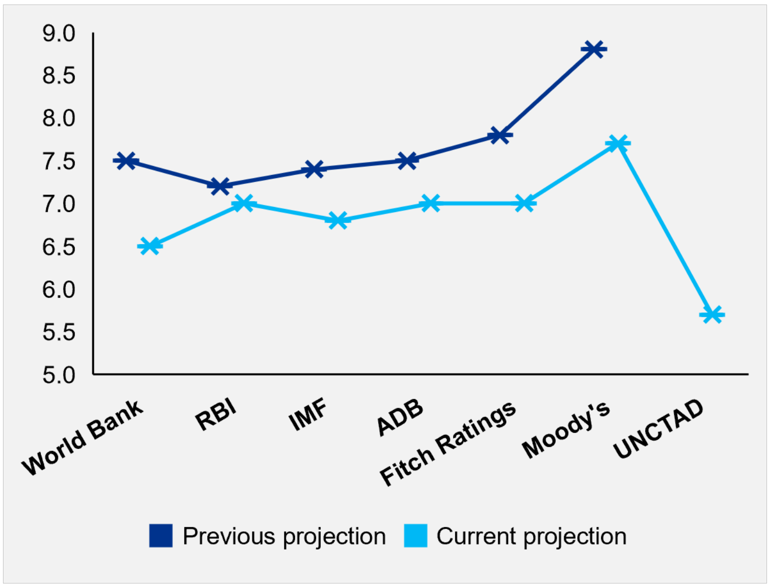
India on a positive path to post pandemic recovery

India is expected to become Asia's fastest growing economy by the end of 2023 with a forecasted growth of about 7 per cent year on year[6].

The Indian economy is on a strong growth trajectory, driven by structural reforms, young working population, increasing urbanization and technology driven transformation. From digital ID to real-time instant payment, the country has leapfrogged in digital revolution, and has undertaken strong efforts in energy transition, especially with regards to the development of renewable energy.

India has evolved from being among the fragile five economies[7] in 2014 to a preferred investment market, at a time when global supply chains are being repositioned following rising geopolitical tensions. Although the country will not be immune to the recessionary trends around the developed world, it will continue to do relatively better than most economies in 2023.

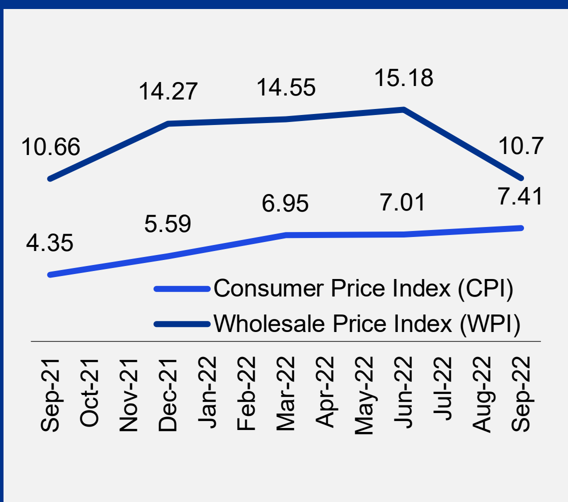
India GDP growth forecasts for 2022-2023 (%)[1]



Strong fundamentals of Indian economy[2]

USD538 bn	USD847 bn	USD2.6 trillion	134.6
Foreign exchange reserves as of 23 September 2022	Cumulative FDI[5] inflows between April 2000 to March 2022	Domestic credit as of September 2022	Index of Industrial Production (IIP) for July 2022

Inflation trends in India (%)[3]



FDI flows in India (USD billion)[4]

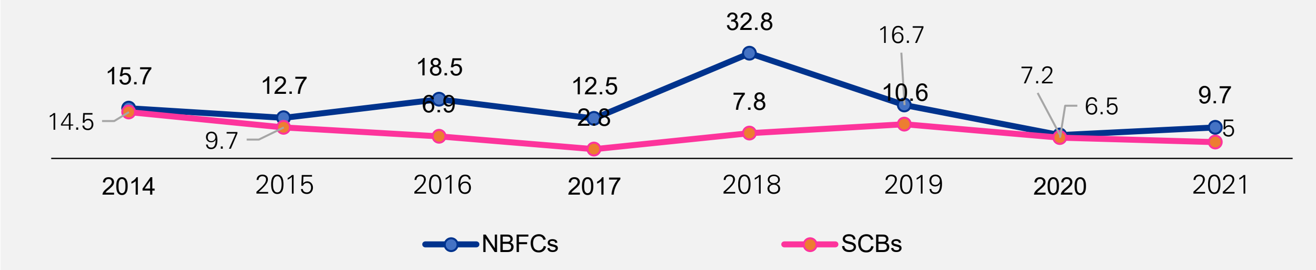
Note: a. RBI stands for Reserve Bank Of India
b. IMF stands for International Monetary Fund
c. ADB stands for Asian Development Bank
d. FICCI stands for Federation of Indian Chambers Commerce and Industry
e. UNCTAD stands for United Nations Conference for Trade and Development

Source: 1. India GDP growth forecasts for fiscal 2022/2023, World Bank; Industry Reports, UNCTAD, IMF, ADB, FICCI, Moody's
2. Indian Economy, IBEF; CEIC Data
3. Inflation Rate In India, Forbes
4. India is on track to attract USD100 billion FDI this fiscal, says government, The Hindu; Indian Economy, IBEF,
5. Foreign direct Investment, IBEF,
6. KPMG in India's analysis 2022
7. India is one of the economies in world's 'Fragile Five', NDTV, all accessed in November 2022

Credit appetite - On a strong recovery trail

Following the setbacks of COVID-19, high levels of bad debt and liquidity stress, uptake of credit has picked up strongly, aided by macroeconomic drivers and able policy support by the government.

Credit growth of Banks and NBFCs (%)[4]



11.3 million MSMEs have availed collateral-free loans worth INR 2.32 trillion till June 2022[1]

01 Credit lines to the rescue of MSMEs[5]

- Emergency Credit Line Guarantee Scheme (ECLGS) and other relief measure such as debt moratoriums introduced during COVID-19 ensured flow of credit to the vulnerable micro, small and medium enterprises
- The scheme was launched with an initial guarantee cover at INR3 trillion and was later enhanced to INR4.5 trillion and further to INR5 trillion
- The government has extended the scheme till March 2023.

The government has set aside capital expenditure of INR 7.5 trillion for fiscal 2022/2023[2]

02 Make in India push

- Government has been relentlessly pushing for capital expenditure on infrastructure projects, such as expansion of highways and modernization of railways; and on energy transition projects, such as solar development.
- Production Linked Incentive (PLI) scheme has given an impetus to local manufacturing, and hence creating more credit demand from businesses and MSMEs.
- Buoyed by these initiatives amid rising inflation, working capital needs have gone up for MSMEs.

S&P Global India Manufacturing PMI[a] rose to 55.3 in October from 55.1 in September 2022[3]

03 Urban consumption and capacity expansion

- Urban consumption has driven the recovery in credit, as demand for consumer durables, such as automobiles, picked up strongly after the pandemic setback.
- Despite global headwinds, local factory output has been on a rising trend and order books are also improving for sectors other than infrastructure.
- Credit to the private sector has made a recovery after two straight years of decline amid the pandemic outbreak and deleveraging campaign.

Note: a. PMI stands for Purchasing Managers' Index; b SCBs refer to scheduled commercial banks
Source: 1. 1.19 crore MSMEs, other businesses benefitted till June 2022, Financial Express
2. Big spending bazooka: Govt to make capital expenditure of Rs 7.5 lakh crore, Financial Express, Link
3. Global India Manufacturing PMI, S&P
4. NBFCs, RBI
5. Cabinet approves enhancement in the corpus of Emergency Credit Line Guarantee Scheme for increasing the limit of admissible guarantees, PIB, all accessed in November 2022

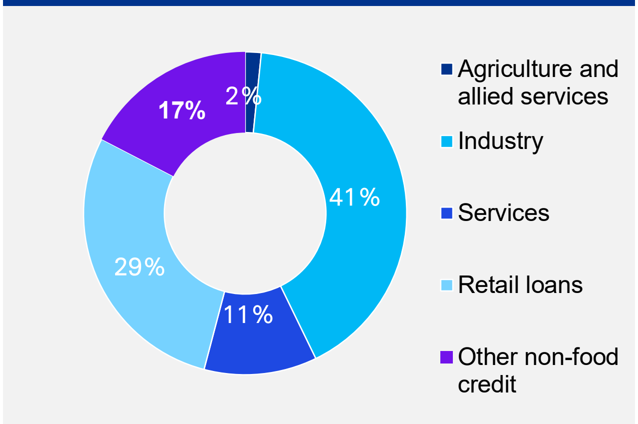
NBFCs – Filling the gaps in financing story

For decades, NBFCs have pursued businesses and customers that banks ignored, expanding their stake in overall credit pie through efficient last mile delivery and innovation of products.

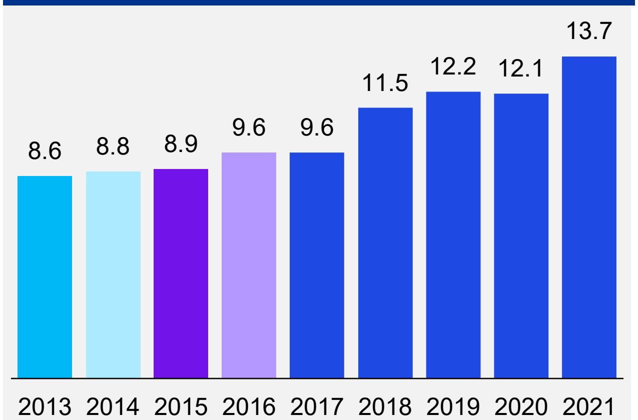
With exposure towards banking as well as capital markets, NBFCs have emerged as an essential part of India's financial ecosystem over the past two decades. Over the years, NBFCs have become an important source of credit for low-income households and businesses that do not have collateral or sufficient credit profile for bank credit. Through wide network of branches, digitalization and innovative solutions, they have grown their presence among MSMEs and consumers, especially for financing vehicles, housing and gold. They all have actively embraced technology and digital tools to bring down the transaction costs, speed up the loan disbursal process and leverage alternate data and practices to improve risk assessment and underwriting. Some of them have also grown larger in size than many banks and have been one of the major stock outperformers.

Following a recent period of sluggish years amid liquidity stress, failure of major players and pandemic hit, Indian NBFCs have bounced back strongly with higher capital levels, reasonable stability in delinquency accounts and larger balance sheets. Stronger risk assessment frameworks, government support, such as debt moratorium and liquidity enhancement measures, and broader economic revival have helped them tide through these challenges and pursue innovative strategies to meet evolving opportunities. They will play a major role in financing India's transition from the world's fifth largest to third largest economy by the end of this decade.

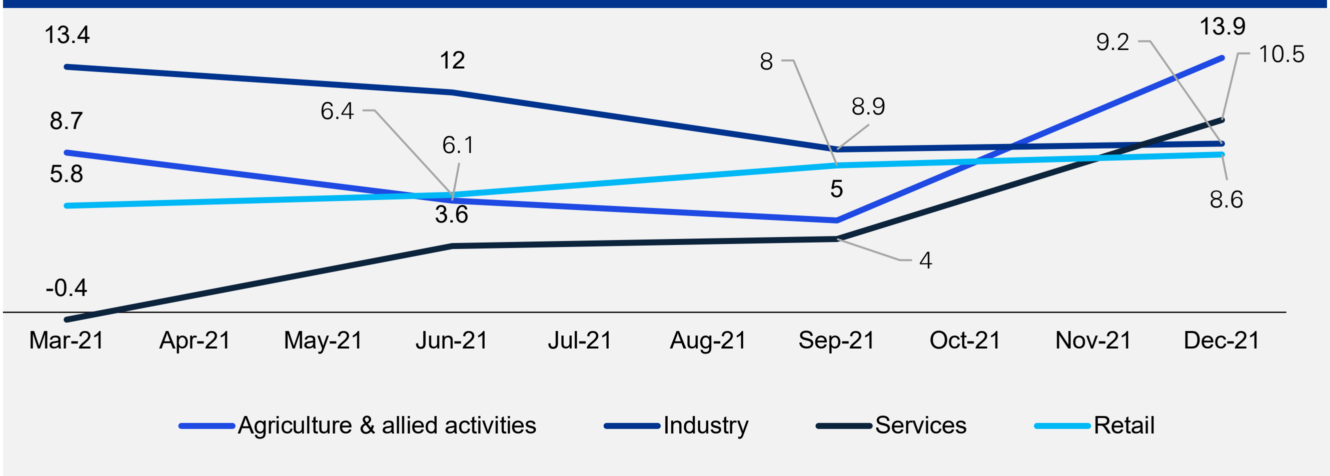
Sectoral split of NBFCs' credit in December 2021 (%) [1]



NBFCs' credit to GDP from March 2013 to March 2021 (%) [2]



Sectoral growth trend of NBFCs' credit in 2021 (%) [1]



Note: a. Fiscal year runs from April to March.
Source: 1.A Steady Ship in Choppy Waters: An Analysis of the NBFC Sector in Recent Times, RBI

2. Nonbanking financial companies (NBFCs) credit to GDP ratio from financial year 2013 to 2021, Statista, accessed in November 2022

01

Housing finance

An overview of the real estate industry

Increasing focus on home ownership by millennials is expected to drive real estate sector growth.

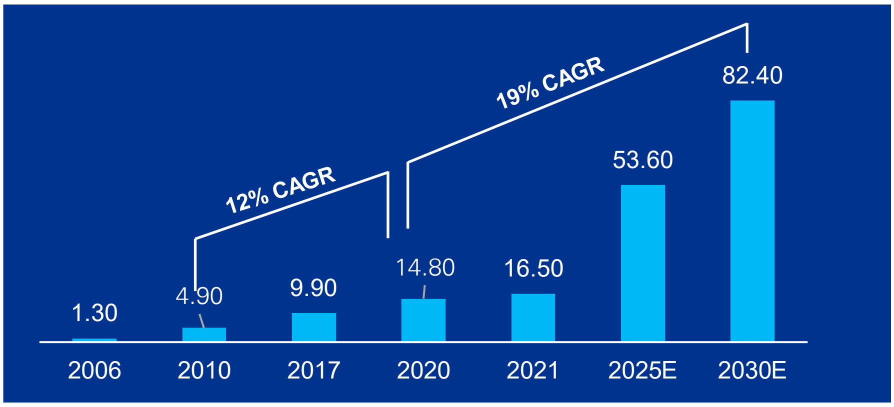
India's real estate sector is expected to grow at a CAGR of 9.6 per cent from 2020 to 2027[1], owing to the significant demand in real estate industry post COVID-19. The asset mix in the portfolios of the investors has been witnessing a change owing to the paradigm shift from traditional asset classes to newer classes including logistics and data centers. This change is primarily driven by factors including increasing focus on home ownership by millennials owing to work from home ultimately leading to higher demand in tier II and III cities, with higher focus on health and well-being amenities.

As of 1H21, the residential segment contributed approximately 80 per cent[2] in the real estate market. The demand has primarily been growing due to increased urbanization and rising household income wherein India is amongst top ten price appreciating housing markets globally.

