6th November 2023

Fedbank Financial Services Limited
Kanakia Wall Street,
A Wing, 5th Floor, Unit no. 511,
Andheri Kurla Road,
Andheri (East), Mumbai- 400 093,
Maharashtra, India

Dear Sir,

Re. **Proposed initial public offering of equity shares of face value of Rs 10 each (the "Offer") by Fedbank Financial Services Limited (the "Company")**

We refer to your e-mail/ request dated 5 October 2023 regarding the content provided to you for your use by CRISIL MI&A as part of your subscription to its Industry Research on the following industry:

- CRISIL MI&A – Analysis of NBFC sector and select asset classes in India, October 2023 ("Report"), released in Mumbai, India

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- Your ensuring that there is no misrepresentation/modification to our views/opinions and that the Material is not mentioned out of context or misguidingly.
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Given below is the disclaimer to be used in the Offer Documents.

"CRISIL Market Intelligence & Analytics (MI&A), a division of CRISIL Limited (CRISIL) has taken due care and caution in preparing this report (Report) based on the Information obtained by CRISIL from sources which it considers reliable (Data). This Report is not a recommendation to invest / disinvest in any entity covered in the Report and no part of this Report should be construed as an expert advice or investment advice or any form of investment banking within the meaning of any law or regulation.Without limiting the generality of the foregoing, nothing in the Report is to be construed as CRISIL providing or intending to provide any services in jurisdictions where CRISIL does not have the necessary permission and/or registration to carry out its business activities in this regard. Fedbank Financial Services Limited will be responsible for ensuring compliances and consequences of non-compliances for use of the Report or part thereof outside India. CRISIL MI&A operates independently of and does not have access to information obtained by CRISIL Ratings Limited, which may, in their regular operations, obtain information of a confidential nature. The views expressed in this Report are that of CRISIL MI&A and not of CRISIL Ratings Limited . No part of this Report may be published/reproduced in any form without CRISIL's prior written approval."

This Material and this letter may be shared by the Company, with the book running lead managers (including their affiliates) and advisers concerned in relation to the Offer (as listed in **Annexure A** of this letter). We also authorise you to deliver this letter of consent to SEBI, the Stock Exchanges and the RoC pursuant to Section 26 and Section 32 of the Companies Act 2013, and the rules thereunder, each as amended, or any other legal, governmental or regulatory authority as may be required, in relation to the Offer.

We also consent to the inclusion of the Report and this letter as a part of "Material Contracts and Documents for Inspection" in connection with the Offer, which will be available for public for inspection from the date of the RHP until the Bid / Offer Closing Date and also be made available online, and the link to where the Report would be accessible would also be included in the DRHP, RHP and Prospectus and any such other form of access to the Report and/or this letter, and/or any engagement letter (Reference number of Technical Proposal: SS/BD/FEDFS/DRHP/2021/CH1211) as may be required under applicable law or regulatory direction, request or order, and we have no objection with you sharing the Report and/or this letter, and/or any engagement letter (Reference number of Technical Proposal: SS/BD/FEDFS/DRHP/2021/CH1211) with any regulatory or judicial authority as required by law or regulation in relation to the Offer or pursuant to a request / order passed by any authority.

We confirm that we are not and have not been engaged or interested in the formation or promotion or management of the Company. As per our records and information submitted by the Company, we confirm tht the Company, its promoters, directors and the book running lead managers as stated in **Annexure A** are not a related party (as defined in the Companies Act, 2013 or applicable accounting standards) of CRISIL Limited as on the date of this letter.

We further confirm that we have, where required, obtained requisite consent or duly acknowledged the source(s), as may be required, by any governmental authority or other person, in relation to any information used by us in the Material.

We represent that our execution, delivery and performance of this consent has been duly authorized by all necessary actions (corporate or otherwise).

This letter does not impose any obligation on the Company or the book running lead managers (as stated in **Annexure A**) to include in any Offer Document all or any part of the information with respect to which consent for disclosure is being granted pursuant to this letter provided that the terms of this letter are complied with.

We agree to keep strictly confidential, the non- public information relating to the Offer until such time that: (A) such disclosure by us is approved by the Company; or (B) such disclosure is required by law or regulation subject to CRISIL intimating the Company/book running lead managers (including their affiliates) in advance if permissible and practicable; or (C) such information is already in public domain or comes into public domain through no fault of ours.

Capitalised terms used herein but not defined shall have the same meaning as ascribed to them in the Offer Documents.

For CRISIL Limited

Suresh

CRISIL Limited Mumbai

Suresh Krishnamurthy

Senior Director, CRISIL MI&A

Annexure A

Name of the Company: Fedbank Financial Services Limited

Name of the Promoter(s) of the Company: The Federal Bank Limited

Fedbank Financial Services Limited – List of Directors

S.No	Name	Designation
1.	Mr. Balakrishnan Krishnamurthy	Chairman and Independent Director
2.	Mrs. Gauri Rushabh	Independent Director
3.	Mr. Shyam Srinivasan	Non-Executive Director
4.	Mr. Maninder Singh Juneja	Non-Executive Nominee Director
5.	Mr. Ashutosh Khajuria	Non-Executive Nominee Director
6.	Mr. Anil Kothuri	Managing Director and Chief Executive Officer

Book Running Lead Managers

- ICICI Securities Limited
- JM Financial Limited
- Equirus Capital Private Limited
- BNP Paribas

Advisors

- Cyril Amarchand Mangaldas
- J. Sagar Associates
- White & Case
- Link Legal

Market Intelligence
& Analytics

CRISIL
An S&P Global Company

Analysis of NBFC Sector and select asset classes in India

For Fedbank Financial

October 2023

Consulting

INDUSTRY OVERVIEW

Macroeconomic scenario

Global economy is witnessing tightening of monetary conditions

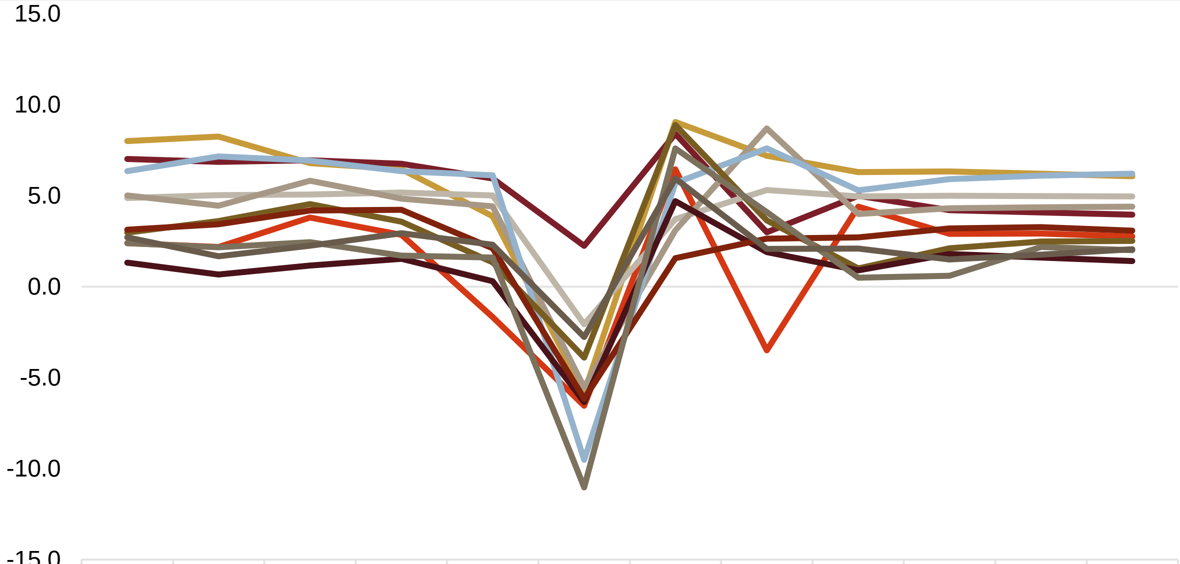
The global economy is witnessing tightening of monetary conditions in most regions. As per the International Monetary Fund ("**IMF**") (World Economic Outlook- October 2023 update), global growth prospects are estimated to fall from 3.5% in 2022 to 3.0% in 2023 and 2.9% in 2024, the impact of which is expected to be witnessed in the Indian economy as well. Global trade is estimated to have reached a record level of approximately US$32 trillion in 2022, but its growth had turned negative during the second half of 2022. The trade outlook for calendar year 2023 is expected to be negatively impacted because of geopolitical frictions, persisting inflation and lower global demand. In addition, deceleration in domestic growth could lead to some softening in imports.

The United States ("**US**") economy grew by an annualised 2.1% in the second quarter of 2023, slowing compared with the previous quarter (2.2%). The United Kingdom ("**UK**") economy grew at 0.2% on-quarter in the second quarter, but the latest data for July 2023 shows that its gross domestic product ("**GDP**") contracted 0.5% on-month. At the same time, manufacturing activity in China contracted for the first time since the country reopened after ending its zero-COVID policy. Inflation, although high, is easing in most economies with different economies witnessing different scenarios. The US Federal Reserve (the "**Fed**") paused rate hikes in its September meeting but signalled rate hikes ahead. Bank of England also paused rate hikes in their September meeting while European Central Bank ("**ECB**") hiked interest rates by 25 bps at their September 2023 policy meetings.

The Reserve Bank of India ("**RBI**") kept the repo rate unchanged for the fourth consecutive meeting in October 2023. However, the RBI's stance on inflation projections have changed with recent flare up in food prices. Monetary Policy Committee (the "**MPC**") retained the consumer price index ("**CPI**") inflation forecast at 5.4% in Fiscal 2023 (since the August meeting). Inflation is expected to move from 4.6% in the first quarter (Q1) to 6.4% in Q2 (revised up 20 bps from previous meeting), 5.7% in Q3 (10 bps down), 5.2% in Q4 (no change). Moreover, bond yields eased significantly as investors factored in a pause in rate hikes. Foreign portfolio investment ("**FPIs**") increased their investment in the Indian markets as global risk sentiment revived with the US banking turmoil staying largely under control. Equity markets also gained amid the pause in rate hike and rising FPI inflows.

External risks remain high because of the possible impact of elevated interest rates in advanced economies on the leveraged market segments. However, CRISIL Market Intelligence & Analytics, a division of CRISIL Limited (CRISIL MI&A), expects India's macroeconomic fundamentals to improve in Fiscal 2024, which should cushion its vulnerability to global shocks. This, coupled with a pause on rate hikes by the RBI and US Federal Reserve, should limit tightening of domestic financial conditions going ahead. Russia – Ukraine war slowed global recovery; but India expected to remain one of the fastest growing economies.

India is expected to remain one of the fastest-growing major economies amid global slowdown (GDP growth, % year-on-year)



	2015	2016	2017	2018	2019	2020	2021	2022	2023P	2024P	2025P	2026P
India	8.0	8.3	6.8	6.5	3.9	-5.8	9.1	7.2	6.3	6.3	6.2	6.1
China	7.0	6.9	6.9	6.8	6.0	2.2	8.4	3.0	5.0	4.2	4.1	4.0
Hong Kong SAR	2.4	2.2	3.8	2.8	-1.7	-6.5	6.4	-3.5	4.4	2.9	2.9	2.8
Indonesia	4.9	5.0	5.1	5.2	5.0	-2.1	3.7	5.3	5.0	5.0	5.0	5.0
Malaysia	5.0	4.5	5.8	4.8	4.4	-5.5	3.1	8.7	4.0	4.3	4.4	4.4
Philippines	6.3	7.1	6.9	6.3	6.1	-9.5	5.7	7.6	5.3	5.9	6.1	6.2
Singapore	3.0	3.6	4.5	3.6	1.3	-3.9	8.9	3.6	1.0	2.1	2.5	2.5
South Africa	1.3	0.7	1.2	1.5	0.3	-6.3	4.7	1.9	0.9	1.8	1.6	1.4
Thailand	3.1	3.4	4.2	4.2	2.1	-6.2	1.6	2.6	2.7	3.2	3.3	3.1
United Kingdom	2.4	2.2	2.4	1.7	1.6	-11.0	7.6	4.1	0.5	0.6	2.2	2.0
United States	2.7	1.7	2.2	2.9	2.3	-2.8	5.9	2.1	2.1	1.5	1.8	2.1

Note: All forecasts refer to IMF forecasts. GDP growth is based on constant prices, Data represented is for calendar years, P: Projected, For India, GDP growth is on a Fiscal Year basis; Source: IMF (World Economic Outlook – October 2023 update)

Indian Economy to be a major part of world trade

Along with being one of the fastest growing economies in the world, India ranked fifth in the world in terms of nominal GDP for 2023 according to IMF forecasts (World Economic Outlook – April Update). India overtook UK to become the fifth largest economy in the world in calendar year 2022. In terms of purchasing power parity ("**PPP**"), India is the third largest economy in the world, only after China and the United States.

GDP Ranking of key economies across the world (2023)

Country	GDP Rank	% Share (World GDP)	PPP Rank	% share (GDP, PPP)
United States	1	25.8%	2	15.4%
People's Republic of China	2	16.9%	1	18.8%
Germany	3	4.2%	5	3.2%
Japan	4	4.0%	4	3.7%
India	5	3.6%	3	7.5%

United Kingdom	6	3.2%	8	2.2%
France	7	2.9%	9	2.2%
Italy	8	2.1%	10	1.8%
Canada	9	2.0%	12	1.4%
Brazil	10	2.0%	7	2.3%
Russian Federation	11	1.8%	6	2.9%
Republic of Korea	12	1.6%	11	1.7%

Source: IMF (World Economic Outlook – October 2023 update), CRISIL MI&A

With continuous growth in the GDP, India is expected to become the third largest global economy by 2030, as per the Centre for Economics and Business Research (the "**CEBR**"). This growth in India's GDP is expected to be driven by rapid urbanisation, rising consumer aspiration and increasing digitalisation coupled with Government support in the form of reforms and policies that are expected to support growth.

CPI inflation to average at 5.5% in fiscal 2024

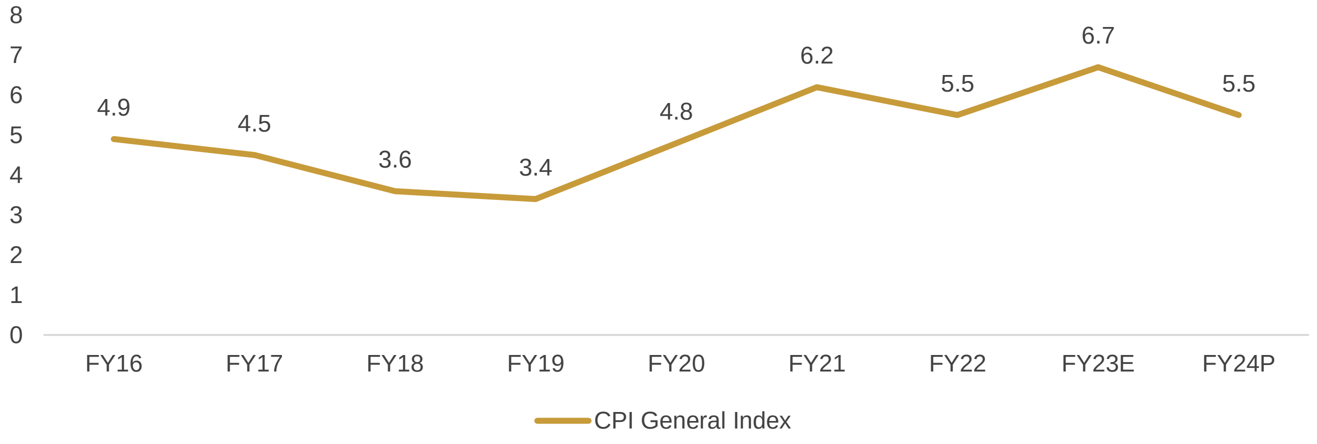
CPI based inflation softened to 6.8% in August after surging to 7.4% in July aided by lower food inflation. While the non-food components stayed unchanged, a slight moderation in food inflation pulled down the headline number. Inflation in all commonly constructed non-food CPI categories remained low and unchanged from July: non-food CPI at 4.8%, core CPI (excluding food and fuel) at 4.9%, services CPI at 4.5% and core CPI goods (excluding food and services) at 5.1%.

Food inflation eased to 9.9% from 11.5% led by some cooling of inflation in vegetables, cereals, pulses and milk. Fuel inflation increased marginally from 3.7% in July to 4.3% in August led by high electricity inflation. Core inflation which has been a major concern in Fiscal 2023, cooled to 4.9% in July and remained the same in August.

Since August's monetary policy, CPI inflation breached the MPC's upper tolerance band of 6.0%, averaging 7.1% in July-August driven by sharp increases in food inflation over the two months. CRISIL MI&A expects CPI inflation to average 5.5% in Fiscal 2024 from 6.7% in Fiscal 2023 on the assumption of a normal monsoon. In the coming months, the key monitorable for food inflation is expected to be the progress of monsoon given the El Niño risk. Core inflation, the pain point for the RBI due to its stickiness, should see limited easing as producers continue to pass on input costs.

For Fiscal 2024, CRISIL MI&A expects CPI inflation to come down, averaging 5.5% on-year, within the RBI's target range of 4-6%. A combination of three factors — impact of rising interest rates on domestic demand, a global demand slowdown leading to falling international commodity prices, and the base effect — should lead to lower inflation.

Annual Inflation (y-o-y%) trend



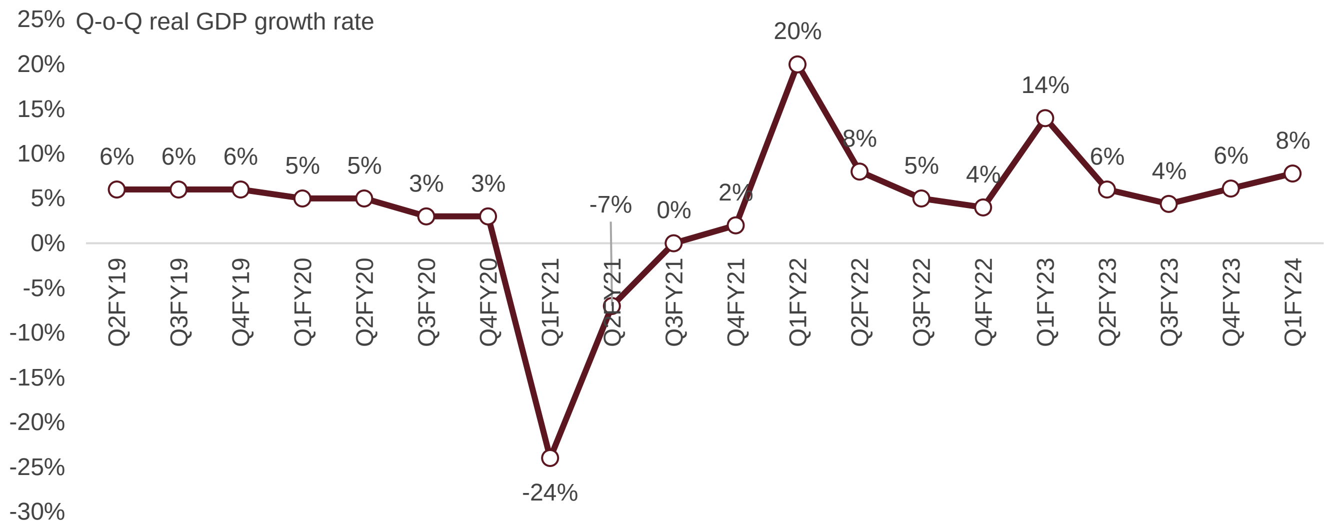
Source: CSO, Ministry of Industry and Commerce, CRISIL

MPC maintains status quo on rates, preferring to watch the price gauge

The MPC kept policy rate unchanged in October for the fourth consecutive time. It also maintained its stance of 'withdrawal of accommodation' to progressively align inflation to 4%, the mid-point of the RBI's target range. The central bank is currently evaluating the impact of past rate hikes on growth and inflation while remaining cautious of the upside risks on the latter. According to MPC's October meet, the real GDP growth for Q1FY24 was 7.8% and for Fiscal 2024 is projected at 6.5%, Q2FY24 at 6.5%, Q3FY24 at 6% and Q4FY24 at 5.7%.

India's real GDP growth rose sharply to 7.8% on year in the first quarter Fiscal 2024 as compared to 6.1% in Q4FY2023. Higher growth was primarily driven by high private consumption and investment growth with rising government capital expenditure ("**capex**"). Exports declined because of lower global demand. Services sector saw a robust growth in Q1FY2024. While GDP growth was robust in Fiscal 2023, a slowdown is inevitable in Fiscal 2024 led by increase in borrowing costs. While major central banks have aggressively raised policy rates in the last fiscal, their transmission into the broader lending rates is taking place with a lag. CRISIL MI&A expects rates to have peaked in Q1FY2024 and hence is expected to face headwinds going forward. Monsoon will have an impact on rural income going forward. External demand will remain a drag on growth as advanced economies undergo a more protracted slowdown under high interest rates scenarios. While strong bank credit growth has supported domestic demand so far, impact of elevated domestic interest rates could weigh in the upcoming quarters. Government capex is expected to remain a key supporter to the investment cycle this Fiscal. Private capex is improving with higher capacity utilisation, but it will take time to get broad based.

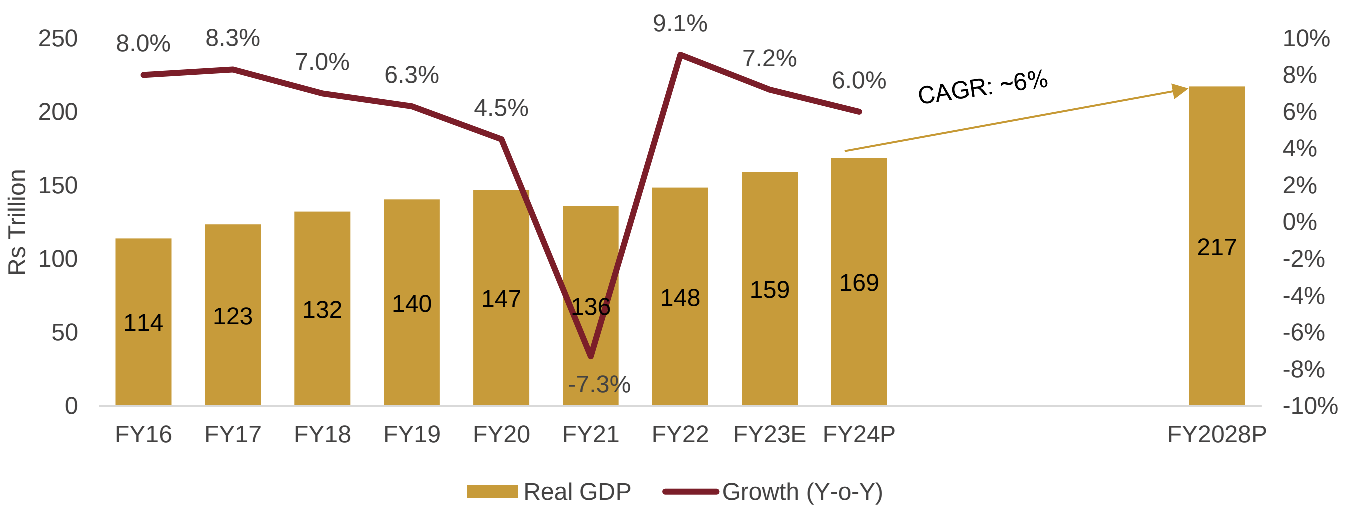
Trend in real GDP growth rate on quarterly basis



Source: CSO, RBI, CRISIL

The advanced economies are expected to inevitably face slower growth in calendar year 2023 as their interest rates are already at decadal highs. They account for 45% of India's exports which is expected to bear the brunt of weaker demand. Besides the global slowdown, the forecast of El Niño disturbing Indian monsoons, is another risk which could hit rural incomes. These factors are expected to slow India's GDP growth to 6.0% in Fiscal 2024 from 7.2% in Fiscal 2023.

India's economy to grow at 6.0% in fiscal 2024



Note: Fiscal 2024 is projected based on CRISIL MI&A estimates. Fiscal 2025-Fiscal 2028 is projected based on IMF estimates; P: Projected; E: Estimated

Source: CRISIL MI&A, IMF World Economic Outlook (October 2023 update)

Macroeconomic outlook for Fiscal 2024

Macro variables	FY23E	FY24P	Rationale for outlook
GDP (y-o-y)	7.2%	6.0%	Slowing global growth is likely to weaken India's export in Fiscal 2024. Domestic demand could also come under pressure as RBI rate hikes are transmitted to consumers.
CPI inflation (y-o-y)	6.7%	5.5%	Lower commodity prices, stable core inflation, softened food inflation to lower inflation expectation in Fiscal 2024. Food inflation although lower as compared to last Fiscal is high and hence will remain a key monitorable.
10-year Government security yield (fiscal-end)	7.4%	7.0%	A moderate increase in gross market borrowings is budgeted for Fiscal 2024. This, coupled with lower inflation and the RBI's rate outs, is likely to moderate yields in Fiscal 2024.
CAD (Current Account Deficit)/GDP (%)	-2.0%	-1.8%	Lower commodity prices, especially in energy space and support from healthy services exports is expected to lead to moderation of trade deficit in Fiscal 2024.
₹/$ (March average)	82.3	83.0	While a lower current account deficit ("**CAD**") is expected to support the rupee, challenging external financing conditions are expected to continue to exert pressure in the next fiscal.

Note: E- Estimated, P – Projected.

Source: Reserve Bank of India (RBI), National Statistics Office (NSO), CRISIL MI&A

Positive government measures to aid economic growth

Going forward, CRISIL MI&A expects India's GDP growth to decelerate to 6.0% in Fiscal 2024 from 7.2% in Fiscal 2023 due to global slowdown, monetary policy impact and volatile geopolitical scenario. However, some optimism can be seen in form of moderating consumer inflation, capital and productivity increases aided by better physical and digital infrastructure. CRISIL MI&A expects this growth to be supported by the following factors:

1. Production linked incentive ("**PLI**") scheme which aims to incentivise local manufacturing by giving volume-linked incentives has been launched by the Government of India for six of the India's top 10 export verticals which is likely to propel incremental exports. In Fiscal 2024, PLI-driven exports are expected to be the lone growth driver for India, helping improve the overall export growth to 2-4%.

2. Focus on investments rather than consumption push enhancing the productive capacity of the economy. Policy push and new age opportunities to lead capex growth in Fiscal 2024.

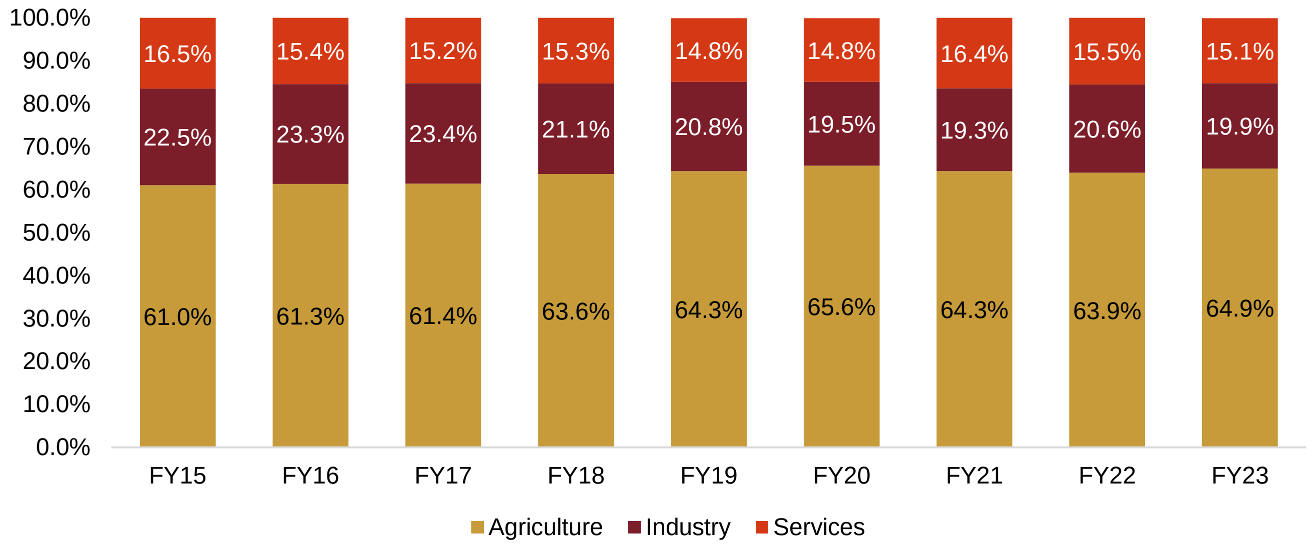
3. Policies aimed towards greater formalisation of the economy, which are bound to lead to an acceleration in per capita income growth.

Despite the mark-down in near-term growth, CRISIL MI&A expects India to remain a growth outperformer over the medium run. Stronger domestic demand is expected to drive India's growth premium over peers in the medium run. Investment prospects are optimistic given the Government of India's capex push, progress of PLI scheme, healthier corporate balance sheets, and a well-capitalised banking sector with low non-performing assets ("**NPAs**"). India is also likely to benefit from the China-plus-one policy as global supply chains get reconfigured with shifting focus from efficiency towards resilience and friend-shoring. Private consumption (approximately 58% of GDP as of March 31, 2023) is expected to play a supportive role in raising GDP growth over the medium run.

Contribution of various sectors to India's GDP

As compared to various developed economies, which witnessed a good contribution from manufacturing and industry first and subsequently in services, the Indian transformation story has been different. A notable feature of Indian economy has been the services sector's rising contribution to the overall output of the economy. Over Fiscals 2018 to 2020, the service sector has grown at a rate of approximately 7%, thereby increasing the contribution of services sector to 65.6% in Fiscal 2020 in terms of Gross Value Added ("**GVA**") at constant prices. In Fiscal 2023, overall GVA expanded by approximately 7.0%.

Share of sector in GVA at constant prices



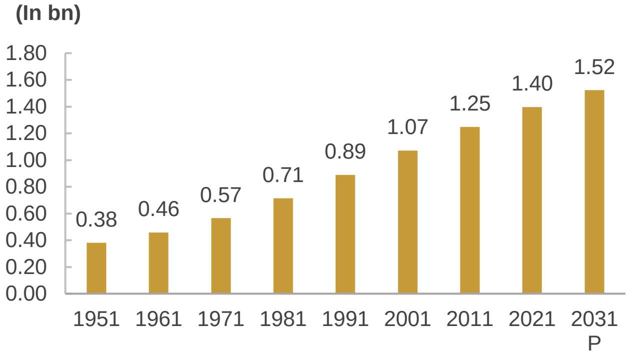
Source: RBI; CRISIL MI&A

Key growth drivers

India has world's second largest population

As per Census 2011, India's population was approximately 1.25 billion, and comprised nearly 245 million households. The population, which grew at nearly 1.5% compound annual growth rate ("**CAGR**") between 2001 and 2011, is expected to increase at 1.1% CAGR between 2011 and 2021, to 1.4 billion. As of calendar year 2022, the population is more than 1.42 billion and has surpassed China as of January 2023 as the most populous country in the world. The population is expected to reach 1.5 billion by 2031, and number of households are expected to reach approximately 376 million over the same period.