53%
of the sales were witnessed from Mumbai and Pune[3]

INR1.3 trillion[3]
worth of opportunity to be created after SEBI approved REIT[1] platform in coming years

Real estate market size (INR trillions)

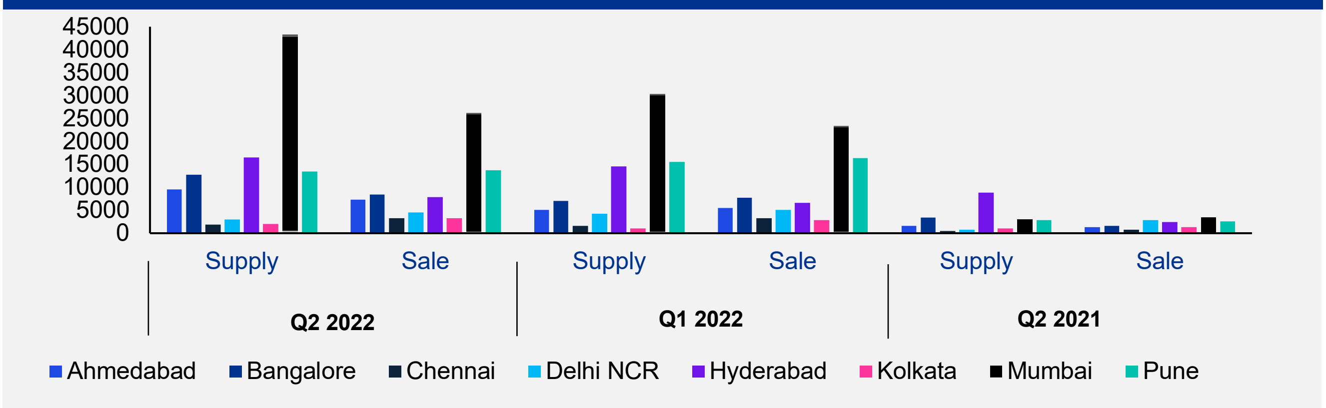


The real estate industry has revived from the COVID-19 pandemic: Despite a surge in interest rates, the demand for housing did not take a hit in the country

With township developments, established SEZs and favourable social infrastructure, North Bangalore, Pune, Mumbai and NCR have emerged as some of the fastest growing residential hubs, recording a 3–9 per cent y-o-y increase in residential sales during 1H22. These regions led the supply of available housing inventory, which grew by 1 per cent in 3Q22 to 7.85 lakh units from 2Q21 with 7.63 lakh units. In 3Q22, the overall residential sales amounted to 83,220 units in comparison to 74,330 units in 3Q21 depicting a 12 per cent surge[3].

Consequently, residential sales witnessed a 61 per cent y-o-y increase in 3Q22 and 3 per cent on a q-o-q basis. Despite the increase in interest rates on home loans (highest since 1H13), a total of 1,58,705 units in 1H22 were sold depicting a 19 per cent rise over 1H21. As of early November 2022, INR3.5 trillion worth of funds were raised by Indian companies through infrastructure and real estate investment trusts[3].

Housing supply and sales in top eight cities (units)[4]



Note: 1. REIT; Real Estate Investment Trust
Source: 1. India Real Estate Sector, Newswires
2. The Outlook of the Real Estate Market in India, RBSA Advisors
3. Industry Reports, Anarock Property Consultants
4. Real estate industry, IBEF
5. Real estate industry report 1H22, Knight Frank
6. Housing sales, ET
7. Indian real estate and construction: Consolidating for growth, KPMG
8. Real Insight Residential July Sep 2022, PropTiger Research, accessed in November 2022

Indian Housing Market: Growth Drivers (1/2)

The recovery has been gradual for housing sector, however affordable housing with low penetration present ample opportunities to drive its growth.

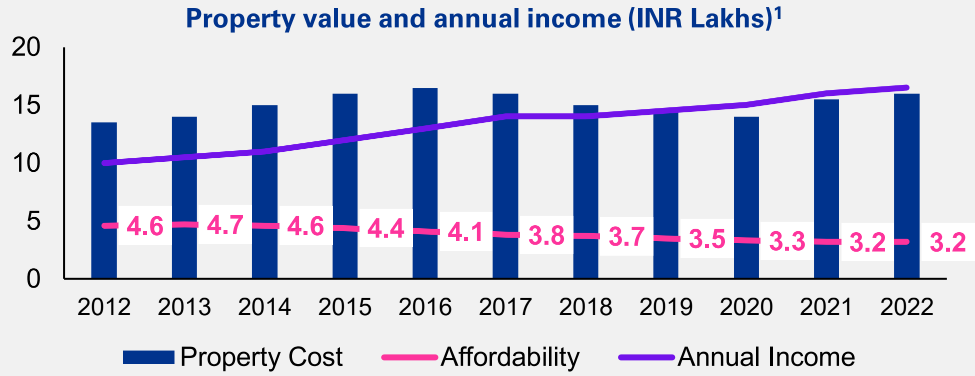
Key challenges

1	Rising interest rates	2	Increasing inflation	3	Stringent housing policies
4	Lack of awareness	5	Inadequate infrastructure	6	Static societal norms
7	Unequally distributed national investment	8	Higher land acquisition costs	9	Hidden costs like processing charges

Above mentioned bottlenecks have been hindering the growth and development for Indian housing sector; however, several drivers can potentially contribute to the growth of housing sector.

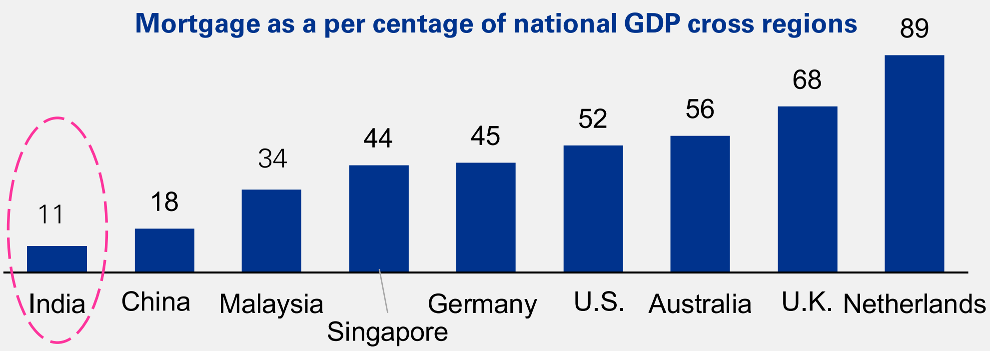
Improved Affordability

- Improvement in Affordability Index: With handsome incomes and correction in housing prices, affordability has considerably improved over the years.



Low penetration

- As of 2022, India's mortgage penetration stands at 13 per cent of the GDP, however with the increase in demand of housing industry, it is expected that India would be able to double its home loans up to USD600 billion by 2027.[2]
- In comparison to other Asian economies wherein the average mortgage to GDP ratio ranges from 20–30 per cent, it is expected that Indian economy would have multifold opportunities to witness an exponential growth trajectory.[3]



Source: 1. Investor Presentation, HDFC
2.India likely to double home loans to D600 billion in 5 years, The Hindu
3.India Real Estate Residential and Office Market H1 – 2022, Knight Frank, accessed in November 2022

Indian Housing Market: Growth Drivers (2/2)

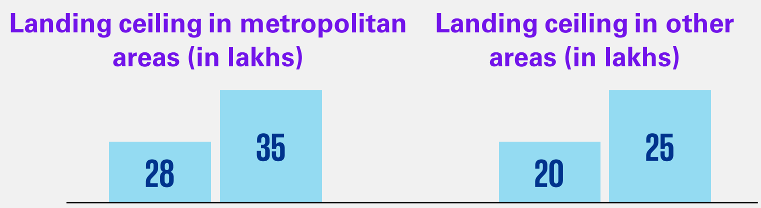
Incentives on affordable financing are a key factor behind the revival of the housing market in India.

Government incentives

- **Demand side:** The government of India has been facilitating higher budget allocations towards affordable housing — the Pradhan Mantri Awas Yojana (PMAY) launched in June 2015 to provide quicker urban housing approvals, was allocated an outlay of INR48 billion[5] from the Union Budget 2022–23 towards the construction of 8 million homes[6]. Additionally, improved tax incentives on interest and principal amount for home loan borrowers proves to be attractive for individuals.
- **Supply side:** Supply-side subsidies can be an important boost to home developers wherein government provides time to time incentives to build affordable housing. The government provided 'Infrastructure status' to affordable housing allowing the projects to seek benefits such as lower borrowing rates, tax concessions and higher inflow of foreign and private capital.
- **Liquidity side:** To enhance liquidity support post pandemic, government provided special refinance facilities with an additional standing liquidity facility (ASLF) of INR5,000 crore to NHB[1].

Increased lending ceilings

- **Special refinance facilities:** The government facilitated special refinance facilities for NBFCs and HFCs. Further, it also revised the lending ceilings for home loans under the priority sector lending programme.



- **Extension of income limits:** Current family income limit of INR2 lakh per annum was modified by RBI for loans to be disbursed for housing projects of Economically Weaker Sections (EWS) as well as Low-Income Groups (LIG) to INR3 and INR6 lakh per annum, respectively.[2]

Other demand drivers

- **Favorable demographics:** About 66 per cent of India's population is below 35 years of age which presents an opportunity of high disbursement of home loans.[3]
- **High urbanization:** It is expected that 40 per cent of India's population would reside in urban regions by 2030, as compared to 32 per cent living currently.[4]
- **Increase in nuclear households:** Over the years, India has been witnessing an uptake in the number of households being shifted towards the concept of a nuclear family.

Source: 1. Aatma Nirbhar Bharat Package – Progress So Far, PIB Delhi
2. PMAY (Pradhan Mantri Awas Yojana), Urban Money
3. Real estate industry, IBEF
4. 40% of Indian population will live in urban centres by 2030, Mint ,
5.Realty Bytes, Grant Thorton
6.Statement on Development and Regulatory Policies, RBI
7. Employment in India, National Institute of Public Finance and Policy, all accessed in November 2022

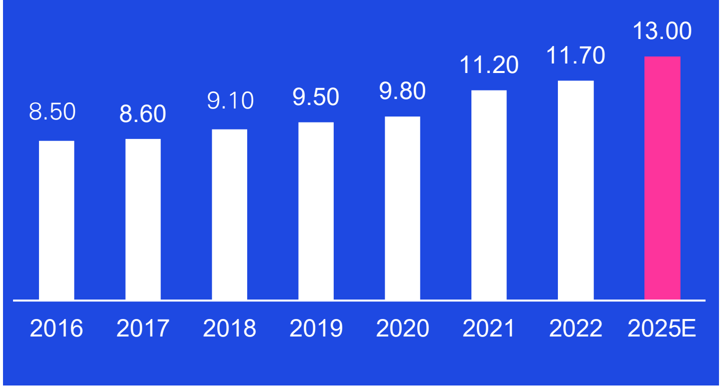
An outline of housing finance

Being a part of the NBFCs, HFCs act as an alternative financing channel to the real estate and housing industry.

In India, housing development and democratized home ownership have been two significant economic and social objectives for individuals. Governments of multiple countries have developed complex procedures to avail finance however, to meet the objectives of affordable housing in India, HFCs have been acting as an alternative financial channel to the real estate and housing sector.

The housing finance market is expected to grow at a CAGR of 20.58 per cent from FY22–31[2] owing to affordable housing, decrease in property prices, attractive tax incentives and a surge in household income. In 2022, the affordable housing segment made up 90 per cent of the market in terms of volume and about 60 per cent based on value.[2]

Housing loans to India's GDP (in per cent)[3]



A survey conducted by Anarock in 1H22 suggests changes in the preferences of buyers to gaining momentum in premium segment homes and consistency in homes located in city peripherals[1]

69 per cent of the survey respondents prefer buying a house for self-use

Millennials and Generation X considers buying a home as an investment

The growth of housing finance companies diluted in 2020 and 2021 owing to the COVID-19 pandemic and low GDP, however the economy witnessed a slight recovery in the residential housing segment in 2022.

The home loan portfolio over the last six years has increased substantially owing to an increase in disbursements with a surge in demand in tier-II and III cities, increase in number of nuclear families, growing disposable income and fiscal incentives including reduction in stamp duty and interest rate cuts on home loans.

Pre-pandemic, the household liabilities and financial savings depicted positive signs of marginal changes suggesting that the household leverage posed risks for stimulating consumption, infusing business confidence and steering economic recovery. Moreover, housing supply seemed to be deeply impacted in the initial months of 2021, however, the situation got better in the second half due to increase in demand, decrease in interest rates and the extension of supportive schemes for the affordable housing segment.

Ticket size split comparison of sales from 3Q21 to 3Q22[4]

Ticket size	3Q22		3Q21	
	No of units	Market share (in per cent)	No of units	Market share (in per cent)
Less than INR 5 million	26,316	36	27,691	43
Between 5–10 million	26,269	36	22,097	35
More than INR10 million	20,038	28	14,222	22

Source: 1. Consumer Sentiment Survey, Anarock
2. Housing Finance Market, Market Research
3. Housing Loans Market in India , Newsblare
4. Ticket size, Knight Frank India , accessed in November 2022

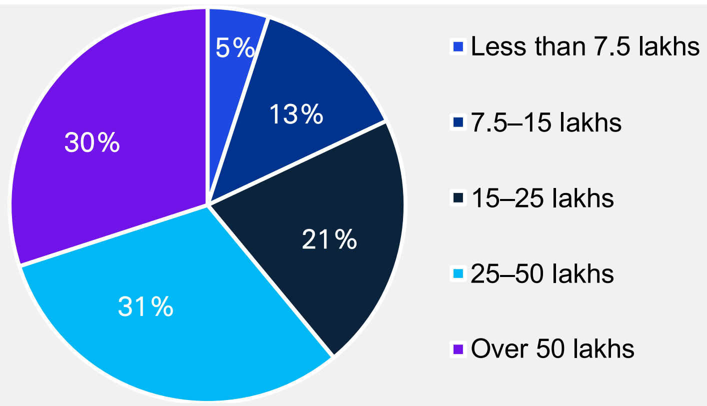
Home-loan market

The home loan market is expected to double in the next five years with 70 per cent of home loans potentially be less than the ticket size of 50 lakh.[1]

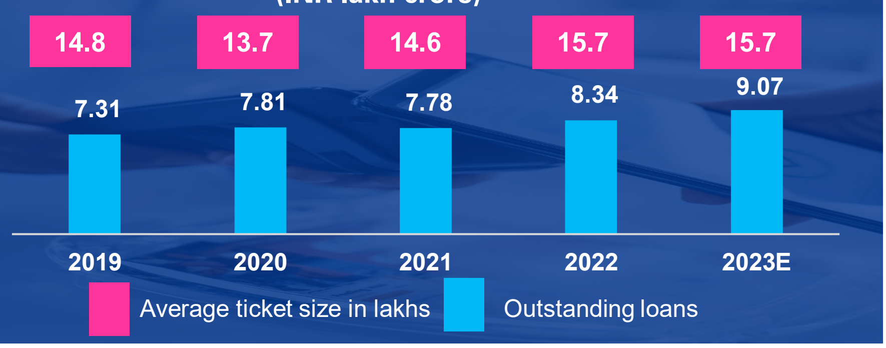
In India, the housing loan rates are on a lower side in comparison to several developing countries which presents abundant opportunities leading its growth. The Indian home loan market presently valued at INR25 trillion, is anticipated to grow at a CAGR of 13 per cent from 2016–22, owing to increasing urbanization and affordable mortgage rates.[2]

It is expected that housing loans contribute to a total of 13 per cent to India's GDP by 2025.

Housing Loans ticket size[4]



Outstanding loans for HFCs in housing loans (INR lakh crore)[3]



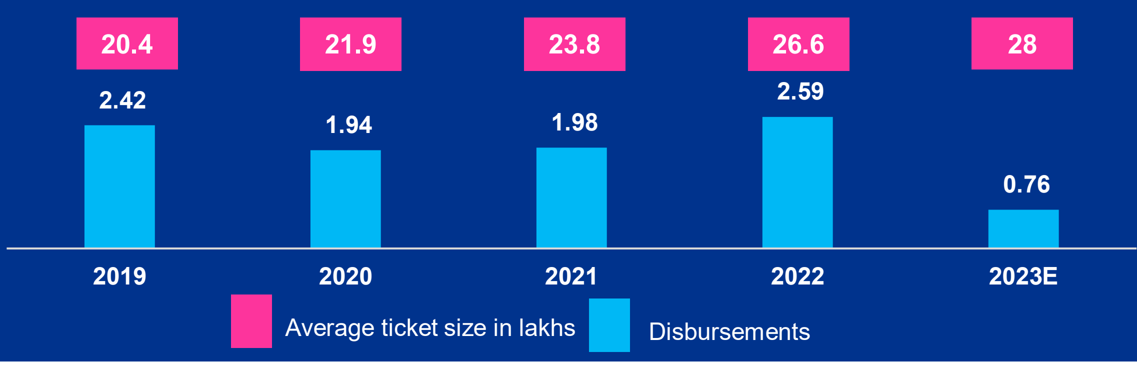
The total outstanding loans for HFCs in housing loans stood at INR7.31 lakh crore in 2019, which is expected to reach INR9.1 lakh crore in 2023, depicting a 24.1 per cent growth.[3]

Consequently, the average ticket size has been in the range of INR14 to 16 lakhs over the five years.

Housing segment contributes to around 50 per cent of the personal/retail loans wherein the share of 'housing loans' in 'bank credit' improved to 14.4 per cent in June 2022 from 13.1 per cent in March 2020. Post the pandemic, the total home loan portfolio grew by 10 per cent showcasing that tier III and IV cities grew at a faster rate than tier I and II cities.[2]

Housing market of India witnessed a 40 per cent increase in the first nine months of 2022, to 232,396 units from 163,426 units in 2021. In June 2022, India's house prices increased by a 3.8 per cent y-o-y showcasing a higher demand for household units. Reforms such as RERA, GST and roll out of Production Linked Incentive Scheme (PLI) to attract individuals after a period of stagnation.[4]

Disbursements for HFCs in housing loans (INR lakh crore)[3]

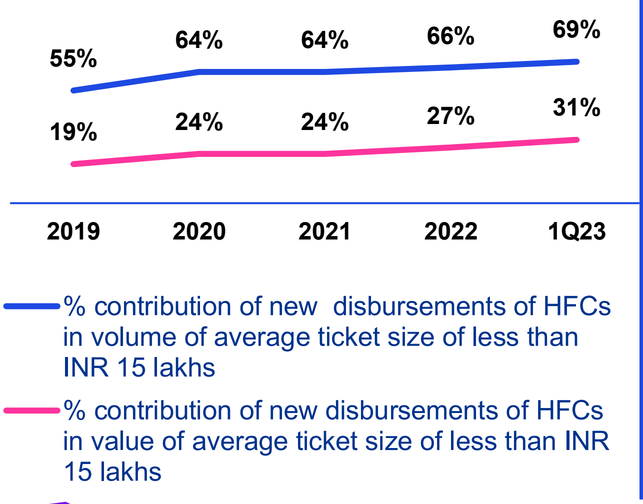


Source: 1. India's home loan market set to double in next 5 years: SBI
2. India's home loan market expected to double to ₹48-lakh cr in 5 years: SBI report
3. Aggregate level data is sourced from Experian Credit Information Company of India Private Limited
4. Industry Reports, CRISIL, ICRA, BOB Economics, accessed in November 2022

Disbursements and AUM in housing finance

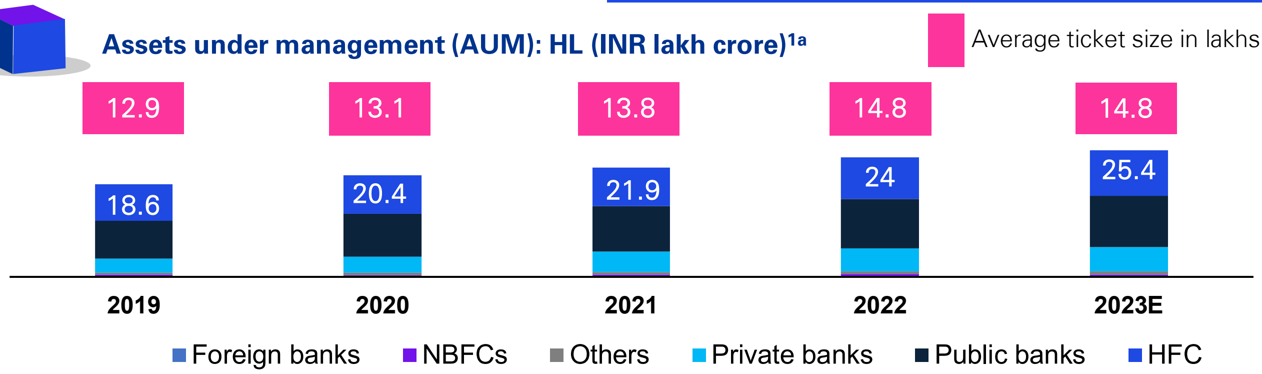
HFCs have been focusing on sub INR10 lakhs LAP product with their share in total disbursements upto ticket size of INR25 lakhs gradually increasing

Contribution of new disbursements in volume of average ticket sizes[1]



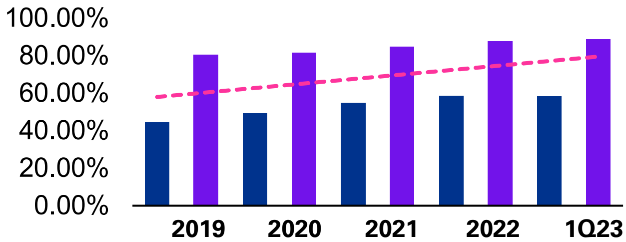
- Out of total disbursements upto average ticket size of INR25 lakhs, contribution of new disbursements in volume for average ticket size less than INR15 lakhs has increased from 55 per cent in 2019 to 69 per cent in 1Q23.
- While average ticket size for HFCs for new disbursements in the category of average ticket size of less than INR15 lakhs has remained around 6 per cent, with a minimal increase from ~INR 3,75,000 in 2019 to ~INR 4,00,000 in 1Q23.
- Out of total disbursements for HFCs, contribution for new disbursements in LAP category in volume terms has increased from ~23 per cent in 2019 to ~34 per cent in 1Q23 while in value terms , it has remained flat around 17 per cent further signaling focus of HFCs on Micro LAP with reduced ticket sizes.[1]

Assets under management (AUM): HL (INR lakh crore)[1a]

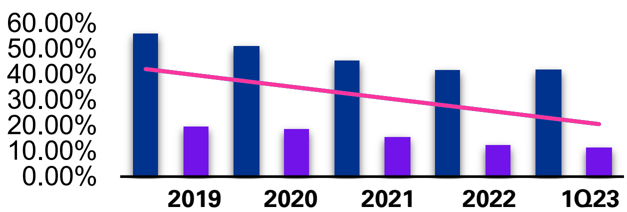


HFCs have been able to reach pre pandemic levels in terms of new disbursements for ticket sizes >15 lakhs while in ticket size < 15 lakhs , recovery is not yet achieved[1]

% contribution of new disbursements in volume and value terms to total disbursements by HFCs for ticket size greater than 15 lakhs



% contribution of new disbursements in volume and value terms to total disbursements by HFCs for ticket size less than 15 lakhs



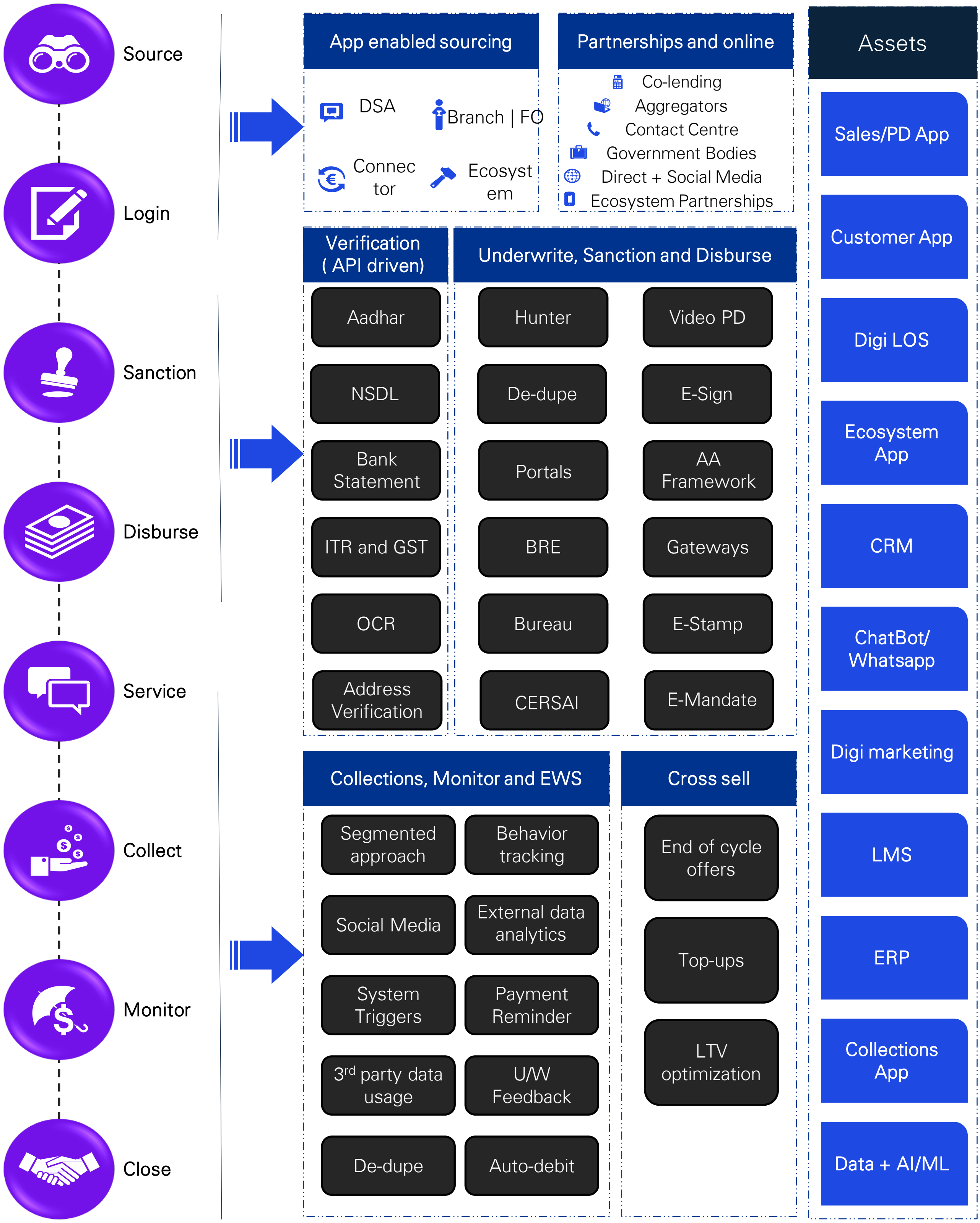
Disbursements in volume terms | Disbursements in value terms

- Post pandemic, HFCs have mainly focused on higher ticket sizes for new disbursements with average ticket size of INR 42 lakhs for 1Q23 exceeding the 36 lakhs ticket size pre pandemic in 2020.[1]
- In affordable housing segment with ticket size less than 15 lakhs, HFCs have maintained a wait and watch stance in order to see the full recovery in MSME/Self employed segment in urban and semi-urban areas.

Note: A. Financial years have been taken into consideration
Source: 1. Aggregate level data is sourced from Experian Credit Information Company of India Private Limited, accessed in November 2022

Digital enablers across the value chain

The digital enablers across the value chain from sourcing to collections present a significant opportunity to improve productivity and TAT1 for HFCs.



Note: 1. Turnaround time
Source: 1.KPMG in India's analysis 2022

02

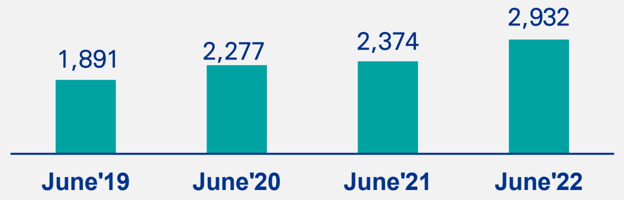
Microfinance

An overview of microfinance industry

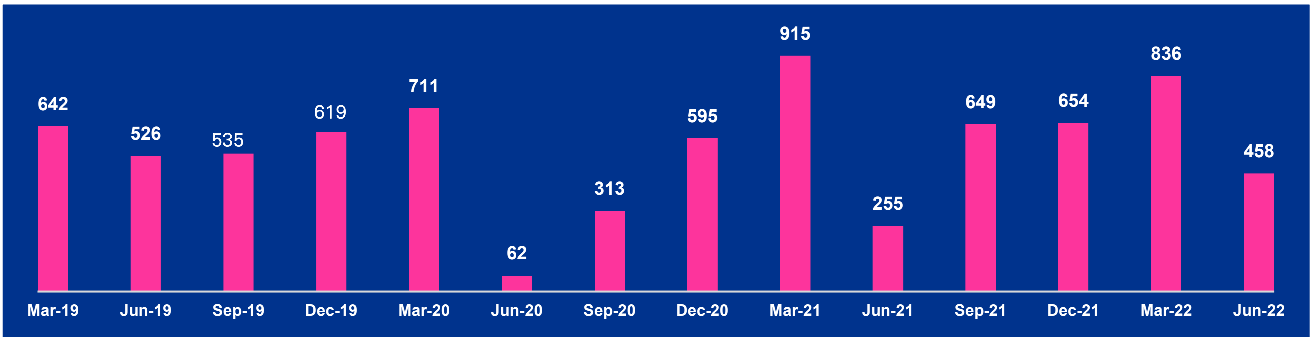
Is the microfinance industry reviving post the pandemic?

Started of as a movement in 1990s in India, microfinance as an industry has gone under massive transformation to enable easier and recognized credit facilities to low-income households. Owing to the introduction of structured guidelines, advent of technological innovations, increased government support, Micro Finance Institutions (MFIs) have been able to become an active channel for strengthening financial inclusion across the country.