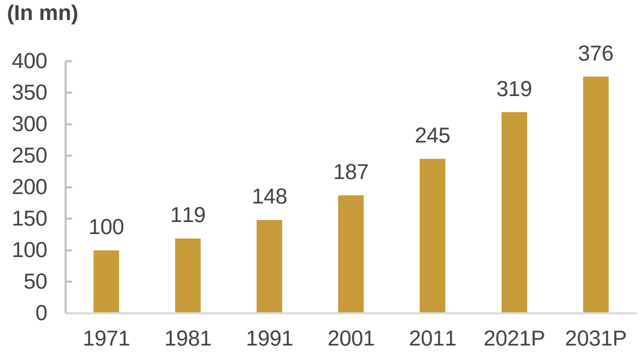
India's population growth trajectory



Note: As at the end of each Fiscal; P: Projected

Source: United Nations Department of Economic and Social affairs[1], CRISIL MI&A

Number of households in India



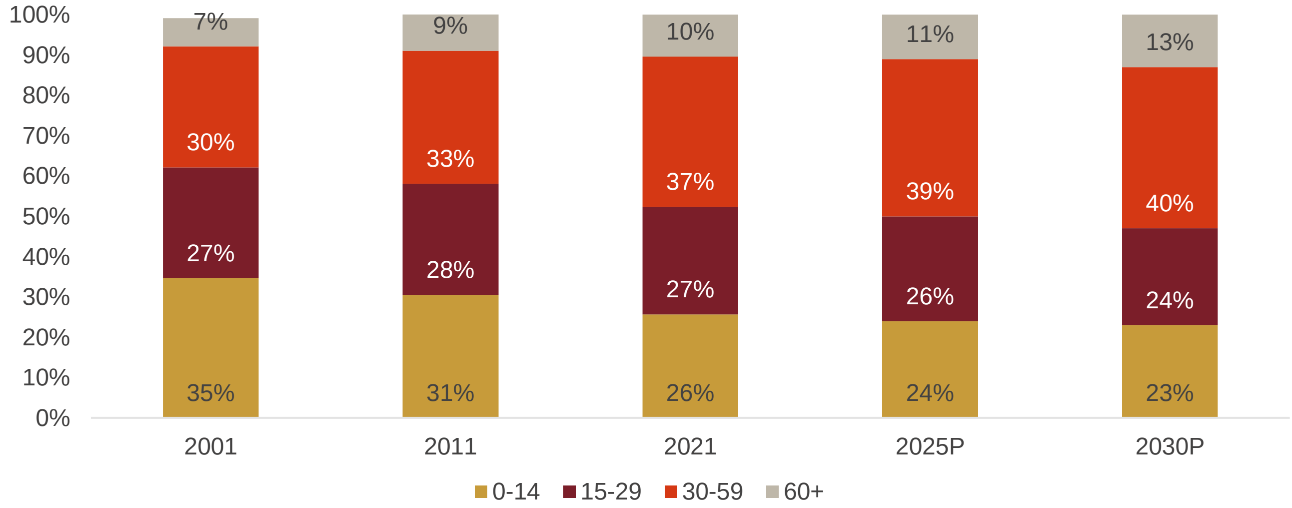
Note: As at the end of each Fiscal; P: Projected

Source: Census India, United Nations Department of Economic and Social affairs2, CRISIL MI&A

Favourable demographics

As of calendar year 2021, India has one of the largest young populations in the world, with a median age of 27.6 years as compared to the world average of 30 years. (*Source: United Nations Department of Economic and Social Affairs, World Urbanization Prospects: The 2018 Revision (UN) (https://population.un.org/wup/)).* As of calendar year 2021, approximately 90% of Indians were below the age of 60 and that 64% of them are between 15 and 59 years of age. *(Source: World Population Prospects 2022).* In comparison, in calendar year 2021, the US, China and Brazil had 77%, 82% and 86%, respectively, of their population below the age of 60. *(Source: World Population Prospects 2022).*

India's demographic dividend



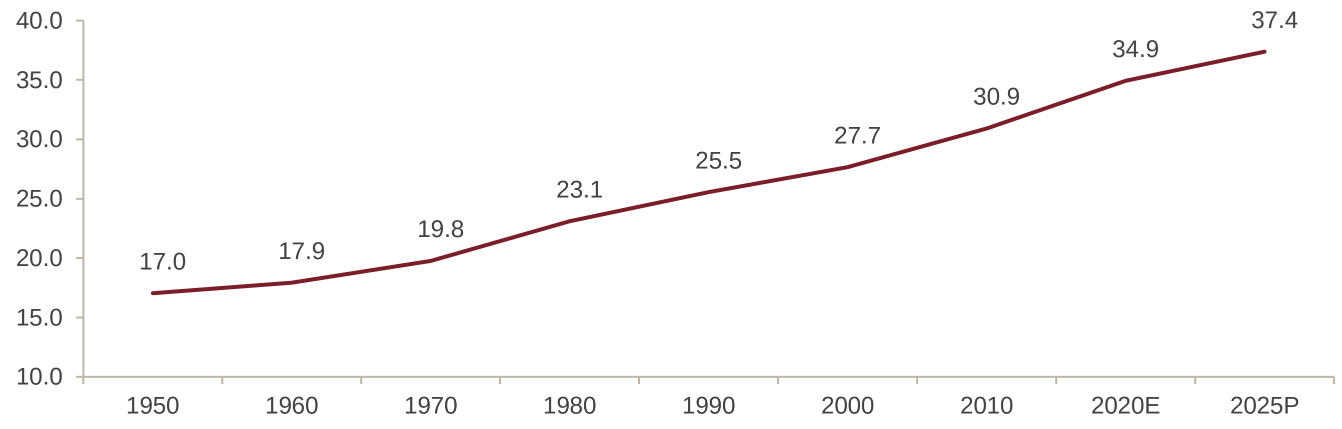
[1] *https://population.un.org/wpp/*
[2] *https://population.un.org/wpp/*

Note: P: Projected; 2001, 2011 and 2021 data from World Population Prospects (2022), 2025P and 2030P is projected by CRISIL MI&A; Source: United Nations Department of Economic and Social affairs[3], World Population Prospects (2022), World Urbanization Prospects: The 2018 Revision (UN) (https://population.un.org/wup/), CRISIL MI&A

Urbanisation

Urbanisation is one of India's most important economic growth drivers. It is expected to drive substantial investments in infrastructure development, which in turn is expected to create jobs, develop modern consumer services and increase the ability to mobilise savings. India's urban population has been rising consistently over the decades. In 1950, the urban population was 17% of the total population of India. (*Source: World Urbanization Prospects*). As per the 2018 revision of World Urbanization Prospects, the urban population was estimated at 34.9% of India's total population. According to the World Urbanization Prospects, the percentage of the population residing in urban areas in India is expected to increase to 37.4% by 2025.

Urban population as a percentage of total population (%)



Note: E- Estimated, P - Projected

Source: Census 2011, World Urbanization Prospects: The 2018 Revision (UN)[4]

Increasing per capita GDP

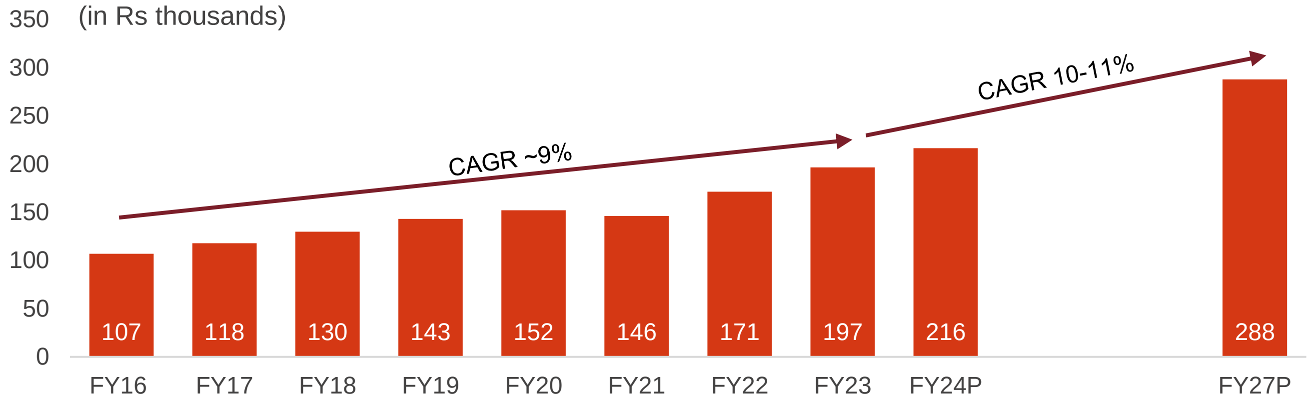
In Fiscal 2023, India's per capita income expanded by 6.0%. As per IMF estimates, India's per capita income (at constant prices) is expected to grow at 5% CAGR from Fiscal 2023 to Fiscal 2026.

Per capita income	Level in FY2023^ (₹ '000)		Growth at constant prices (%)										
	Current prices	Constant prices	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	FY22	FY23	FY26P
	172	98	4.6	6.2	6.7	6.8	5.7	5.8	2.9	-7.6	7.6	6.0	5.3*

Note – P: Projected, (^) Per Capita NNI as per second advanced estimates of national income, 2022-23; (*) – 3-year CAGR growth (FY2023-FY2026), as per IMF estimates (2023 October Update); Source – Ministry of Statistics and Program Implementation (MOSPI), International Monetary Fund (IMF), CRISIL MI&A

[3] *https://population.un.org/wpp/*
[4] *https://population.un.org/wup/*

Trend in Nominal GDP per capita (at current prices)



Note: P- Projected; FY23 estimates based on second advanced estimates by Ministry of Statistics and Program Implementation, FY24 – FY27 Projections based on IMF – World Economic Outlook (October 2023 update)

Source: MOSPI, IMF, CRISIL MI&A

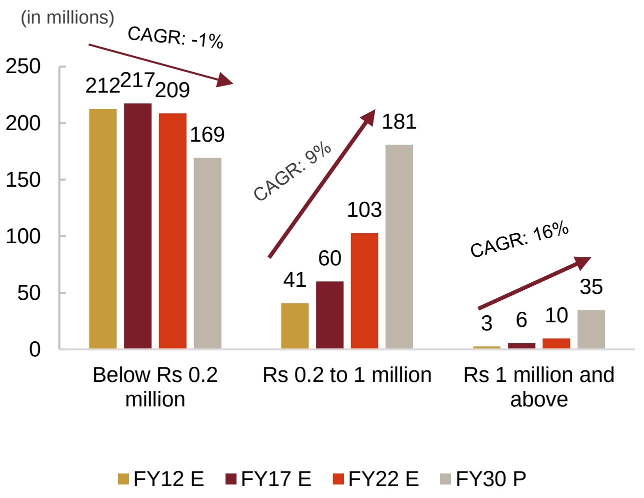
Rising Middle India population to propel economic growth

Proportion of Middle India (defined as households with annual income of between ₹ 0.2 to 1 million) has been on a rise over the last decade and is expected to grow further with continuous increase in the GDP and household incomes

To illustrate, CRISIL MI&A estimates that there were 41 million households in India in this category as of Fiscal 2012, and by Fiscal 2030, they are projected to increase to 181 million households translating into a CAGR of 9% over this time period. This growth in the number of middle-income households is expected to lead to enhanced opportunities for retail and MSME financiers as well as consumer goods marketers. A large number of these households, which have entered the Middle-Income bracket in the last few years, are likely to be from semi-urban and rural areas. The rise in incomes in these areas is also evident when one observes the trend in share of deposits coming into banks.

Consistent improvement in the literacy levels, increasing access to information and awareness, increase in the availability of basic necessities such as electricity, cooking gas, toilets and improvement in road infrastructure has led to an increase in aspirations of Middle India, which is likely to translate into increased opportunities for financial service providers. In fact, some of these trends are already visible. Smart phone ownership, internet users and the proportion of users accessing social media is increasing at a breakneck speed. Smaller cities and towns (with population less than 1 million) account for a significant portion of sales of e-retailers.

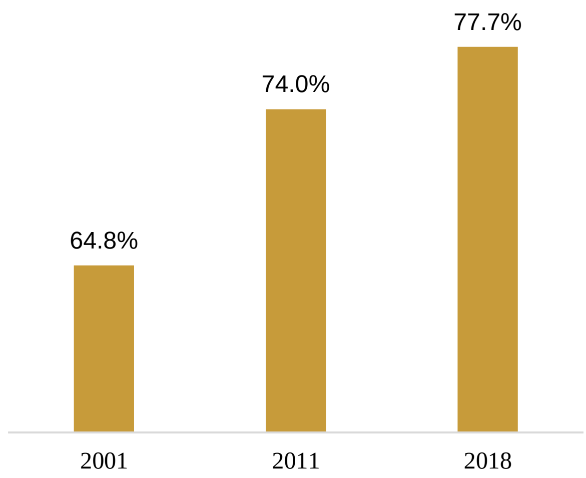
Middle India households to witness high growth over Fiscal 2012 to Fiscal 2030



Note: E: Estimated, P: Projected

Source: CRISIL MI&A

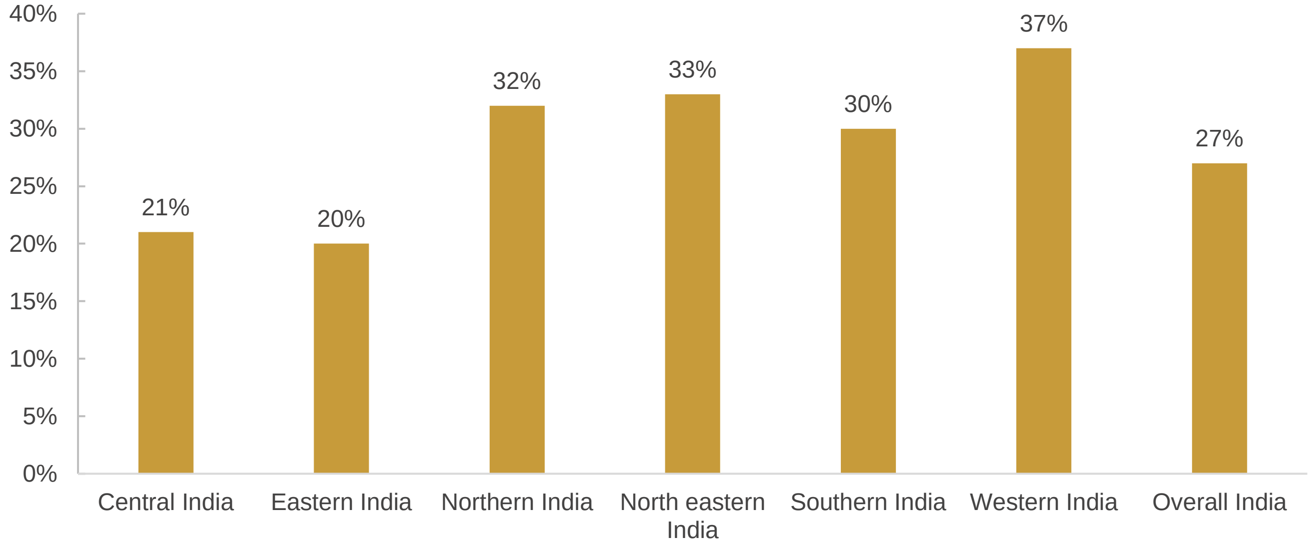
Overall literacy rate on the rise in India



Source: Census 2011, NSO Survey on household social consumption (2017-18), CRISIL MI&A

With increasing financial literacy, mobile penetration, awareness and the Prime Minister's Jan Dhan Yojana bank accounts (scheme aimed at bringing the unbanked under the formal banking system), there has been a rise in the participation of individuals from non-metro cities in banking. With more people attached to the formal banking sector, the demand for financial products in smaller cities has seen a major increase in recent years. Going forward, CRISIL MI&A expects financial penetration to increase on account of increasing financial literacy.

Financial Literacy across India

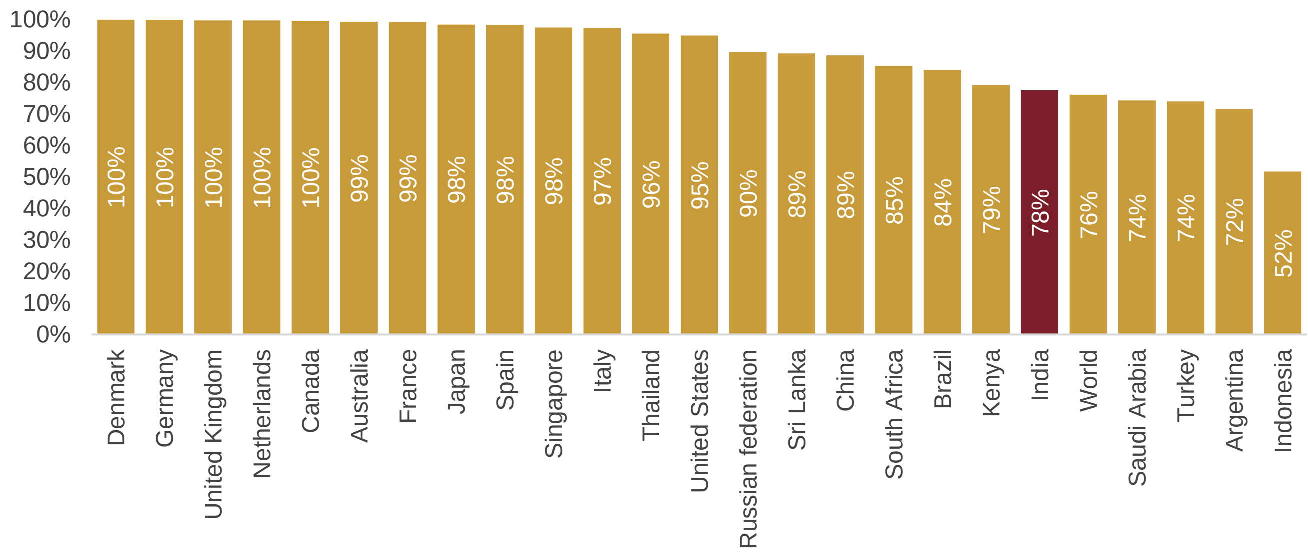


Source: National Financial Literacy and Inclusion Survey (NCFE-FLIS) 2019 Report, National Centre for Financial Education

Financial Inclusion on a fast path in India

Overall literacy in India is at 77.7% as per the results of recent National Sample Survey Office survey conducted from July 2017 to June 2018 which is still below the world literacy rate of 86.5%. However, according to the National Financial Literacy and Inclusion Survey ("**NCFE-FLIS**") 2019, only 27% of Indian population is financially literate indicating huge gap and potential for financial services industry. The survey defines financial literacy as combination of awareness, knowledge, skill, attitude and behaviour necessary to make sound financial decisions and ultimately achieve individual financial wellbeing. According to the World Bank's Global Findex Database 2021, the global average of adult population with an account opened with a bank, financial institution or mobile money provider, was approximately 76% in calendar year 2021. India's financial inclusion has improved significantly over calendar years 2014 to 2021 as adult population with bank accounts increased from 53% to 78% (*Source: Global Findex Database*) due to the Indian government's concentrated efforts to promote financial inclusion and the proliferation of supporting institutions.

Adult population with a bank account (%): India vis-à-vis other countries



Note: 1. Global Findex data for India excludes northeast states, remote islands and selected districts. 2. Account penetration is for the population within the age group of 15+,

Source: World Bank - The Global Findex Database 2021, CRISIL MI&A

The two key initiatives launched by the Government of India to promote financial inclusion are the Pradhan Mantri Jan Dhan Yojana ("**PMJDY**") and Pradhan Mantri Jeevan Jyoti Bima Yojana ("**PMJJBY**"). Under the PMJDY, the Government of India's aim is to ensure that every household in India has a bank account which they can access from anywhere and avail of all financial services such as savings and deposit accounts, remittances, credit and insurance affordably. PMJJBY is a one-year life insurance scheme that offers a life cover of ₹ 0.2 million at a premium of ₹ 330 per annum per member, which can be renewed every year. The Government of India has also launched the Pradhan Mantri Suraksha Bima Yojana ("**PMSBY**"), an accident insurance policy that offers an accidental death and full disability cover of ₹ 0.2 million at a premium of ₹ 12 annually. As per the Government of India, more than 100 million people have registered for these two social security schemes.

PMJDY launched in August 2014, is aimed at ensuring that every household in India has a bank account which they can access from anywhere and avail of all financial services such as savings and deposit accounts, remittances, credit and insurance affordably. PMJDY focuses on household coverage compared to the earlier schemes that focused on coverage of villages. It aims to extend banking facilities to all within a reasonable distance in each sub-service area (consisting of 1,000-1,500 households) across India.

Account Aggregators framework to build a financial data ecosystem in India

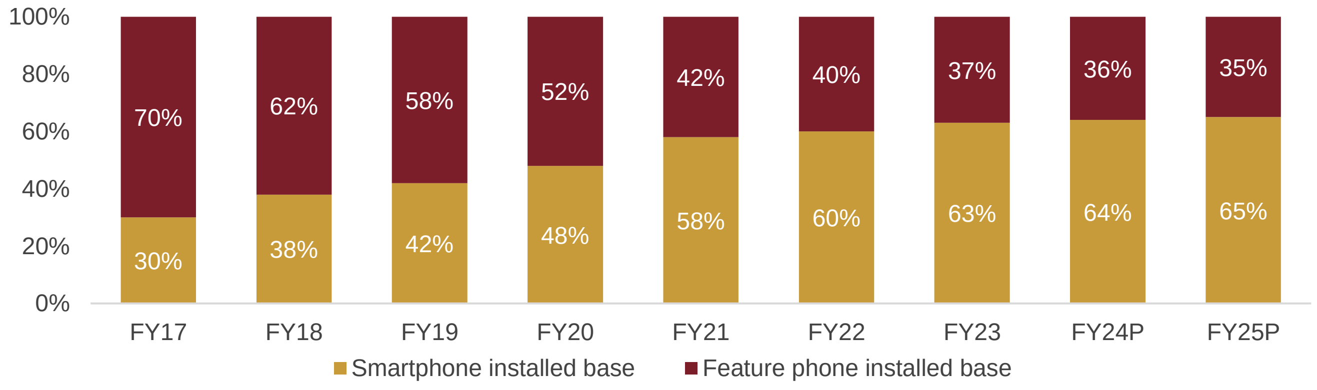
The RBI launched the account aggregator system on September 2, 2021, which has the potential to transform the MSME finance space once there is widespread adoption amongst the lending community. These account aggregators would provide granular insights to lenders into customers' financial assets and their borrowing history centrally, based on customer consent. Inclusion of additional data such as electricity bill payments and mobile recharges/bill payment data under the purview of account aggregators would further enhance its utility.

Digitisation to support economic growth and financial services

Technology is expected to play a pivotal role in taking the financial sector to the next level of growth, by helping to surmount challenges stemming from India's vast geography, which makes physical footprints in smaller locations commercially unviable. Technology is conducive for India, considering its demographic structure where the median age is less than 30 years. The young population is tech savvy and at ease with using it to conduct the entire gamut of financial transactions. With increasing smartphone penetration and faster data speeds, consumers are now encouraging digitisation as they find it more convenient. Digitisation is expected to help improve efficiency and optimise cost. Players with better mobile and digital platforms are expected to draw more customers and emerge as winners in the long term.

Mobile penetration: Higher mobile penetration, improved connectivity, and faster and cheaper data speed, supported by Aadhaar and bank account penetration have led India to shift from being a cash-dominated economy to a digital one.

Data-savvy and younger users to drive adoption of smartphones



Note: E: Estimated, P: Projected

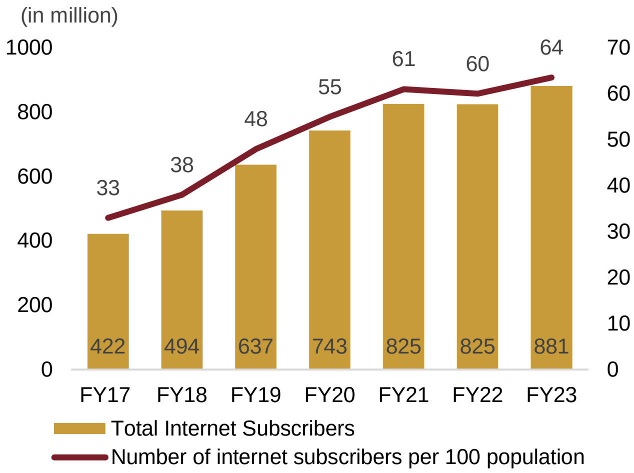
Source: CRISIL MI&A

Rise in 4G penetration and smartphone usage

India had 1,143.21 million wireless subscribers at the end of May 2023. The reach of mobile network, internet and electricity is continuously expanding the subscriber footprint to remote areas leading to rising smartphone and internet penetration in India. Internet subscribers have risen sharply in India from 422 million subscribers in Fiscal 2017 to 881 million subscribers in Fiscal 2023 growing at a CAGR of 13%. In terms of number of internet subscribers per 100 population, number has almost doubled from 33 in Fiscal 2017 to 64 in Fiscal 2023.

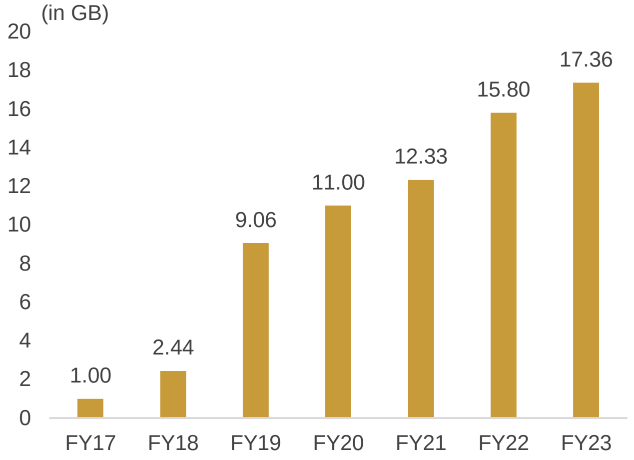
Average wireless data usage per month per subscriber has seen an increasing trend over the last eight years. Per subscriber per month data usage was 0.1 gigabyte ("**GB**") in Fiscal 2015, which has increased to 17.36 GB in Fiscal 2023. This is due to increasing internet data penetration in India.

Trend in internet subscribers in India



Source: TRAI, CRISIL MI&A

Trend of average wireless data usage per wireless data subscriber per month



Source: TRAI, CRISIL MI&A

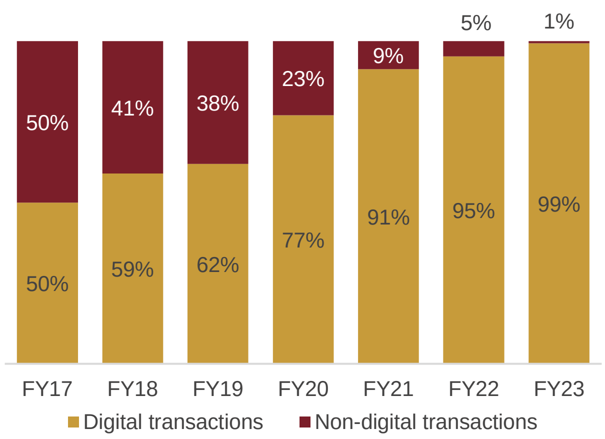
Increasing share of digital channels in domestic monetary transactions

The share of different channels in domestic money transfer has changed significantly over the past five years. Banks, for example, are witnessing a change in customer behaviour with fewer customers visiting bank branches for transactions. This change in behaviour was led by demonetisation when cash transactions slowed down, many new accounts were opened, and digital banking witnessed a surge in use and continued its growth trajectory. The preference has also shifted from cost factors to convenience and ease of performing transactions, which helps in saving time spent in queues, not disturbing the daily working hours and avoiding any potential monetary loss. Post-COVID, with consumers preferring to transact digitally rather than engage in physical exchange of any paper or face-to-face contact, digital transactions have received another shot in the arm.

Digital payments have witnessed substantial growth

Total digital payments in India have witnessed significant growth over the past few years. Between Fiscal 2016 and 2022, the volume of digital payments transactions has increased from 6.3 billion to 113.9 billion, causing its share in overall payment transactions to increase from 39% in Fiscal 2016 to 99% in Fiscal 2023. During the same period, value of digital transactions has increased from ₹ 920 trillion in Fiscal 2016 to ₹ 2,087 trillion in Fiscal 2023.

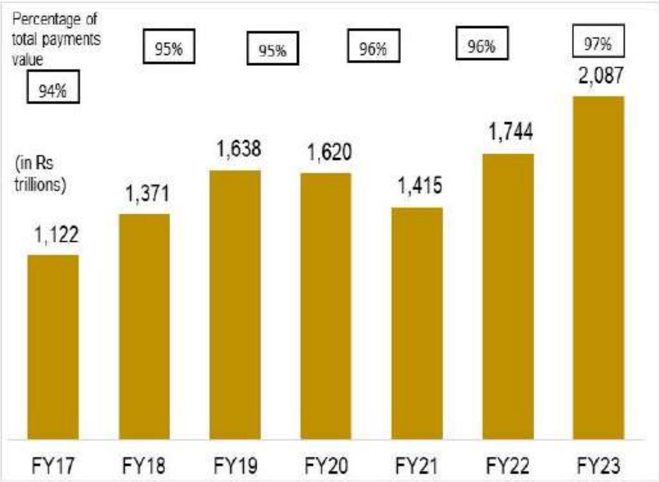
Trend in volume of digital payments



Note: Digital Payments includes RTGS payments, Credit transfers (AePS, APBS, ECS Cr, IMPS, NACH, NEFT, UPI), Debit Transfers (BHIM, ECS Dr, NACH Dr, NETC), Card Payments (Debit and Credit Cards) and Prepaid Payments Instruments

Source: RBI, CRISIL MI&A

Trend in Value of Digital Payments



Note: Digital Payments includes RTGS payments, Credit transfers (AePS, APBS, ECS Cr, IMPS, NACH, NEFT, UPI), Debit Transfers (BHIM, ECS Dr, NACH Dr, NETC), Card Payments (Debit and Credit Cards) and Prepaid Payments Instruments

Source: RBI, CRISIL MI&A

Measures deployed to counter the COVID-19 pandemic's onslaught on growth

RBI goes all out to combat the crisis

The MPC of RBI slashed the repo rate by 115 basis points ("bps") to address financial market stress in the wake of the COVID-19 pandemic and the subsequent lockdown. In an unusual move, the MPC also asymmetrically slashed the reverse repo initially by 90 bps and by another 25 bps and 40 bps subsequently.

RBI also announced a host of other measures to address financial market stress due to the COVID-19 pandemic or lockdown:

- **Reducing debt-servicing burden through moratorium period:** RBI initially permitted lending institutions to allow a moratorium of three months on repayment of instalments for term loans outstanding as on March 1, 2020 and defer interest payments due on working capital facilities outstanding.
- **Loan restructuring:** RBI constituted a committee which identified 26 sectors for restructuring which included aspects related to leverage, liquidity and debt serviceability to be factored by the lending institutions while finalising resolution plans for borrowers.
- **Enhancing liquidity**: Apart from reducing repo and reverse repo rate, RBI reduced the cash reserve ratio ("**CRR**") requirements of all banks by 100 bps to 3% of net demand and time liabilities ("**NDTL**").
- **Supporting financial market liquidity:** RBI initially announced targeted long-term repo operations ("**TLTROs**") of up to three years' tenure for a total of up to ₹ 1 trillion. Liquidity availed under the scheme by banks had to be deployed in investment grade corporate bonds, commercial paper, and non-convertible debentures.
- **Measures during second wave of COVID-19:** In May 2021, RBI announced several measures to protect small and medium businesses and individual borrowers from the adverse impact of the intense second wave of COVID-19 across India. Resolution framework 2.0 was announced wherein individuals and MSMEs having aggregate

loan exposure of up to ₹ 250 million, who have not availed restructuring under any of the earlier restructuring frameworks (including under the Resolution Framework 1.0 dated August 6, 2020), and who were classified as 'Standard' as on March 31, 2021, were allowed to restructure their loans.

'Aatmanirbhar' package is a timely relief amid the COVID-19 pandemic

Liquidity boost for NBFCs

The Indian government announced a ₹ 450 billion partial guarantee scheme for non-banking financial companies ("**NBFCs**") and ₹ 300 billion special liquidity scheme for NBFCs, housing finance companies ("**HFCs**") and mutual fund institutions ("**MFIs**"), aimed at covering the concern of credit risk perception on mid and small size non-banks.

Emergency Credit Line Guarantee Scheme ("ECLGS") for MSMEs (₹ 4.5 trillion)

Banks and NBFCs are directed to offer up to 20% of entire outstanding credit to MSMEs. MSMEs with up to ₹ 250 million outstanding credits and ₹ 1 billion turnover are eligible for these loans.

1. Subordinated debt to MSMEs (₹ 200 billion)

The Indian government is also facilitating the provision of ₹ 200 billion as subordinate debt for stressed assets of MSMEs. It is expected to also provide ₹ 40 billion as partial credit guarantee support to banks for lending to MSMEs.

2. Equity infusion in MSMEs (₹ 500 billion)

The Government of India has committed to infuse ₹ 500 billion in equity of MSMEs having growth potential and viability. It is expected to also encourage MSMEs to list on stock exchanges.

3. Clearing MSME dues; guarantee scheme

The Government of India has requested central public sector enterprises to release all pending MSME payments within 45 days. It is expected to boost transaction-based lending by financial technology entities ("**finTechs**") enterprises.

4. Global tenders disallowed up to ₹ 2 billion

The Indian government is expected to not allow foreign companies in government procurement tenders of value up to ₹ 2 billion. This is likely to ease the competition faced by the MSMEs against foreign companies.

5. Loan interest subvention scheme (₹ 15 billon)

Under this scheme, the Indian government has provided 2% interest subvention for loans given under Mudra-Shishu scheme. These loans are up to the ticket size of ₹ 50,000 and are mostly given by NBFC-MFIs that benefit low-income groups customers.

6. Special credit facility for street vendors (₹ 50 billon)

The Government of India announced this scheme to facilitate easy access of credit to street vendors to offset the adverse effect of COVID-19 pandemic on their livelihoods.

7. "Aatmanirbhar 3.0" stimulus package rolled out to boost economy in November 2020

The finance minister, on November 12, 2020, announced a stimulus package amounting to ₹ 2.65 trillion. Under the package, 12 stimulus measures were rolled out to, among other things, boost employment in the formal and informal economy, help housing infrastructure, enhance ease of doing business and extend the deadline for the Credit Line Guarantee Scheme.

An additional outlay of ₹ 180 billion for PM Awaas Yojana ("**PMAY**") Urban was announced, which is expected to help ground 1.2 million houses and complete 1.8 million houses. The move is expected to create additional 7.8 million jobs and improve production and sale of steel and cement, resulting in a multiplier effect on the economy. Stimulus packages worth ₹ 2.65 trillion were announced by the Government of India.

Following are the twelve announcements made in the Aatmanirbhar 3.0 stimulus package:

1. Aatmanirbhar Bharat Rozgar Yojana: Aatmanirbhar Bharat Rozgar Yojana, operational during October 1, 2020 to June 2021 to incentivise creation of new employment opportunities during COVID-19 recovery phase.
2. ECLGS 2.0: Launch of an ECLGS 2.0 for guaranteed credit to 26 stressed sectors. Tenure of additional credit under ECLGS 2.0 to be 5 years, including 1 year of moratorium on principal repayment. ECLGS extended till March 31, 2021.
3. PLI scheme: Introduction of the PLI scheme in 13 key sectors for enhancing India's manufacturing capabilities and exports.
4. PMAY – Urban: ₹ 180 billion is expected to be provided over the Budged Estimates for 2020-21 PMAY – Urban through additional allocation and extra-budgetary resources. This is over and above the ₹ 80 billion already budgeted this year.
5. Support for construction and infrastructure – Relaxation of earnest money deposit ("**EMD**") and performance security on Government tenders.