Gross Loan Portfolio (INR billion)[1]

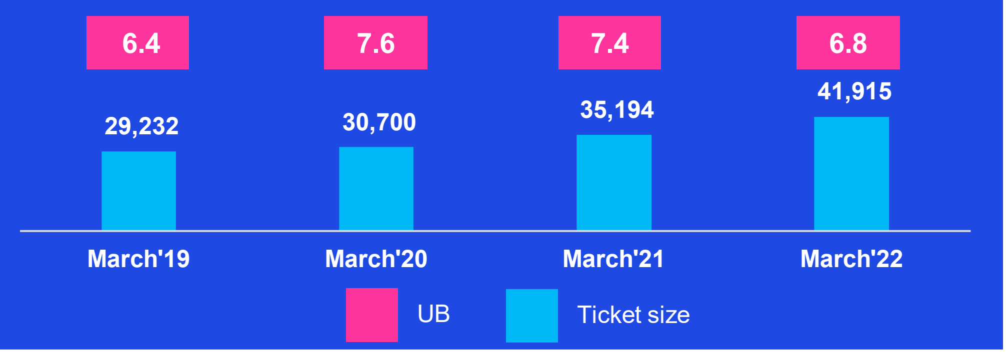


Disbursements (INR billion)[1]



In June 2022, there was a major decline in loan disbursement, i.e., lenders were taking cautious approach to expand portfolio and disburse fresh credit attributable to the pandemic. MFI sector, however, started reviving as the disbursements increased post September 2021 quarter to reach pre-pandemic levels, driven by increase in average ticket size, such that larger amount disbursed to the existing customer base

Ticket size on closing AUM (INR) and Unique borrowers (UB) (Crores)[1]



Ticket size on closing AUM has been growing steadily post covid, with an average ticket size on closing AUM in Q1 of FY23 lies in the range of INR40,000–50,000[1], highlighting the headroom for growth before hitting regulatory ceilings.

Where is the industry headed from here?

- With new regulations bringing credit from all REs under common ambit, more customers may hit the Fixed Obligations to Income Ratio (FOIR) ceilings, to impede growth from existing customer base
- Increasing household coverage upto INR3 lakhs will potentially expand the universe of target households for microfinance lenders. While the expected impact is yet unknown, NBFC-MFIs can expect increased competition from fintech companies, personal lenders and unorganized market due to overlapping customer base
- It is pertinent to note that overleveraging of customers and stagnant borrower base may result in excessive risk build up in the ecosystem.

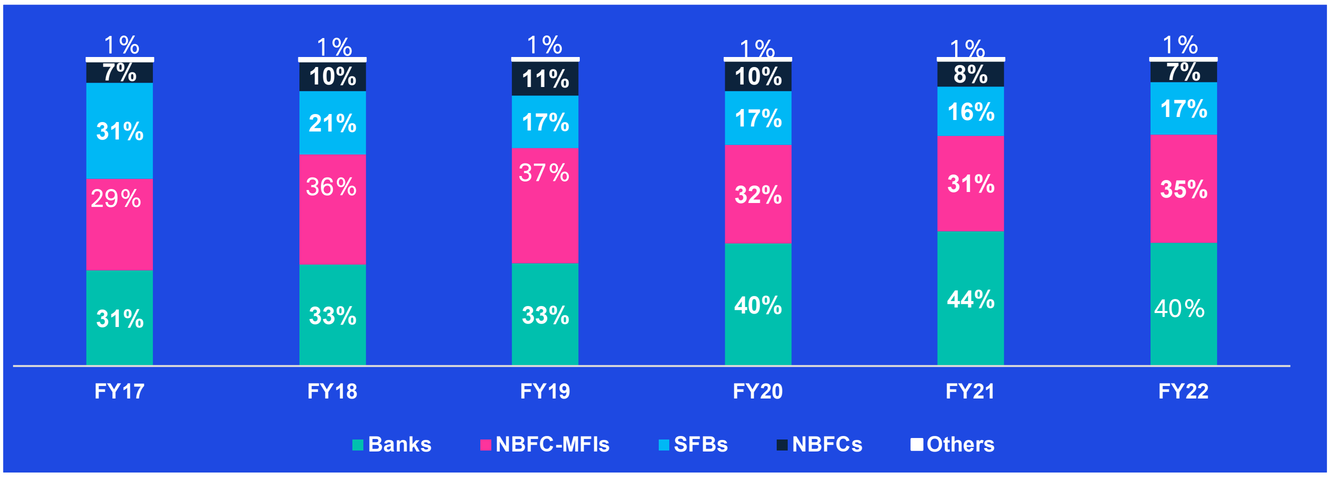
Source: 1. MFIN micrometer from FY19 – FY22, accessed in November 2022

Microfinance ecosystem involving different entities

Are NBFC-MFIs facing disruptive headwinds from non-MFI NBFCs, bank aggression for micro-credit?

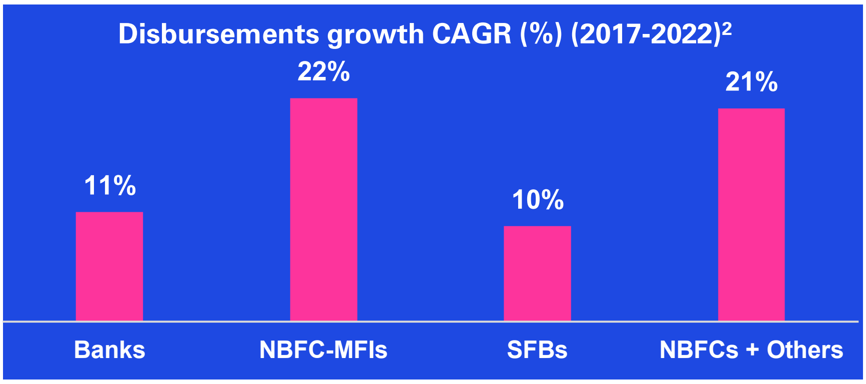
Within a broad micro finance ecosystem, a broad categorization comprises of Non-Bank Financial Company-MFIs (NBFC-MFIs), Banks, Small-Finance Banks (SFBs) and NBFCs. As of 30 June 2022, portfolio of banks holds the biggest share of 38 per cent[1] as the total outstanding micro credit loans across lender group, while NBFC-MFIs hold 35 per cent[1].

MFI ecosystem - GLP outstanding (INR billion)[2]



Over a period, SFBs have lost market share due to their diversification efforts and capital being redeployed towards non-microcredit products

Banks have gradually been gaining market share, reaching 40 per cent in FY22 from 31 per cent in 2017[2]. The trend can be attributed largely to the growth of micro-finance focused banks like Bandhan bank, IndusInd bank, Kotak and RBL. On other hand, irrespective of non-MFI focused NBFCs losing the market share, their disbursement growth has been growing in last 3-5 years.



Various micro-lenders like Muthoot, GrameenKota, Ujjivan SFC, are venturing into various credit-plus products

Home improvement	Solar	Home appliances	Water and sanitation	Mobile	Cycle and personal

What is the future of microfinance ecosystem looks like?

- Within the industry, there is higher ongoing focus on micro-credit by non-MFI NBFCs and banks, uncovering consumers to non-microfinance products, along with cross-selling of financial micro-products and credit-plus products
- There is a shift experienced in the operating models of microfinance lenders from group-based lending to individual lending practices, along with an increase in micro-credit distribution by Non-MFI NBFCs. This has resulted in creation of varied bouquet of products/services for customers, necessitating additional monitoring measures to ensure efficient risk management and mitigation.

Source: 1. MFIN micrometer June 2022, MFIN
2. KPMG in India's analysis 2022 based on data from MFIN Micrometer 2017-2022, accessed in November 2022

Regulatory environment of microfinance industry

How does recent MFI regulations shape the industry and all the regulated entities involved?

Prior to December 2011, MFI industry was self-driven by NGOs and NBFCs, however, as industry started picking up, various challenges such as high indebtedness, high-interest rates started growing. These challenges forced RBI to intervene and introduce strict lending norms for MFI sector in 2011.

In recent years, owing to external factors such as the advent of technology and fintech players, along with pandemic, forced the state governments to reassess the regulations. In December 2020, Assam state passed The Assam Microfinance Institutions (Regulation of Moneylending) Bill, 2020[1], to regulate MFIs in the state to support continuity of the industry and positively impact the asset-quality for MFIs. The bill, however, faced some reservation from RBI, as the central bank stated that the bill can cause dual regulation of key component of the credit market, and consequently decided to publish centralized regulation for all microfinance players across the country.

On 14 March 2022, RBI introduced set of regulations to govern microfinance lending[2], as a bid to shift customer base, expand the range of borrowers from urban locations, stimulate greater management within lenders landscape, enhance the operational flexibility of NBFC-MFIs to support their profitability.

Sa-Dhan, a self-regulatory organization for MFI sector, introduced the Credit Assessment Framework (CAF) for microfinance borrowers, for improved risk profiling through a Credit Worthiness Score (CWS)[3].

Recent guidelines published by RBI for MFIs: A snippet

Microfinance loan defined

RBI redefined 'Microfinance loan' to collectively bring all entities involved in a sector, as a collateral-free loan disbursed to a household with annual household income up to INR3 lakhs

Household income assessment

RBI regulated entities with MFI sector will be required to set a policy approved by the respective boards, to assess the household income, which can be adopted or modified frameworks from SRO or any other agencies

Obligations of loan repayment

Entities will have to set policy in place for the limit on the repayment outflows of monthly loan obligations of a household as a per centage of their monthly household income, limited to 50 per cent of the income.

Pricing

Entities will have to set policy in place for pricing of the microfinance loans, which will include a thoroughly documented interest rate model, detailed explanation of interest rate components, range of spread and any other charges on loan.

Will the regulations strengthen the sector or more can be achieved?

1. **Expansion of market** as inclusion of all REs in single ambit will increase overall GLP, to move all unqualified loans under the definition of micro-finance loans

2. Gradual reversion in the book size can be expected as the **FOIR ceiling of 50 per cent would impact the next cycle of lenders**, hindering their ability to churn the books in their subsequent cycle.

3. Credit Assessment Framework (CAF) introduced by Sa-dhan for microfinance borrowers, however, there is a need for a **mandatory policy around it like RBI**

4. Welcome move of **risk-based pricing will eventually lead to differential pricing** basis customer behaviors, with an expectation to stabilize risk-adjusted NIMS at the industry level because of market recalibrations

Source: 1. Assam Micro Finance Institutions(Regulation of Money Lending) Act, 2020, Government of Assam,
2. Master Directions - Reserve Bank of India (Regulatory Framework for Microfinance Loans) Directions, 2022, RBI
3. Sa-Dhan introduces credit assessment framework for microfinance borrowers, Business Standard, accessed in November 2022

Impact of the pandemic on the sector

Has the MFI industry revived from latest credit shock, i.e., the pandemic?

Microfinance has historically been highly sensitive to credit events, and such was the impact of the pandemic. It impacted the liquidity and asset quality of MFIs, hampering their ability to pay interest on borrowings. Industry data indicates that the write offs in FY21 and FY22 as a per centage of AUM of top MFI players in March'20 stays within the range of 5-8 per cent[1]. Players had offered restructuring mainly in the form of moratorium, reduction in EMI incidence in order to accommodate the borrowers. Similarly, restructured book as a per centage of AUM of top MFI players in March'22 is within range of 5-8 per cent[1].

Performance of Mar-20 book[1]

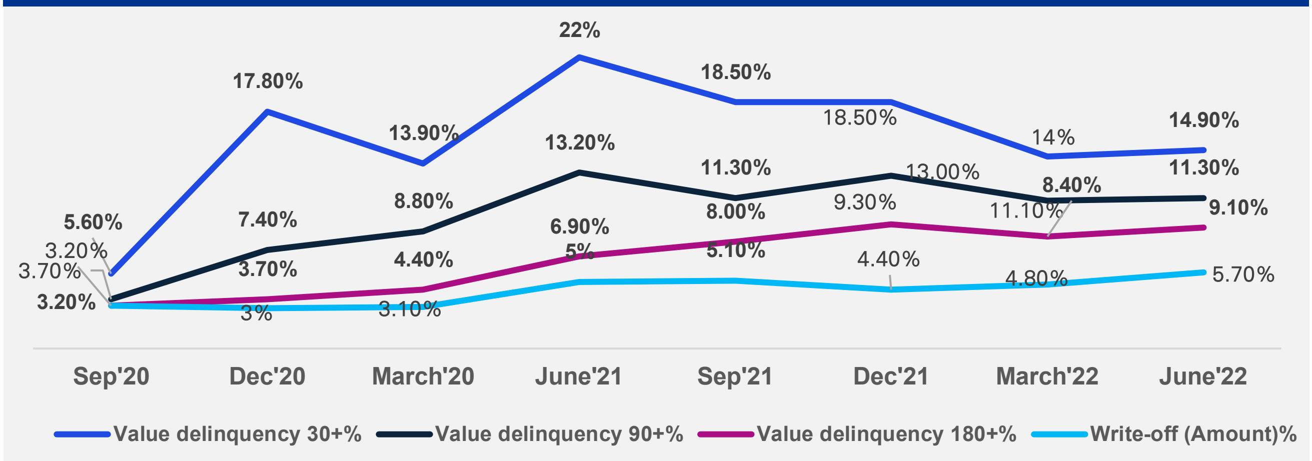
Small Finance Banks[a]

Combined AUM as of March'20	INR 506.095 billion
Restructured books % as of March'20 AUM	6 – 8 %
Write off book % of March'20 AUM	3 – 5 %

NBFC-MFIs[a]

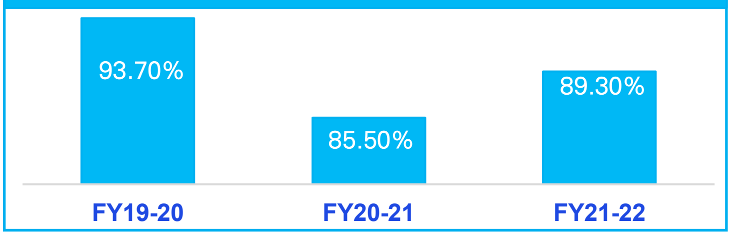
Combined AUM as of March'20	INR 39.594 billion
Restructured books % as of March'20 AUM	2 – 4 %
Write off books % as of March'20 AUM	2 – 4 %

Delinquency trends[2]



Delinquency levels are higher in the recent period on account of slippages from restructured book and have still not been back to pre-pandemic era. In terms of the collection efficiency, there has been an improvement in the recent period, however, the collection efficiency is lower than pre-pandemic levels.

Collection efficiency[1]



What will credit cost for the microfinance stabilize?

There is an expected potential stress towards restructured cases of about 5-8 per cent, which could ultimately result in impending ballooning to cause strain in the recent period.

The overall high credit cost, however, is expected to continue for a prolonged period, stretching over three to four quarters, once the overall restructured book matures. In the current scenario, it is imperative to identify the growth opportunity and assess the emerging needs, basis the various learning from the pandemic.

Note: A. Average cost of credit presents a collective number of top SFB and MFI players taken in consideration.
Source: 1. KPMG in India's analysis 2022 2. MFIN micrometer from FY20 – FY22, accessed in November 2022

03

Micro, Small & Medium Enterprises (MSME)

MSMEs - India’s growth engine

Accelerating the flow of credit to these small enterprises is essential for India to achieve her USD5 trillion dream by 2025.