Performance security on contracts to be reduced to 3% instead of 5-10%

EMD is expected to not be required for tenders and is expected to be replaced by Bid Security Declaration

Relaxations are expected to be given till December 31, 2021

1. Demand booster for residential real estate income-tax relief for developers and home buyers: Increase in the differential from 10% to 20% for the period from the date of the announcements to June 20, 2021 for only primary sale of residential units of value up to ₹ 2 billion.
2. The Government of India is expected to invest ₹ 60 billion as equity in the NIIF debt platform. Infra project financing of ₹ 1.1 trillion is expected to be provided by the Government of India.
3. The Government of India is expected to provide support to farmers with ₹ 650 billion for subsidised fertilisers
4. Boost for the rural employment – Enhanced outlays under PM Garib Kalyan Rozgar Yojana: ₹ 400 billion was additionally provided in Atmanirbhar Bharat 1.0. Further outlay of ₹ 100 billion to be provided for PM Garib Kalyan Rozgar Yojana in the current Fiscal.
5. Boost for exports – ₹ 30 billion to EXIM Bank for lines of credit: ₹ 30 billion is expected to be released to EXIM Bank for promotion of project exports through lines of credit under the IDEAS scheme.
6. Capital and industrial stimulus: ₹ 102 billion additional budget outlay is expected to be provided towards capital and industrial expenditure.
7. Research and development grant for COVID-19 vaccine development: ₹ 9 billion provided for COVID-19 Suraksha Mission for research and development of an Indian COVID-19 vaccine to the Department of Biotechnology

Scope of ECLGS Scheme further expanded post the COVID-19 second wave

In September 2021, with a view to support various businesses impacted by the second wave of COVID-19 pandemic, the timeline for ECLGS has been extended till March 2022 or till guarantees for an amount of ₹ 4.5 lakh crore are issued under the scheme, whichever is earlier. In addition, the last date of disbursement under the scheme has also been extended to June 2022. Out of the targeted amount of ₹ 4.5 trillion, ₹ 3.32 trillion has been sanctioned as of April 30, 2022 of which ₹ 2.54 trillion has been disbursed.

In June 2021, the Government of India increased the overall admissible guaranteed limit from ₹ 3.0 trillion to ₹ 4.5 trillion. In addition, the limit of admissible guarantee and outstanding loan amount was increased from 20% to 40% of outstanding for COVID-affected sectors like hospitality sector, travel and tourism sector, leisure and sporting sector and civil aviation sector, subject to a maximum of ₹200 crore per borrower. In Union budget 2022-23, the allocation under ECLGS was increased from ₹4.5 trillion to ₹5.0 trillion, and the timeline for sanctions has been extended till March 2023. The enhancement of ₹500 million is earmarked exclusively for hospitality and related enterprises.

Earlier, in May 2021, the Government of India announced the following further modifications to the ECLGS scheme:

- The scope was expanded to cover loans up to ₹ 20 million to hospitals/ nursing homes/ clinics/ medical colleges for setting up on-site oxygen generation plants with interest rate capped at 7.5%
- Additional ECLGS assistance of up to 10% of the outstanding loans as on February 29, 2020 was allowed to borrowers covered under ECLGS 1.0
- Civil aviation sector was included in the list of sectors covered
- Ceiling of ₹ 5 billion of loan outstanding for eligibility under ECLGS 3.0 was removed, subject to maximum additional ECLGS assistance to each borrower being limited to 40% or ₹ 2 billion, whichever was lower
- Borrowers who had availed loans under ECLGS 1.0 of overall tenure of 4 years comprising of repayment of interest only during the first 12 months with repayment of principal and interest in 36 months were allowed to increase the tenure to 5 years (repayment of interest only for the first 24 months with repayment of principal and interest in 36 months thereafter)

Earlier, in March 2021, the Government of India had made the following modifications to the scheme

- The scope of ECLGS was expanded to cover business enterprises in hospitality, travel and tourism, leisure and sporting sectors which had, as on February 29, 2020, total credit outstanding not exceeding ₹ 5 billion and were less than or equal to 60 days past due as on that date.
- The validity of ECLGS was extended up to June 30, 2021 or till guarantees for an amount of ₹ 3 trillion were issued.

Key structural reforms: Long-term positives for the Indian economy

- Financial inclusion improved significantly with the help of schemes like PMJDY, PMJJBY and PMSBY.
- GST has spawned structural changes in the supply chain and logistics network in India which ensures that more players in the supply chain come under the tax ambit. The GST regime has been stabilising fast and is expected to bring more transparency and formalisation, eventually leading to higher economic growth.
- Production-Linked Incentive scheme aims to spawn a handful of globally competitive large scale manufacturing units in the identified sectors. Furthermore, the Government of India also hopes to reduce India's dependence on raw material imports from China. The scheme is expected to provide a boost to economic growth over the

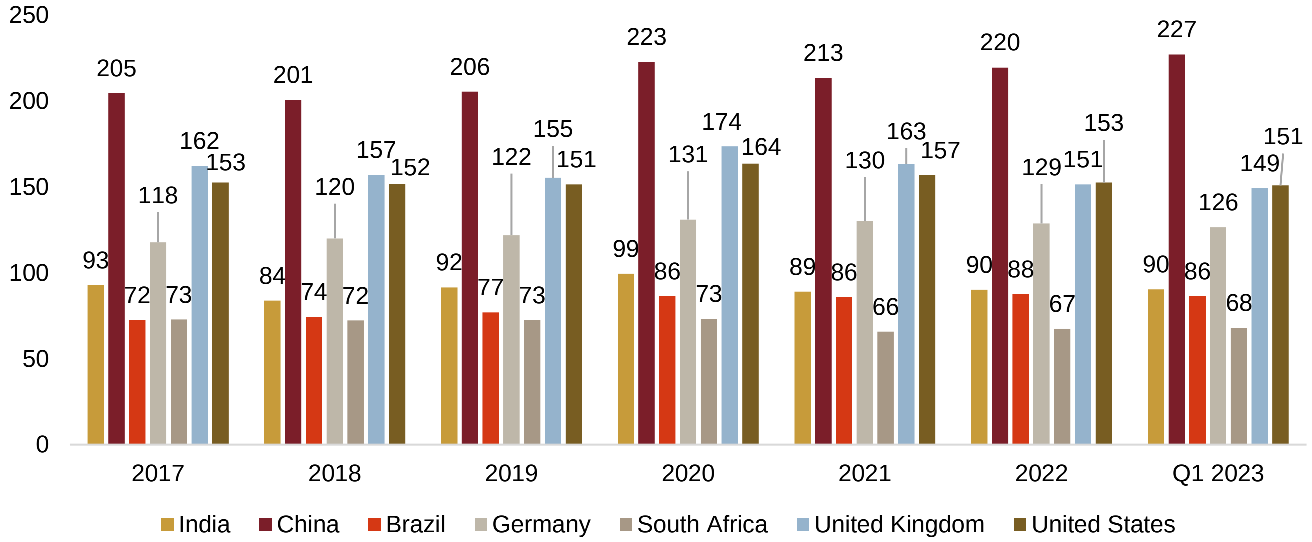
medium-term and create more employment opportunities as many of these sectors are labor intensive in nature.

- The Insolvency and Bankruptcy Code ("**IBC**") is a reform that is expected to structurally strengthen the identification and resolution of insolvency in India. It attempts to simplify legal processes, preserve value for creditors and provide them with greater certainty of outcome. With this reform, RBI has sent a strong signal to borrowers to adhere to credit discipline and encourage banks to break resolution deadlocks by introducing definite timelines. IBC is expected to enhance investors' confidence when investing in India.
- On September 20, 2019, the finance minister announced Taxation Laws (Amendment) Ordinance, 2019 to make certain amendments in the Income Tax Act, 1961, to allow any domestic company the option to pay income tax at the rate of 22%, subject to the condition that they are expected to not avail of any exemption/incentive. The amendments could boost the capital base of the financial institutions and help revive growth in the financial services sector, which has been battling with high NPAs, increasing defaults and liquidity concerns.

Credit penetration is lower in India compared to other countries

In terms of the credit to GDP ratio, India has a low credit penetration compared with other developing countries, such as China indicating that the potential that can be tapped. Similarly, in terms of credit to households as a proportion of GDP as well, India lags other markets, with retail credit hovering at around 26% of GDP as of Fiscal 2023.

Credit to GDP ratio (%) (Q1 CY2023)



Note: Data is represented for calendar years for all countries except India. For India, numbers are for fiscal year

Source: Bank of International Settlements[5], CRISIL MI&A

Delhi, Maharashtra, Telangana and Chandigarh have a higher credit penetration compared to other states

Delhi, Maharashtra, Telangana and Chandigarh have a credit to GDP ratio of more than 100% as of March 2023 which indicates that credit penetration in the state is higher as compared to other states in India. Chandigarh has the highest credit penetration of 271% as of March 2023 followed by Delhi at 240%. Maharashtra has the third highest credit penetration in Indian states at 206% which has the highest contribution to Indian GDP.

[5] *https://www.bis.org/statistics/c_gaps.htm?m=6_380_670*

In terms of credit growth, among the top ten states, Andhra Pradesh (16%) and Rajasthan (15%) witnessed the highest credit growth from Fiscal 2016 to Fiscal 2023. Amongst the top 15 states, the asset quality in states such as Andhra Pradesh, Telangana, Gujarat, Rajasthan and Kerala is better as compared to other states as of Fiscal 2023. In states such as Maharashtra and Karnataka, the asset quality is slightly worse compared to Andhra Pradesh and Rajasthan but is better than India average.

Delhi and Chandigarh which are smaller states have high credit concentration, for example Chandigarh has an urban credit share of 100% and Delhi has a metropolitan credit share of 99%. Densely populated states like Bihar and Uttar Pradesh have rural credit share at 21% and 16%, respectively, which is low considering majority of the population lives in rural areas.

State-wise credit penetration (Fiscal 2023)

State	Credit Penetration as of March 2023	Credit Growth (FY16-FY23)	GSDP (FY21-FY22) in Rs billion	Percentage share in India's GDP	Rural Credit Share	Semi Urban Credit Share	Urban Credit Share	Metropolitan Credit Share
Maharashtra*	206%	8%	18,893	12.7%	2%	4%	4%	90%
Tamil Nadu	94%	9%	13,451	9.0%	11%	23%	14%	51%
Karnataka	73%	10%	12,522	8.4%	8%	12%	16%	64%
Gujarat*	58%	9%	12,482	8.4%	8%	13%	17%	62%
Uttar Pradesh	57%	12%	11,231	7.5%	16%	16%	32%	36%
West Bengal*	62%	6%	7,927	5.3%	13%	10%	20%	58%
Andhra Pradesh	77%	16%	7,469	5.0%	15%	25%	30%	30%
Rajasthan	62%	15%	7,330	4.9%	13%	24%	25%	38%
Telangana	102%	10%	6,763	4.5%	7%	11%	9%	74%
Delhi	240%	6%	6,224	4.2%	0%	1%	0%	99%
Madhya Pradesh	60%	13%	6,217	4.2%	11%	22%	18%	48%
Haryana	68%	13%	5,888	4.0%	9%	15%	68%	8%
Kerala	83%	11%	5,509	3.7%	2%	50%	48%	0%
Bihar	46%	16%	4,281	2.9%	21%	24%	25%	30%
Punjab	68%	6%	4,275	2.9%	18%	29%	26%	28%
Odisha	46%	14%	4,203	2.8%	19%	23%	58%	0%
Chhattisgarh*	61%	13%	2,455	1.6%	8%	17%	26%	49%
Jharkhand	42%	12%	2,368	1.6%	17%	20%	28%	35%
Assam*	45%	15%	2,285	1.5%	21%	30%	49%	0%
Uttarakhand	37%	12%	1,899	1.3%	21%	21%	58%	0%

State	Credit Penetration as of March 2023	Credit Growth (FY16-FY23)	GSDP (FY21-FY22) in Rs billion	Percentage share in India's GDP	Rural Credit Share	Semi Urban Credit Share	Urban Credit Share	Metropolitan Credit Share
Himachal Pradesh	34%	11%	1,244	0.8%	58%	32%	10%	0%
Jammu and Kashmir	71%	14%	1,215	0.8%	35%	26%	21%	19%
Goa*	48%	8%	534	0.4%	18%	82%	0%	0%
Tripura	27%	14%	405	0.3%	27%	27%	46%	0%
Chandigarh*	271%	5%	279	0.2%	0%	0%	100%	0%
Puducherry	62%	11%	266	0.2%	9%	20%	71%	0%
Meghalaya	41%	16%	257	0.2%	33%	18%	49%	0%
Manipur*	50%	24%	208	0.1%	30%	21%	49%	0%
Sikkim	28%	18%	207	0.1%	28%	10%	62%	0%
Arunachal Pradesh*	37%	16%	189	0.1%	28%	72%	0%	0%
Nagaland*	42%	16%	180	0.1%	22%	46%	32%	0%
Mizoram*	28%	15%	144	0.1%	8%	25%	67%	0%

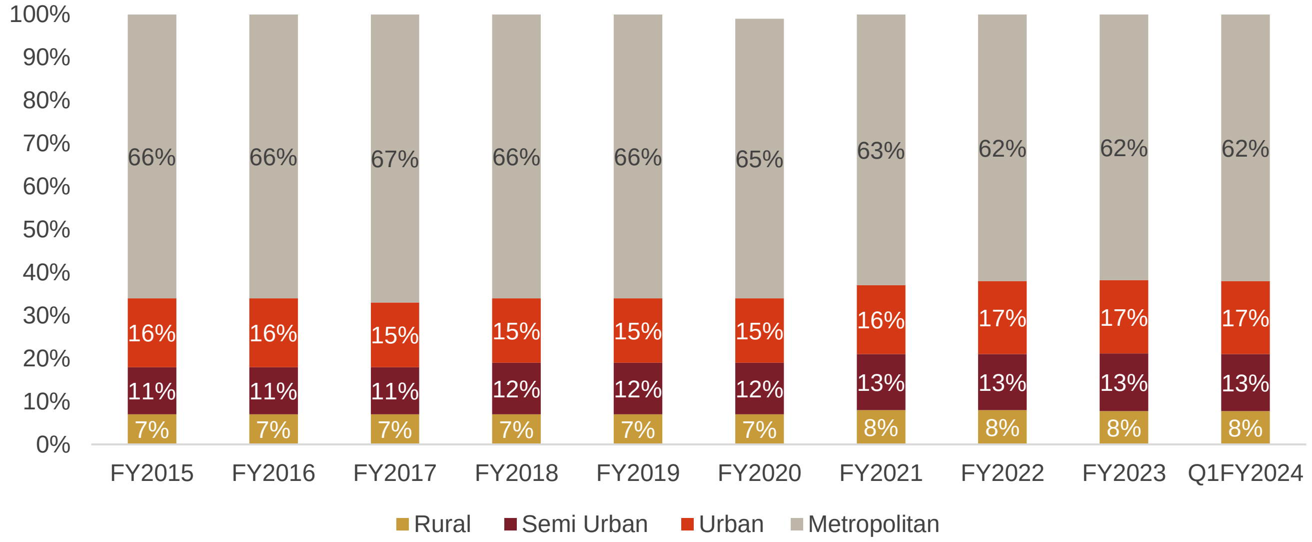
*Note: Credit penetration calculated as banking credit to states as of Fiscal 2023 divided by state GSDP (at constant prices) as of Fiscal 2022; Region wise credit % calculated as credit divided by total credit, GDP taken as GSDP at constant prices, Base Year: 2011-12., * GDSP taken for Fiscal 2021, Source: RBI, MOSPI, CRISIL MI&A Estimates*

Rural India – Under penetration and untapped market presents a huge opportunity for growth

Credit to metropolitan areas has decreased over the past few years with its share decreasing from 66% in Fiscal 2015 to 62% as at June 30, 2023. Between the same period, credit share has witnessed a marginal rise in rural and urban areas. For semi-urban areas, credit share has gone up from 12% as of March 31, 2018, to 13% as of June 30, 2023.

At at March 31, 2023, rural areas, which account for 47% of GDP, received just 8% of the overall banking credit, which shows the vast market opportunity for banks and NBFCs to lend in these areas. With increasing focus of the Government of India towards financial inclusion, rising financial awareness, increasing smartphone and internet penetration, CRISIL MI&A expects delivery of credit services in rural area to increase. In addition, usage of alternative data to underwrite customers is expected to also help the financiers to assess customers and cater to the informal sections of the society in these regions.

Share of rural and semi-urban credit has increased marginally between Fiscal 2015 and Fiscal 2023



Source: RBI, MOSPI, CRISIL MI&A

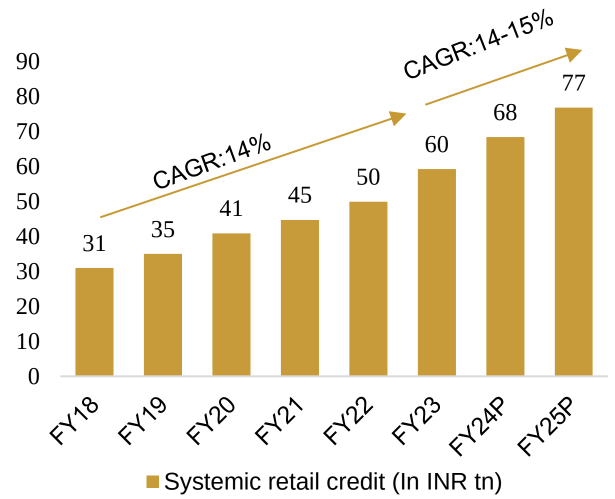
Retail credit market to grow at a healthy pace and remain profitable

Over last few years, retail credit grew at a strong pace from ₹ 30 trillion in Fiscal 2018 to ₹ 60 trillion in Fiscal 2023 and it constituted 32% of total systemic credit in India. The credit gap is much larger in case of Emerging Self-Employed Individuals.

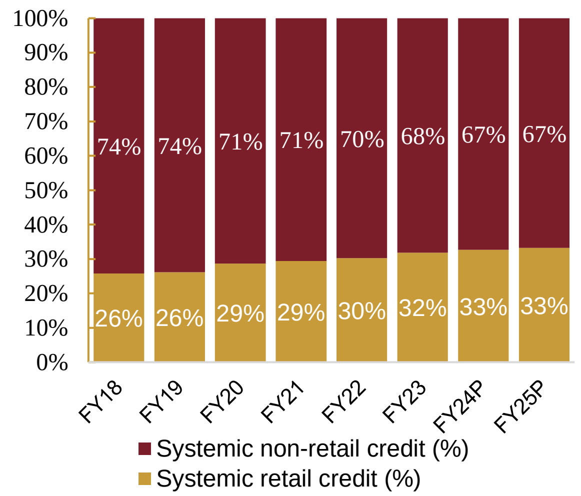
Retail credit is expected to further log a CAGR of 14-15% between Fiscals 2023 and 2025. It is likely to be propelled by an increase in private consumption with a steady rise in GDP growth, a shift in attitude of consumers towards debt, the continuing trend of urbanisation and nuclearization, increased availability of data from credit bureaus as well as non-traditional data and financiers leveraging technology and data analytics to serve their target markets more efficiently. In addition, CRISIL MI&A sees that despite fast growth in retail credit, India's household debt in relation to its GDP still remains low at 21% compared with the BRICS countries – 34% in Brazil, and 62% in China.

From a profitability perspective as well, retail lending is an attractive proposition with NBFCs across various asset classes being able to earn fairly healthy return on assets over the course of a business cycle. Given that the market is large, has good growth prospects, is under penetrated and profitable, CRISIL MI&A expects retail credit to continue to remain a key focus area for banks and NBFCs.

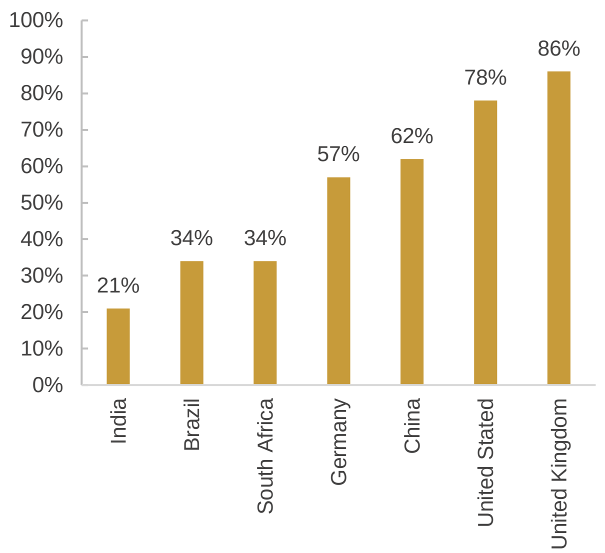
Retail credit growth to continue on a strong footing in Fiscal 2024 and 2025



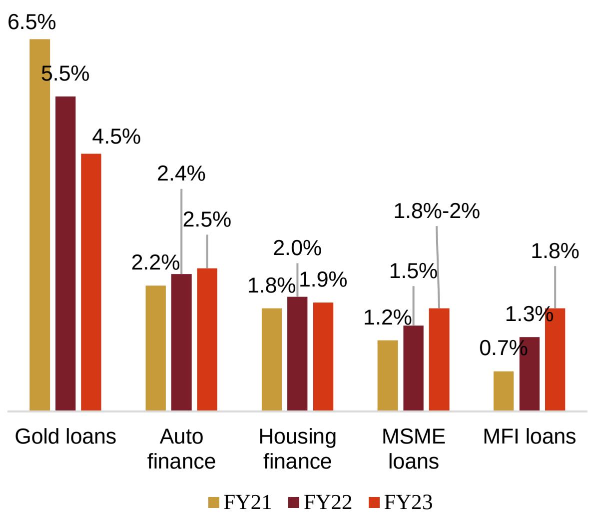
Retail segment is estimated to account for 32% of overall systemic credit as of Fiscal 2023



India most underpenetrated in terms of retail credit indicating significant potential for growth



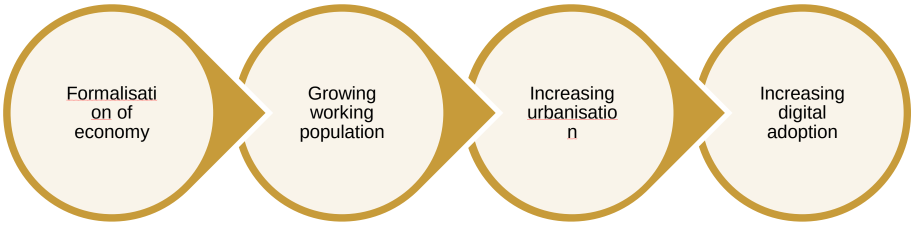
Retail lending is profitable for NBFCs across various asset classes as indicated by their Return on Assets



Note: E = Estimated; P = Projected, above retail credit market includes housing finance, Auto finance, microfinance, gold loans, construction equipment finance, consumer durable finance, MSME loans and education loans
For countries except India, data is represented for calendar years. For India, data represented is for fiscal year 2022.

Source: RBI, Bank of International Settlements, Company reports, CRISIL MI&A

Factors that are expected to support retail credit growth

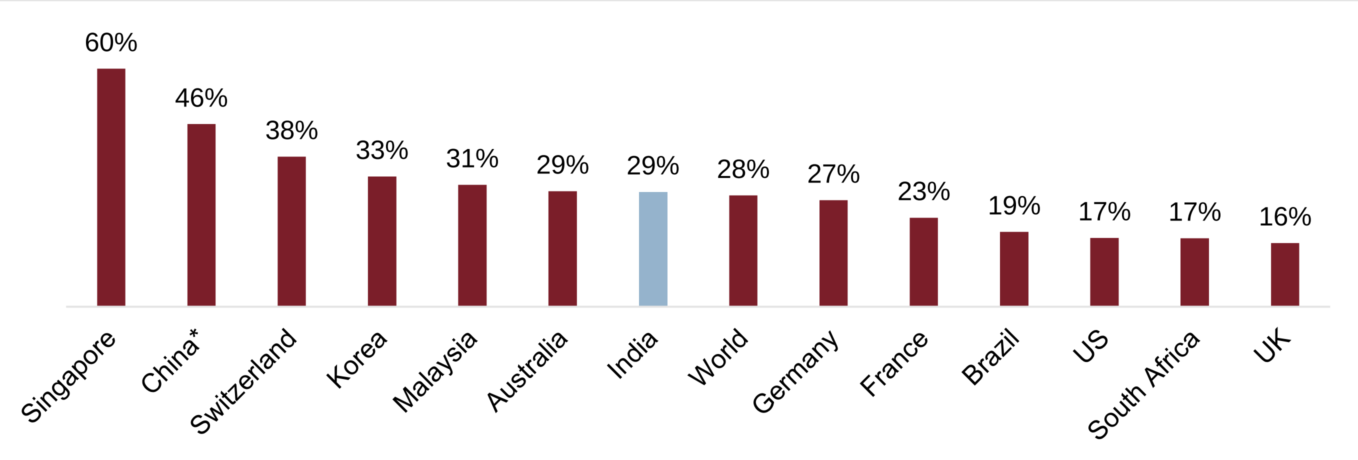


Source: CRISIL MI&A

Household savings to increase

India's slowing economy took a toll on much-needed savings too, with the savings rate touching a 15-year low in Fiscal 2020 to 27.1%, post which in the next two fiscals the savings have witnessed a growth and touched ~29% during fiscal 2022. Despite the slow-down, India remains favourable in terms of gross domestic savings rate compared with most other emerging market peers at 29% in fiscal 2022, greater than the world average of 28%.

Gross Domestic Savings rate (in %): India vs other countries (CY 2022)

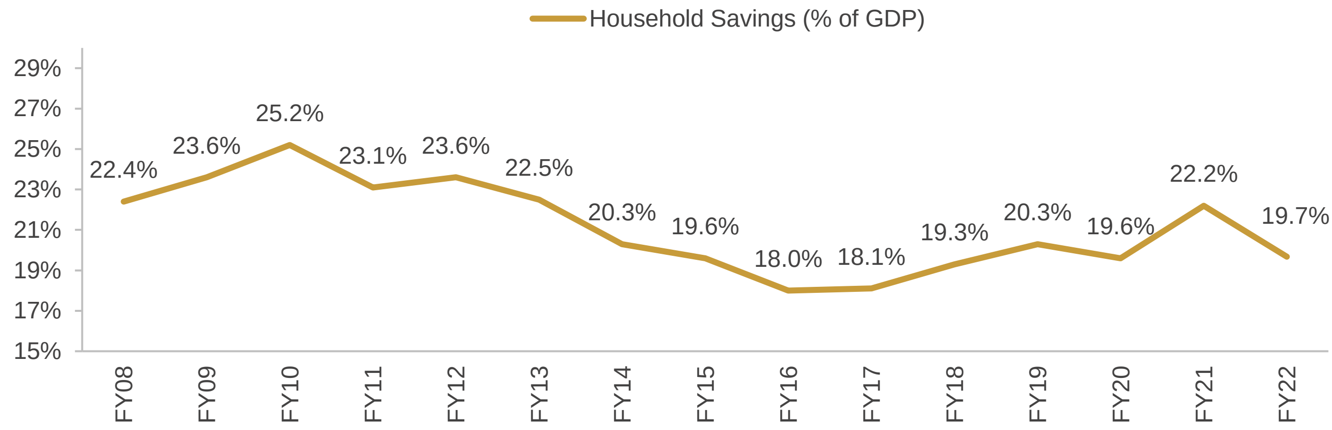


Note: Gross Domestic Saving consists of savings of household sector, private corporate sector and public sector; (*) Data as of CY2022; Source: World Bank[6], Handbook of Statistics on Indian Economy 2020-21, RBI, MOSPI, CRISIL MI&A

Specifically, household savings as a percentage of GDP has been sliding since Fiscal 2012, with its share as a proportion of GDP falling significantly from 23.6% in Fiscal 2012 to 18.0% in Fiscal 2016. The household savings as percentage of GDP rose to 19.7% in Fiscal 2022.

[6] *https://data.worldbank.org/indicator/NY.GDS.TOTL.ZS*

Household savings as a percentage of GDP has increased to 22.2% in fiscal 2021, declined in fiscal 2022



Source: Ministry of Statistics and Programme Implementation (MOSPI), RBI, CRISIL MI&A

Gross domestic savings trend

Parameters (₹ billion)	Mar-14	Mar-15	Mar-16	Mar-17	Mar-18	Mar-19	Mar-20	Mar-21	Mar-22
GDS	36,082	40,200	42,823	48,251	54,807	60,003	59,959	55,924	54,266
Household sector savings (net financial savings, savings in physical assets and in the form of gold and silver ornaments)	22,853	24,391	24,749	27,871	32,966	38,446	39,291	43,906	46,195
Household sector savings as proportion of GDS (%)	63%	61%	58%	58%	60%	64%	66%	79%	85%
Gross financial savings	11,908	12,572	14,962	16,147	20,564	22,636	23,991	31,089	25,979
Financial liabilities	3,587	3,768	3,854	4,686	7,507	7,712	7,866	8,052	8,071
Savings in physical assets	14,164	15,131	13,176	15,946	19,442	23,094	22,735	20,484	27,690
Savings in physical assets as a proportion of GDS (%)	39%	38%	31%	33%	35%	38%	38%	37%	51%
Savings in the form of gold and silver ornaments	368	456	465	465	467	427	431	384	597

Note: The data is for financial year ending March 31. Physical assets are those held in physical form, such as real estate, etc.

Source: MOSPI, National Accounts National Accounts Statistics, CRISIL MI&A

Household savings growth

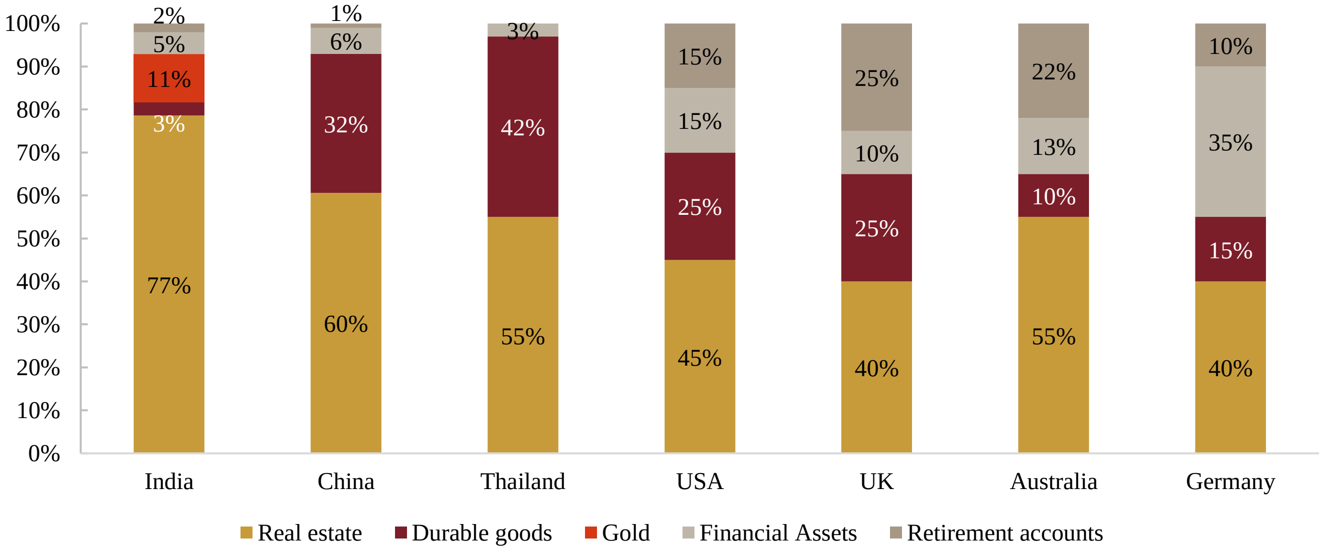
Note: The data is for financial year ending March 31.
Source: MOSPI, CRISIL MI&A

CRISIL MI&A expects India to continue being a high savings economy. CRISIL MI&A is also sanguine on savings rate increasing in the medium-term, as households become more focused post the COVID-19 pandemic-induced uncertainty on creating a nest egg for the future post the COVID-19 pandemic-induced uncertainty. In addition, according to the SEBI, during Fiscal 2021, until the third quarter, the household financial savings deployed in securities market had grown significantly to 1.2% of GDP as compared to 0.3% earlier. Going forward, if the amount of savings deployed in securities market sustained, it is expected to boost the capital markets and economy.

Physical assets still account for majority of the savings

Unlike most other countries, where financial savings account for a significant proportion of savings, physical assets in the form or real estate, gold and silver still account for most household savings in India.