MSME sector is the backbone of India’s development story, and it has a been major driver in the country’s rise as the world’s fifth largest economy. From employing millions of people to exporting billions of Make in India products, MSMEs have significantly lifted their role in Indian economy over the past decades. And now they are going to play a major role in helping India score more wins from the current makeover in global supply chain networks and accomplish her desire in ‘Aatmanirbhar Bharat’ or an economically self-reliant country.

The outbreak of COVID-19 and subsequent economic hurdles were a major blow to the MSME sector, which is still largely unorganized and suffers from limited access to traditional credit channels. Although the economic losses were huge, the sector has been recovering well on the back of strong policy initiatives from the government. While the current global slowdown and rising interest rates have raised concerns for the near-term outlook, the sector is on a cusp of major transformation on the back of deeper digitalization initiatives, a wider pool of young entrepreneurs and closer collaboration between the private and public sectors.

Why MSMEs[a] matter to India’s growth story?

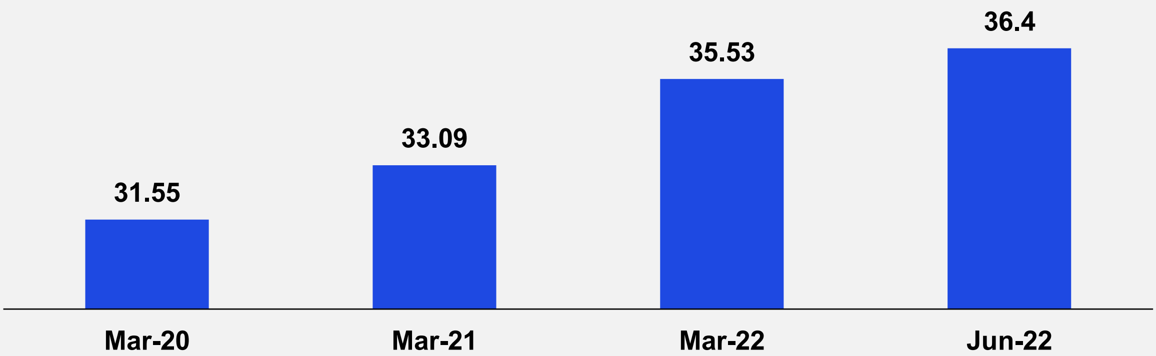
30%
Of GDP[1]

45%
Of exports[2]

90%
Of enterprises[3]

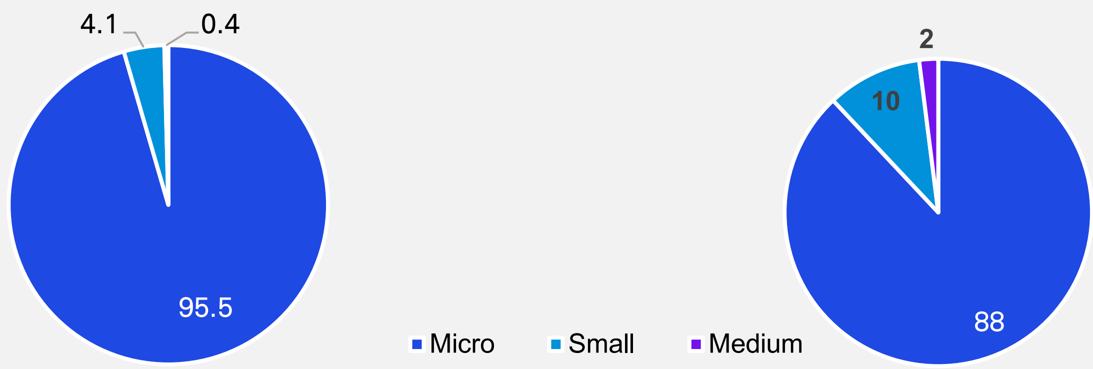
110 million
Workforce

MSME loans market (INR trillion)[4]



Share of registered entities (%)[5]

Share of registered borrowers (%)[6]



Note: a, MSMEs refer to Micro, small and medium enterprises..
Source: 1. Contribution of MSMEs to GDP, PIB;
2. Share of MSMEs in India’s total exports declined from nearly 50%: Govt data, Financial Express;
3. Union Minister Dr Jitendra Singh says, new business enterprises are heavily dependent on scientific technology in contemporary India, PIB;
4 MSME loans market, Experian,
5. Indian MSME Industry Analysis, IBEF
6 Share of registered borrowers, KPMG in India's analysis 2022, accessed in November 2022

Growth drivers of MSME credit

The sector is recovering well from the pandemic setback, supported by wider digitalization of the economy, government's credit incentives and a strong push towards manufacturing sector.

Government initiatives and policy support

MSMEs[a] are the cornerstone of the government's Make in India campaign and they have been supported with a series of policies and initiatives across financing, marketing and technology.

- Pradhan Mantri MUDRA Yojana (PMMY) - Loans sanctioned under the scheme, which was launched in April 2015, reached INR20 trillion[1] as of 3 November 2022.
- Special Credit Linked Capital Subsidy Scheme (SCLCSS) – As of March 2022, subsidies worth INR1.1 billion[2] were disbursed in this scheme, which was launched in 2021 to aid services enterprises in their technology needs.
- SAMBHAV, a national-level awareness program to push economic growth by promoting entrepreneurship and domestic manufacturing was launched in 2021.

Increasing labour force and favourable demographic conditions

Young population, growing base of skilled labor and rapid urbanization have put India as a major customer market as well a favorable destination for firms looking to reorganize their global supply chain networks amid geopolitical tensions.

- By 2030, about **42 per cent of the country's population**[3] is estimated to be urbanized from 31 per cent in 2011.

Digital architecture

The government has been building digital tools and solutions to simplify processes, addressing grievances and monitoring delivery of payments to MSMEs. Introduction of GST[b] , UPI and other digital footprint have also improved the access to finance for MSMEs.

- Surging digital transactions: According to a survey (published in June 2021)[4] conducted by Bluehost, MSMEs are rapidly turning less reliant over cash, clocking 72 per cent of their payments using digital platforms.
- Udyog Aadhaar Memorandum (UAM) - A one-page online registration system for MSMEs based on self-certification. There are about 6.8 million Udyog Aadhar registered MSMEs, according to the Union Budget 2021-22[5]

Increased budgetary support and fiscal incentives

Over the past few years, the government has accelerated its outlays for several schemes, technology and promotional activities of MSMEs. It had also widened the sector's ambit and introduced tax benefits for start-ups and small businesses.

- In the Union Budget of 2022-23, **Emergency Credit line Guarantee Scheme (ECLGS)** of INR500 billion and collateral-free automatic loans worth INR3 trillion were introduced.
- **'India Export Initiative' and 'IndiaXports 2021'** portal were launched in 2021, in a bid to help exports reach USD400 billion target by the end of FY22 and further push it to USD1 trillion by FY27[6].

Note: a, MSMEs refer to Micro, small and medium enterprises..b. Goods and Services Tax
Source: 1. Loan worth ₹20 lakh crore disbursed under MUDRA scheme, The Hindu; 2.. Special Credit Linked Capital Subsidy Scheme, Ministry of Micro, Small and Medium Enterprises; 3. Transferable development rights: A robust policy tool to address India's urban infrastructure voids; 4. KPMG in India's analysis 2022; 5. Indian MSME Industry Analysis, IBEF, 6 India Export Initiative and IndiaXports 2021 Portal launched by Minister of MSME, Ministry of External Affairs, Government of India, accessed in November 2022

NBFCs – Advancing credit flow to MSMEs

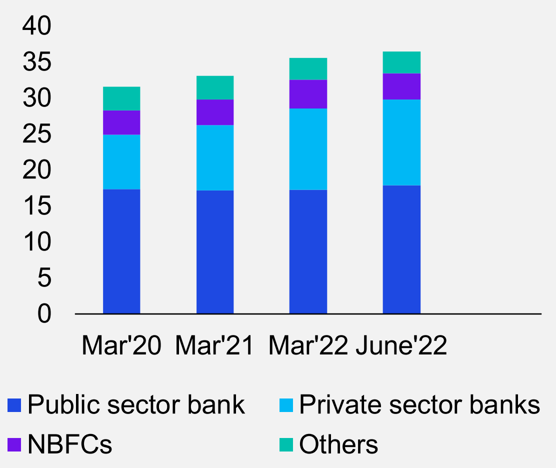
Deploying innovative tools, unconventional risk modelling and personalized offerings, NBFCs have boosted the flow of credit to MSMEs[a], especially in underserved pockets of the country.

INR3.6 trillion	6.1%	INR40 trillion
NBFCs' outstanding credit to MSMEs as of June 2022[1]	CAGR of MSME loans in March 2020-March 2022[2]	Credit opportunity in the MSME market[2]

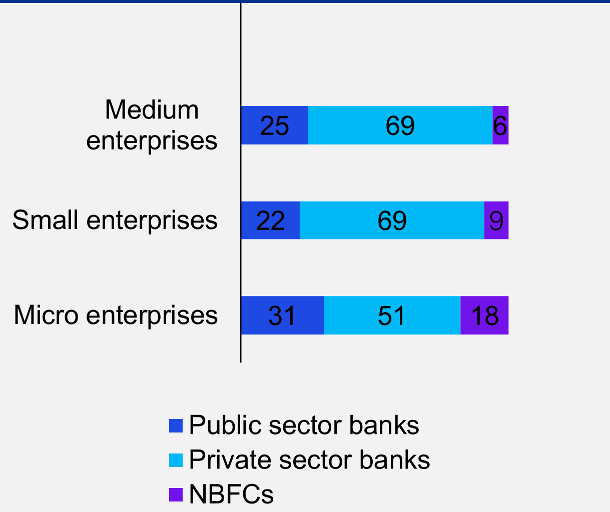
Non-banking financing companies (NBFCs) have been another major driver in pushing more credit to the MSME sector, especially in the vast unbanked pockets of the country. In addition to building a wide network of distribution channels, they have embraced digitalization of processes, leveraged technology for data analytics and adopted unconventional credit underwriting practices to meet the requirements of the small businesses.

Compared to banks, they have been more agile and have introduced personalized products and offerings based on the risk profiles and demands of different segments of the sector. NBFCs are also striking partnerships with fintech players, banks and alternative lenders to extend credit and bundled products for businesses. While the banks still dominate the flow of term loans to the sector, NBFCs have taken a lead in providing unsecured loans.

Credit to MSMEs (INR trillion)[3]



Share of lenders in June 2022 (%)[4]



Why NBFCs have emerged as a go-to lender for MSMEs?

- Faster disbursement of credit
- Personalized products based
- Unconventional credit risk assessment approach
- Streamlined on-boarding process with less frictions

How NBFCs can increase their leading opportunities with MSMEs?

- Innovative lending initiatives with digital processes that would help in better service
- Lending in areas that are underbanked and thus driving financial inclusions
- Complementing formal banking credit with partnerships

Note: a, MSMEs refer to Micro, small and medium enterprises. Goods and Services Tax
Source: 1 NBFCs' outstanding credit to MSMEs as of June 2022, Experian;
2. KPMG in India's analysis 2022; 3. Aggregate level data is sourced from Experian Credit Information Company of India Private Limited
4 Share of lenders in June 2022, Experian, accessed in November 2022

Digital enablers for affordable credit

While NBFCs offer flexibility and improved disbursement, MSMEs[d] should also leverage emerging low-cost digital tools and solutions to streamline their payments, financing, and core functional processes.

Leveraging Digital India for accessing formal credit lines[1]

Creating digital trails for improved access to working capital and long-term finance[2]

Digital ecosystem for payments

- Real-time instant UPI has ensured smooth digital transactions
- E-filing of the GSTs has made the tax credit process simpler
- Increase adoption of POS terminal-based payments
- Emergence of fintech firms, such as Khatabook, have enabled MSMEs adopt digital tools to manage their balance sheets and cashflows.

Digital enablers for efficient processes

- Multiple APIs assisting in verification of data at source for:
  - ITR[a]
  - GST[b]
  - Banking
  - Invoice details
  - KYC[c]
  - Address verification
  - Bureau
- E-KYC, E-Stamp, E-signature to fulfil the lending journey

Effective credit infrastructure

- Digital lead generation via:
  - Aggregators and partnerships
  - Direct via web/mobile
  - Co-lending arrangements
- Digital Credit assessments – models based on digitally available data for real time decision making.
- Analytical driven portfolio monitoring and review

Embedded finance option

- E-commerce marketplace lending
- Invoice discounting
- Supply chain financing
- Cash flow-based lending
- Faster working capital financing based on credit history

Over 47 per cent of micro enterprise and 53 per cent of SMEs have adopted for digital sales platforms[3]

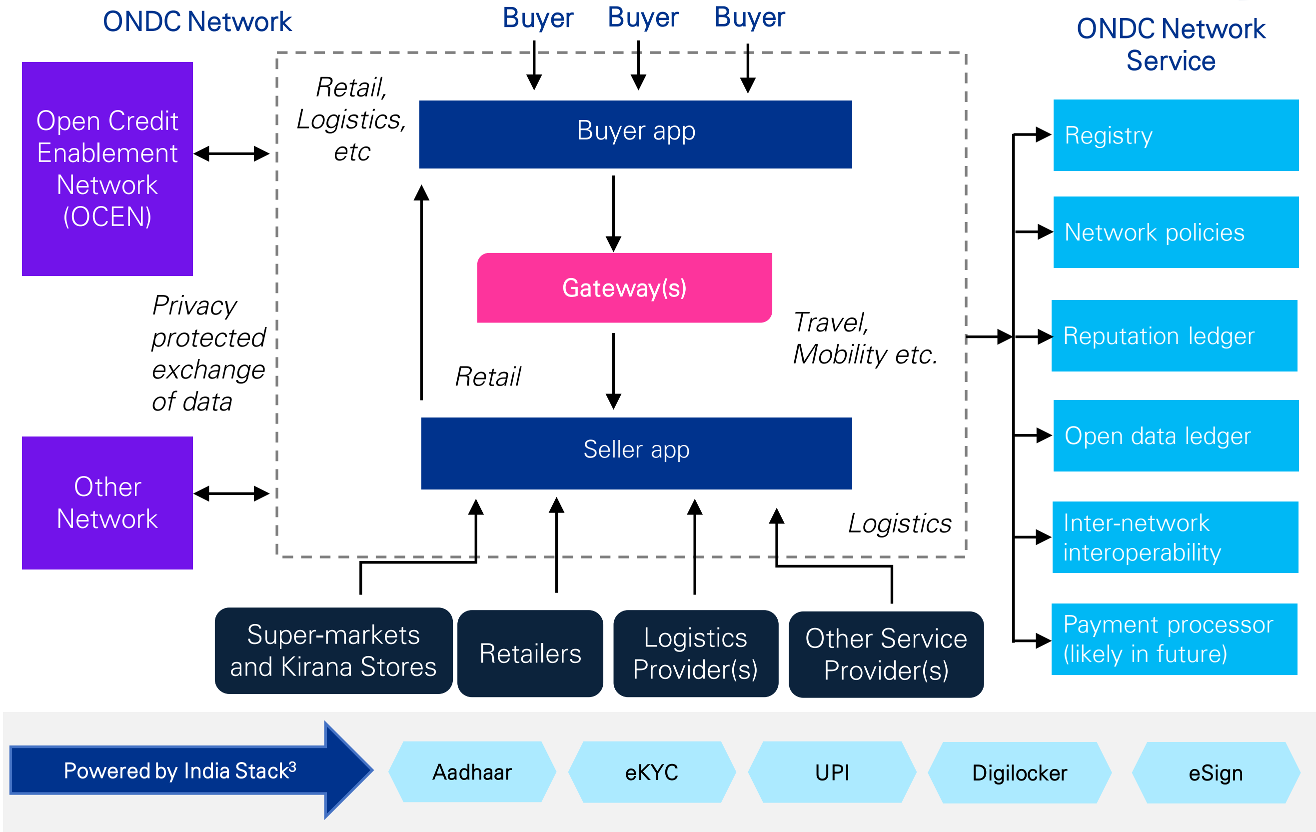
Note: a. ITR stands for Income Tax Return
b. GST stands for Goods and Services Tax
c. KYC stands for Know Your Customer
d. MSME stands for Micro, Small and Medium Enterprises

Source: 1. KPMG in India's analysis 2022; 2 Sub-group on flow of private sector investments to MSME, Planning Commission, 2011–12
, accessed in November 2022
3 Industry Reports, Crisil

Leveraging ONDC network to reach MSMEs

Democratization of digital commerce will help MSMEs widen their network and online presence through low-cost technology platform.