Trend of savings in India and other economies



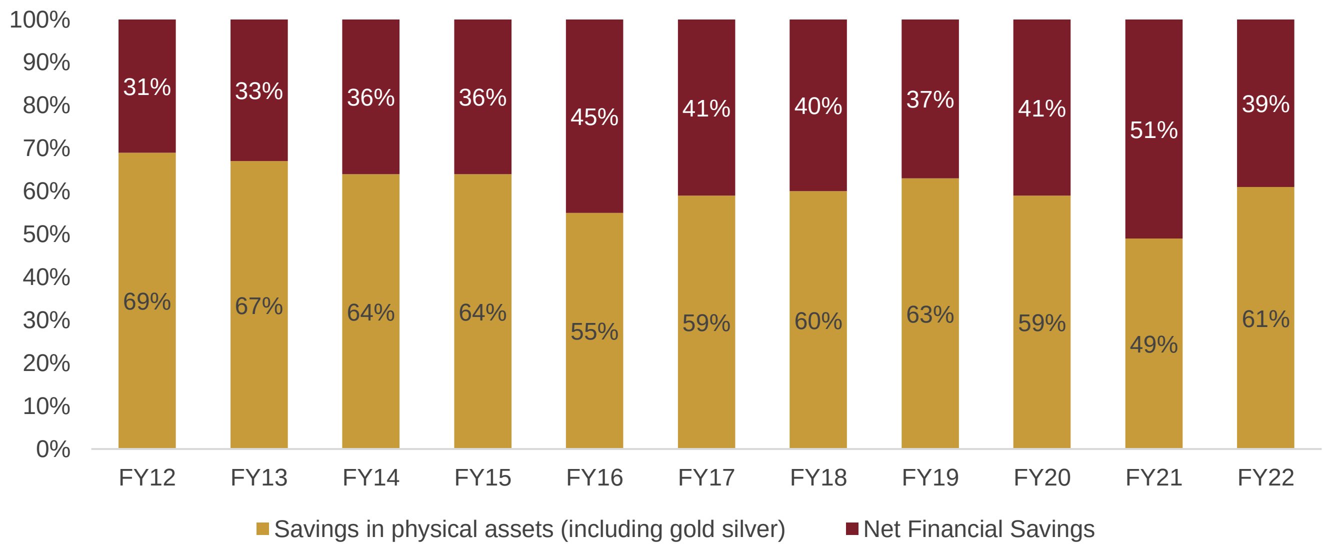
Source: Report of the Household Finance Committee- July 2017[7], RBI, CRISIL MI&A

[7] *https://rbidocs.rbi.org.in/rdocs/PublicationReport/Pdfs/HFCRA28D0415E2144A009112DD314ECF5C07.PDF*

Although households' savings in physical assets has declined to 61% in Fiscal 2022 from 69% in Fiscal 2012, it constitutes a substantial share in overall savings. On the other hand, the share of financial savings has witnessed an uptrend to 39% in Fiscal 2022 from 31% in Fiscal 2012.

In the long-term, with increase in financial literacy, CRISIL MI&A expects the share of financial assets as a proportion of net household savings to increase over the next five years, thereby boosting investments in assets such as insurance and mutual funds.

Trend of household savings in India

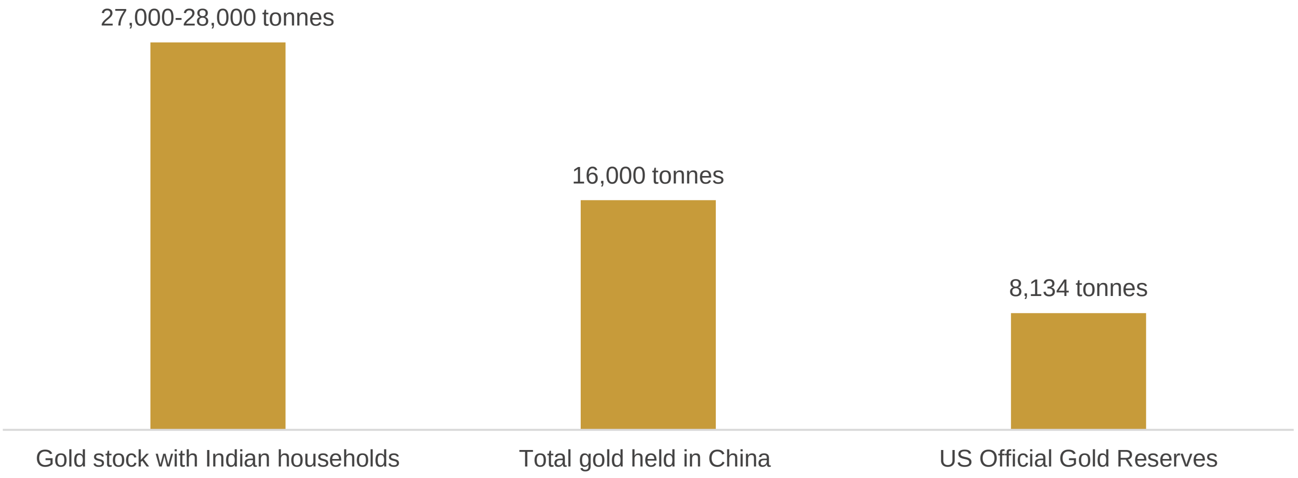


Note: The data is for financial year ending March 31

Source: Handbook of Statistics on Indian Economy 2020-21, RBI, MOSPI, CRISIL MI&A

As of March 2011, Indian households had gold stock of around 19,000 to 20,000 tonnes. In addition, as of March 2023, the gold pledged with financiers constituted around 7% of the 28,000 tonnes of gold holdings in Indian Households as per CRISIL MI&A estimates.

India has world's largest private gold holdings



Source: World Gold Council, CRISIL MI&A estimates

As more and more households become more open to monetising their gold holdings to meet either personal or business needs and the ease of obtaining a gold loan improves, the addressable market for financiers would expand significantly. At the average market price of ₹ 58,718 per 10 gram of gold in August 2023, monetising even 20% of the gold stock in the form of a loan at a 70% loan-to-value ratio ("**LTV**") is expected to lead to a ₹ 23 trillion market opportunity for financiers.

NBFC OVERVIEW

Constituents of NBFC industry in India

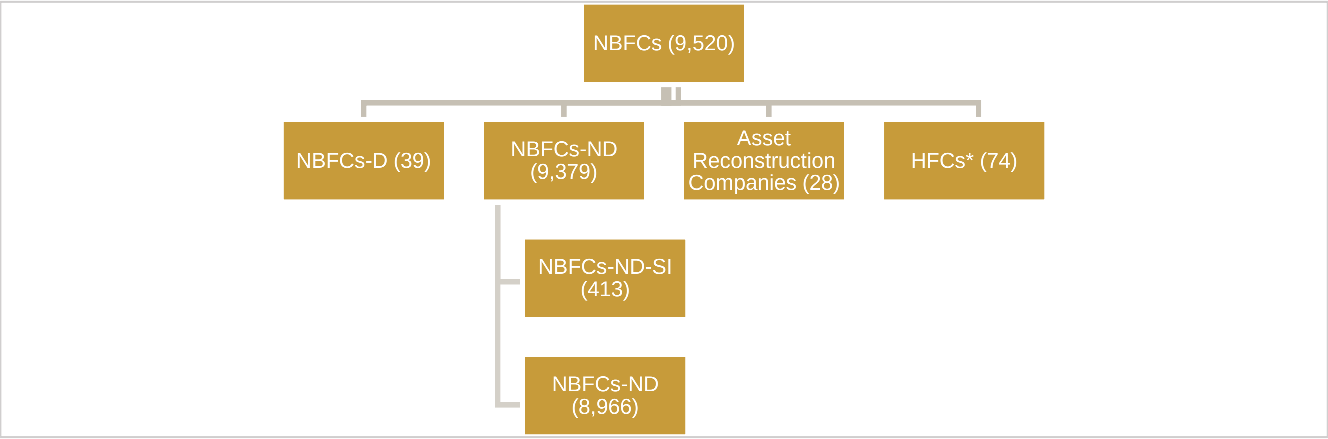
The Indian financial system includes banks and NBFCs. Though the banking system dominates financial services, NBFCs have grown in importance by carving a niche for themselves by catering to customers in underbanked regions or those who would not be catered to by traditional financial institutions, due to absence of credit history or lack of proper collateral records.

Classification of NBFCs

NBFCs are classified on the basis of liabilities into two broad categories – deposit-taking and non-deposit-taking. Deposit-taking NBFCs (“**NBFC-D**”) are subject to requirements of capital adequacy, liquid assets maintenance, exposure norms, etc.

In addition, in 2015, non-deposit-taking NBFCs with an asset size of ₹ 500 crore and above were labelled as “systemically important non-deposit taking NBFCs” (“**NBFC–ND–SI**”) and separate prudential regulations were made applicable to them.

Classification of NBFCs based on liabilities



Note: Figures in brackets represent the number of entities registered with RBI as of March 2023.

Source: RBI, CRISIL MI&A

Key regulations for NBFC

Over the past three decades, NBFCs have become part and parcel of formal credit system. RBI, on its part, has been continuously refining the regulations with a view to improve regulatory oversight as well as to be in tune with business dynamics of NBFC segment.

Here are a few key legislative and regulatory developments:

Amendments to the RBI Act in 1997 bestowed comprehensive powers on RBI to regulate and supervise NBFCs. Prominent features of the amendments include:

- Making it mandatory for NBFCs to obtain certificate of registration from RBI and maintain a minimum level of net owned funds (“**NoF**”)

- Requiring deposit taking NBFCs to maintain a certain percentage of assets in unencumbered approved securities
- Empowering RBI to determine policy and issue directions with respect to income recognition, accounting standards, etc
- Empowering RBI to order special audit of NBFCs
- Asset Liability management guidelines
- Corporate governance framework

Key regulations pertaining to NBFCs

Given the importance of NBFCs in financial system especially by accessing public funds and inter-connectedness with banking, they are subject to prudential regulations by RBI as given below

Regulatory distinction between banks and NBFCs

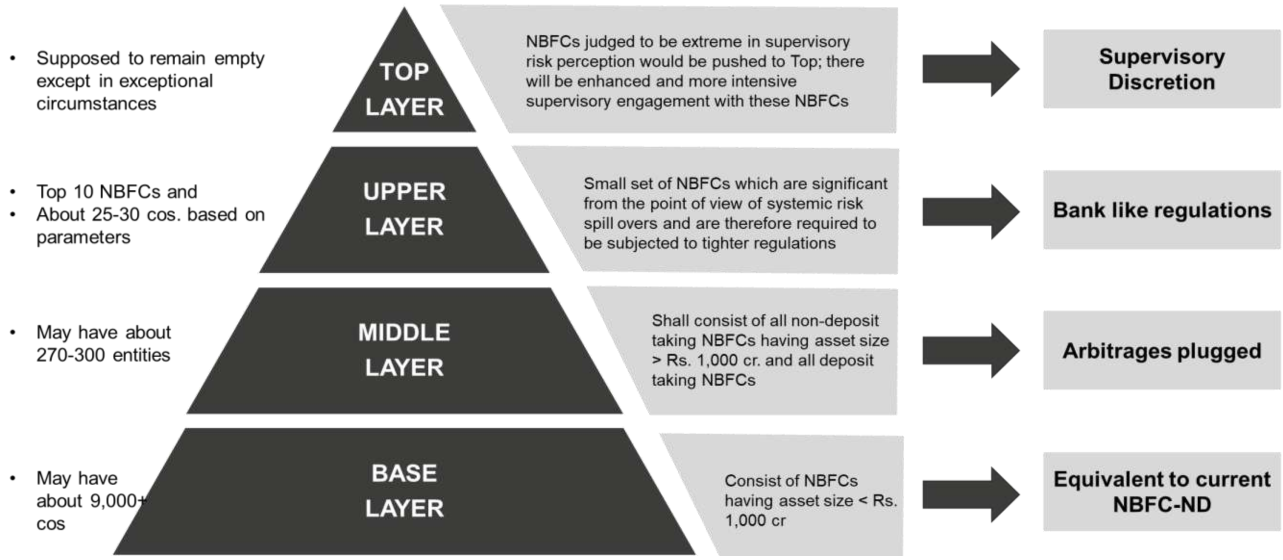
	NBFC – ND –SI	NBFC – D	Banks (Basel-III)
Minimum NoF	*₹ 20 million*	*₹ 20 million*	*N.A.*
Capital Adequacy	*15.0%*	*15.0%*	*11.5%*
Tier I Capital	*10.0%*	*10.0%*	*9.5%*
Stage III assets	*90 days#*	*90 days#*	*90 days*
Cash Reserve ratio (CRR)	*N.A.*	*N.A.*	*3.0%*
Statutory liquidity ratio (SLR)	*N.A.*	*15.0%*	*18.00%*
Priority Sector	*N.A.*	*N.A.*	*40% of advances*
SARFAESI eligibility	*Yes**	*Yes**	*Yes*
Exposure norms (% of NOF)	*Single borrower: 15% (+10% for IFC)*	*Single borrower: 15%*	*Single borrower: 15% (+5% for infrastructure projects)*
	Group of borrowers: 25% (+15% for IFC)	*Group of borrowers: 25%*	*Group of borrowers: 30% (+10% for infrastructure projects)*

Note: NA = Not applicable
Minimum NoF for NBFC-MFI and NBFC - Factors is Rs 50 million, while for IFC it is Rs 3000 million
**The Ministry of Finance in its union budget of 2021 has proposed the SARFAESI threshold to be reduced from the existing level of ₹5 million to ₹2 million*
 # Discretion with the audit committee of NBFCs to defer stage 3 classification beyond 90+dpd
Source: CRISIL MI&A

Scale based approach proposed for NBFCs

RBI in January 2021 had proposed a tighter regulatory framework for NBFCs by creating a four-tier structure with a progressive increase in intensity of regulation in a discussion paper titled “Revised Regulatory Framework for NBFCs – A Scale-based Approach”. Based on the inputs received, in October 2021, RBI put in place a revised regulatory framework for NBFCs which is slated to be effective from October 2022.

In Framework for Scale Based Regulation for NBFCs, RBI has said the regulatory and supervisory framework of NBFCs should be based on a four-layered structure based on their size, activity, and perceived riskiness: Base Layer, Middle Layer, Upper Layer and Top Layer. NBFCs in lower layer are expected to be known as NBFC-Base Layer (“**NBFC-BL**”). NBFCs in middle layer are expected to be known as NBFC-Middle Layer (“**NBFC-ML**”). An NBFC in the Upper Layer is expected to be known as NBFC-Upper Layer (“**NBFC-UL**”) and is expected to invite a new regulatory superstructure. There is also a Top Layer, ideally supposed to be empty.



Source: RBI, CRISIL MI&A

RBI has taken a balanced view, and instead of going for a one size fits all, it has opted for differential regulation based on size and the systemic importance of an NBFC. In addition, the importance of NBFCs in providing credit to underserved customers has been recognised. RBI has not proposed imposition of CRR and SLR on NBFCs, which would come as a relief to NBFCs.

The proposed 9% common equity tier-1 ratio should not be difficult to manage as majority of the NBFCs remain well capitalised. Cap on leverage levels would impact NBFCs in the mortgage business if limits are proposed in line with other asset classes. Differential standard asset provisioning is expected to have a negative impact for NBFCs who have large exposure to sensitive sectors like commercial real estate (for example: CRE @ 1.00%, CRE-RH @ 0.75%; current norm for NBFCs is 0.4%). Cap of ₹ 1 crore on IPO financing per individual would hurt NBFCs operating in this space. Post this regulatory change, few NBFC-UL category may consider conversion into universal banks.

Overall, we believe the scale-based approach is expected to translate into greater regulatory oversight and better governance practices, which is expected to structurally strengthen the sector.

RBI tightens provisioning norms on Standard assets for NBFC Upper Layer

On June 6, 2022, RBI released a circular aligning provisioning for standard assets by NBFCs in the upper layer as per RBIs scale-based regulations with that prevalent with the banks, which would be effective from October 1, 2022. The impact of the norms is unlikely to be material as most large NBFCs already maintain Stage 1 and Stage 2 provisioning, which is comfortably higher than the required levels.

Supreme Court removes regulatory overhang for NBFCs

The legislatures of Kerala and Gujarat had sought to bring NBFCs under the ambit of their respective legislations (the Kerala Money Lenders Act, 1958 and the Gujarat Money-Lenders Act, 2011) to regulate the interest rate charged by moneylenders and protect borrowers. However, in May 2022, the Supreme Court put to rest the uncertainty around applicability of state legislations on NBFCs, underscoring the primacy of RBI as the regulator and supervisor of NBFCs in India, with oversight on the rate of interest they charge the borrowers.

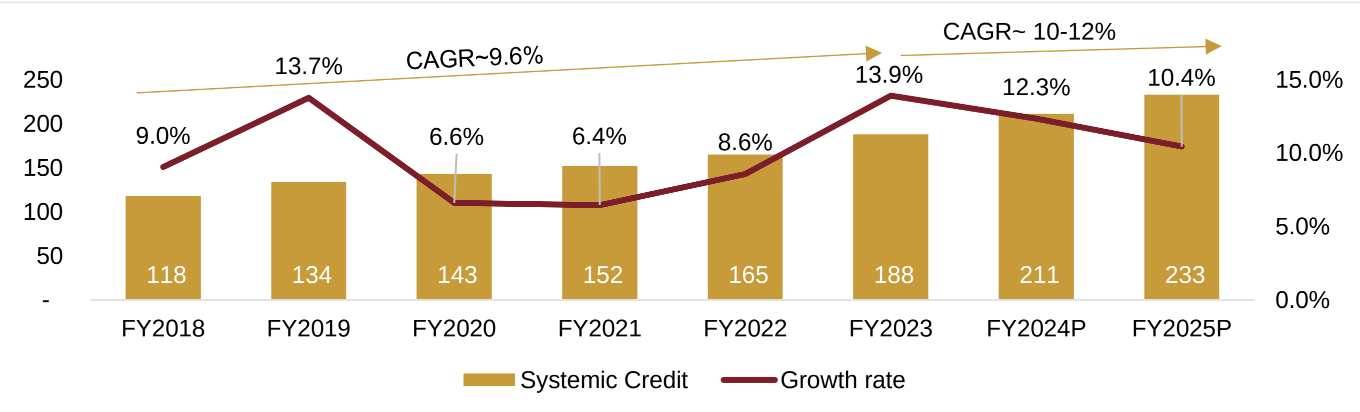
The ruling has two big takeaways- First, it has effectively reaffirmed regulatory sanctity for NBFCs registered with RBI as a separate category of lenders, distinct from the traditional moneylenders. Second, while the Supreme Court has not specifically commented on the appropriateness of interest rates being charged by NBFCs, it has implicitly stated that RBI has the jurisdiction and powers to look into the same and is already doing so through the various regulations, circulars and directions issued by it. CRISIL believes that the ruling is specifically beneficial to gold loan NBFCs and other regulated NBFCs, including NBFC-MFIs, where sensitivity over interest rates is higher.

Systemic credit to grow at 10-12% CAGR between fiscal 2023-2025

Overall systemic credit growth took a hit in first half of fiscal 2021 on account of a significant slowdown in retail credit and intensifying COVID-19 pandemic which triggered a national lockdown. The COVID-19 pandemic came as a jolt for an already slowing economy with a decadal low growth in GDP, low private consumption, cautious lending by financial institutions, poor capex, and in turn, weakening credit growth. However, with a slew of the Government of India and regulatory measures announced, Indian economy started to revive in the second half of the fiscal. In Fiscal 2021, credit grew by approximately 6.4% supported by disbursements to MSMEs under the ECLGS and an uptick in economic activity post the COVID-19 lockdown.

In Fiscal 2022, the systemic credit growth picked up steam despite the second wave of COVID-19 hurting economic growth in the first quarter of the fiscal. The systemic credit grew at 8.6% from the previous year to reach approximately ₹ 165 trillion. The growth was mainly driven by the budgetary push towards investments, pick-up in private investment, and business activity also slowly humming back to pre-COVID levels. In Fiscal 2023, Systemic credit showed strong growth on back of pent-up retail demand from sectors like housing and auto. Credit demand also grew due to strong credit demand from NBFCs and trade segment. CRISIL MI&A projects systemic credit to grow at 10-12% CAGR between Fiscals 2023 and 2025.

Systemic growth to grow by 10-12% over Fiscals 2023-2025

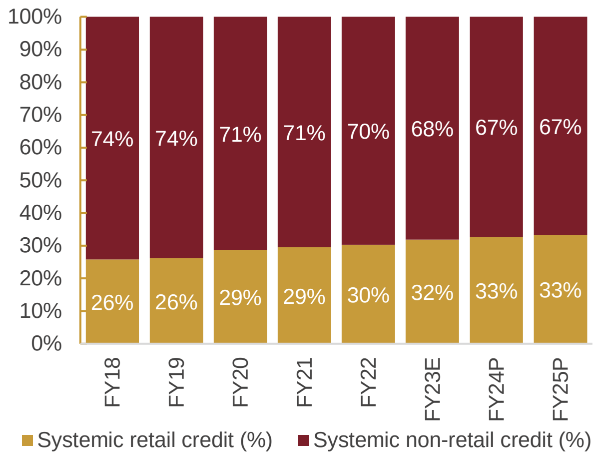


Note: P: Projected; E: Estimated, Systemic credit includes domestic banking credit, NBFC credit, commercial papers, external borrowings, corporate bonds excluding those issued by Banks and NBFC

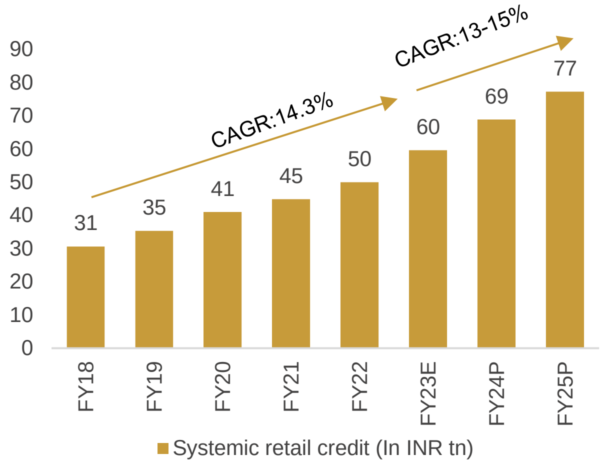
Source: RBI, Company Reports, CRISIL MI&A

While systemic credit in India grew at a tepid rate of 9.6% CAGR annually between Fiscal 2018 and Fiscal 2023, systemic retail credit grew at a much faster rate of 14.3% CAGR during the same period. Retail credit growth in Fiscal 2020 was around approximately 16.3% which came down to approximately 9.5% in Fiscal 2021. However, post-COVID-19 pandemic, retail credit growth revived back to reach approximately 11.3% in Fiscal 2022. CRISIL MI&A estimates retail credit to have grown at approximately 19-20% year on year in Fiscal 2023. CRISIL MI&A thus expects retail credit growth to continue in the long term with banks and NBFCs' continued focus on the segment.

Retail segment accounts for 32% of overall systemic credit as of Fiscal 2023



Retail credit growth to continue on a strong footing in Fiscal 2024

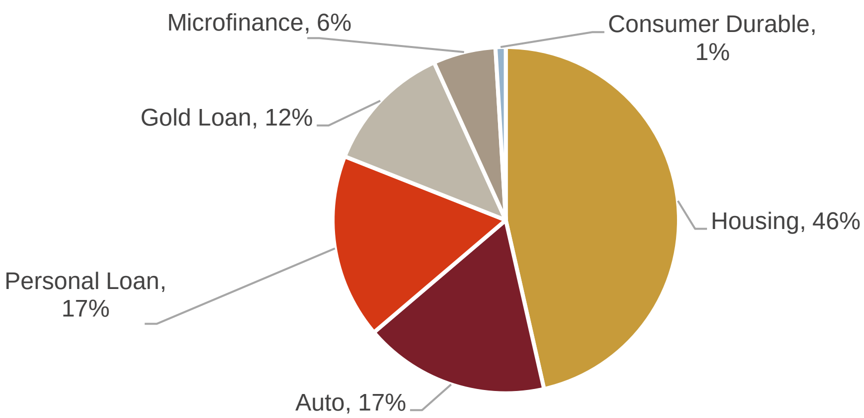


Note: P = Projected
Source: RBI, CRISIL MI&A

Home loans accounts for 46% of overall retail loans at end of Fiscal 2023

Housing finance and gold loans cover 46% and 12% of the retail loans industry, respectively, in India in Fiscal 2023

Retail credit mix as of Fiscal 2023



Source: RBI; CRISIL MI&A

NBFC credit to grow faster than systemic credit between Fiscals 2023 and 2025

Over the past decade, banking credit growth lagged systemic credit growth for several years as NBFCs grew at a much faster pace. However, the NBFCs suffered a blow after IL&FS defaulted in September 2018. NBFCs that did not have the advantage of size, rating and / or parentage had to grapple with a liquidity crisis and raising funds became difficult. Initially, post the IL&FS crisis, banks were expected to fill the space left out by NBFCs.

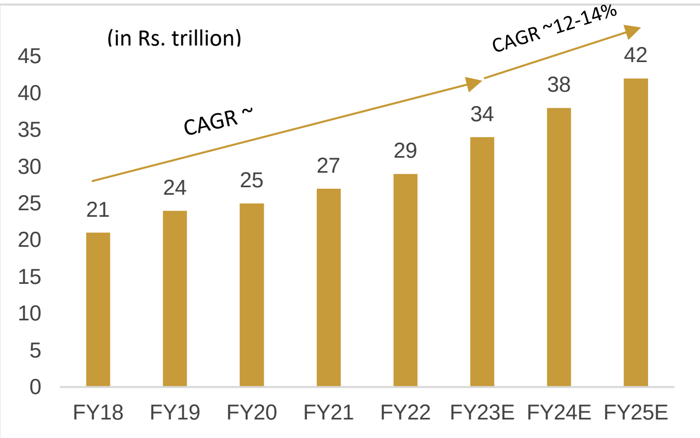
In the fourth quarter of Fiscal 2020 and the first quarter of Fiscal 2021, with the outbreak COVID-19 pandemic, challenges had intensified for both banks and NBFCs. NBFCs were hit harder in terms of demand, and they also turned cautious as they lend to borrowers with relatively weaker credit profile. Due to COVID-19 pandemic, demand for credit reduced drastically on account of economic activity coming down to standstill due to lockdown led sharp fall in disbursements. Few NBFCs also experienced credit rating downgrades and/or negative outlook changes during fiscal 2021. In the second half of Fiscal 2021, the Indian economy showed signs of improvement, the effect of which was seen in the credit growth.

In Fiscal 2022, the second wave of the COVID-19 pandemic led to weak demand for credit in the first quarter of the year. However, the pace of credit recovered, with overall credit growing by 9% and retail credit increasing by 11.3% year-on-year as of March 2022. With the effect of COVID-19 waning, vaccination coverage progressively improving, the situation and growth improved further.

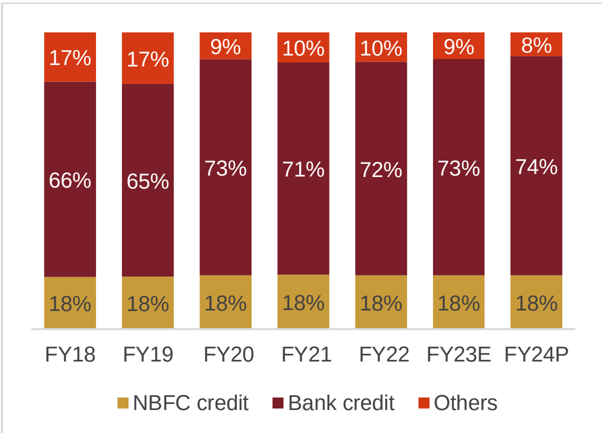
In Fiscal 2023, pace of credit further improved and is at par with pre-COVID level. Banking credit has grown at 15% in Fiscal 2023 as compared to 16% for NBFCs. NBFC credit is expected to grow at a higher rate of 13-14% in Fiscal 2024 as compared to 12-14% expected for banking credit. CRISIL MI&A projects NBFC credit to grow at 12%-14% between Fiscal 2023 and Fiscal 2025. The credit growth is expected to be driven by the retail vertical, including housing, auto, and microfinance segments. Rapid revival in the economy is expected to drive consumer demand in Fiscal 2024, leading to healthy growth NBFCs.

Moreover, organic consolidation is underway with larger NBFCs gaining share. In addition, growth of the non-banking industry is expected to be driven mainly by NBFCs with strong parentage who have funding advantage over other NBFCs.

NBFC credit to grow at CAGR 12-14% between Fiscals 2023 and 2025



Share of NBFCs credit in overall systemic credit remained 18% in Fiscal 2023



Note: P = Projected; Note: Others include Commercial papers, External borrowings, corporate bonds excluding those issued by Banks and NBFCs

Source: RBI, Company reports, CRISIL MI&A

NBFCs have shown remarkable resilience and gained importance in the financial sector ecosystem, growing from less than ₹ 2 trillion assets under management (“**AUM**”) at the turn of the century to ₹ 34 trillion at the end of Fiscal 2023. CRISIL MI&A expects NBFC credit to grow at 12-14% CAGR between Fiscal 2023 and Fiscal 2025. Their share in the overall credit pie has increased from 12% in Fiscal 2008 to 18% in Fiscal 2023 and projected to be remained stable in fiscal 2024. CRISIL MI&A believes that NBFCs are expected to remain a force to reckon within the Indian credit landscape, given their inherent strength of providing last-mile funding and catering to customer segments that are not catered by Banks.

Retail segment to support NBFCs overall credit growth

The NBFC sector has, over the years, evolved considerably in terms of size, operations, technological sophistication and entry into newer areas of financial services and products. The number of NBFCs as well as the size of the sector have grown significantly, with a number of players with heterogeneous business models starting operations.

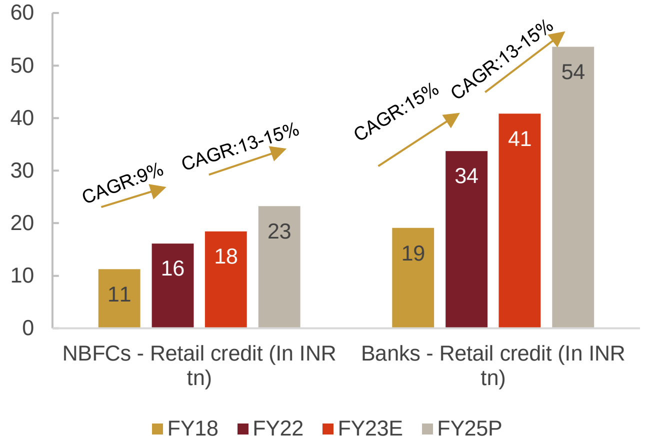
Over the last few years, CRISIL MI&A has seen a transformation in the Indian financial services landscape. The increasing penetration of neo-banking, digital authentication and mobile phone usage as well as mobile internet has resulted in the modularization of financial services, particularly credit.

The sector has also seen the emergence of a number of finTechs that leverage technology, data, and business insights to provide various financial products and services to identified customer segments. FinTech players in India started lending in Fiscal 2015 but they started gaining traction from Fiscal 2017 onwards. The business model of finTech firms differ widely but in almost all cases they use technology to change or support existing way of doing business, and hold the promise of enhancing customer convenience, facilitating access to credit for unserved or underserved customer segments and/or improving operating efficiency. Many times, finTechs enter into tie-ups with financing partners (banks and NBFCs) for taking the loans originated by them on the balance sheet of the partner.

Reflecting the growing importance of NBFCs in the financial services landscape and their ability to offer differentiated solutions to meet the requirement of target customers, the market share of NBFCs in overall systemic credit has increased from approximately 16% in Fiscal 2017 to approximately 18% in Fiscal 2023.

After a moderation in growth post COVID-19 pandemic, NBFCs are back on track with an expected credit growth of 13-14% during Fiscal 2024. The industry is expected to continue to witness the emergence of newer NBFCs catering to specific customer segments. The COVID-19 pandemic and consequent acceleration in both adoption of technology and change in consumer habits as well as increasing availability of data for credit decision-making has made it possible to build an NBFC lending business without investing large sums to have brick-and-mortar presence on the ground. Overall, between Fiscal 2023 to Fiscal 2025, CRISIL MI&A forecasts NBFC credit to grow at a CAGR of 12%-14%. In addition, retail credit given out by NBFCs is forecast to grow at a pace of 13%-15% CAGR over the same time.

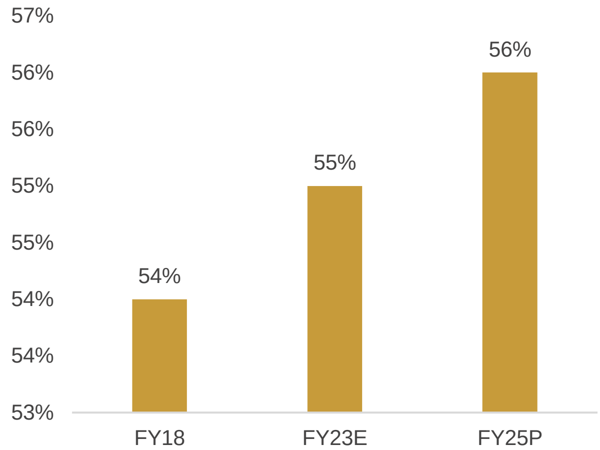
NBFCs retail credit is expected to grow at 13-15% CAGR in next 3 years



Note: Above retail credit includes housing finance, Auto finance, microfinance, gold loans, construction equipment finance, consumer durable finance, MSME loans and education loans

Source: Company reports, RBI, CRISIL MI&A

Share of retail credit in total NBFC credit to continue to grow



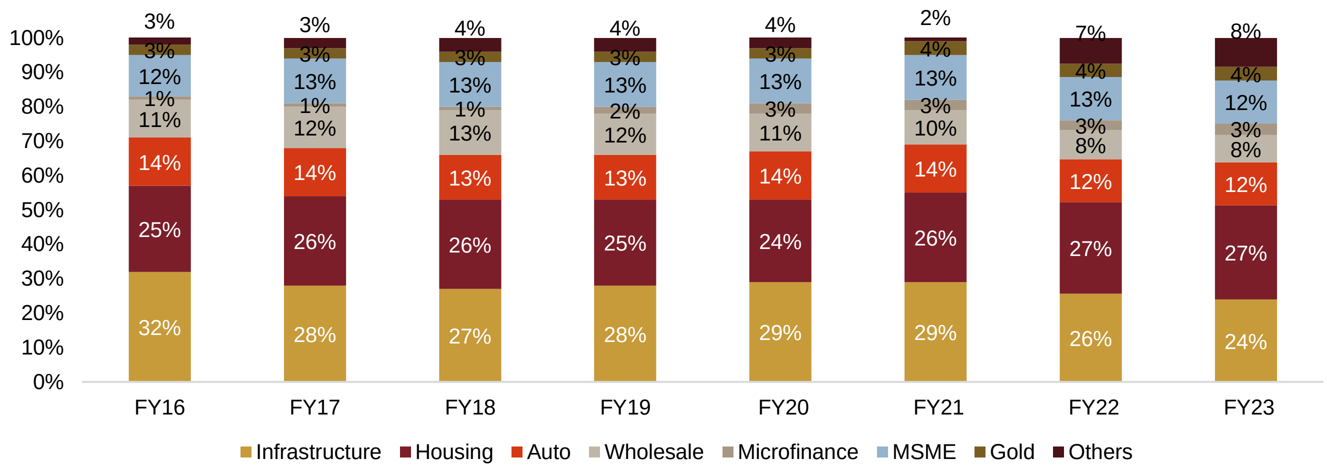
Note: P = Projected; Retail credit includes housing finance, auto finance, microfinance, gold loans, construction equipment finance, consumer durable finance, MSME loans and education loans

Source: Company reports, CRISIL MI&A

Housing and infrastructure loans account for more than 50% share in overall NBFC portfolio as of Fiscal 2023

In terms of asset size wise mix, housing loans and infrastructure loans continue to account major chunk of overall NBFC portfolio. Microfinance loans have increased their share from approximately 2% to 3% between Fiscal 2019 and Fiscal 2023. CRISIL MI&A expects housing and infrastructure loans to maintain their share in overall NBFC credit. In addition, auto, personal loan and microfinance loans are expected to perform better as compared to other segments in Fiscal 2024.

Distribution of NBFC credit across asset classes



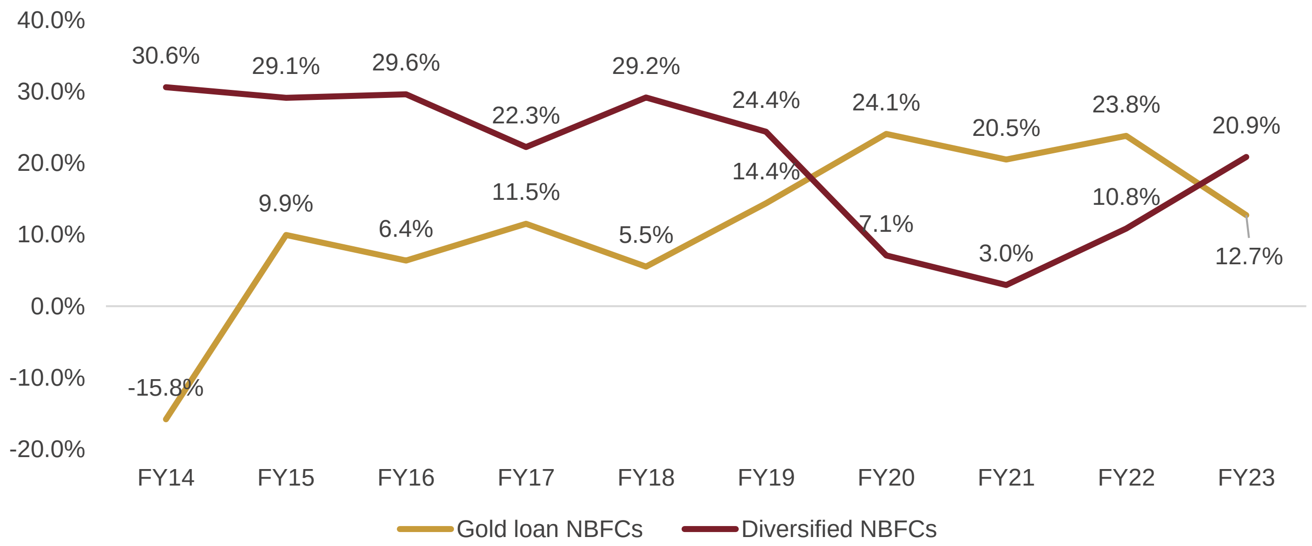
Note: Others include Personal loans, Construction equipment finance, Consumer durable finance and Education loans

Source: RBI, Company reports, CRISIL MI&A

Gold loan and non-gold loans being counter cyclical in nature

Most lenders tend to be pro-cyclical, lending aggressively during good times and pulling back during periods of distress and slowdown in economic growth. Small businesses and enterprises especially find it tough to get credit during periods of economic downturn as established lenders tend to tighten their underwriting standards. One asset class that tends to see healthy growth when the economy or other loan segments are not doing well is gold–backed lending. As lenders become more cautious and stringent due to slowdown in economy, gold loans serve as a quick, easy and convenient avenue to fund short term needs of customers. For example, during Fiscal 2020 and Fiscal 2021, when growth for diversified NBFCs witnessed sharp decline, gold loan NBFCs witnessed strong double-digit year on year ("**y-o-y**") growth of over 20% during the same period. This counter cyclical nature of gold loans provides cushion and acts as an active hedge for overall growth of NBFCs which have a good portfolio mix of gold loans and other loans.

Y-o-Y growth trend of gold loans NBFCs vs diversified NBFCs



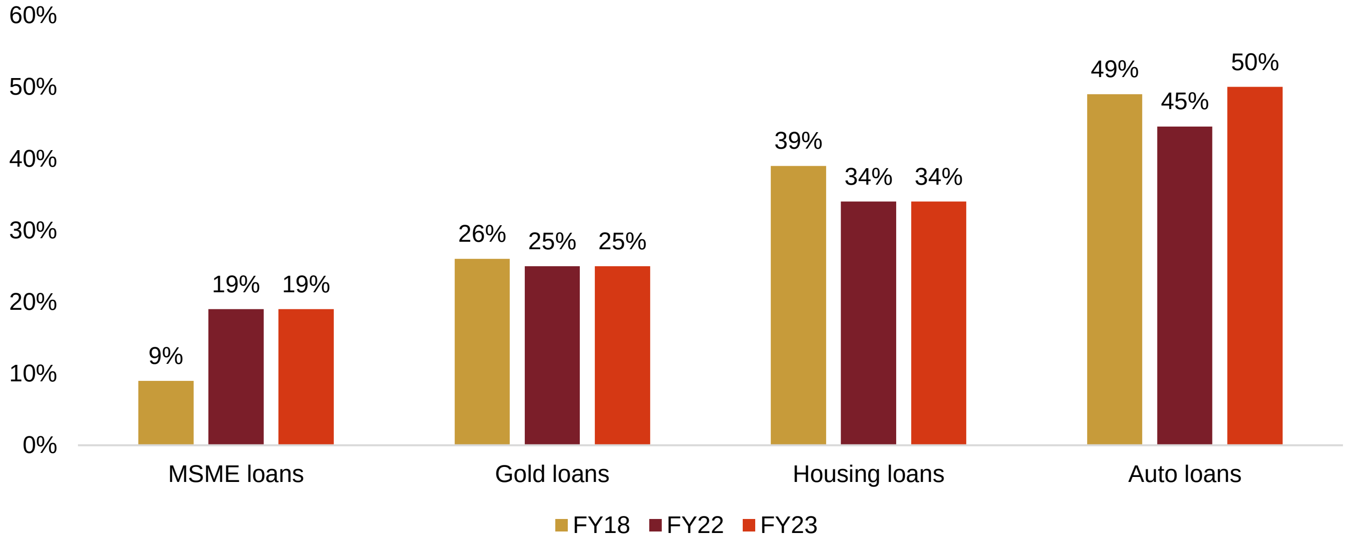
Note: Gold loan NBFCs includes – Muthoot Finance, Manappuram Finance, Kosamattam Finance and Muthoottu mini; Diversified NBFCs includes – Aditya Birla Finance, Bajaj Finance, Fullerton India Credit, HDB Financial Services, IIFL Finance, L&T Finance and Tata Capital;
Source: Company reports, CRISIL MI&A

NBFCs have a reasonable market share across segments

NBFCs have consistently gained or maintained market share across most asset classes over the last few years. Though, in certain segments such as housing finance to prime customers, they have lost market share to banks due to the decline in market interest rates. In the gold loans market, NBFCs slightly lost market share in Fiscal 2022 due to increasing focus of banks (both public and private) towards gold loans as well as RBI permitting banks to offer gold loans at a higher loan-to-value amidst the COVID-19 pandemic. However, in Fiscal 2023 and first quarter of Fiscal 2024, LTV in gold loans have shrunk owing to rise in prices of gold and a conservative approach taken by banks. Nevertheless, NBFCs continue to have a healthy market share across other segments.

NBFCs have been able to compete with banks mainly on account of their strong origination skills, extensive reach, better customer service, faster processing, fewer documentation requirements, digitalisation of customer on-boarding process, customised product offerings, local knowledge, and differentiated credit appraisal methodology. Furthermore, by catering to under banked, lower income and mass market customers who are unserved or underserved by banks, NBFCs have enhanced financial inclusion and expanded the market for formal financial services. The rapid evolution of finTechs over the last few years has added another dimension to the market served by NBFCs and has fuelled rapid growth across the landscape.

Market share of NBFCs in overall credit across select asset classes



Source: Company reports. RBI, CRISIL MI&A estimates

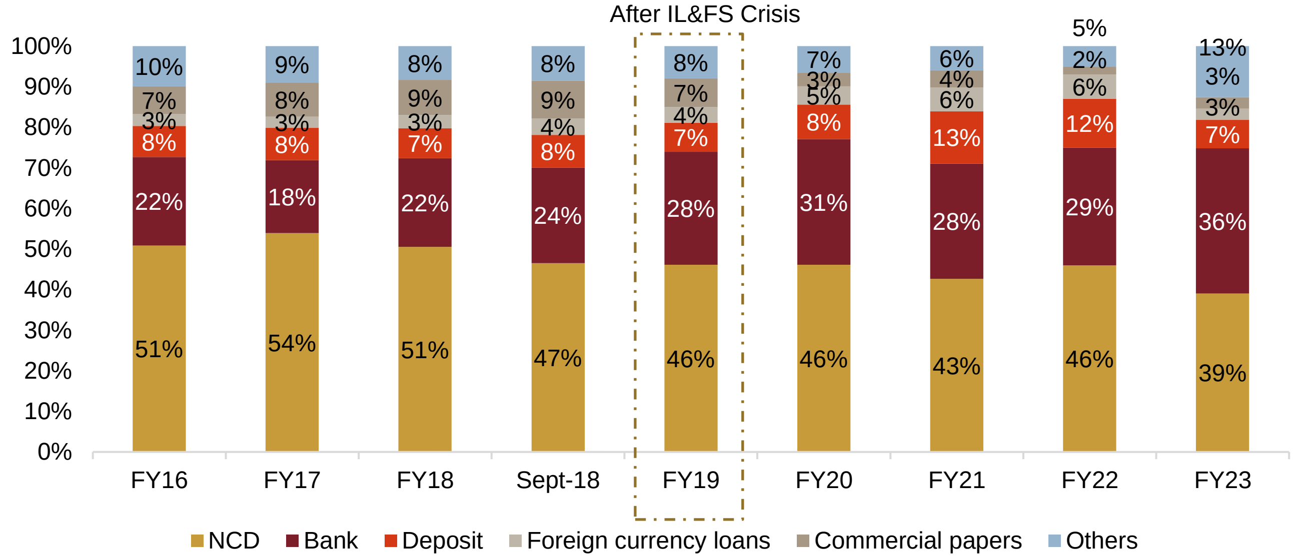
Resources profile of NBFCs

NBFC's borrowing mix has been changing over the past couple of years. Capital market investors have become cautious given the challenging environment and concerns over the asset quality. Investors' risk perception has increased significantly towards players with negative asset liability management mismatch. On the other hand, NBFCs with diversified sources of borrowings, and conservative approach to asset-liability management ("**ALM**") have been able to overcome the severe liquidity crunch and volatile interest rates following IL&FS crisis. Therefore, access to the capital markets has been restricted to limited players, with others relying more on bank borrowings and borrowings from larger NBFCs and overseas debt investors to meet their requirement. This has resulted in reduction in share of Commercial Papers ("**CPs**") and non-convertible debentures ("**NCDs**") and a corresponding increase in banks borrowings during Fiscal 2019 to Fiscal 2021.

In Fiscal 2023, NBFCs' borrowings from banks witnessed high growth resulting in an increase in share to 36% of total funding up from 29% at the end of Fiscal 2022. Share of bank's lending to NBFCs have almost doubled during last 10 years. During Fiscal 2023, with interest rate tightening and repo increasing by 250 bps to 6.50%, the cost of debt market borrowing increased leading to high-risk premium for lower rates NBFCs, leading to banks term loans becoming the preferred source of borrowing. This was also supported by improved credit growth during Fiscal 2023 across all segments leading to higher demand of bank credit from NBFC.

Going forward, CRISIL MI&A believes that funding access would gradually improve for NBFCs who are able to demonstrate strong performance and strong parentage. However, reliance on bank funding and funding from other NBFCs and small finance banks is expected to remain high in Fiscal 2024.

NCDs and banks expected to remain primary lenders for the NBFCs



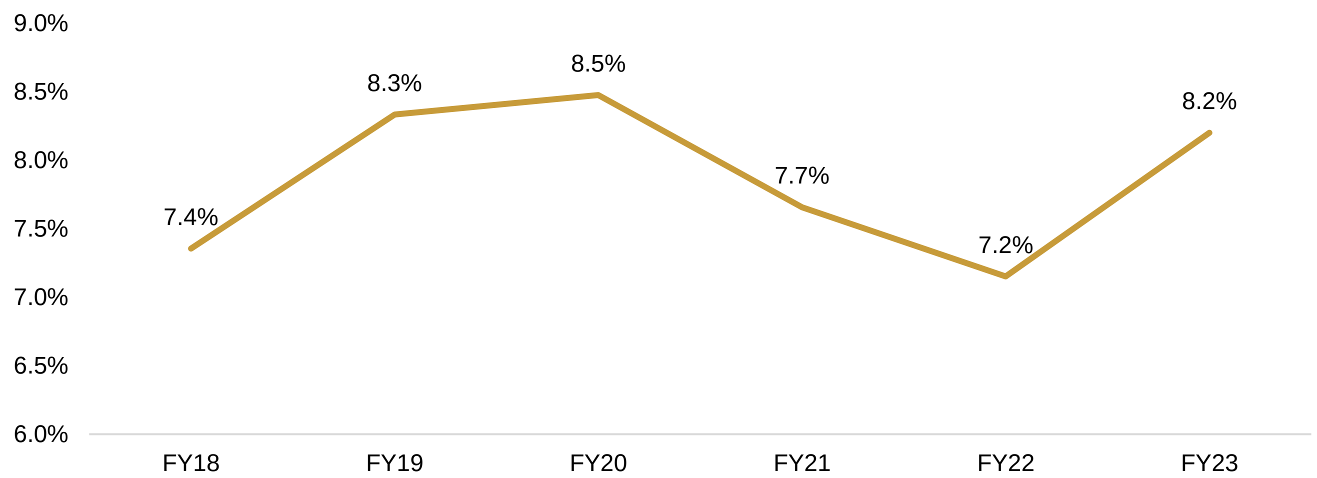
Note: Based on sample set of NBFCs accounting for more than 80% of overall borrowings of NBFCs as of March 2022; For Fiscal 2022, NCD includes Debt Securities and NCDs, Bank includes Banks and National Housing Bank, and Others include Related Parties, Foreign Institutions, External Commercial Borrowings and other sources.

Source: Company reports, CRISIL MI&A

NBFC borrowing cost is expected to increase in Fiscal 2024 with reversal in interest rate cycle

Soaring inflationary pressures have resulted in RBI reversing its accommodative monetary policy stance. As of February 2023, the benchmark repo rate has already been increased by 250 bps to 6.5% from the base level of 4% on October 2020. As per CRISIL MI&A estimates, the upward movement in interest rates is anticipated to lead to NBFC debt being repriced at a higher cost. However, the borrowing costs for NBFCs in Fiscal 2023 is still below the pre-COVID level.

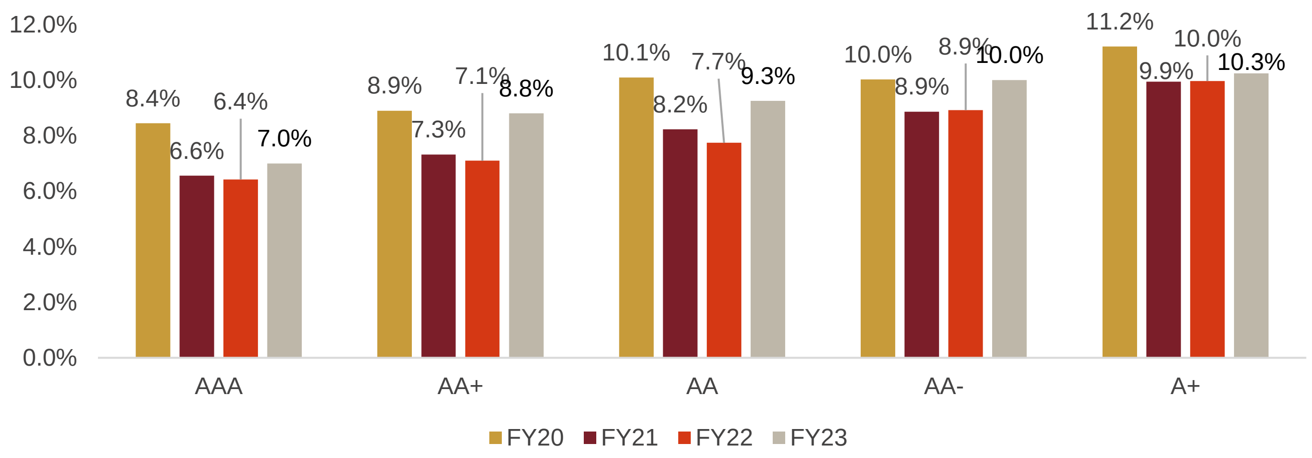
Increased borrowing cost for NBFC in Fiscal 2023



Note: P = Projected, Data represents cost of borrowing of players which cumulatively accounts for 85% of overall NBFC AUM; Source: Company reports, CRISIL MI&A

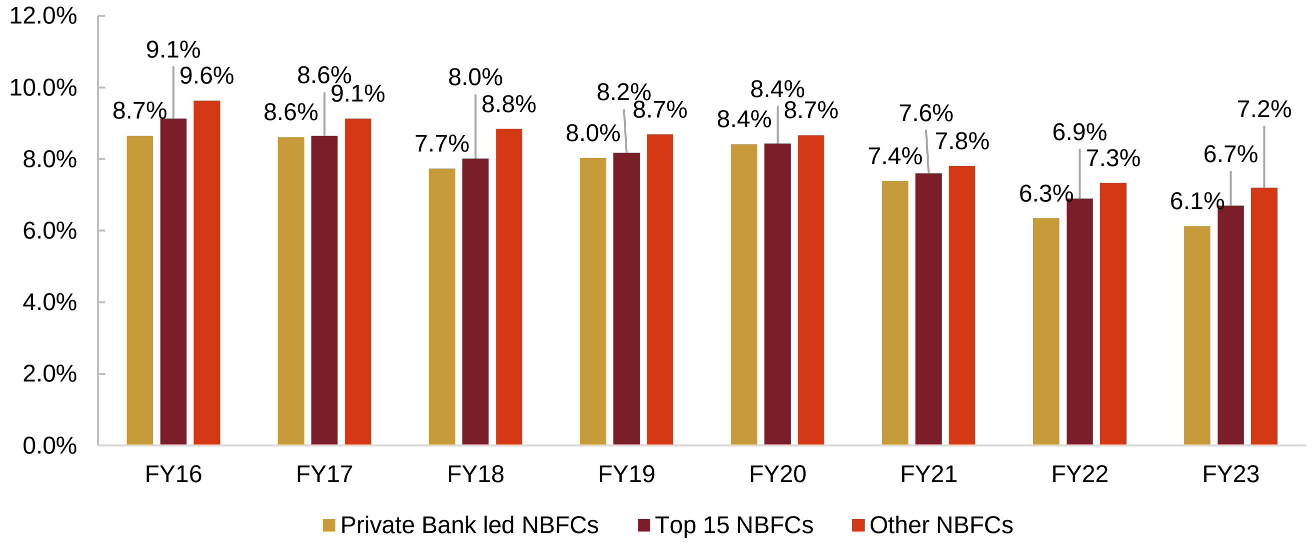
For AAA rated entities, cost of borrowings remained well below 7% as of Fiscal 2023 and has reduced from approximately 9%-10% in Fiscal 2016. For A+ and above rated companies as well, cost of borrowings has been below 10.3% in Fiscal 2023. Cost of borrowing has remained high for BBB category NBFCs.

Average Cost of borrowing trend by Ratings category



Source: CRISIL MI&A

Cost of borrowings trend by NBFC type



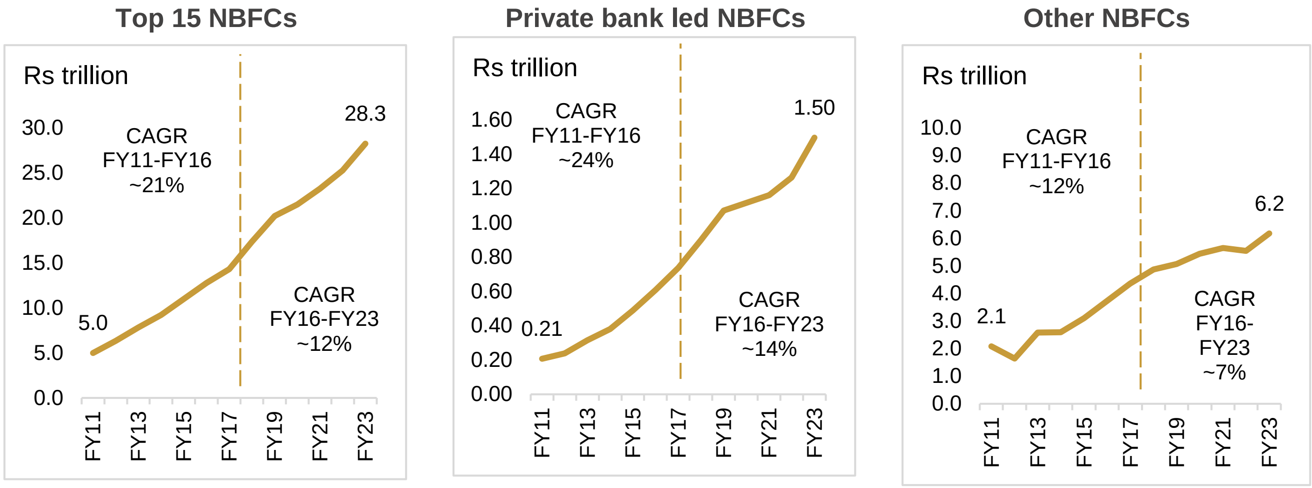
Note: The private bank led NBFCs are Axis Finance, Fedbank Financial Services, HDB Financial Services, ICICI Home Finance and Kotak Mahindra Prime; Top 15 NBFCs include are selected on the basis of consolidated AUM as of fiscal 2023; DHFL is excluded from top 15 NBFCs and other NBFCs;

Source: Company reports, CRISIL MI&A

Significant headroom for growth for NBFCs with access to funding at competitive costs

The developments over the last 4 years since the IL&FS crisis has clearly brought out the importance of continued access to funding at competitive costs for NBFCs. The key determinants of funding access in the current milieu are size, track record, credit rating and parentage as well as ability to raise equity funding to control leverage. CRISIL MI&A's analysis of trends over the past decade indicate that NBFCs promoted by private banks and large NBFCs (the top 15 NBFCs by book size as of March 2023) have been able to consistently grow across market cycles. Cumulatively, these NBFCs accounted for approximately 83% of the NBFC loan book as of March 2023.

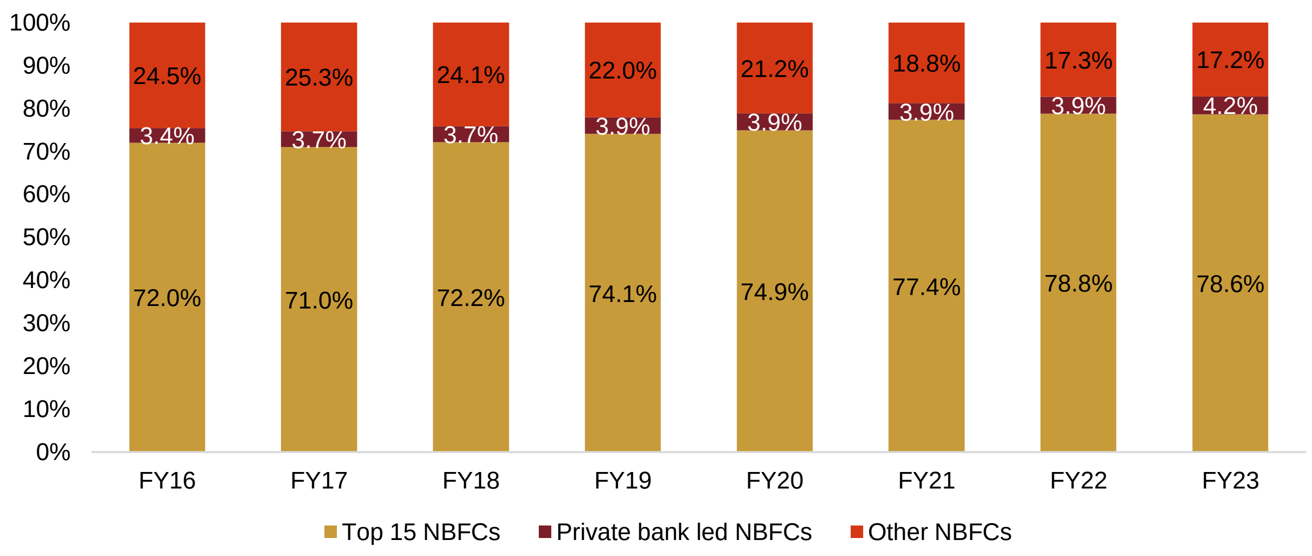
AUM of Private bank led NBFCs have grown at the fastest pace in the last 12 years



Note: The private bank led NBFCs are Axis Finance, Fedbank Financial Services, HDB Financial Services, ICICI Home Finance and Kotak Mahindra Prime; Top 15 NBFCs[8] include are selected on the basis of consolidated AUM as of fiscal 2023; DHFL is excluded from the analysis

Source: Company reports, CRISIL MI&A

Share of top 15 NBFCs and private bank led NBFCs has increased over the years



Note: Private Bank led NBFCs include – Axis Finance, Fedbank Financial Services, HDB Financial Services, ICICI Home Finance and Kotak Mahindra Prime; Top 15 NBFCs include are selected on the basis of consolidated AUM as of fiscal 2023; DHFL is excluded from the analysis; Source: Company reports, CRISIL MI&A

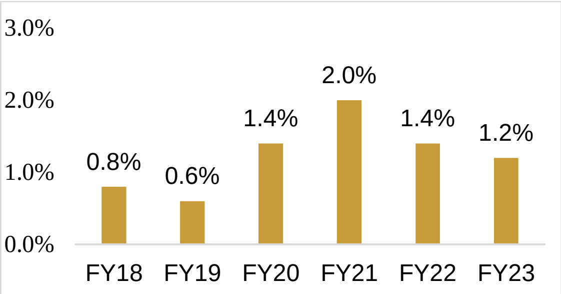
Credit cost further declines, and profitability improved in Fiscal 2023 despite increase in borrowing costs

In Fiscal 2023, credit cost further declined on account of gradual recovery across sectors with the waning impact of COVID-19 pandemic and improving collection efficiency aiding it. Despite increase in borrowing costs, the overall

[8] *Top 15 NBFCs - HDFC Limited, REC Limited, PFC Limited, LIC Housing Finance, Bajaj Finance, Shriram Transport Finance, L&T Finance, Tata Capital, HUDCO Limited, Mahindra and Mahindra Finance, Cholamandalam Investment and Finance, Indiabulls Housing Finance, PNB Housing Finance, Muthoot Finance and Aditya Birla Finance*

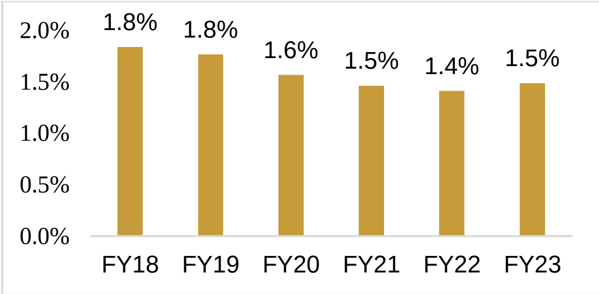
profitability of NBFCs improved in Fiscal 2023, primarily on account of lower credit costs due to contingency provisioning buffers created over the course of the previous two Fiscals.

Reduction in credit costs for NBFCs in Fiscal 2023



Note: E: Estimated; P: Projected; Source: CRISIL MI&A

Profitability (RoA) improved on account of decline in credit costs in Fiscal 2023



Note: E = Estimated; P: Projected; Source: CRISIL MI&A

Asset quality improved on account of efficiency in collection process and improvement in economic activity in Fiscal 2023

Asset quality for NBFCs is influenced by various factors such as economic cycle, target customer segment, geographical exposure, and local events. Within the NBFC universe itself, it is observed that various asset classes tend to exhibit heterogeneous behaviour. For example, the asset quality in small business loans and personal loans tends to be highly correlated with the macroeconomic environment. On the other hand, microfinance loans have shown lower historic correlation with macroeconomic cycles. This is because asset quality is more influenced by local factors, events that have wide ranging repercussions such as demonetisation and COVID-19 and relative leverage levels amongst borrowers.

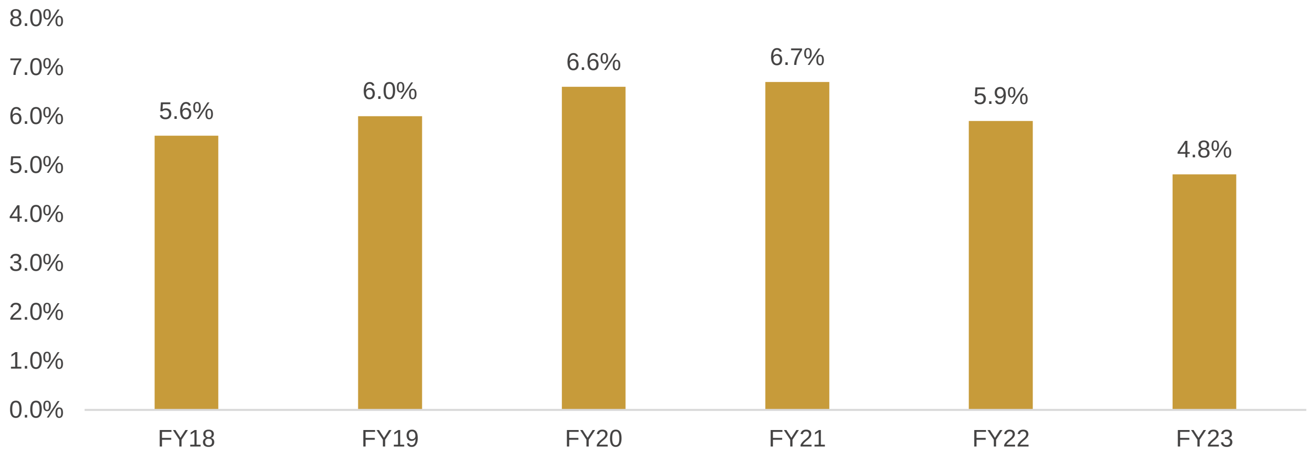
Prior to Fiscal 2018, smaller NBFCs were aggressively expanding in terms of both market penetration and lending across asset classes, which led to rising asset quality concerns. The proportion of standard assets declined, as slippages to sub-standard category increased. After the NBFC crisis in Fiscal 2019, smaller NBFCs slowed down their lending activity and focused on improving their asset quality and shifting to retail segments that are less risky. In Fiscal 2020, doubtful assets for NBFCs registered a marginal uptick due to funding challenges and slower credit growth. However, efforts were made by NBFCs to clean up their balance sheets, as reflected in their write off and recovery ratios, which caused the NNPA to remain stable, and the provision coverage ratio ("**PCR**") to improve.

In Fiscal 2021, proportion of doubtful and loss assets increased, largely driven by infrastructure and wholesale finance. In addition to funding challenges faced by the sector along-with slower credit growth, COVID-19 escalated asset quality deterioration further owing to restricted movement, which affected collections. Moratorium and restructuring schemes announced by the Government of India came as an interim relief for the sector and delayed the asset quality concerns for some time. However, with the NPA standstill provision lifted in August 2020, gross NPAs ("**GNPAs**") in segments such as auto, microfinance and MSME spiked as of March 2021.

In addition, the second wave of COVID-19 adversely affected the fragile recovery witnessed in the fourth quarter of Fiscal 2021 and affected collection efficiencies across asset classes in the first quarter of Fiscal 2022. However, the impact was not as severe as in the first wave, and players across segments reported improvement in GNPAs from the second quarter.

In November 2021, RBI gave a clarification to the "Prudential norms on Income Recognition, Asset classification and Provisioning pertaining to Advances", which requires the NBFCs to recognise NPAs on a daily due basis as part of their day-end process which is expected to lead to higher GNPA. Typically, the NBFCs ramp up their collection activity between due-date and month-end, leading to lower dues by end of month. This flexibility is expected to no longer be available to the NBFCs which could cause some proportion of loans in the 60–90-day period category to slip into over 90 days period category. In addition to the end of the day recognition, RBI has also clarified that upgradation of an account from NPA to standard category can only be done after all overdues are cleared (principal + interest), resulting in a borrower slipping into the NPA category to remain in the same category for longer time compared to the past. Hence, NBFC GNPAs increased in third quarter of Fiscal 2022 due to adherence to the said RBI clarifications. But with NBFCs bolstering their collection efforts and processes, and improvement in economic activity, CRISIL estimates GNPAs for NBFCs to have reduced significantly at the end of Fiscal 2022.