Open Network for Digital Commerce (ONDC) is a network based open protocol that aims to revolutionize e-commerce just like UPI did for payments in India[1]



Govt targets to lift e-commerce reach to 25 per cent of the Indian consumer purchases by 2024 from 8 per cent currently.

ONDC Network Participants[2]

Name	Role	Live Categories
Dunzo	Logistics	Hyperlocal
PhonePe	Buyer	NA
Paytm	Buyer	Grocery, Food and Beverage
Spice Money	Buyer	Food and Beverage
Digit	Seller	Grocery, Food and Beverage
Bizom	Seller	Grocery
Shiprocket	Logistics	Hyperlocal

How ONDC Network will help in MSME financing?[4]

- ONDC will allow direct customer access to MSMEs, resulting in lower cost of customer acquisition
- Offers real-time lending options like 'buy now, pay later' for sellers to meet their working capital needs and other financial requirements.
- Along with the Account Aggregator network , ONDC will be a powerful tool for a formal access of credit for MSME industries.
- IDBI Bank has joined the ONDC Network to help MSMEs and other retail merchants to launch digital stores.
- Nine banks, including State Bank of India, Bank of Baroda, HDFC Bank and Axis Bank have purchased stake in ONDC network to integrate their MSME customers in the network.

Source: 1. Industry Reports, ONDC
2. Network Participants, ONDC
3. The promise of IndiaStack, and how the world is watching, Your Story,
4. Nine banks buy stakes in ONDC, will integrate their MSME customers with the network, Financial Express; IDFC First Bank joins ONDC, Live Mint , accessed in November 2022

Access to credit – A lingering challenge for MSMEs

While rapid digitalization augurs well, it's vital for all stakeholders to address MSMEs' hurdle in accessing formal credit, which leaves them with higher costs and limited capacities for growth and development.

Collateral and stricter requirement in financing[3]

MSMEs financing are usually perceived to be risky by formal lenders, as most firms lack credit history or collaterals to avail secured loans. Besides, majority of the firms are mostly unorganized, carry transactions in cash and lack sufficient accounting practices in maintaining a track record of their operations.

- About 86 per cent of the manufacturing MSMEs are unregistered in the country.
- Nearly 80 per cent of the country's MSMEs lack access to traditional lending channels.

Low penetration in rural and poor regions

Lack of sufficient financial literacy coupled with poor economic conditions have hindered access to credit for MSMEs in poor parts of the country, which suffer from lack of connectivity and access to resources. Although banking penetration has gone up significantly and the government has introduced new league of lenders for small businesses, most of the institutions shy away from extending credit on the back of low recovery rates and lack of commercial visibility of the businesses.

- According to an estimate from World Bank Group[3], Indian MSMEs face a credit gap of about USD380 billion.

Liquidity crunch amid delays in payments

Owing to lack of a formal recovery mechanism and huge dependence on large businesses, most MSMEs are usually hit with working capital crisis amid delays in payments or terminations in orders that affect their cash flows. The COVID-19 pandemic has hit the industry very hard, forcing many MSMEs to either reduce their operations or dissolve their businesses.

- According to MSME SAMADHAAN[2], a delayed payments monitoring portal, there were 62,965 pending cases for amount worth INR181.8 billion as of 8 November 2022.

Higher cost of capital amid rising levels of bad debt

Institutional players have turned wary of MSMEs, owing to rising levels of bad loans in the segment. This forces them to pursue unsecured lenders, resulting in higher outlays of interest and thus increased cost of capital. And the current macroeconomic challenges, including slowing global trade and rising interest rates, have exacerbated the challenges for firms.

- At the end of March 2022, total NPA[1] in the sector stood at 12.8 per cent of the overall loans, higher than 12.5 per cent a year earlier and 12.6 per cent in March 2020.

Note: 1. NPA: Non-performing assets
Source: 1. NPAs in MSME sector increased by 12.5% in Q4 FY22 from year-ago period, Financial Express
2. MSME SAMADHAAN, Ministry of Micro Small and Medium Enterprises
3. MSME: The Agent of Economic Growth and Development in India, ACCA

04

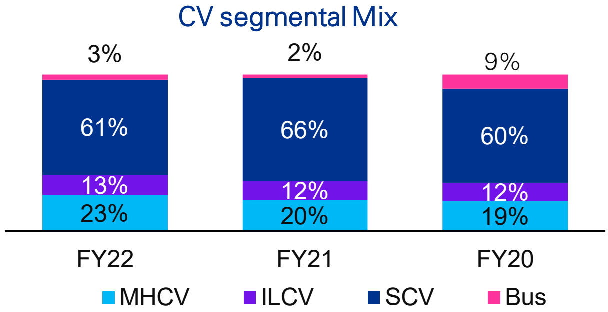
Asset finance

Asset finance: Commercial Vehicle (CV)

Post the COVID-19 pandemic, the CV industry has been on its path of recovery

India's CV industry is expected to report positive volume growth of 22-24 per cent in the FY23 owing to the positive demand drivers from multiple industries and surging freight movements. Based on the data released by Society of Indian Automobile Manufacturers(SIAM), the total sales volume in 1H23 was 4.56 lakhs, against 1H22 sales volume of 2.72 lakhs. Consequently, the demand momentum of CV is moderately stable with improvement in demand post monsoons.[1]

FY22 saw a growth in M and HCVs and I and LCVs segment with a market share of 36 per cent from 32 per cent in FY21 and will continue the trend in FY'23[1]. With truck utilization moving to an all-time high of 90 per cent in FY22 across all sectors, activity in construction and infrastructure sectors have fueled the demand for MHCVs. Increased rural consumption and e-commerce stood as growth levers for LCVs. Effect on bus segment by the pandemic continue to prevail.

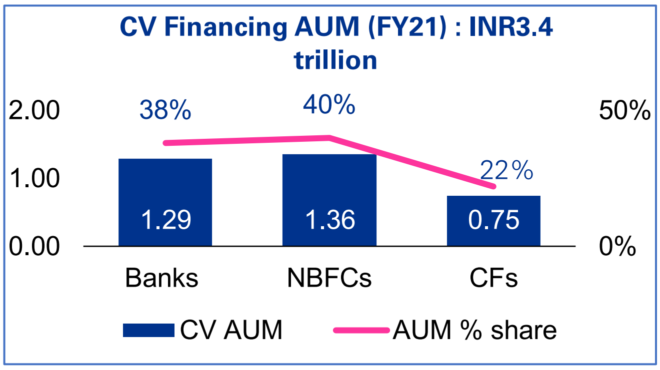


Decarbonizing the transport sector

According to The Automotive Component Manufacturers Association of India (ACMA) , HCVs are expected to account for and 5 to 10 per cent of new vehicle sales by 2030, however the Government of India intends to have a sales penetration of 70 per cent for CV by 2030[4]. Multiple OEMs are testing the new waters to introduce E-variants in commercial vehicle category. Higher E-LCV adoption will be seen in Tier-1 cities due to the factors such as higher last mile delivery demand and the urge to reduce pollution.

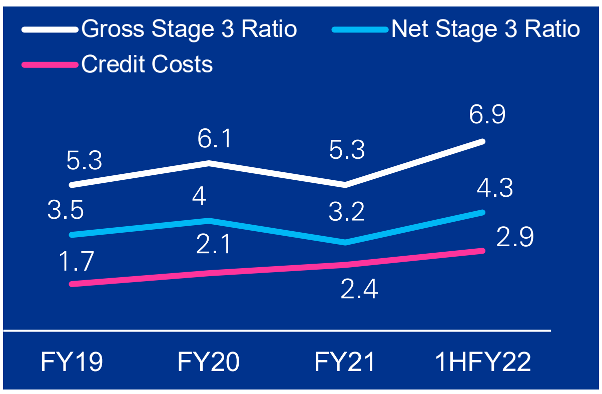
NBFC's CV AUM to grow 13-19 per cent in FY23[5]

NBFCs are aiming to create value proposition through digital adoption across various stages of the loan life cycle and favorable financing options. NBFCs are partnering with fleet management institutions to provide finance options beyond the asset purchase such as fuel and tire credit, repair and annual maintenance of the vehicles and leverage third-party providers for their insurance and security needs.



91 per cent of the used CV financing, which is one third of the total CV financing industry and 15 per cent of new CV financing comes from NBFCs[6]. Depressed load availability, portfolio restructuring and increase in fuel prices decreased the ability for the borrowers to earn positive cashflows. However, it is expected that CV financiers would grow by 13–19 per cent in 2023 with improvement in the economic activities. The trend in financing ECVs is yet to go full fledged owing to factors like lack of clarity on resale value. [8]

The CV financing NBFCs AUM growth rate is expected to be in the range of 13-19 per cent for FY23. With the second wave of the pandemic badly hitting the rural borrowers who form a major part of NBFC-CV financing, the GS3 assets increased in 1HFY22. According to a recent report, unless CV finance records higher AUM, the asset quality might not improve notably in FY23 from the current range due to the significant proportion of the restructured loan book in the NBFC CV portfolio. With the change in the consumer adoption ,inclusion of ECVs into the loan portfolio will help to build higher AUM going further.



Source: 1. H1 FY23 CV, 3W Sales Analysis: Industry on growth track
2. Strong fundamentals likely to make FY23 a breakout year for CV industry, ET
3. The future of mobility: Transforming to be ahead of the opportunity
4. Global Two-wheeler Outlook, 2022, Frost and Sullivan
5. NBFCs AUM growth to touch 4-year high in FY23,CRISIL
6. Future Leaders in Used Commercial Vehicle Finance, Avendus
7. Tata Motors, Bajaj Auto, Economics Times
8. CV financing NBFCs AUM growth expected to be in double digit in FY23, CARE accessed in November 2022

Gold market has been driven by a steady increase in prices

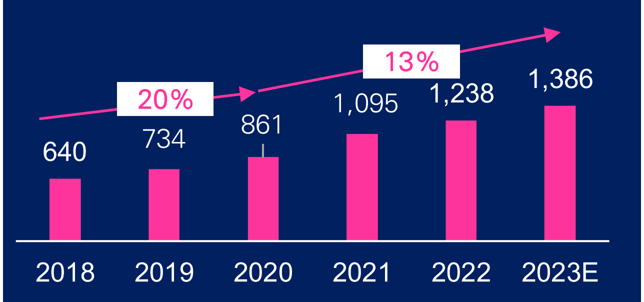
How has gold marked shaped over the years in India?

India is one of the largest gold markets contributing 1.3 per cent to Indian GDP[1], owing to its security, ease of liquidity conversion and culture affinity. Gold loan market has also been positively correlated with gold price movements on account of macro-economic and global factors i.e., during the pandemic, gold prices reached INR4,332 per one gram in July 2020[2] whereas after the economy started gaining momentum with relaxed lockdown, gold prices dropped to INR4,082 per one gram in April 2021.

Changes in customer behavior

Increase in customer orientation towards gold loans: no longer seen as a loan of last resort.	Gold loan has moved from being a traditional product availed at the time of emergency to meeting the consumption and business led requirements.
Onset of digital fintech players such as Rupeek and Manipal have made the process of availing gold loans seamless and convenient by facilitating doorstep evaluation, digital loans etc.	In the NBFC ecosystem, innovative models are being identified to increase the tenure of gold loans from 3–6 months to 12 months owing to a significant uptick in the online gold loan sourcing.

Organized gold loan market holds 35 per cent (~INR5.1 trillion) assets under management in 2022 of which banks have a 76 per cent share and NBFCs hold 24 per cent share[3]. NBFCs have driven the market with targeted USPs whereas banks offer better prices and branch convenience. In unorganized sector, individuals avail loans at a rapid pace but at high prices. Overall, NBFCs are well-poised for a growth in coming years, enabling digital transformation in gold loan life cycle process basis the partnership-based models. However, there are several areas wherein NBFCs can seek regulatory guidance of having a parity or improving loan to value ratios.



NBFC gold loan AUM[4] (INR billion)

Key asks from NBFCs

NBFCs are demanding for gold loans to be a part of the PSL category if used for agriculture as an end use, or if digital gold bonds can be a part of the category and can be allowed to facilitate locker facilities to provide loans based on the procured assets.

Tractor and farm equipment

Tractor as a segment was not disrupted significantly by the COVID-19 pandemic owing to the rural demand and agriculture sector largely keeping up the momentum. Consequently, NBFCs contribute around 54 per cent of financing of tractors, out of which OEMs such as Mahindra and Eicher contribute 67 per cent of the entire contribution by NBFCs. There are a total of 20 financial institutions which provide loans to businesses to buy new or pre-owned tractors. 70 per cent of the total trackers sold each year are financed by private banks and NBFCs, 10 per cent by public banks and 20 per cent in cash with no finance.[5]

Increasingly in the agriculture and rural segment, a bunch of agriculture technology has mushroomed in order to help lenders understand crop patterns and underlying geographical conditions seamlessly for accurate credit assessment which can be further leveraged for tractor financing and agriculture-based financing holistically. The rural financing has also moved beyond secured asset financing through products such as tractor and farm equipments to have a holistic coverage with the help of agriculture technology.

Source: 1. Domestic Gold Industry Contributes 1.3% To Indian GDP, Business Standard
2. Gold Prices, Gold Price
3. KPMG in India's analysis 2022
Budget 2022: Gold loan NBFCs require adequate policy support for growth, BFSI
4. India NBFC Sector Update – H1 FY22, CRISIL
5. Indian Agricultural Tractor Market Report 2019-2023 with a Focus on Key Industry Players, GlobalNewswire, accessed in 11 November 2022

05

Key Business initiatives, other Sectors and Regulatory updates

Co-lending model

Co-Lending and partnership model is expected to gain traction as banks and NBFCs align the underwriting parameters basis market feedback and overcome operational challenges

An ecosystem where banks and non-banks co-originate priority sector lending while sharing risks with an 80:20 ratio[1] wherein 80 per cent of the loan is with the bank and a minimum of 20 per cent is with the non-banks. Banks and NBFCs can price their part of the exposure whereas repayment and recovery of interest is shared. The main purpose of CLM is to boost the flow of credit to the unserved and underserved segment of the economy at an affordable cost by leveraging greater reach of NBFC's beyond tier-2 centers.