NBFCs' GNPA ratio improved significantly at the end of Fiscal 2023



Source: RBI, CRISIL MI&A

Asset quality metrics improved in Fiscal 2023 for two reasons. First is RBI's follow-up circular dated February 15, 2022, deferring the implementation of the NPA upgradation norm till September 30, 2022. This provides a reasonable transition time for NBFCs to recalibrate processes, revamp their collection infrastructure and teams, and persuade borrowers to align with the new dispensation. Second is the expected improvement in macro-economic activity, which is expected to act as a tailwind. The behaviour of loans restructured post COVID-19 is expected to, however, need to be closely watched, in light of cost push being felt by industries across the board.

Co-lending model to enhance business opportunities for NBFCs

RBI, in November 2020, issued co-lending norms that enable banks and NBFCs to collaborate with each other for priority sector lending ("**PSL**"). All scheduled commercial banks (excluding Regional Rural Banks and Small Finance Banks) are allowed to co-lend with all registered NBFCs (including HFCs) for the creation of priority sector assets under CLM based on a prior agreement between both the parties. Earlier, in September 2018, RBI had allowed all SCBs to co-originate loans with only non-deposit taking systemically important NBFCs ("**NBFC-ND-SI**") for fulfilling their mandatory PSL requirements. As per RBI notification, the guidelines are aimed at providing greater operational flexibility to lending institutions and improving the credit flow to unserved and underserved sector of the economy and make funds available at affordable cost, considering lower cost of funds from banks and greater reach of NBFCs.

Some of the key highlights of co-lending norms are:

- The co-lending banks are expected to take their share of the individual loans on a back-to-back basis in their books. However, NBFCs shall be required to retain a minimum of 20% share of the individual loans on their books
- The banks and NBFCs shall formulate Board approved policies for entering into CLM and place the approved

policies on their websites

- The Master Agreement may provide for the banks to either mandatorily take their share of the individual loans originated by the NBFCs in their books as per the terms of the agreement, or to retain the discretion to reject certain loans after their due diligence prior to taking in their books
- The CLM shall not be applicable to foreign banks with less than 20 branches

While co-lending arrangements have been in place amongst various lenders for the last few years now, this is the first time RBI has put in place a framework for the same, clearly outlining the responsibilities and requirements from both the partners. The emphasis on the CLM by RBI indicates that the regulator is looking at leveraging the reach and capability that NBFCs have in servicing underserved segments. While RBI introduced the co-origination or co-lending system in response to the liquidity crisis faced by NBFCs in order to enhance the credit flow to unserved and underserved segments. Banks have already had various models available with them in order to meet their PSL targets like:

- ***Purchase of priority* sector *lending certificates ("PSLCs"):*** PSLCs are issued by banks that have surpassed their PSL targets. As per the RBI guidelines, banks can issue four types of PSLCs – agriculture, small and marginal farmer, micro enterprise and general.
- ***Investing in securitised pools:*** Securitisation involves investing in instruments that provide access to cash flows against a pool of assets such as mortgage or vehicle loans.
- ***Leveraging Business correspondents ("BCs"):*** BCs are agents engaged by banks for providing banking services on their behalf. BCs offer a variety of services such as sourcing, distribution, collection and recovery.

Various models available with banks to engage with NBFCs to meet the PSL targets

PSLCs	Securitisation	BCs
No operational and underwriting risks are involved, as the underlying asset, along with the risks and rewards, is held by the issuer	It requires an understanding of the market and the instrument, as there is a transfer of underlying receivables, including risks and rewards	It enables banks to take exposure across multiple regions and explore newer geographies
No mark-to-market ("**MTM**") and capital requirement	MTM and capital requirement	No MTM, but requires capital
No impact on the banks' book sizes	Helps banks increase their book sizes	Helps banks increase their book sizes
Has a life cycle only for a particular financial year	It involves large ticket size and have a longer life cycle of around 3-4 years	Involves tie ups with BCs like NBFCs to manage business for longer run
Involves no credit risk	Credit enhancement is available in case of Pass-through certificates ("**PTCs**")	Involves a hurdle rate or initial loss-sharing
Yields are not relevant	Yields are relatively lower, as originators bargain with various banks for better pricing	Yields are comparatively higher
A clear classification of assets for buyers	Risk of RBI questioning the classification of assets	Risk of RBI questioning the classification of assets
Availability of certificates can be an issue	Application of GST (18%) could be a dampener, as it increases the cost, thus impacting volume	Difficult for both parties to exit, as it can impact the overall portfolio

Source: CRISIL MI&A

Future co-lending market opportunity

Currently, the co-origination model is largely being used for small ticket size products like MSME loans, consumer finance, gold loans and vehicle loans in the industry. However, with RBI putting in place a framework for co-lending and several NBFCs facing challenges in accessing capital, players are now also focusing on longer tenure and relatively higher ticket size loans like housing finance and loan against property.

The largest public sector bank ("**PSB**"), for example, has already partnered with NBFCs and finTechs for doing co-lending in home loans segment. The bank is also in the process of digitising the entire value chain where the loan leads would flow directly from an NBFC or finTech platform to the bank with very little human intervention. Bank of Baroda, in January 2020, entered into a strategic co-lending agreement with JM Financial Home Loans Limited for offering retail loans to home buyers. In February 2020, online lending platform Lendingkart entered into partnership with Northern Arc Capital for MSME segment. PNB Housing Finance in March 2021 entered into co-lending model with Yes Bank to offer customised retail loans to home buyers.

Also, there are plethora of new-age finTech companies who are using innovative algo-based originations and aggressively using the internet for originations. These finTechs either build books on their own balance sheet or pass a substantial part of their book with their partner banks or NBFCs. Strong demand and rapid innovations in technology and business integration has enabled finTechs and smaller NBFCs to partner with credible partners and engage with them in co-lending model.

Some of the key growth drivers for co-lending market are:

- **Operational leverage –** Co-lending model is operationally convenient for both partners as it enables partners to offer multiple products to customers which are not otherwise present in their current portfolio, thus providing diversification to the portfolio without actually having a separate operational setup for each product. Co-lending thus enhances operating leverage for financiers as it enables them to increase lending with existing infrastructure and resources.
- **Capital optimisation** – Entering into co-lending model allows smaller NBFCs to cater to a larger customer base with lesser capital by leveraging the larger balance sheet of their partners. Such NBFCs can leverage their origination skills and expertise in assessing specific customer segments while at the same time conserving their capital.

Risk sharing and risk adjusted returns – Co-lending partnership enables banks and NBFCs/ HFCs to enter into an arrangement where the risks and rewards are shared by all parties throughout the lifecycle of the loan, as per a pre-decided ratio. The NBFCs use various innovative mechanisms for credit risk assessment like usage of non-traditional sources of data, understanding individual's motive to avail finance and evaluating cash flow patterns of borrowers. These strengths can be leveraged by their partners to optimise capital usage and improve their risk adjusted returns.

Digitisation trends

Over the last few years, NBFCs have been increasingly adopting business and operational models, powered by technologies, that seamlessly facilitate execution of tailored products and services. Investing in new technologies and strategic partnerships with incumbent financial institutions and finTechs has allowed NBFCs to lower their costs while enhancing their customer base and servicing existing customers. According to the Working Group Report on Digital Lending issued by RBI, the share of loans disbursed in terms of value by NBFCs through digital channels has increased from 6.3% in Fiscal 2017 to 30.3% in Fiscal 2020 which shows the increasing diffusion and adoption of digital technologies in the credit ecosystem. The major products disbursed digitally by NBFCs are personal loans followed by loans under ‘Other’ category which mostly comprises of consumer finance loans.

Traditionally, high cost of reaching out and delivering services to un-served and underserved regions and credit risk in catering to the lower-income segment within this spectrum has constrained the availability of credit from traditional lenders. Thus, players, with their technology-led solutions, have disrupted the process of lending to these segments, particularly the client acquisition and on-boarding and credit assessment process. For example, lenders are increasingly using artificial intelligence and machine learning models in credit underwriting as also prioritising collections.

Enabling measures by RBI and the Government of India such as putting in place of IndiaStack, allowing Aadhaar based eKYC and the launch of UPI that has transformed digital payments have helped players adopt technology in a seamless manner and provide services in a cost-efficient manner. By keeping the customer at the centre and also having appropriate rules and regulations, the Government of India has also supported growth of various retail products.

GOLD LOANS

Overview of gold loan market in India

Gold loans are typically small ticket, short duration, convenient and instant credit. While the industry has been around for several decades with local financiers and moneylenders extending finance against gold, especially in semi-urban and rural areas, the industry has witnessed a spurt in organized financiers offering gold loans since 2008 with the specialized gold loan NBFCs expanding their branch network and making available loans in a very easy and consumer friendly manner by putting in place strong systems and processes. Though moneylenders and pawn brokers understand the psyche of local borrowers and offer immediate liquidity without any documentation formalities, customers are left vulnerable to exploitation, due to the absence of regulatory oversight. Such players also give lower LTV compared with organized ones while charging exorbitant interest.

As banks and NBFCs aggressively moved in to seize this vast untapped market, they cornered a significant market share from unorganized lenders, growing at CAGR of 76% between Fiscals 2009 and 2012. Sustained increase in gold price till 2012 also supported the gold loan business boom in India. In such a scenario, customers would be offered higher and higher loan amounts on their gold, while lenders would benefit by price increases acting as a natural hedge, in the event of default.

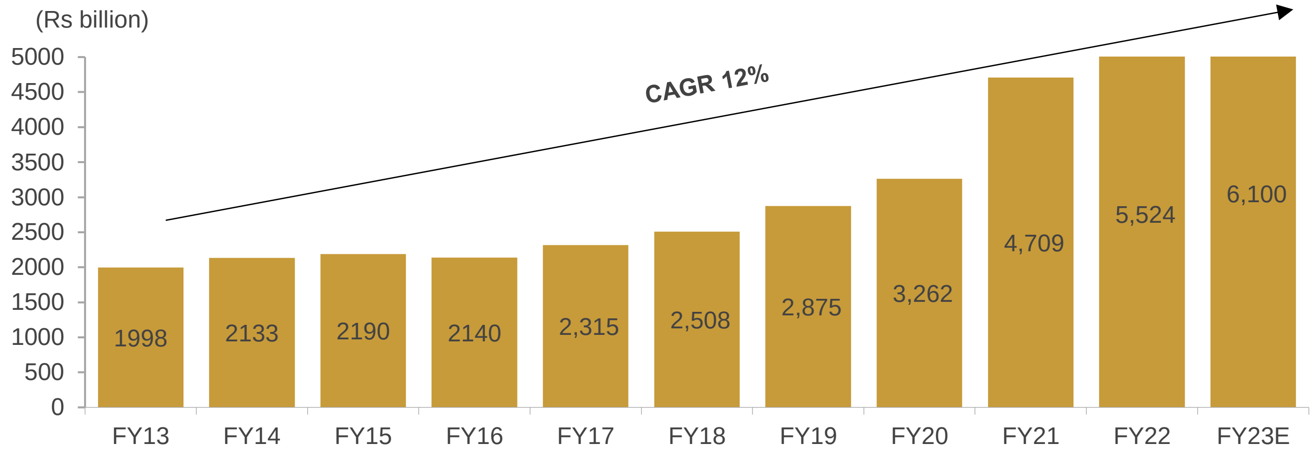
The high growth in the NBFCs' gold loan offtake because of high LTVs, the speed at which the NBFCs opened branches, the decline in the capital adequacy ratios of NBFCs offering gold loans and increase in gold prices alarmed RBI, leading to a slew of regulatory steps being taken. The measures initiated included capping the loam-to-value of gold loans at 60% (which was subsequently increased to 75% in January 2014), prohibiting grant of loans against bullion and gold coins, standardization of the value of gold while calculating the loan to value ratio and streamlining the process for auctioning gold. Furthermore, NBFCs were directed to disburse gold loans of greater than ₹ 1,00,000 ticket size through cheques only. RBI also directed that if the loans extended by a NBFC comprise 50% or more of its financial assets, it shall maintain a minimum Tier-I capital of 12% by April 01, 2014. These measures derailed the growth of NBFCs gold loan offtake for a brief period of time and they lost considerable ground to banks.

The industry has however bounced back subsequently. With regulations in respect of key aspects such as loan to value for NBFCs now being on par with banks, players compete on parameters such as interest rates, customer service, turnaround time, convenience, and trust developed.

Gold loans market has witnessed consistent growth over the last decade

As can be witnessed from the chart below, the industry has witnessed consistent growth over the last decade, even as gold prices have seen periodic fluctuations. As of March 2023, CRISIL MI&A estimates the outstanding value of loans given out by organised financiers' – banks and NBFCs – to be ₹ 6.1 trillion, with NBFCs accounting for one-quarter of the market.

Gold loans have grown at a strong growth rate over the last decade



Note: Includes agriculture lending by banks with gold as collateral

Source: CRISIL MI&A

Gold loans AUM is expected to grow at 10-12% CAGR between Fiscals 2023 and 2025

In Fiscal 2020, gold loan industry (including Banks and NBFCs) AUM grew approximately 13% y-o-y to reach ₹ 3.26 trillion on account of increased focus of players on diversifying their regional presence, strong growth in non-southern regions and rise in gold prices by approximately 19% in Fiscal 2020 along with the convenience provided by the short turnaround time in disbursing gold loans.

In Fiscal 2021, the demand for gold loan finance witnessed a massive spurt in AUM from ₹ 3.26 trillion to ₹ 4.7 trillion, as India's economy coped with the devastating effect of the global COVID-19 pandemic supported by players continued focus to acquire unorganised gold loan market by means of awareness and diversifying their regional presence with the help of branch as well as digital channels. Many consumers, who had gold stock and ornaments lying with them, considered gold loans as an option to meet their credit requirements during this period. The demand for gold loans was also supported by a consistent surge in gold price, liquidity crunch in the immediate aftermath of the COVID-19 pandemic and lenders' hesitancy to give unsecured loans due to risk aversion. RBI also revisited its guidelines for banks' lending gold loans by increasing the maximum LTV allowed to 90% from existing 75% for non-agricultural gold loans extended during August 2020 to March 2021 to help stressed borrowers to unlock more value. The growth was also supported by players continued focus to wean away consumers from the unorganised gold loan market by means of awareness and diversifying their regional presence with the help of branch as well as digital channels.

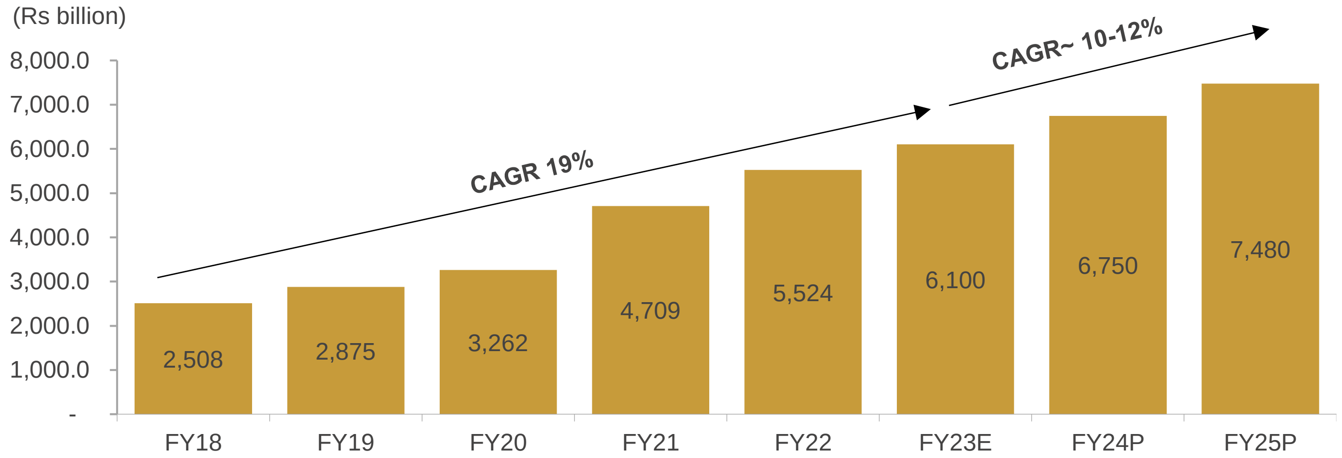
In Fiscal 2022 as well, the gold loan market continued to witness strong growth, with industry AUM increasing by 17% on-year to touch ₹ 5.52 trillion as of March 2022. Increase in AUM can be attributed to factors such as high gold prices, strong demand and increased promotion by financiers to acquire unorganised gold loan market by means of awareness and diversifying their regional presence with the help of branch as well as digital channels. During fiscals 2020-21, when growth for diversified NBFCs witnessed sharp decline, gold loan NBFCs witnessed 11% y-o-y growth. Financiers also were very aggressive in tapping new customers during the year with some of them running campaigns offering gold loans at a lower interest rate for short tenures. For instance, Manappuram Finance introduced low interest rate, for retail customers with a tenure of 3 months. In Fiscal 2023, the growth for gold loans NBFCs is estimated to have moderated owing to increased competition from banks and lower demand from the target audience.

Online gold loans and doorstep model to aid in market expansion

The industry, which has traditionally grown through expansion of branch network across the nook and corner of India, has witnessed the emergence of branchless finTechs and doorstep model gold loans over the last 3-4 years. These players offer doorstep pickup and disbursement of gold loans directly to the account of the customer. Under this model, when a user requests for a loan, the loan agent visits the customer with a gold appraisal kit and necessary tools to measure the purity of the gold. After proper due diligence and a credit check, the loan is processed digitally and the amount is transferred instantly to the customer. After the amount is transferred, the gold is packed in a tamper proof packets and transported to the nearest branch in a GPS enabled secured box, which is tracked on a real time basis until the collateral is deposited in the lender's vault. This new doorstep model gold financing has addressed some of the key inhibitors in wider acceptance of gold loans such as risk involved in carrying gold to the branch, the social stigma attached to mortgaging gold for availing loans and increasing branch catchment area.

Going forward, CRISIL MI&A believes that the scope to capture share from unorganised gold loan financiers', initiatives to increase awareness and increasing comfort of customers with gold loans due to the convenience are expected to help the industry grow moderately along with geographic diversification to markets beyond the Southern part of India. Demand for gold loans from micro enterprises and individuals to fund working capital and personal requirements is expected to increase owing to pickup in economic activity. In addition, with demand reviving and market expansion through doorstep gold loans model, CRISIL MI&A expects AUM to touch close to ₹ 7,480 billion by March 2025, translating into a 10-12% CAGR between Fiscals 2023 and 2025.

Growth in gold loan AUMs of organized lenders



Note: P: Projected, includes agriculture lending by banks with gold as collateral

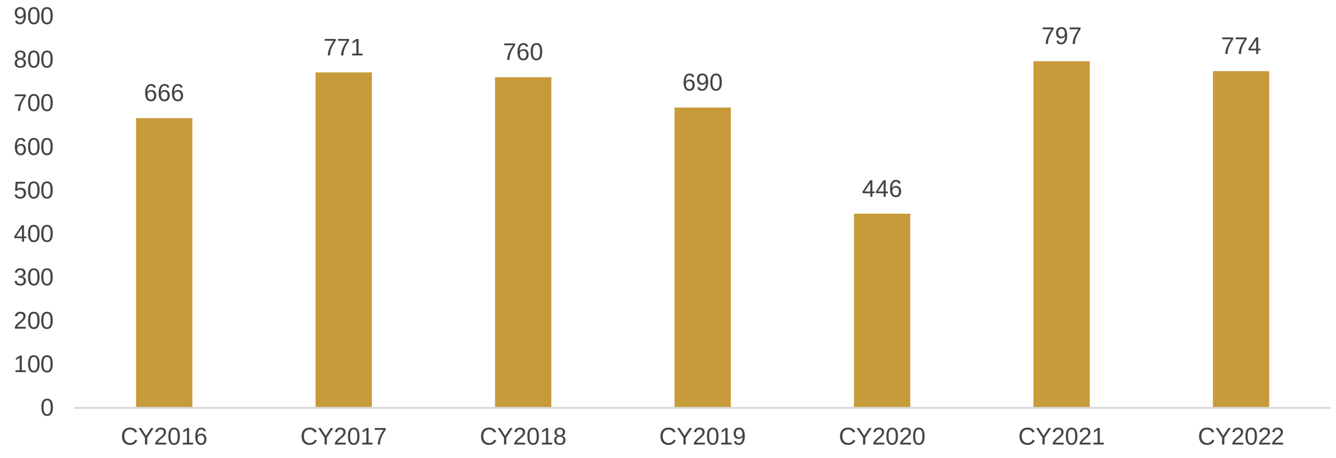
Source: CRISIL MI&A

Gold demand to increase in calendar year 2023

In calendar year 2020 and first half of calendar year 2021, consumer demand for gold plunged by 35% on year because of curtailed discretionary spending following the onset of COVID-19 and rising prices of gold. However, gold demand bounced back strongly in second half of calendar year 2021, causing it to reach 797 tonnes at end of calendar year 2021. The higher growth was on account of a low base, higher discretionary spending, festive season and waning impact of COVID-19 pandemic. Lower import duty on gold and reduced gold prices is further expected to aid demand for gold in India. Gold imports to India also moves in line with consumer demand, as over 95% of the demand in India is met through imports.

In the first quarter calendar year 2022, the gold demand witnessed a slump owing to lack of auspicious and wedding days coupled with a sharp rise in gold prices in late February or early March which dented consumer appetite for jewellery. In addition, as of calendar year 2022, gold demand stood at 774.1 tonnes, decreasing by 3% year on year. The demand bounced back in the fourth quarter of calendar year 2022 on account of festival purchases and wedding season buying. In addition, retail investors increased focus on gold's haven attributes amid global volatility is also expected to aid demand for gold in calendar year 2023. Going forward, consumer demand for gold in India is expected to remain resilient throughout calendar year 2023. However, demand could face some headwinds arising out of global heighted volatility and broad-based inflation, which could squeeze disposable income.

Trend in yearly demand for gold in India (in tonnes)



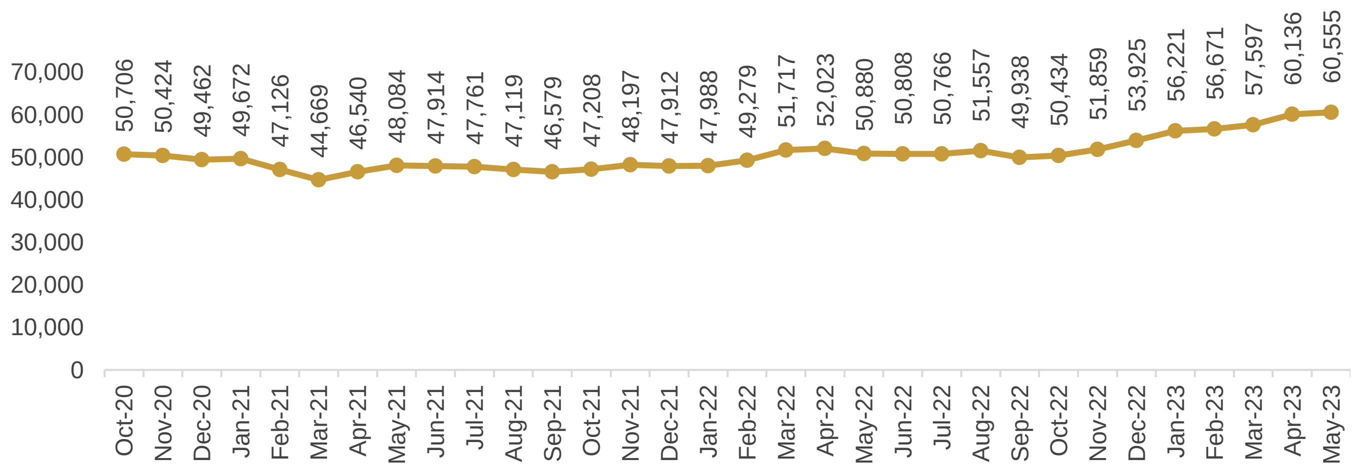
Note: Mentioned years are Calendar Years

Source: World Gold Council, CRISIL MI&A

Higher geopolitical risks and inflationary environment to support gold prices in Fiscal 2023

Domestic gold prices increased by 19% on year to reach ₹ 60,555 per 10 grams in May 2023 from ₹ 50,880 per 10 grams in May 2022. CRISIL MI&A expects domestic gold prices to rise further in Fiscal 2024 on account of higher international prices as well as rupee depreciation during the year. Considering all these factors, CRISIL MI&A domestic gold prices is expected to rise 3-5% in Fiscal 2024.

Trend in gold prices (in ₹ per 10 grams)



Source: MCX, CRISIL MI&A

Growth Drivers

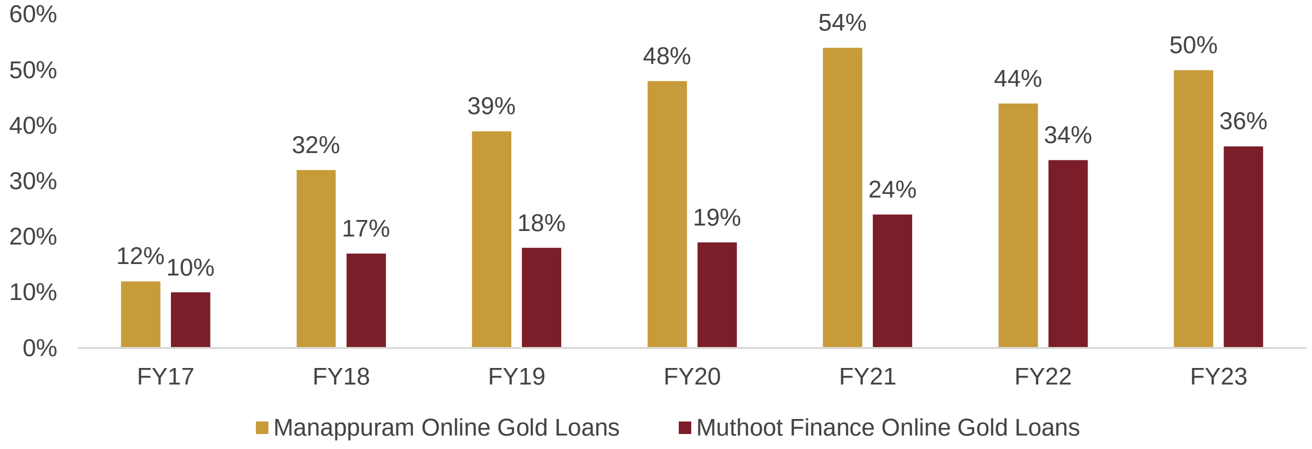
Due to the inherent benefits of gold loans and prevailing economic scenario, the sector is witnessing a strong demand and disbursal growth. Small businesses and individuals who are facing cash flow problems are leveraging gold to meet their liquidity demands. Going forward, CRISIL MI&A believes that the organized gold loan market is expected to be driven by increasing gold loan penetration, rising share of organized financiers and market expansion through geographical diversification.

- Organised gold loan penetration in India (computed as gold stock with organized financiers divided by total gold stock in India) is estimated to be approximately 7% as of March 2023, which indicates that organised gold loan market has significant headroom for growth. Going forward, gold loan penetration is expected to increase further on geographical diversification, rising branch network, and households increasingly looking to monetise their gold holdings for personal and business needs. In addition, increase in gold prices and expectations of micro-enterprises using gold loans to fund working capital requirements is expected to also aid growth of gold financing.
- According to CRISIL MI&A, due to increasing awareness about benefits of availing gold loans from organised segment, the share of organised gold loan financiers has increased from 56-58% in Fiscal 2017 to approximately 61-63% (in terms of value) in Fiscal 2023. Going forward, CRISIL MI&A expects the trend to continue, and the share of organised loan market is expected to further improve from approximately 61% to approximately 63%.
- India has world's largest private gold holdings which is estimated to almost 3 times US official gold reserves and around twice the total gold held in China. According to World Gold Council Report (A Central Banker's Guide to Gold as a Reserve Asset), gold reserves with Indian households account for approximately 75% of the total gold reserves of 35,568 tonnes held by Central Banks across the world as of March 2022. The massive gold reserve can be potentially unlocked by the owners to avail funds at a short notice at the time of need.

Online gold loans and doorstep model to help in market expansion

Digital gold loans products offer the feature of loan sanction within few hours through the online process. These loans can be accessed through mobile applications, online platform, prepaid card etc. Know your customer ("**KYC**"), registration and disbursements are all possible through online platform. For example, entities such as IIFL Finance, Manappuram Finance and Muthoot Finance are constantly making investments in digital and technological capabilities to adapt to constantly changing world. For example, IIFL Finance launched digital gold loans for top up and online renewal of gold loans. Similar shift towards digital modes is witnessed for Muthoot Finance, which saw its share of online gold loans increase from 24% in Fiscal 21 to 36% in Fiscal 2023. At end of Fiscal 2023, the share of online gold loans further increased to 50% for Manappuram Finance.

Share of online gold loans continue to see traction in Fiscal 23



Source: Company Reports, CRISIL MI&A

New age finTech players such as Rupeek along with players like Fedbank Financial, Muthoot Finance, IIFL and Manappuram Finance also offer gold loans at customer's doorstep wherein the customer can get a gold loan sitting at home. The complete the loan underwriting-to-disbursal process takes place within 30 minutes, just as it happens in case of a loan availed through a NBFC branch. In case of doorstep model offering, verification of the gold ornaments as well as gold collection is done at the customer's residence. These are managed through a central application that is simultaneously accessed by all branches for each and every transaction.

Due to these advantages as well as increasing focus by players in both doorstep delivery and online gold loans, the addressable market for gold loans is expected to expand.

Doorstep gold loans operating model

	Traditional Models	Door step model
Loan Application	Branch walk in	Phone call, Mobile or app based request
Gold Valuation	Valuation by employee/loan officer at branch	Doorstep valuation by loan officer
Loan Processing	Manual entry of customer data and Paper based KYC	TAB based data entry and KYC
Gold Storage	Vaults in Branch	Vaults in branch, Barcodes and RFID for tracking and retrieval
Loan Disbursement	Disbursal in 10-20 minutes	Disbursal in 10-20 minutes after completion of entire process at doorstep
Collection	Cash or Cheque at branch, Electronic Clearing System ("**ECS**") / National Automatic Clearing House ("**NACH**"), Direct transfer from customer account	Cash collection at doorstep, ECS/NACH, Direct Transfer

Source: CRISIL MI&A

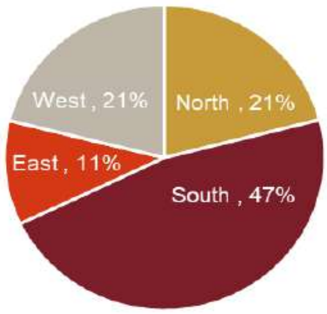
Geographic diversification and improvement in operational efficiency of business to drive growth in the coming years

In India, the southern zone commands major share of demand of gold loans at 47% as of Fiscal 2023. This can be explained by the culture found in Southern India compared to the rest of India. It is followed by the North region at 21%. The western zone and the eastern zone lag behind in gold loan demand with their share standing at 21% and

11% respectively. People in Southern India have lower taboo associated with borrowing against gold and are more ready to pledge gold. In addition, majority of the NBFCs and banks (that have strong presence in gold loans) have deep rooted distribution network in the Southern India.

In Fiscal 2017, Southern India accounted for 61% of the total NBFC gold loans portfolio in India. However, changing consumer perceptions about gold loans, driven by increasing awareness, as well as rising funding requirements and increase in penetration of gold loans in the non-southern regions has led to a change in the regional mix of the portfolio. Going forward, incremental additions of branches by gold loan NBFCs in North and West region where the existing number of branches are relatively lower, presents a good geographical expansion opportunity in these regions. Hence, CRISIL MI&A expects other regions to witness stronger growth momentum in gold loans as compared to the Southern region.

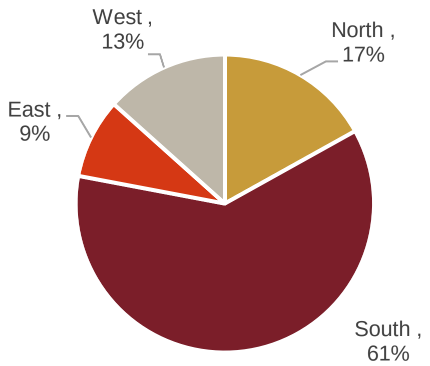
South account for major share of gold loans NBFCs (Fiscal 2023)



Note: Aggregate includes region-wise AUM split of Muthoot Finance, Manappuram Finance & IIFL Finance which constitute ~72% of the overall NBFC Gold Loan market as of FY23.

Source: CRISIL MI&A

Branch distribution of gold loans NBFCs (Fiscal 2023)



Note: Aggregate includes region-wise branch split of Muthoot Finance and Manappuram Finance which constitute 58% of overall NBFC gold loans market as of FY23.

Source: CRISIL MI&A

South account for major share of gold loans NBFCs (Fiscal 2023) ‘

Since there is major demand from Southern region, Southern India has a higher share in branches in India. Inspite of introducing online gold loans, these branches serve as an important touchpoint for the customers of these NBFCs.