While co-lending has potential to drive growth in affordable housing , MSME and agri sectors given the PSL benefits, key operational challenges will need to be tackled to achieve the below parameters.

01 Collection and monitoring

- Automated splitting of escrow funds between banks and NBFCs,
- Loan booking date for interest calculation,
- Broken period interest allocation logic,
- Splitting logic in case of moratorium, short EMI, early EMI and foreclosure of loan, Single unified statement by reconciliation between NBFC LMS and Bank's CBS

03 Pre-Sanction

- Customer due diligence and KYC without direct contact with customer,
- Handling of cases rejected by bank (legally and operationally), and
- Digital legal vetting of executed documents

02 Disbursement

- Signing of assignment deed between banks and NBFC,
- Charge creation in case of secured loans,
- Creation of customer specific escrow account for collections, and
- Set-up of revised NACH on escrow account

04 Accounting Logic

- Accounting Standard Applicability (IND AS vs Indian GAAP), accounting calendar (360 vs 365 days) and NPA classification,
- CIP vs PIC structure for collections, and
- Calculation of interest rate charged to customer

Centralized processing setup for co-lending business is critical to drive the business at scale

Centralized Processing Model for CLM processing will be required for co-Lending business unit including:

- Centralized cell/CPC as a 'single' processing center operating at PAN India level.
- CPC caters to all possible CLM products and partner NBFCs.
- The CPC will process both option 1 and option 2 loan applications as defined by the RBI guidelines.
- Due-diligence/credit appraisal should not be done at any local/nodal/specialized branch.
- Centralized CPC handles activities ranging from bank level due diligence to escrow management.

Digital Co-Lending platform is critical to drive Co-lending business at scale

Plug and play single platform

Single platform for sanction of loans belonging to all NBFCS and co-lending products

API Integration with CBS and escrow

API for auto disbursement from loan account in CBS to escrow account and tracking of final disbursement to borrower

Business rule engine

Sanction/reject or raise deviation of proposal basis underwriting validation

Document management system

Store the agreement and documents on DMS

Collection Management

Generation of demand request through integration with CBS, and monitor and auto-update collection status through integration with CBS

Virtual Account for Collection

Collection from escrow account to enable tracking of collection payments by customers.

Fintech integration partner

API integration to collect digitally verifiable data

Source: 1. What is co-lending by banks and NBFCs?, Moneycontrol, accessed in November 2022

Overview of scale-based regulations

How are the changes prescribed RBI within 'scale-based' framework aligns with the regulatory framework?[1]

February 2021

- CFSS (CBS) mandated for NBFC in ML and UL with > = 10 branches

October 2021

SBR released

April 2022

- Detailed guidelines for LEF and CET-1 ratio released for UL
- KMP and Senior Management of NBFCs excluded from guidelines.

July 2022

- Guidelines released for granting loans and advances. Framework for compliance function and role of CCO in NBFC-ML and UL
- Disclosure templates released for SBR

September 2022

- RBI releases list of 16 NBFCs identified in the Upper Layer

October 2022

- Clarification issued for consideration of consolidated asset size of NBFC group, being classified in BL or ML (not for classification in UL)

Key changes under the SBR framework

Governance: BoDs will have at least one director with relevant experience

Capital: Minimum NOF increased to INR10 crores for NBFC-ICC, NBFC-MFI, and NBFC Factors

NPA classification and provisioning: All NBFCs required to classify overdue >90 days as NPA

Concentration and leverage: For NBFCs in ML and UL, Sensitive Sector Exposure (SSE) limits will be fixed and approved by BoD

Board composition and risk management: For NBFC-UL, board must have a mix of educational qualification and experience. Removal of IDs to be reported to RBI prior to exit

Other changes: Expanded disclosure norms to include exposure type, related party transactions, customer complaints, and loans to senior officers

SBR- impact on NBFCs and the road ahead

	Key impact of SBR	Road ahead
Capital	CET 1 of at least nine per cent of risk weighted assets for NBFC-UL may shore up reserves for absorbing stressed assets	Enhanced capital planning and monitoring framework to incorporate the economic capital required for mitigation of pillar 2 risks.
Risk management	Mitigation of systemic risks, posed by the immense growth in NBFC asset size, through regulation of excessive risk taking	Enhancement of ERM framework for managing credit, liquidity and operational risk including AML and financial crime risks. Integration of ERM with the ICAAP framework
Governance	Enhanced responsibilities placed on the Board for ensuring appropriate and periodic monitoring	Setting up of stronger governance framework with clear delineation of roles and responsibilities of senior management/board.
Technology	Introduction of Core Financial Service Solution (CFSS akin to CBS in banks) may require strengthening of systems and processes and aid in convergence with banking operations	NBFCs to develop CFSS providing seamless customer interface in digital offerings and act as a centralized database for generation of MIS reports for reporting and internal purpose.

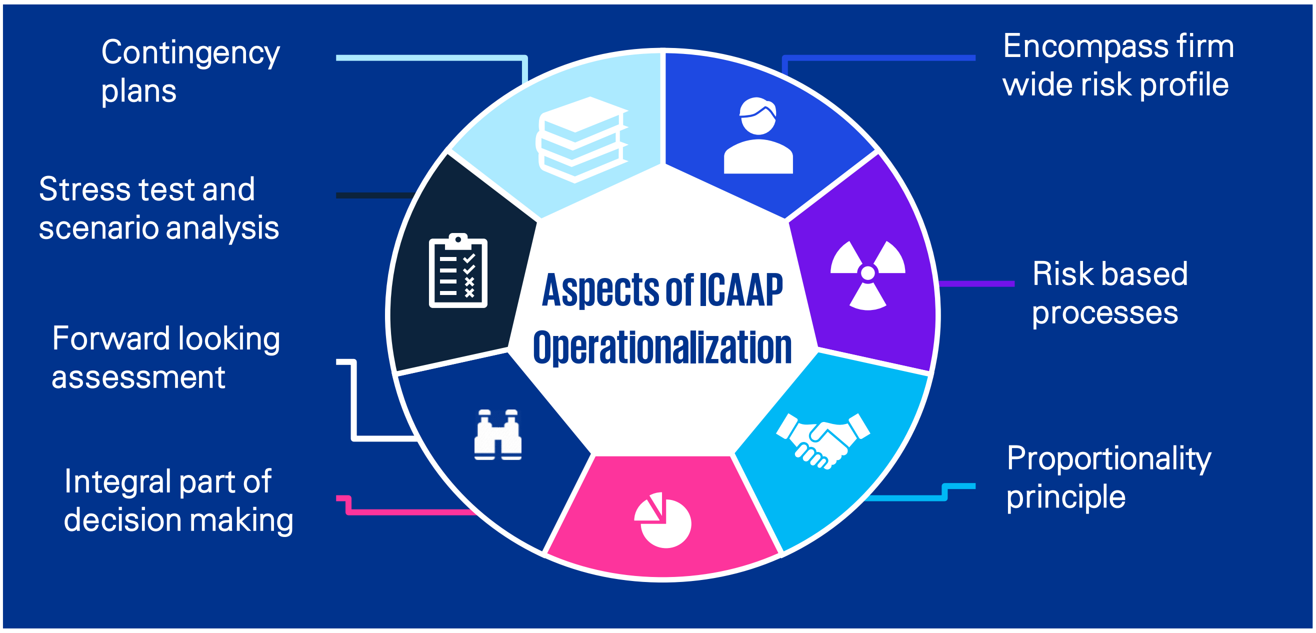
Source: 1. KPMG in India's analysis 2022

ICAAP and its challenges

How is ICAAP ensuring risk management within NBFC and what are its growing challenges within the industry?

NBFC-NDSI and NBFC-D are on Basel I type framework and are mandated to have a minimum capital of 15 per cent of the Risk Weighted Assets (CRAR). NBFCs, which are in the middle and upper layer, need to make a thorough internal assessment of the need for capital, commensurate with the risks in their business, on similar lines as ICAAP for banks.

The main aim of ICAAP is to ensure availability of sufficient capital to support all risks in the business and to encourage NBFCs to develop and use better risk management techniques through continuous involvement of senior management personnel in developing, defining and reviewing the risk governance framework and associated strategy for monitoring and managing their risks.
ICAAP framework will enable NBFCs to compute institution specific material risks in excess of those covered for regulatory purpose. The goal is to incorporate various aspects including forward-looking assessment of business strategies commensurate with risk appetite, processes and controls to ensure internal capital and liquidity adequacy.



Challenges faced in its implementation

Risk assessment	• Developing distinct risk capacity, appetite, tolerance and limits with implementation • Development of holistic stress testing scenarios to ensure accurate simulation
Effectiveness of risk governance, appetite and strategy	• Defining the extent of responsibility, accountability, and involvement of senior management • Reconciling regulatory capital with strategic planning and return expectations
Assessment of capital requirements	• Capital adequacy assessment needs to go beyond regulatory reporting to realize opportunities of capital management within strategic planning and business operations • Sound identification and quantification of all material risks, allowing the determination of an economic capital measurement consistent with the institution's risk profile
Operational requirements	• Ensuring data accuracy of the input data and appropriates of the model selected • Training and development of resources to ensure adequate understanding for ICAAP implementation and ongoing reporting

Source: KPMG in India's analysis 2022

P2P lending

How is P2P lending landscape in India shaping up?

The digital intervention in financial services has opened new avenues of accessing funds which has revolutionized the entire credit landscape. P2P lending platforms act as an alternative mode of obtaining finances for traditional banks and societies.

P2P lending as a marketplace models is rightly positioned to cater the needs of un-served population

P2P-Consumer (Personal Loans, Car Loans, Home Loans)	P2P- Business (SME lending)	P2P-Real Estate	P2P-Invoice Lending

Unique Selling Proposition of the P2P credit providers

- **Ease of Credit:** Rapid credit dissemination in a matter of few hours from the time of credit application
- **Unconventional underwriting model:** Use of alternative data to assess borrowers credit worthiness allows those with no credit history to obtain loans
- **Technology adoption:** Functioning as a marketplace, it is imperative for P2P lenders to remain agile and ahead of the technology adoption curve. Thus, APIs led real time insights, early warning signals RPA driven contracting, and disbursement and AI-ML driven underwriting are some of the examples setting trends for industry.

P2P lending market[1]

Market Size[a] (2021)

INR30 billion

CAGR (2021 -26)

~22%

NBFC-P2P platforms in India

25

Driving forces for P2P lending growth

- **Demography:** India as a country has higher proportion of young population who are digital natives and aspiration consumers driven by high experiential needs.
- **Untapped Potential:** Low credit penetration in the rural part of India and hesitation by financial institution in lending money to first time/small borrowers with no credit history has fueled the growth of digital lending. Internet and smartphone penetration to the rural parts of India helped meet the unmet demands of users.
- **Pandemic woes:** Covid-19 turned out to be a boon for the digital lending industry as their was stress and financial instability across places and it was becoming difficult for individuals to make ends meet. Easier access to credit was enabled by these organization helping user to meet their financial requirements.

Where do we go from here?

- FinTech lenders are targeting credit gap of USD300 billion[3].
- By 2023, retail credit demand is expected to reach USD736 billion[3] which further provides opportunity for growth of FinTech lenders
- Entry of P2P lenders will improve efficiency of traditional banking companies as technology flows from FinTech peers
- Tighter regulatory supervision as the volume and value of P2P originated credit grows. RBI would ensure that the risks of such model (such as wider access to credit and increased competition may result into reduced lending standards) do not overweigh the benefits of financial inclusions
- As this segment grows, bigger players in the FinTech sector could make their entry into P2P lending space that would change the pace of technology adoption etc
- As decentralized financial service offerings penetrate deeper across cross product/service value chains the scope for P2P lending would grow

Note: A.Market size refer to the amount of loan that has been disbursed by P2P platforms in 2021
Source: 1. Report of the Working Group on Digital Lending including Lending through Online Platforms and Mobile Apps, RBI
2. Credit risk and reward: P2P offers returns but needs cautious investments, Business Standard
3. A REVIEW OF INDIA'S CREDIT ECOSYSTEM, Experian
4. List of P2P NBFCs registered with RBI, RBI

Factoring

How does factoring play the role?

Factoring refers to a process involves selling some or all a businesses' invoices and accounts receivable to a financial service provider known as a factor. A factor advances cash to a business based on the value of its accounts receivable or unpaid invoices, typically around 85 per cent[1]. Factoring can be an effective financial assistance model to small and medium sized businesses, helping them manage their cash flow, administer accounts receivables and acquire finance for business growth.

Total Factoring volume (in INR million)[1a]

Challenges in Factoring business

01 Lack of public awareness about factoring process

02 Scalability challenges faced by Trade Receivables Discounting System (TReDs) platform

03 Low market penetration-Factoring Credit constitutes below 5 per cent of total formal SME credit finance in India

04 TReDs platform accepting factoring invoices from MSMEs with buyers that have Rs 500 Crore plus turnover

05 Extreme delays in receipt of invoice payments and litigation delays

Regulatory changes

- Entity intending to enter factoring business shall apply for Certification of Registration (COR) with RBI subject to below eligibility criteria:
  - Minimum Net Owned Fund (NOF) of INR 5 Crores
  - Financial assets in factoring should be >= 50 per cent of total assets and income derived from factoring should be >= 50 per cent of gross income
- Existing NBFC ICC (Investment and Credit Company) shall apply for Certification of Registration (CoR) with RBI subject below eligibility criteria:
  - Does not accept or hold public deposits
  - Total Assets >= INR1000 crores as per last audited balance sheet
  - Minimum Net Owned Fund (NOF) of INR 5 Crores
- Existing NBFC-ICC intending to enter factoring business but not able to comply with above eligibility criteria shall approach RBI for conversion from NBFC-ICC to NBFC-Factor

Impact

- This will lift the number of NBFCs eligible to undertake factoring business considerably from 7 to 182.
- NBFC-ICC intending to enter factoring business but not meeting eligibility criteria can seek RBIs exceptional approval
- Increase in participation by NBFC-Factor on TReDS system will help in faster realization of receivables for MSMEs and lower cost of customer acquisition for NBFC-Factor

Note: A. For calculating Total Factoring volume, CAGR of 5 per cent has been assumed due to data unavailability.
Source: 1. KPMG in India's analysis 2022
2. Registration of Factors (Reserve Bank) Regulations, 2022, RBI

Fintech

Are we due to see any more revolution in the Fintech space?

Fintech sector has an exemplary decade, being at the forefront evident from the launch of new form of credit lines. India has been one of the fastest growing fintech market expected to reach USD1 trillion by 2030[1]. It is a consolidated whole of diverse players bringing sophisticated mix of financial service offering on back of high-tech operating model driving better customer experience and process efficiency.