Gold has been known to act as a hedge against inflation and is also attractive for financiers

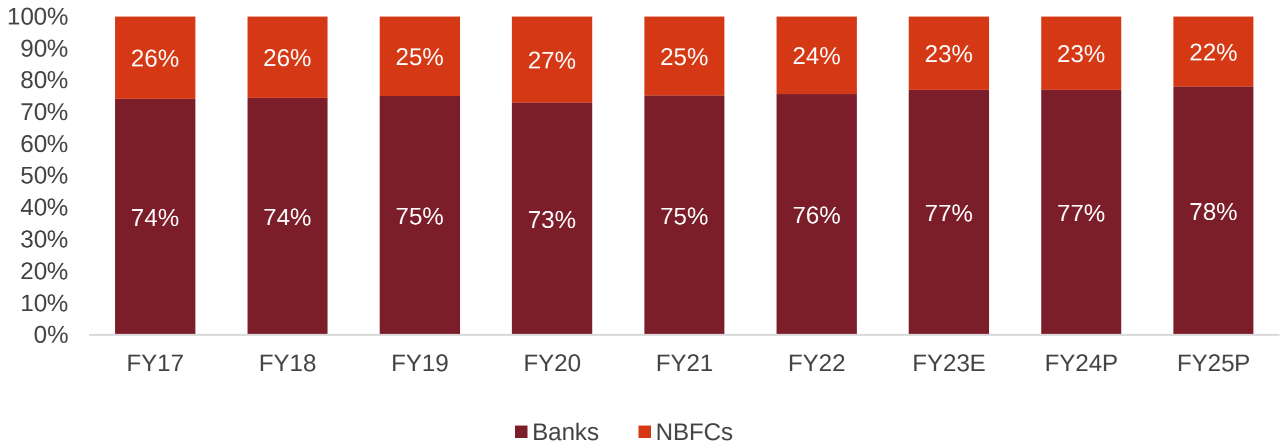
Over the years, gold prices have shown a consistent increase, and have, in most part, increased at a pace higher than the annual rate of inflation. For instance, during Fiscal 2011 to Fiscal 2016, gold prices increased at a CAGR of approximately 7%, as against an approximately 8% inflation observed in this period. During the subsequent five-year period between Fiscals 2016 and 2022, the gold price and inflation increased at a CAGR of approximately 12% and 5%, respectively.

The hedge against inflation provided by gold has attracted consumers to gold over the years. From a financier perspective, the yield on gold loans and minimal risk of credit losses due to security provided in the form of the gold being pledged and the additional cushion due to the loan-to-value (average of 65% for NBFCs) makes gold loans a profitable product.

Competitive landscape

In Fiscal 2021, banks have witnessed a faster growth in gold loans as compared to NBFCs on account of increasing LTV offered by banks (till March 2021), rising gold prices, demand from small businesses for cash and increasing focus of banks towards this asset class. A similar trend was evident in Fiscal 2022 as well. Banks' gold Loan AUM increased by around 20% and NBFCs AUM increased by 11% in Fiscal 2022. For instance, State Bank of India's ("**SBI**") personal gold loan book jumped by 465% on year from ₹ 37 billion in Fiscal 2020 to reach ₹ 210 billion at end of Fiscal 2021. It further increased by 9.9% in Fiscal 2022 to reach ₹ 230 billion. The overall gold loan portfolio of CSB Bank also increased by a 2-year CAGR of 31% from ₹ 38 billion in Fiscal 2020 to reach ₹ 65 billion at end of Fiscal 2022, leading to an increase in banks share in overall gold loans industry. In Fiscal 2023, the gold loan portfolio for banks continued to grow with SBI's personal gold loan book increasing to ₹ 287 billion as of March 31, 2023. For CSB, the gold loan portfolio increased to ₹ 97 billion at end of March 2023. However, it must be noted that banks' mix of gold loans is higher owing to agriculture gold loans, where gold loans are granted to farmers for purpose of crop production.

Banks to hold majority share in overall gold loans market

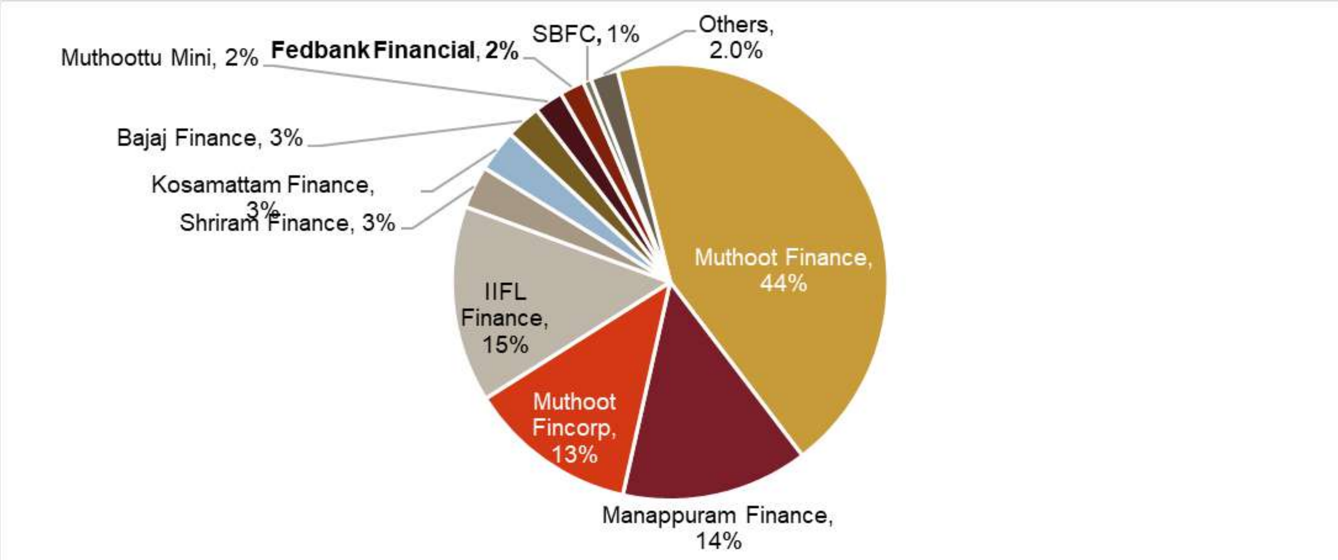


Note: E: Estimated, P: Projected, includes agriculture lending by banks with gold as collateral

Source: CRISIL MI&A

Within NBFCs, Muthoot Finance, Manappuram Finance and Muthoot Fincorp are the largest players, who together account for 70% of the gold loan portfolio of NBFCs as of Fiscal 2023. Other players in top 10 includes key players such as IIFL Finance, Shriram Finance, Kosamattam Finance, Bajaj Finance, Muthoottu Mini, Fedbank Financial, HDB Financial Services and SBFC Finance.

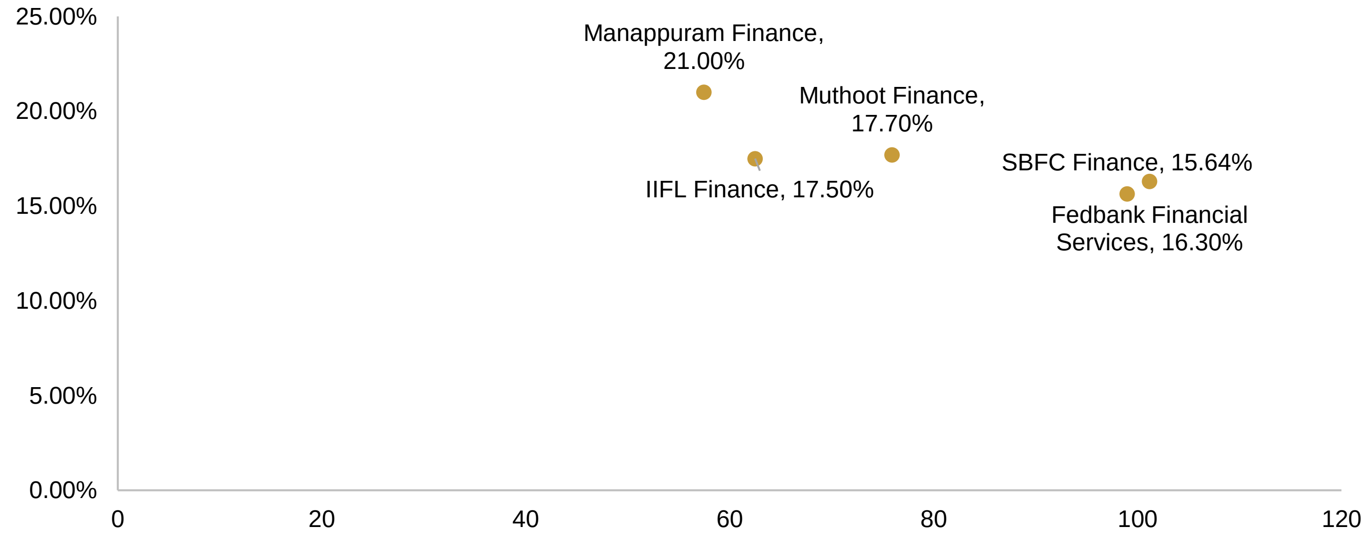
Top three gold financing NBFC account for approximately 70% share in overall NBFC gold loans book in Fiscal 2023



Source: Company Reports, CRISIL MI&A

The average ticket size for NBFCs in the gold loans business stands at ₹ 55,000-₹ 70,000 as of Fiscal 2023. There is considerable variation in the competitive positioning and target segment of various players, as reflected in the average ticket size of loans and yields offered. Among the gold loan NBFCs, players like Muthoot Finance and Manappuram Finance targets customer at the lower end of the economic strata with an average ticket size in the range of ₹ 55,000- ₹ 75,000 and yield in the range of 17-21%. IIFL Finance lends at an average ticket size of ₹ 63,000 with an average yield of close to 18%.

Comparison of various players based on yield on advances and average ticket size (Fiscal 2023)



Source: Company Reports, CRISIL MI&A

NBFCs compete on the basis of operating efficiency, turnaround time, local connect while managing risks

Despite banks having a competitive advantage of offering gold loans at lower cost, gold loan NBFCs have been trying to compete with banks through aggressive expansion of branch and increased focus on customer experience. NBFCs focus more single-mindedly on the gold loans business and have, accordingly, built their service offerings by investing significantly in manpower, systems, and processes as per the needs of the customer, some of which are listed below:

1. **Lower turnaround time and lesser documentation**: The gold loan borrower generally wants to procure the loan as quickly as possible and availability of well-trained and experienced employees in assessment and valuing gold helps NBFCs to disburse loans faster as compared to a bank.

2. **Wider reach and better local connect**: NBFCs have a geographically wider and deeper reach, especially in rural and semi-urban regions, where demand for gold loans is higher

3. **Risk management process**: Most NBFCs have put in place a comprehensive and robust risk management process taking into account their experiences over the years and the key risks in the process including steps taken to prevent fraud, store the gold safely, and recoup losses in case of a loan turning non-performing.

Comparison of Gold loan institutions on select business parameters

	Banks	Gold loan NBFCs	Unorganised moneylenders
Interest rate	9-18%	21-26%	25-45%
LTV	Up to 75% (Up to 90% in Fiscal 2021)	Up to 75%	More than 75%
Processing fee	Higher than NBFCs	No/minimal processing fees	None
Regulator	RBI	RBI	None
Documentation required	KYC Compliance	Minimal	Minimal
Product focus and customer service	Non-core product	Gold loan is core focus, excellent customer service	Gold loan is core focus
Mode of disbursements	Mainly cheque and direct transfer to account	Cash/ cheque and direct transfer to account	Mostly cash
Average turnaround time	30 minutes - 2 hours	10 - 20 minutes	10 - 20 minutes
Opening hours	Banking hours	Beyond banking hours	More flexible than banks in terms of working hours

Source: CRISIL MI&A

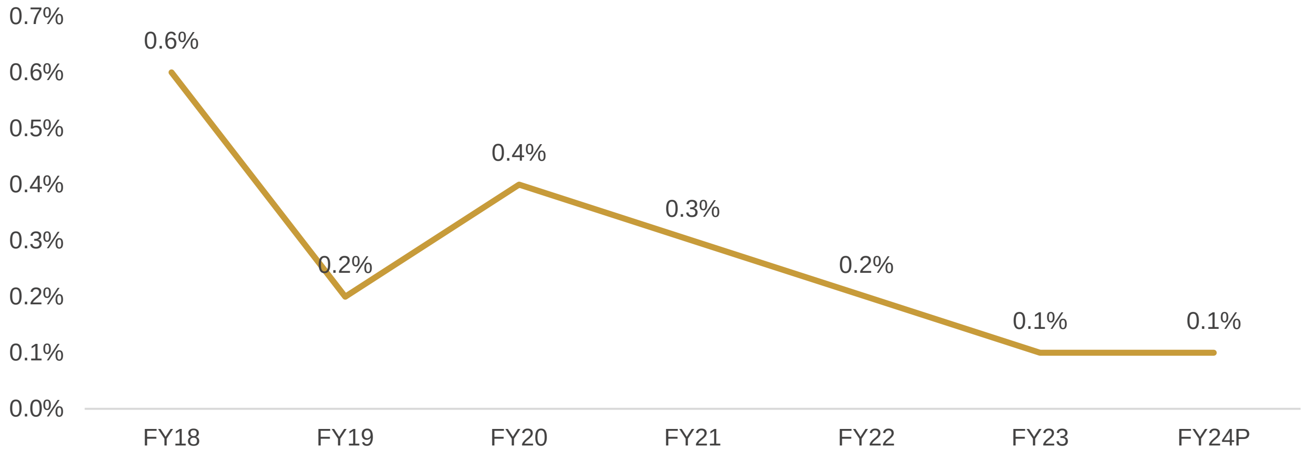
Asset Quality

Credit costs of gold loans low across market cycles; Gold Loan NBFCs NPA to remain restricted

Gold loans are a highly secured and liquid asset class that tends to generate superior returns with minimal credit losses over market cycles. NBFCs offering gold loans are better placed, on a relative basis compared to other retail asset classes, to withstand any asset quality pressures spawned by economic slowdowns or events such as the COVID-19 pandemic.

In addition, shorter tenure of loans shields the companies from any sharp volatility in gold prices. Loss given default for a gold finance company is also generally miniscule, as the loan is fully secured, and the collateral is highly liquid. In case of default, the gold gets auctioned, and the lender recovers its dues and returns the balance amount to the borrower. Maintaining LTV at reasonable levels provides a further cushion to financiers. Credit cost decreased in Fiscal 2023 on account of improvement in asset quality. In addition to improvement in asset quality, credit cost is estimated to have subdued in Fiscal 2023 due to excess provisions carried into Fiscal 2023 post the asset quality deterioration witnessed in Fiscal 2022. Additionally, higher gold prices have led to lower LGD for ECL calculations thereby leading to lower provision coverage and consequently lower credit costs.

Credit cost for gold loan NBFCs



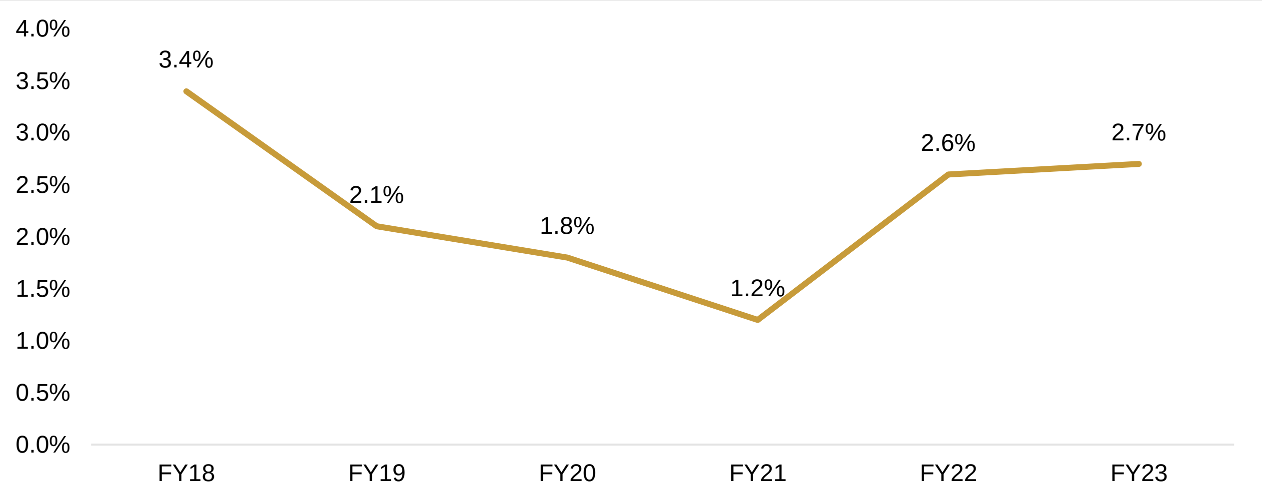
Source: CRISIL MI&A Estimates

In Fiscal 2018, gross NPA for gold financiers stood at 3.4% after RBI changed the NPA recognition norms for NBFCs. Since then, players have been continuously focusing on de-risking their business models from volatility in gold prices, by tightening their interest collections (regular interest collections versus bullet system in the past) leading to improvement in their asset quality in Fiscals 2019 and 2020.

Gross non-performing assets witnessed a decline in Fiscal 2021 due to improved collections. However higher disbursements in second half of the fiscal led by second and third waves of the COVID-19 pandemic resulted into higher GNPAs in Fiscal 2022. The asset quality for Manappuram Finance rose to 3.0% as of March 2022 from 1.9% as of March 2021. During the same period, GNPA for Muthoot Finance rose from 0.9% to 3.0%.

GNPA of gold loan NBFCs remained elevated in Fiscal 2023 and is expected to improve in Fiscal 2024 owing to better collection efficiency and recovery via auctions to some extent. However, going forward, volatility in gold prices could pose some challenges to the asset quality in an otherwise relatively safe segment.

Asset quality for gold loan financiers



Note: Aggregate includes data for Muthoot Finance, Manappuram Finance and IIFL which constitute approximately 72% of the overall NBFC Gold Loan market in fiscal 2023; Source: Company Reports, CRISIL MI&A Estimates

Comparative Assessment of NBFCs in Gold loans financing

In this section, CRISIL MI&A has undertaken a relative comparison of Fedbank Financial with the two largest NBFCs offering gold loans in India (Muthoot Finance and Manappuram Finance) based on the latest available data for Q1 Fiscal 2024.

Fedbank Financial has the fastest year on year growth among gold loan NBFCs in India as of Q1 Fiscal 2024, but smallest in terms of gold loan AUM

As of Q1 2024, Fedbank Financial witnessed the fastest year on year gold loan portfolio growth of 30% followed by Muthoot Finance (18%). However, the growth is on a lower base as compared to Muthoot Finance, which is the largest gold loan financier amongst the peers with 98% of its overall loan portfolio (₹ 676 billion) comprising of gold loans at end of Q1 Fiscal 2024.

Fedbank Financial is the 2nd most efficient gold loan NBFC amongst its peers

At the end of Q1 Fiscal 2024, Muthoot Finance was the most efficient gold loan financier, having the highest AUM per branch of ₹ 112.0 million followed by Fedbank Financial (₹ 71.5 million). As at end of Q1 fiscal 2024, Muthoot Finance and Fedbank Financial have high AUM per employee of Rs 23.8 million and ₹ 14.8 million respectively.

Operational parameters for key gold loan NBFCs (Q1 Fiscal 2024)

Players (Q1FY24)	Gold Loan AUM (in Rs Billion)	Y-o-Y growth	Branch	Employees	AUM per Branch (in Rs. Million)	AUM per Employee (in Rs. Million)	Share of Gold Loan in total AUM
Muthoot Finance	660	18%	5,897	27,701	112.0	23.8	98%
Manappuram Finance	206	1%	4,039*	45,000	51.0^	4.6	56%
Fedbank Financial Services	**31**	**30%**	**437***	**2,105***	**71.5^**	**14.8^**	**33%**

Note: Players are arranged in decreasing order of gold loans AUM; (*) Gold loan branches/employees; (^) AUM per gold loan branch/ employee,

Source: Company Reports, CRISIL MI&A

Fedbank Financial is the fastest growing gold loan NBFC in India among the peer set as of March 31, 2023, but smallest in terms of gold loan AUM

At the end of Fiscal 2023, Fedbank Financial witnessed the fastest 3-year gold loan portfolio growth of 42% on-year followed by Muthoot Finance (15%). However, the growth is on a lower base as compared to Muthoot Finance, which is the largest gold loan financier amongst the peers with 98% of its overall loan portfolio (₹ 632 billion) comprising of gold loans at end of Fiscal 2023.

Fedbank Financial is the 2nd most efficient gold loan NBFC amongst its peers

At the end of Fiscal 2023, Muthoot Finance was the most efficient gold loan financier, having the highest AUM per branch of ₹ 105.6 million followed by Fedbank Financial (₹ 68.3 million). As at end of fiscal 2023, Muthoot Finance and Fedbank Financial have high AUM per employee of Rs 22.7 million and ₹ 14.3 million respectively.

Operational parameters for key gold loan NBFCs (Fiscal 2023)

Players (Fiscal 2023)	Gold Loan AUM (In Rs Billion)	3 year CAGR	Branch	Employees	AUM per Branch (in ₹ Million)	AUM per Employee (in ₹ Million)	Share of Gold Loan in total AUM
Muthoot Finance	619	15%	5,858	27,273	105.6	22.7	98%
Manappuram Finance	197	5%	3,985*	45,000	49.6^	4.4	56%
Fedbank Financial Services	30	42%	437*	2,085*	68.3^	14.3^	33%

Note: Players are arranged in decreasing order of gold loans AUM; (*) Gold loan branches/employees; (^) AUM per gold loan branch/ employee,

Source: Company Reports, CRISIL MI&A

Fedbank Financial witnessed faster growth in gold stock however, Muthoot Finance has the highest gold stock per branch

Gold stock for Fedbank Financial grew at the faster CAGR of 34% between Fiscal 2018 and Q1 Fiscal 2024 but on a relatively lower base. On the other hand, Muthoot Finance has the highest gold stock per branch at 30.86 kg per branch, followed by Fedbank Financial at 18.54 kg as of June 2023.

Gold stock (in tonnes)	FY18	FY19	FY20	FY21	FY22	FY23	Q1FY24	CAGR (FY18-Q1FY24)
Muthoot Finance	155	150	176	171	187	180	182	3%
Manappuram Finance	64	67.5	72.4	65.3	68	60	59	-1%
Fedbank Financial Services	1.86	2.13	4.13	5.90	7.00	8.13	8.10	34%

Source: Company Reports, CRISIL MI&A

Gold stock per branch (in kg)	FY18	FY19	FY20	FY21	FY22	FY23	Q1FY24
Muthoot Finance	35.84	33.48	38.54	36.92	40.50	30.73	30.86
Manappuram Finance*	19.22	20.02	20.52	18.53	17.76	15.06	14.61
Fedbank Financial Services*	16.79	15.55	16.51	19.59	17.25	18.60	18.54

Note: (*) Gold stock is per gold loan branch

Source: Company Reports, CRISIL MI&A

Muthoot Finance has the lowest cost of borrowings amongst gold loan NBFCs as of Q1 Fiscal 2024

Amongst the gold loan NBFCs, Muthoot Finance has the lowest cost of borrowing of 8.4 % as of Q1 Fiscal 2024.

Fedbank Financial has a higher average gold loan ticket size amongst gold loan NBFCs as of Q1 Fiscal 2024

Amongst the gold loan NBFCs, Fedbank Financial has an average ticket size of ₹ 104,300 which is higher as compared to Muthoot Finance and Manappuram Finance which have average ticket size of around ₹ 55,000 – ₹ 75,000.

Operational parameters for key gold loan NBFCs (Q1 Fiscal 2024)

Players (Fiscal 2023)	Average Ticket Size (in ₹ 000)	Loan to Value (%)	Yield on Gold Loans (%)	Cost of Borrowings (%)**
Muthoot Finance	75.9*	68%	18.1%	8.4%
Manappuram Finance	58.8	64%	21.4%	8.5%
Fedbank Financial Services	104.3	72%	16.9%	9.2%

Note: Players are arranged in decreasing order of Gold loans AUM, (*) As of Fiscal 2023, (**) Annualized numbers

Source: Company Reports, CRISIL MI&A

Fedbank Financial has the second lowest cost of borrowings amongst gold loan NBFCs in fiscal 2023

Amongst the gold loan NBFCs, Muthoot Finance has the lowest cost of borrowing of 7.4 % in Fiscal 2023. It is followed by Fedbank Financial (7.8%).

Fedbank Financial has a higher average gold loan ticket size amongst gold loan NBFCs in Fiscal 2023

Amongst the gold loan NBFCs, Fedbank Financial has an average ticket size of ₹ 101,200 which is higher as compared to Muthoot Finance and Manappuram Finance which have average ticket size of around ₹ 55,000 – ₹ 75,000.

Operational parameters for key gold loan NBFCs (Fiscal 2023)

Players (Fiscal 2023)	Average Ticket Size (in ₹ 000)	Loan to Value (%)	Yield on Gold Loans (%)	Cost of Borrowings (%)
Muthoot Finance	75.9	NA	17.7%	7.4%
Manappuram Finance	57.5	60%	21.0%	8.1%
Fedbank Financial Services	101.2	72%	16.3%	7.8%

Note: Players are arranged in decreasing order of Gold loans AUM,

Source: Company Reports, CRISIL MI&A

Fedbank Financial has the best asset quality in gold loans segment amongst its peers

At the end of Q1 Fiscal 2024, Fedbank Financial had GNPA of approximately 0.88% followed by GNPA of Manappuram Finance at 1.45%.

Asset quality of gold loan NBFCs (Fiscal 2023 & Q1 Fiscal 2024)

	Fiscal 2023		Q1 Fiscal 2024	
	GNPA (%)	NNPA (%)	GNPA (%)	NNPA (%)
Muthoot Finance	3.79%	3.40%	4.26%	3.82%
Manappuram Finance	1.33%	1.15%	1.45%	1.24%
Fedbank Financial Services*	0.85%	0.80%	0.88%	0.78%

Note: Players are arranged in decreasing order of Gold loans AUM, (*) For Gold Loan Portfolio

Source: Company Reports, CRISIL MI&A

MSME LENDING IN INDIA

Brief overview of MSMEs in India

The National Sample Survey ("**NSS**") 73rd round dated June 2016 estimated that there are around 63.5 million MSMEs in India. Since then, the number of MSMEs is estimated to have increased further to around 70 million as of Fiscal 2022. MSMEs complement large corporates as suppliers or directly cater to end users. The MSME sector contributes to India's socio-economic development by providing huge employment opportunities in rural and backward areas, reducing regional imbalances, and assuring equitable distribution of national wealth and income. The segment currently contributes to 30% of the GDP, over 40% of exports and creates employment for about 110 million people in India, thus supporting economic development and growth.

MSME segment account for 30% of India's GDP

Rs trillion	Total MSME GVA	Growth (%)	Total GVA	Share of MSME in GVA (%)	All India GDP	Share of MSME in All India GDP (in %)	Number of MSMEs (in millions)*
FY16	41	11.0%	126	32.3%	138	29.5%	63.5
FY17	45	10.9%	140	32.2%	154	29.3%	65.5
FY18	51	13.0%	155	32.8%	171	29.7%	66.5
FY19	57	12.9%	171	33.5%	190	30.3%	68.5

Note: (*) - Estimated

Source: MSME Ministry Annual report for FY21, CRISIL MI&A

Snapshot of MSMEs in India

*Note: *Data as of FY19, ** Data as of FY22, ^The numbers are estimated*

Source: MSME Ministry Annual report for FY21, CRISIL MI&A

RBI has adopted the definition of MSMEs in line with the Micro, Small and Medium Enterprises Development ("**MSMED**") Act, 2006. This definition is based on investments in plant and machinery in the manufacturing and services sectors.

To bring in more enterprises under the ambit of MSMEs and widen the definition of MSMEs taking into account inflation over the past few years, in June 2020, the Government of India revised the MSME investment limit across each category and introduced an alternate and additional criteria of turnover buckets to the definition. It further removed the difference between the definition of manufacturing based and services based MSMEs.

In June 2021, the Government of India has included retailers and wholesalers under the MSMEs definition to extend the benefits of priority sector lending to traders as well. The move is structurally positive from long-term perspective, as it is expected to enable entities operating in the segment to register on the Government of India's Udyam portal, participate in government tenders and also avail financing options/benefits available to the category.

Given below is the composite new, revised definition of MSMEs in comparison to the old existing one:

New MSME definition removed distinction between manufacturing and services

Old MSME classification			
Criteria : Investment in plant and machinery or equipment			
Classification	**Micro**	**Small**	**Medium**
Manufacturing enterprises	Investment < ₹ 2.5 million	Investment < ₹ 50 million	Investment < ₹ 100 million
Services enterprises	Investment < ₹ 1 million	Investment < ₹ 20 million	Investment < ₹ 50 million
Revised MSME classification			
Composite Criteria : Investment and annual turnover			
Classification	**Micro**	**Small**	**Medium**
Manufacturing and Services enterprises	Investment < ₹ 10 million and Turnover < ₹ 50 million	Investment < ₹ 100 million and Turnover < ₹ 500 million	Investment < ₹ 500 million and Turnover < ₹ 2.5 billion

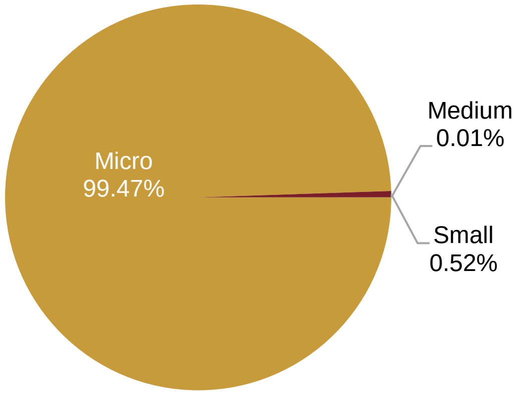
Source: MSME Ministry, CRISIL MI&A

Financial institutions also use internal business classifications to define MSMEs, based on their turnover. Most banks and non-banks follow this practice.

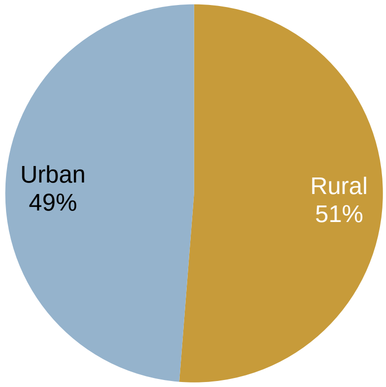
According to the NSS 73rd round dated June 2016, micro segment accounted for as much as approximately 99.47% of total estimated number of MSMEs in India. Small and medium sector accounted for 0.52% and 0.01%, respectively of the total estimated MSMEs. At a region level, rural regions accounted for marginally higher share of 51% as compared to urban region. MSMEs units are largely dominated by bigger states including Uttar Pradesh, West Bengal, Tamil Nadu, Maharashtra and Karnataka. The top 5 states together accounted for approximately 50% of the total number of MSMES in India. Service sector accounts for dominant 79% share in MSMEs, of which retail forms major share.

In terms of constitution, close to 94% of the entities in the MSME universe in India are estimated to be sole proprietorship firms, wherein a small business undertaking is run and managed by the business owner and the business and the owner can virtually not be separated.