BNPL

BNPL market is expected to grow 15 times in the next five years[2]	BNPL users are expected to surpass credit card users by FY26[2]	12 per cent of loans originated through BNPL were disbursed through NBFCs[3]

Indicators for growth

- Household debt to GDP ratio of 11.3 per cent[2] highlights untapped potential.
- 41.1 per cent[2] smartphones penetration in India signifies easier access to digital credit.
- BNPL's partnership-based business model benefits e-commerce players with higher customer retention owing to simplified customer journey/experience.
- Data and technology driven underwriting facilitates simplified user journey

Outlook

- Indian BNPL segment will move towards a merchant focused revenue model as adopted by peers in developed economies.
- Some of the players thriving on regulatory arbitrage would require to re-look to ensure compliance with the guidelines.
- Given its potential and ability to serve the unserved class, BNPL in its current form might get regulated by RBI with due emphasis around customer protection, exposures etc.

Digital and co-lending

Consumer credit gap in India is around USD300 billion[4]	Retail credit demand is expected to reach USD736 billion by 2023[4]	In India, Digital lending market is expected to grow at a CAGR of 17 per cent[6]

Indicators for growth

- Government led policies and frameworks changes such as IndiaStack, Regulatory Sandbox and other financial inclusion schemes have opened multiple opportunities.
- Digital lending space has seen an exorbitant growth in terms of volume of disbursement, to reach INR1,418.21 billion in 2021 from INR116.71 billion in 2017[3].

Outlook

- With strict regulatory landscape, significant investment would be required on co-lending framework which will help mitigate risks emanating from FLDG arrangements.
- Marketplace startups such as hyper local delivery, food aggregators etc. have a strong network in form of stores (merchants) and customers therefore their entry can prove to be a sector disruptor.
- Government's mandate for PSBs to onboard an Account Aggregator system will change the dynamics of credit industry by enhancing efficiency

Payment Aggregators

45 per cent of online transaction in 2021, carried out using digital wallets[3]	As of 2020, there are 4.6 million POS terminal available in India[3]	Payment transaction volume grow at a CAGR of 21 per cent from 2017-2021[3]

Indicators for growth

- 34 per cent of the market share in terms of volume is controlled by UPI and 20.57 billion transaction in volume were recorded for 2Q22[5].
- Government of India have proactively promoted the Digital India initiatives and the recent one of linking credit cards for UPI transactions can be a game-changer in the payments industry fostering new opportunities for aggregators.
- Higher digital, mobile and internet penetration has facilitated growth of payments in India

Outlook

- Entities that pose as a challenger to the incumbents could foray into the payment aggregator space on the back of strong data flow such as technology and telecom companies which could potentially change the industry dynamics such as Zero Merchant Discount Rate (MDR), etc.

Source: 1. Indian FinTech market to reach $1 trillion by 2030, The Hindu
2. THE INDIA BUY NOW PAY LATER REPORT 2021, Zest Money
3. Report of the Working Group on Digital Lending including Lending through Online Platforms and Mobile Apps, RBI
4. A REVIEW OF INDIA'S CREDIT ECOSYSTEM, Experian
5. Worldline's 'India Digital Payments Report' Q2 2022, Worldline;
6. KPMG in India's analysis 2022 based on industry reports and market research
, all accessed in November 2022

Digital lending

How does digital lending regulations shape the future of NBFCs?

Digital lending opportunity is expected to grow at 17 per cent[1] over the next few years creating massive business opportunity for the financial institutions, attributable to the increase in account aggregator model adoption, bureau coverage, data availability, fintech collaborations, higher government support and increasing internet penetration. While the digital lending ecosystem is evolving and banks are increasingly adopting innovative approaches in digital processes, NBFCs are playing at the forefront of partnered digital lending.

Key takeaways for stakeholders

Chief Executive Officer

- Appoint nodal grievance redressal officer and ensure Regulated Entities (RE) are not storing personal data.
- Ensure state level coordination committee meetings cover reports on digital lending.

Chief Information Officer

- Change in API integration around disbursements and repayments, efficient customer data recording and automation in lending process
- Creation of consent management mechanism.
- Create comprehensive data policy for governance, storage and disclosure.

Chief Operations Officer

- Ensure efficient direct disbursement system, establish customer consent process, determine customer cooling off period and implement efficient onboarding review system.
- Implementation of new stage before e-signing of document displaying KSF to borrower in system.

Chief Risk Officer

- Reporting of digital lending products to the credit bureaus, compliance of cyber security, data privacy and storage norms, and implementation of grievance redressal review system.

Potential impact

People	Process	Product	Technology
Direct execution of loan servicing in the account, with exceptions considered for disbursals under statutory mandate.	New process of direct disbursement to be established, and pooling of money into collection account will also be discontinued.	Change in customer experience managed by lending platforms, and no products backed by prepaid cards	API integration, mandate registration, data storage methodology and security architecture and repayment application to be modified.

Recent guidelines published by RBI around digital lending aims to protect customers, however, hold a significant impact on digital lending companies. Some of the key considerations include:

- Greater onus of regulatory compliance on REs
- Lending Service providers (LSP) to reassess business models
- Data privacy related guidelines limiting the use of customer data and requisition of customer consent
- Need for LSPs and Digital Lending Apps (DLA) to increase their investment in technology to meet cyber security requirements and prevent data leakages

Regulatory outlook – Where do we go from here?

- RBI's inclusive growth agenda focuses on growing digital lending, along with enhancing customer confidence and preventing entry of unscrupulous entities in the system.
- Account and payment aggregators, marketplace lenders and LSPs are expected to implement change in their business models and strategies.
- Reassessment of the contract between RE and LSP, consolidation of LSPs/DLAs with their partner REs and an evaluation of FinTechs which do not have capital support can be expected.
- REs are expected to transform and invest in technology, develop customer experience strategy, robust framework to address financial crimes, customer data privacy to meet market demand and regulatory requirements.

Source: 1. KPMG in India's analysis 2022 based on industry reports and market research

Technology, AML, fraud, technology and data risks

In addition to the guidelines on digital lending, The Reserve Bank of India has recently issued Draft Master Directions pertaining to Outsourcing of IT Services and IT Governance, Risk, Controls and Assurance Practices. The key action items for NBFCs would be to focus on the following

Digital Lending	• Document a comprehensive privacy policy regarding the access, collection, storage and use of customer data, to be made publicly available. • Implement a robust process for handling customer data covering all phases including data collection, data storage, use, retention, deletion. • Ensure data is stored in local servers within India, along with complying as per technology standards and requirements stipulated by RBI and other agencies.
IT Governance, Risk, Controls and Assurance	• Ensure appropriate IT Strategy planning and Governance are performed involving senior management. • Define performance metrics, KRIs and Data Dictionary, and document comprehensive policies, SOPs for various IT and IS operations. • Implement suitable IT and IS controls to mitigate the overall inherent risk faced by the organization. • Keep BCP and DR plans current and review readiness of supporting infrastructure to sustain operations Perform independent risk-based IS Audits periodically, to highlight critical issues to the management
Outsourcing of IT Services	• Document a comprehensive IT Outsourcing policy and governance framework. • Perform appropriate due diligence before onboarding any service provider. • Sign outsourcing agreements including all critical clauses with vendors. • Create inventory of service providers and map their dependency on third parties and periodically evaluate the information received from service providers. • Perform Periodic Internal and External audits depending upon nature and risk of service outsourced.

Incidents in recent years have exposed financial crime related risks manifesting at the highest level exposing the sector abuse of authority, and various forms of misappropriation of funds. These risks not only involve various shades and elements of risk involving Fraud, Money laundering, Conduct, but pose a larger question on how Financial Crime risk is holistically and proactively managed within NBFCs?

Money laundering

- Proceeds of crime entering in NBFC having unclear source of funds, by way of:
  - At entity structuring stage by way of capital infusions (e.g., inter-corporate deposits, performance guarantees), or;
  - even during repayment (partial/complete) stages
- Abuse of co-lending models by way of misutilization of security deposits or other vulnerable areas
- Product provision to entities which have unclear entity structuring involving multiple layers, potential shell/shelf companies or even involved in violation of forex exchange norms

Fraud risks

- NBFC's have exposures to various forms of risks allowing manifestation of fraud both from an Internal (I) and External (E) standpoint, the key ones are:
  - a. Abuse of Authority including conflict of interest (I)
  - b. Window dressing of financials including manipulation of internal accounts (I and E)
  - c. Misutilization/Diversion of funds including Evergreening of accounts (I and E)
  - d. Onboarding known-bad customers including fabricated documents or inflated/dubious valuations (I and E)
  - e. Theft or misutilization of sensitive client data

With surge in overall credit demand in NBFC sector, to foster and maintain customer "Trust" it is imperative to adopt following key points:

- **Technology enabled proactive Financial Crime Management framework** is key to sustained growth. Predictive models leveraging internal and external intel for identification of early warning signals not only in borrower assets but including internal conduct of the Bank.
- **Clear control standards** to be established, adopted, monitored for effective and proactive management of financial crime risks. Special focus required on periodic and proactive threat assessments to identify, assess and take effective measures to mitigate emerging risks.
- **Customer centricity** including putting customer's data at pivotal position for a secure digital eco-system. Other fundamental pillars to include end to end encryption of customer data robust customer complaint management framework including extrapolation and thematic reviews to identify vulnerabilities.
- **Board level committee** to track risk of financial crime and misconduct.

Driving value proposition through ESG

How will ESG drive the value for Financial services and specially NBFCs in the future?

India is the 19th largest Green, Social and Sustainability (GSS) market across the globe and sixth in the APAC region, behind China, Japan, South Korea, Australia, and Singapore. We witnessed a growth of 585 percent[1] in bonds issuance amount from 2020 to 2021, to become the fastest growing APAC country.

In India, BSE S&P 100 ESG Index has generated total returns of 96 percent[2] over the last five years. The non-ESG equivalent index has generated returns of 82 percent over the same period. Indian IT firms have clearly been at the forefront of the ESG race, demonstrating that the use of digital technology in ESG service will have a key role to play. The transition to sustainable and resilient future entails a continual flow of funds towards renewable energy production and decarbonization of transport, industry and buildings. While India has made a healthy start, the country faces a huge gap in supply of sustainable finance. The country require approximately INR11 lakh crores (USD 170 billion)[3] per year to meet Paris Agreement commitment. Multilateral DFIs has provided INR11,027 crores in FY19 and FY20[3], with an overall contribution by commercial FIs, DFIs, and PSUs of approximately 65 percent, 17 percent, and 17 percent, respectively.

ESG integration at the epicenter of Indian economy ..

Affordable housing

India has USD0.62 trillion[4] funding opportunities. Green building in affordable housing is fastest growing segment, with a market share of two percent.

Integrating with MSME

In 2021, INR5,400 crore[5] were spent by top Indian corporates associated with Science Based Targets initiative (SBTI) to reduce about 5.5 million tones of carbon dioxide emissions. In total, Indian companies have raised US$13.7 billion worth of ESG debt in 2021[6].

Green Bond Market in India[1]
USD18 billion

Sustainability Bond Market in India[1]
US$600 million

Social Bond Market in India[1]
USD500 million

Policy overview

- The Green Bonds Framework was released by the government, rated as "Medium Green" with a "Good" governance score[7].
- RBI recently joined the Network for Greening the Financial System (NGFS) in April 2021[8], to learn and contribute to global efforts on green finance and help achieve country's target to cut its emissions to net zero by 2070.
- From FY23, it will be mandatory for top 1,000 companies to publish their Business Responsibility and Sustainability Report[9].
- Task Force on Sustainable Finance of the NITI Aayog and the Ministry of Environment, Forests and Climate Change constituted working group in January 2021 to create taxonomy of sustainable activities
- The announcement of Development Finance Institution (DFI) in Budget 2020-2021 is a welcome step.
- Large-scale renewable energy segment is expected to dominate., while solar rooftop and EVs are expected to remain the next prospects.
- Interest rate movements would affect GSS issuance volumes.

Impact

- Green bond is a new asset class. The initiatives introduced by Government of India will improve liquidity in ESG bond market.
- Mandatory disclosure for listed companies will add more comforts to the ESG investors as access to ESG related information will be a quick win.
- Finance and technology know how are two must have for ESG projects. Recent initiatives announced by Government of India address Finance part of the project however private sector need to look at technology-driven solutions.

Source: 1.Indian Sustainable debt state of the market, Climate Bonds Initiative,
2. S&P BSE 100 ESG Index", S&P Dow Jones Indices
3. Landscape of Green Finance in India 2022, Climate Policy initiative
4. Brick by Brick - Long term capital to fund affordable housing for all, Knight Frank
5. Many India Inc majors may be Net-Zero by 2050, Economic Times,
6. 'It's early days, but India's ESG ecosystem is growing rapidly', Eco-Business,
7. Union Finance Minister Smt. Nirmala Sitharaman approves India's First Sovereign Green Bonds Framework", Ministry of Finance India,
8. Reserve Bank of India Commits to Support Greening India's Financial System- NGFS", RBI;
9. SEBI issues Circular on "Business Responsibility and Sustainability Reporting by listed entities", SEBI, accessed in November 2022.

Acknowledgements

Abhijeet Lakule	Partner, FS Deal Advisory
Somdeb Sengupta	Partner - Financial Risk Management
Muralidharan Venkataraman	Partner - FS Business Consulting
Sachin Bhatia	Partner - FS Governance Risk and Compliance Services
Rohan Padhi	Partner - FS Digital Trust
Anoop Sharma	Technical Director - FS Forensic Services
Devang Patel	Director - FS Business Consulting
Ashish Ranjan	Director - FS ESG
Chintan Kapadia	Vice President - Deal Advisory
Omkar Sawant	Senior Associate Director - FS Sector, Markets
Gautam Bhagat	Associate Director - Financial Risk Management
Siddhartha Pappala	Manager - Business Consulting
Krishnayan Chakraborty	Manager - Business Consulting
Nandini Iyer	Manager - Financial Risk Management
Yogesh Kulkarni	Assistant Manager - ESG
Debarghya Goswami	Assistant Manager - Financial Risk Management
Vaibhav Khanolkar	Assistant Manager - Financial Risk Management
Raaghav Sekhri	Consultant - FS Governance Risk and Compliance Services
Aadish Jain	Consultant - FS Business Consulting
Aravindan R	Consultant, FS Business Consulting
Siddharth Soni	Senior Associate - Deal Advisory

KPMG Global Services (KGS)

Priyanka Sethi	Assistant Manager
Shriya Aggarwal	Consultant
Vishal Sridhar	Consultant
Rudhrika Agarwal	Associate Consultant
Aman Kothari	Associate Consultant

Markets

Marketing Compliance	Nisha Fernandes
Brand and Design	Anupriya Rajput, Darshini Shah

KPMG in India contacts:

Vinay Narkar
Partner, FS Business Consulting
E: vinaynarkar@kpmg.com

Sanjay Doshi
Partner and Head, FS Advisory
E: sanjaydoshi@kpmg.com

Amit Wagh
Partner and Co lead, Banking and NBFC
E: amitwagh@kpmg.com

Suveer Khanna
Partner and Head, FS Risk Advisory
E: skhanna@kpmg.com

home.kpmg/in/socialmedia

KPMG Assurance and Consulting Services LLP, Lodha Excelus, Apollo Mills Compound, NM Joshi Marg, Mahalaxmi, Mumbai - 400 011 Phone: +91 22 3989 6000, Fax: +91 22 3983 6000.