Micro segment accounts for dominant share



Rural region accounts for marginally higher share



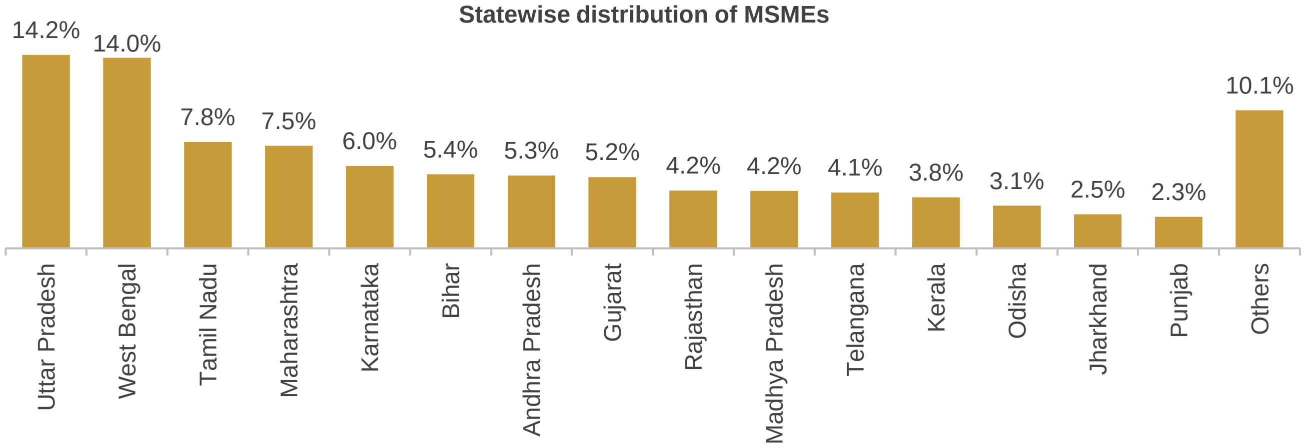
Source: National Sample Survey (NSS) 73rd round dated June 2016, CRISIL MI&A

MSMEs are largely dominated by individuals

Entities	Share in number of MSMEs
Proprietorship	93.83%
Partnership	1.53%
Private Company	0.23%
Cooperative	0.13%
Public Company	0.04%
Others	4.24%

Source: IFC9, CRISIL MI&A

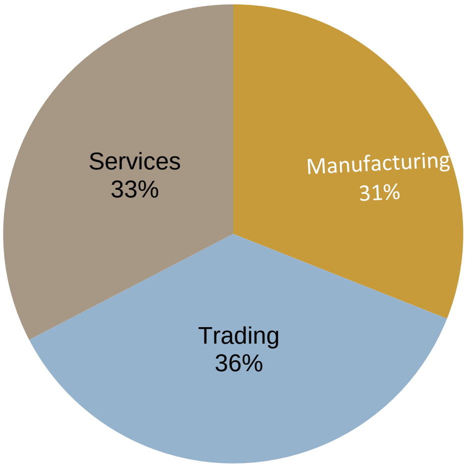
Top 5 states together form approximately 50% of total MSME units



Source: National Sample Survey (NSS) 73rd round dated June 2016, CRISIL MI&A

[9] *https://www.ifc.org/wps/wcm/connect/dcf9d09d-68ad-4e54-b9b7-614c143735fb/Financing+India%E2%80%99s+MSMEs+Estimation+of+Debt+Requirement+of+MSMEs+in+India.pdf?MOD=AJPERES&CVID=my3CmzI*

Trading sector accounts for higher share in number of MSMEs



Source: MSME Ministry, CRISIL MI&A

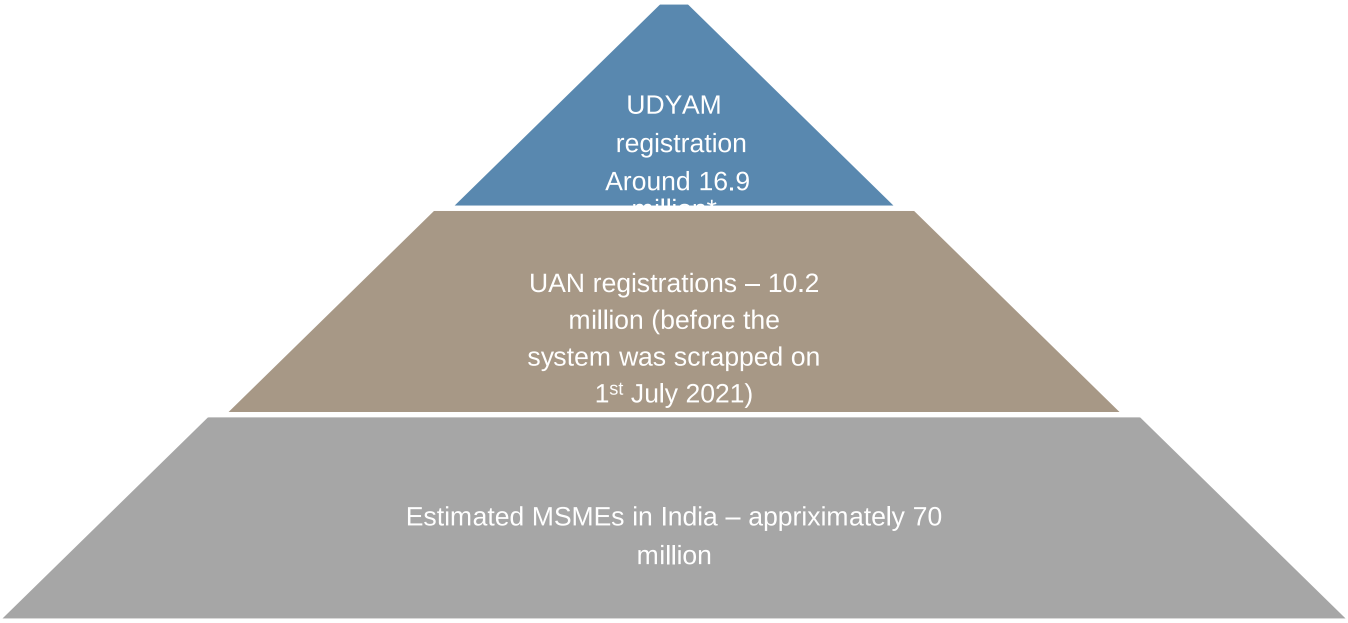
Small fraction of MSMEs in India registered under UDYAM system

After the Government of India revised the definition of MSMEs (in June 2020), MSMEs that had an existing MSME registration (Udyog Aadhaar Number or UAN) or Enterprise Memorandum ("**EM**") were required to re-register themselves under UDYAM. Thereafter, in August 2020, RBI issued a notification allowing financiers to obtain the UDYAM certificate from entrepreneurs for lending purposes.

As of June 20, 2023, close to 16.9 million MSMEs have registered on UDYAM. Around 10.2 million – were registered on the erstwhile UAN system. This number pales in comparison to the total number of MSMEs in India, estimated at around 70 million.

Like UAN, UDYAM also offers free, paperless online and instant registration through a web portal. Small businesses aren't required to upload any documents or proof except the Aadhaar number for registration. Earlier GST registration was mandatory for UDYAM Registration but from March 2021 onwards, it is exempted for those units who are not eligible for GST registration.

UDYAM certificate is expected to be required by MSMEs for taking benefit of any scheme of the Central government. The UDYAM portal is also integrated with the Government e-Marketplace ("**GeM**") and the Trade Receivables and Discounting System ("**TReDS**") so that enterprises can participate in government procurement and have a mechanism for discounting their bills.



*As of June 2023

Source: MSME Ministry, CRISIL MI&A

Probable reasons for low registration rates

Earlier, the requirement was that companies that wanted to register under UDYAM had to provide their GSTIN. Since many entities have a turnover of less than ₹ 40 lakh and hence do not need to be GST compliant, they were ineligible to register on the UDYAM system. This requirement was removed by the MSME Ministry in early March 2021.

Low levels of awareness regarding the roll-out of schemes, their eligibility conditions, paperwork requirements and grievance redressal mechanisms could have also impacted the registration of MSMEs. As per the NCAER Business Expectations Survey (“**BES**”) in December 2020, 75% of MSMEs were not even aware of ECLGS launched by the Government of India post COVID-19.

MSME Credit gap estimated at ₹ 92 trillion as of Fiscal 2023

High-risk perception and prohibitive cost of delivering services physically have constrained formal lending to MSMEs. The emerging self-employed individual and micros, small and medium enterprise segment is largely unaddressed by lending institutions in India. An IFC report titled Financing India’s MSMEs (November 2018) estimated the MSME credit demand at ₹ 69.3 trillion in fiscal 2017, of which only approximately 16% of demand was met through formal financing[10] and consequently, the MSME credit gap *(defined as the gap between the demand for funds amongst MSMEs and the supply from formal financiers)* was estimated at ₹ 58.4 trillion. This gap was met through informal sources including moneylenders, chit funds and personal sources from friends and relatives. The interest rate for these sources generally ranges between 30-60% per annum. r

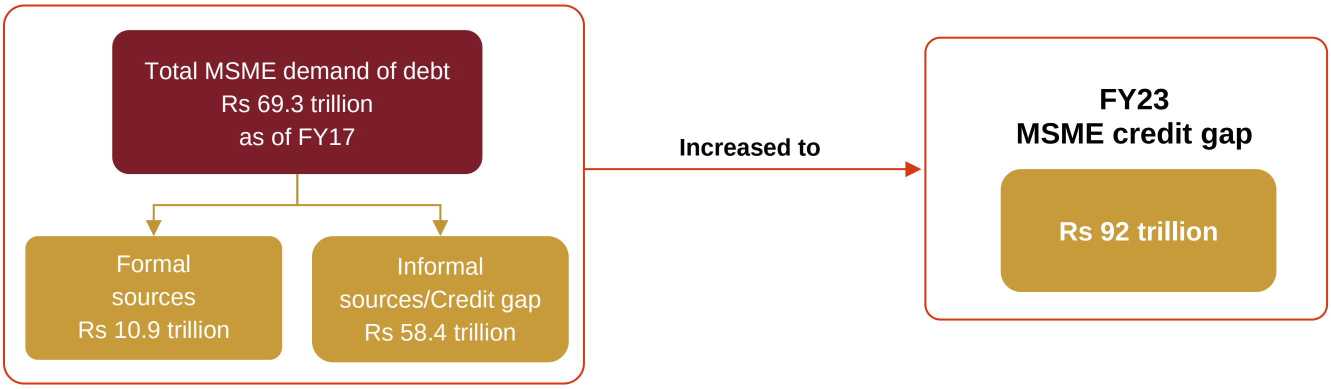
The credit gap is estimated to have further widened over the last 4 years due to slower economic growth in fiscal 2020, followed by the COVID-19 pandemic in Fiscal 2021. In Fiscal 2021, the nationwide lockdown to contain the spread of the COVID-19 pandemic disrupted economic activity, hurt demand, impacted working capital needs and supply chain along with future investments and expansions. Domestic supplies and supplies from imports also suffered, affecting both, their availability and cost. Contractual and wage labor were also hit due to lower demand

[10] *Formal sources include Public sector banks, Private sector banks, Foreign banks, Regional rural banks (RRBs), Urban Cooperative Banks (UCBs), NBFCs, and government institutions including SIDBI and State Finance Corporations (SFCs).*

and layoffs. MSMEs and businesses in the sectors such as hotels, tourism, logistics, construction, textiles ,gems and jewellery suffered the most during the first half of the fiscal. Businesses in the retail sector, especially those catering to daily usage goods and everyday cash and carry businesses such as grocery shops, fruits and vegetables sellers, etc., however, fared relatively better as their availability close to the residences of customers' increased the demand for their services.

Furthermore, government schemes post the COVID-19 pandemic such as the ECLGS scheme provided relief only to MSME units with existing loans from a formal financial institution. With economic recovery in Fiscal 2022, MSME credit growth also recovered. As of Fiscal 2023, the MSME credit demand is estimated to be around ₹ 117 trillion, of which 21% of demand met through formal financing. Assuming an increase of around 9% annually[11] in the demand for credit and the availability of credit from formal sources, CRISIL MI&A estimates the credit gap to have increased to ₹ 92 trillion as of Fiscal 2023.

MSME credit demand largely met by informal sources



Source: IFC report on Financing India's MSMEs dated November 2018[12], CRISIL MI&A

Even while the credit gap has increased, new MSME units continue to be set up across India. Between Fiscals 2016 and 2022, 18.3 million units were set up, according to the Government of India registration data of MSMEs. Thus, though a myriad of small businesses is set up every day in India, access to credit remains a challenge. However, the industry has witnessed an increase in access to formal credit to MSME, which could be attributed to the increase in the number of registered MSMEs to 13,093,698 in Fiscal 2023 from 495,013 in Fiscal 2016. According to Udhyam Registration Publication, Maharashtra, Tamil Nadu and Gujarat cumulatively accounts for 36% of overall MSME registration as of June 2023. In addition, under the micro category, the maximum number of registrations were from Maharashtra followed by Tamil Nadu, Uttar Pradesh, Rajasthan and Gujarat. Under small and medium category, maximum registrations were from Maharashtra followed by Gujarat and Tamil Nadu.

[11] *Based on MSME credit growth over fiscal 2017-23*

[12] *https://www.ifc.org/wps/wcm/connect/dcf9d09d-68ad-4e54-b9b7-614c143735fb/Financing+India%E2%80%99s+MSMEs+Estimation+of+Debt+Requirement+of+MSMEs+in+India.pdf?MOD=AJPERES&CVID=my3Cmzl*

Year-wise and MSME category-wise registration of MSMEs

Year/ Category	FY16	FY17	FY18	FY19	FY20	FY21*	FY22^	FY23$
Micro	4,21,516	21,47,908	13,44,612	18,70,932	22,48,730	35,95,577	49,75,082	126,17,959
Small	70,866	2,16,558	1,66,259	2,41,187	3,02,299	4,00,525	1,72,432	4,35,885
Medium	2,631	8,592	6,584	9,426	11,229	35,541	11,294	39,854
Total	**4,95,013**	**23,73,058**	**15,17,455**	**21,21,545**	**25,62,258**	**40,31,643**	**51,58,808**	**130,93,698**

*Note: * Based on UAN and UDYAM registrations, ^Based on UDYAM registrations, $ Based on Udyam registrations as on December 2022 as stated in the MSME Annual Report 2022-23; Source: Development Commissioner Ministry of Micro, Small and Medium Enterprises (DCMSME), CRISIL MI&A*

State-wise category-wise registration of MSMEs

State	Cumulative MSME Registration *	Share in overall MSME registration	Growth in MSME Registration (March 2022-June 2023)
Maharashtra	3,057,608.00	18%	88%
Tamil Nadu	1,737,814.00	10%	103%
Gujarat	1,272,221.00	8%	96%
Uttar Pradesh	1,511,846.00	9%	139%
Rajasthan	1,262,078.00	7%	100%
Karnataka	968,158.00	6%	107%
Madhya Pradesh	789,572.00	5%	120%
Bihar	693,733.00	4%	123%
Punjab	630,391.00	4%	123%
Haryana	578,670.00	3%	105%

Note: (*) Based on Cumulative MSME registration as of June 2023 (https://dashboard.msme.gov.in/Udyam_Statewise.aspx), MSME Registration for Fiscal 22 based on Udyam Registration Publication: Registration of Micro, Small and Medium Enterprises (MSMEs) in India 2020-22;

Source: Development Commissioner Ministry of Micro, Small and Medium Enterprises (DCMSME), CRISIL MI&A

Potential market for residential property backed secured MSME lending is estimated at ₹ 22 trillion

The sheer size of the gap between the supply and demand of credit and the number of enterprises impacted indicates a veritable opportunity in MSME financing. There therefore exists a plethora of players – universal banks, small finance banks, traditional NBFCs, new age finTechs, MFIs, as well as local moneylenders – who try to meet the financing requirements of MSMEs by offering secured or unsecured loans straddling various tenures.

CRISIL MI&A has attempted to decipher the size of the potential opportunity in secured residential property-backed secured MSME lending (hereafter referred to as the Addressable market for secured MSME loans), using data, information and insights at a state-level pertaining to:

- Number of households from NSS 76th round (July 2018-December 2018)
- Self-employed non-agricultural households in both urban and rural areas from Periodic Labor Force Survey ("**PLFS**") dated July 2019-June 2020

- Proportion of self-employed households, which are staying in their own pucca or semi-pucca home (which can be taken as a collateral by financiers) from NSS 76th round (July 2018-December 2018)

Based on our analysis and assumptions detailed in the chart below, small ticket size secured (SORP – Self occupied residential property) MSME lending market potential is estimated at ₹ 22 trillion. Players such as SBFC Finance, Five Star Business Finance, Vistaar Finance, Veritas Finance and AU SFB currently operate in this market; our analysis indicates the Addressable Market available for these players. The top 5 states including Uttar Pradesh, West Bengal, Bihar, Maharashtra and Tamil Nadu together account for almost half the addressable market.

While the latent market opportunity is indeed significant, we observe that there are not many formal financiers who cater to this segment and have built scale. This can be attributed to the high cost of serving the market and the time it takes to build expertise, the requirement of having a strong knowledge of the local market and regional dynamics, and the challenges associated with building a credit underwriting model for non-income proof customers and collections infrastructure.

Most small businesses in India do not maintain documents such as income proof, business registration, GST registration, income tax filings, and bank statements, making credit assessment challenging. To illustrate, as per GST council data, only 13.7 million enterprises across various size dimensions were registered under GST as of May 2022. Hence, these businesses have limited or no access to formal credit from banks and financial institutions due to the requisite documentation and stringent underwriting norms.

Examples of such businesses include provision stores, building materials stores, tea shops, vegetable vendors and others. The small business in manufacturing and services include small fabrication units, machine tools manufacturers (using lathe machines), tailors, saloons, Gym owners, vehicle service centres, etc.

Addressable market estimation methodology for secured MSME loans given to non-agriculture self-employed households with residential self-occupied property as collateral

Source: National Sample Survey (NSS) 73rd round (July 2015 – June 2016) and NSS 76th round (July 2018 – December 2018), CRISIL MI&A

State wise split of addressable market

Top 15 states	Total Households ('000)	Total Non-agri Self Employed Households ('000)	Total Non-agri Self Employed Households - SORP ('000)	Total Non-agri Self Employed Households - SORP - Pucca + Semi Pucca ('000)	Overall MSME Addressable Market Size (₹ billion)
Uttar Pradesh	38,224	7,776	7,023	6,674	3,337
West Bengal	23,781	5,923	5,143	4,849	2,424
Bihar	19,960	4,498	4,270	3,953	1,976
Maharashtra	24,120	4,353	3,316	3,270	1,635
Rajasthan	13,384	3,075	2,743	2,685	1,342
Tamil Nadu	20,200	3,715	2,584	2,523	1,262
Gujarat	13,064	3,188	2,471	2,428	1,214
Madhya Pradesh	15,251	2,360	1,988	1,922	961
Andhra Pradesh	14,279	2,677	1,956	1,895	947

Top 15 states	Total Households ('000)	Total Non-agri Self Employed Households ('000)	Total Non-agri Self Employed Households - SORP ('000)	Total Non-agri Self Employed Households - SORP - Pucca + Semi Pucca ('000)	Overall MSME Addressable Market Size (₹ billion)
Kerala	8,577	1,988	1,795	1,789	895
Karnataka	14,928	2,740	1,822	1,786	893
Assam	6,740	1,965	1,702	1,660	830
Odisha	10,401	1,909	1,647	1,415	707
Punjab	5,922	1,636	1,415	1,409	705
Telangana	9,793	1,788	1,205	1,188	594
Others	32,483	6,585	5,317	5,180	2,590
All India	**2,71,105**	**56,115**	**46,397**	**44,624**	**22,312**

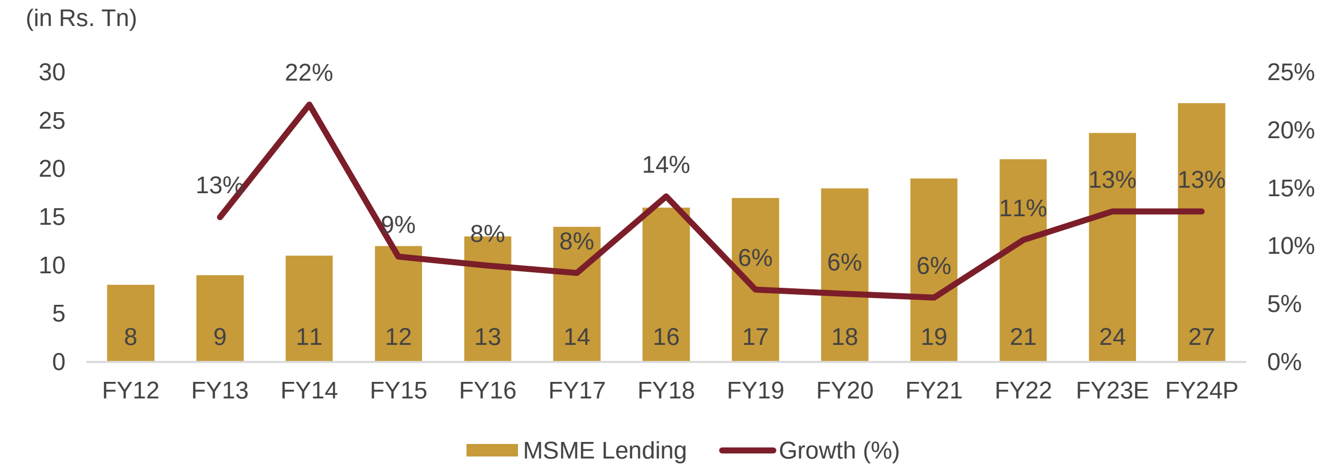
Note: States are arranged in order of Addressable market size, Source: National Sample Survey (NSS) 73rd round (July 2015 – June 2016) and NSS 76th round (July 2018 – December 2018), Periodic Labor Force Survey (PLFS) dated July 2019-June 2020, CRISIL MI&A

Overall MSME lending has grown at a CAGR of 10% in the past decade

CRISIL MI&A estimates the total size of MSME lending market across ticket sizes and various player groups (banks, NBFCs, small finance banks, and other formal lenders) to be around ₹ 24 trillion as of March 2023. This market size includes loans taken by MSMEs across various constitution types (sole proprietorships, partnership firms, private and public limited companies, and co-operatives) and the ticket size spectrum, and includes loans extended in the name of the firm/entity/company as well as the individuals in case of micro enterprises or entrepreneurs.

CRISIL MI&A estimates loans to MSMEs to have grown at a CAGR of 10% during Fiscal 2012 to Fiscal 2023, which is similar to the nominal GDP growth in this period. This can be attributed to various events during this time span that has impacted MSMEs – demonetisation of high-value currency loans in November 2016, the implementation of GST subsequently, the economic slowdown in Fiscal 2020 followed by the COVID-19 pandemic. In Fiscal 2023, with recovery in economic activity, MSME lending is estimated to have grown at a 13% growth rate year-on-year. In addition, in Fiscal 2024, CRISIL MI&A projects the MSME overall industry growth to be at 13% - 15% owing to budgetary push and rise in entrepreneurship in India.

MSME credit outstanding estimated at ₹ 24 trillion as of March 2023



Source: CRISIL MI&A estimates

COVID-19 pandemic led a heavy impact in the MSME industry in Fiscal 2021 which was also seen in the first quarter of Fiscal 2022. ECLGS schemes aimed to reduce the impact of the COVID-19 pandemic on the MSME sector. The first half of Fiscal 2022 was also impacted by the second wave leading to lower disbursements to these MSMEs. This led to extension of the ECLGS scheme which cushioned the impact of COVID-19 pandemic. ECLGS scheme led by revival of economic activities, strong exports and domestic growth prompted MSME lending to grow at 13% in Fiscal 2022.

NBFCs have managed to carve out a strong presence in MSME loans due to their focus on serving the needs of the customer segment, faster turnaround time, customer service provided and expansion in geographic reach. Over the years, the MSME portfolio of NBFCs have grown at a faster rate than the overall MSME portfolio at a systemic level. Going forward CRISIL MI&A expects the competitive positioning of NBFCs to remain strong, given their strong target customer and product focus.

ECLGS scheme has provided some relief to MSMEs hurt by the COVID-19 pandemic

Given the pain suffered by MSMEs due to the COVID-19 pandemic and the importance of MSMEs in India, the Government of India undertook several initiatives to support MSMEs and keep them afloat. This scheme provided much-needed liquidity to MSMEs that are known to have faced severe working capital crunch during downturns.

ECLGS 1.0

May 2020 to Aug 2020

- ECLGS was introduced by providing the MSMEs additional funding of up to ₹ 3 trillion in the form of a fully guaranteed emergency credit line.
- **Eligible entities**: All MSME borrower accounts with outstanding credit of up to ₹ 250 million as on February 29, 2020, which were less than or equal to 60 days past due as on that date and with an annual turnover of up to ₹ 1 billion
- In August 2020, the upper ceiling of outstanding credit was revised to ₹ 0.5 billion and annual turnover to ₹ 2.5 billion.

ECLGS 2.0 Mar 2021	• The Government extended ECLGS through ECLGS 2.0 for 26 sectors identified as stressed due to the COVID-19 pandemic by the Kamath Committee and the healthcare sector. • **Eligible entities:** Entities with outstanding credit above ₹ 0.5 billion and not exceeding Rs. 5 billion as on February 29, 2020, which were less than or equal to 30 days past due as on February 29, 2020
ECLGS 3.0 Nov 2020	• Government extended the scope of ECLGS to cover business enterprises in Hospitality, Travel & Tourism, Leisure & Sporting sectors which had, as on February 29, 2020, total credit outstanding not exceeding ₹ 5 billion and were less than or equal to 60 days past due as on that date. • The validity of ECLGS was extended up to June 30, 2021 or till guarantees for an amount of ₹ 3 trillion are issued.
ECLGS 4.0 May 2021	• ECLGS scope expanded to cover loans up to ₹ 20 million to hospitals/nursing homes/clinics/medical colleges for setting up on-site oxygen generation plants with interest rate capped at 7.5% • Civil Aviation sector included under ECLGS 3.0 • Ceiling of ₹ 5 billion of loan outstanding for eligibility under ECLGS 3.0 to be removed, subject to maximum additional ECLGS assistance to each borrower being limited to 40% or ₹ 2 billion, whichever is lower. • Borrowers who had availed loans under ECLGS 1.0 of overall tenure of 4 years comprising of repayment of interest only during the first 12 months with repayment of principal and interest in 36 months can increase the tenure to 5 years (repayment of interest only for the first 24 months with repayment of principal and interest in 36 months thereafter) • Additional ECLGS assistance of up to 10% of the outstanding as on February 29, 2020
ECLGS 5.0 June 2021	• Additional allocation of ₹ 1.5 trillion towards ECLGS scheme; limit of admissible guarantee and loan amount increased above existing level of 20% of outstanding on each loan • Sector wise details to be finalized as per evolving needs • Loan guarantee of ₹ 1.1 trillion for COVID-affected sectors:₹ 0.5 trillion towards health sector and ₹ 0.6 trillion towards other COVID-affected sectors, including travel and tourism stakeholders • Working capital/personal loans will be provided to people in tourism sector to discharge liabilities and restart businesses impacted due to COVID-19. • Loan guarantee of ₹ 75,000 million for loans extended by SCBs to MFIs for on lending up to ₹0.125 million to ~2.5 million customers; guarantee cover provided till March 31, 2022 or till guarantees for an amount of ₹ 75,000 million are issued, whichever is earlier

Source: CRISIL MI&A

In September 2021, with a view to support various businesses impacted by the second wave of COVID-19 pandemic, the timeline for ECLGS has been extended till March 2022 or till guarantees for an amount of ₹ 4.5 lakh crore are issued under the scheme, whichever is earlier. In addition, in March 2022, the scheme was extended till March 2023 as was announced in Union Budget 2022-23. Out of the targeted amount of ₹ 4.5 trillion, ₹ 3.32 trillion has been sanctioned as of April 30, 2022 of which ₹ 2.54 trillion has been disbursed. As on January 31, 202

3, guarantees amounting to ₹ 3.61 trillion has been issued under ECLGS, benefitting 1.19 crore borrowers.

However, considering the entire universe of around 70 million MSMEs, the proportion of MSMEs that have benefitted remains limited at approximately 17% (11.6 million) of entire universe as on November 12, 2021. This is because the scheme covered only MSMEs having loan exposure to formal financiers as of February 2020. Among the eligible MSMEs, small and micro MSMEs have benefitted the most from ECLGS with 76% share in amount of guarantees issued to MSMEs and 93% share in number of guarantees issued as of November 12, 2021.

The cap of 14% on final interest rate charged to MSME customers for NBFCs meant that customers of many NBFCs, which typically charge more than 14% due to high operating costs and the relatively riskier profile of their borrowers, could not avail the benefits under the ECLGS scheme.

Overall MSME market consists of various players; asset quality relatively better for private banks

In absolute terms, the aggregate size of extending MSME loans is estimated to be around ₹ 24 trillion as of March 2023. With growth in number of MSMEs and increasing requirement of credit for scaling their businesses, CRISIL MI&A believes that MSME loans would provide a huge opportunity for lenders to grow their loan book. There are various kind of players serving this segment including Banks, NBFCs and Small Finance Banks that offer loans to MSMEs, self-employed individuals and businesses.

Key Industry Parameters for overall MSME loans

	NBFCs	Public sector banks	Private Banks
Average ticket size	₹ 8 lakhs	₹ 13 lakhs	₹ 23 lakhs
Market size for overall MSME (Rs billion)	₹ 4,382	₹ 6,643	₹ 12,397
Average GNPA (as of March 2023)	4.9%	3.8%	1.4%

Source: CRISIL MI&A Estimates

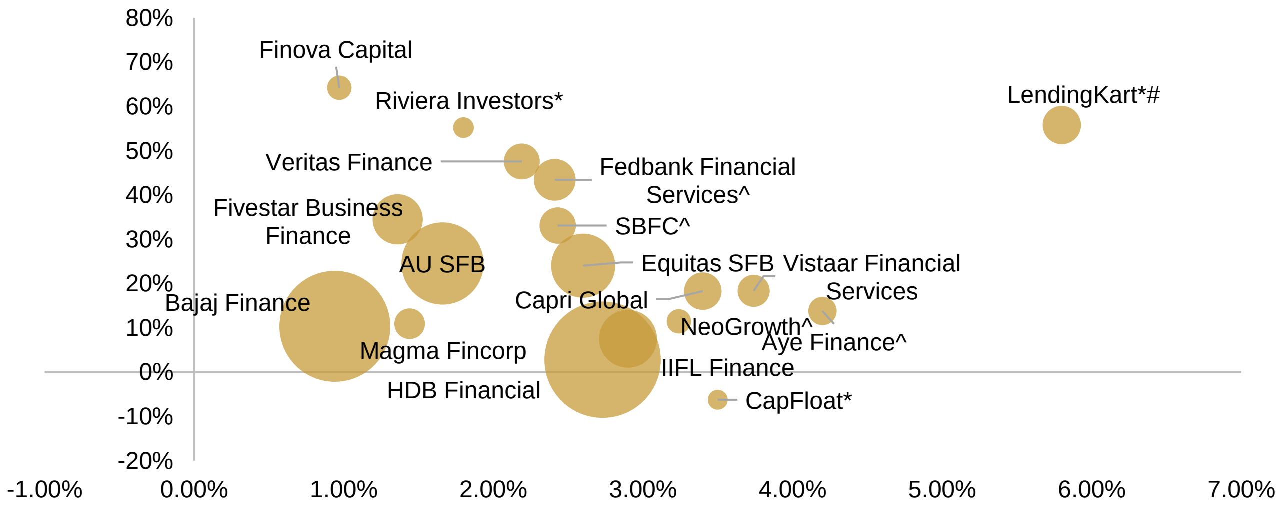
Within NBFCs, there are players that operate at relatively higher ticket sizes and offer both secured and unsecured business loans. These NBFCs offer loans at the most competitive rates among other NBFCs, target customers that are relatively better in terms of credit profile and have lower cost of borrowings compared to other NBFCs. Compared to these, NBFCs that have singular focus on business loans or have significant proportion of business loans in their portfolio and operating at ticket sizes of less than ₹ 10 lakhs offer loans at a higher rate due to much riskier customer profile. FinTech firms with NBFC license and SFBs are other players that operate in the MSME loans landscape. FinTechs leverage data and technology in their business models and are more focused on unsecured business loans. Hence, they also have higher yields in the range of 24-30% because of the higher risk associated with the customer profile catered and the product segment they operate in.

Comparison of various NBFCs based on yield on advances and average ticket size (Fiscal 2023)

	Yield less than 16%	Yield between 16% and 22%	Yield more than 22%
Average ticket size more than or equal to ₹ 10 lakhs	Fedbank Financial Services Ugro Capital Capri Global Poonawalla Fincorp	Bajaj Finance	IIFL Finance Neogrowth
Average ticket size less than ₹ 10 lakhs	AU Small Finance Bank	SBFC Finance Equitas Small Finance Bank CapFloat Financial Services^	Veritas Finance Five-Star Business Finance Aye Finance Lendingkart^ Finova Capital Riviera Investors*

*Note: ^Based on Fiscal 2021 data, * Based on Fiscal 2022 data, Source: Company Reports, CRISIL MI&A*

Comparison of various players based on portfolio size, portfolio growth and GNPA ratio (Fiscal 2023)



*Note: Size of the bubble denotes relative size of the MSME loan portfolio as of March 2023, ^AUM, GNPA as of December 2022, *AUM, GNPA as of September 2022, # CAGR growth from Fiscal 2018-2023*

Source: Company Reports, CRISIL MI&A

Moreover, compared to different loan products like affordable housing loans, microfinance loans, auto loans and personal loans, small to medium ticket size MSME loans is one of the most attractive asset classes offering competitive yields over a medium tenure with good collateral quality, lower default risk as the loans are secured predominantly with self occupied residential property ("**SORP**") and high collateral enforceability due Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act ("**SARFAESI**").

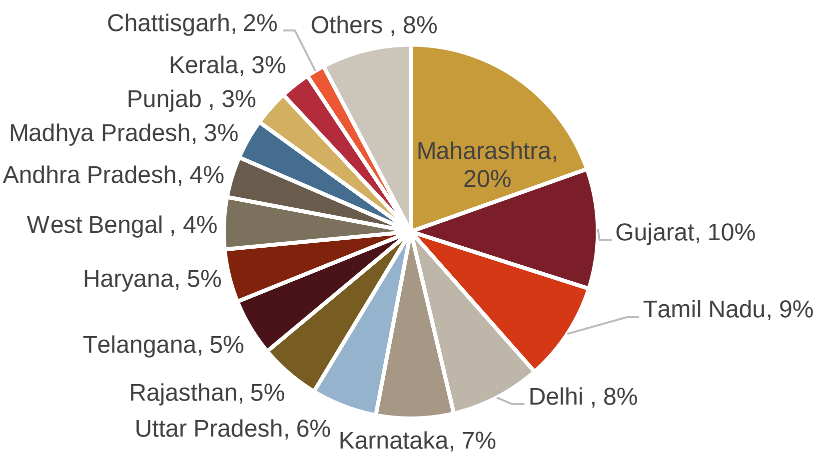
	Estimated Market Size – Portfolio outstanding March 2023 (₹ trillion)	Ticket size	Yields	Typical tenure	Collateral Quality	Tendency to default	Collateral enforceability
Secured property-backed micro-mortgage Loans (< ₹ 15 lakhs)	1.8	Small	High	Medium	Good	Medium	Low
Secured Property-backed small -business loans (₹ 15 lakhs to ₹ 50 lakhs)	2.1	Small to Medium	Medium	Medium	Good	Low	High
Secured non-LAP loans	15.4	Small to Medium	High	Low	Good	Low	Low
Microfinance loans	4.8	Small	Medium	Low	No collateral	Relatively High	NA
Housing loan	30.0	Large	Medium	High	Very good	Low	High
Auto Loans	11.5	Small to Medium	Low to Medium	Low to medium	Moderate	Medium	Low
Personal Loans	10.0	Small	High	Low	No collateral	Medium to High	NA

Source: CRISIL MI&A

State-wise analysis of overall MSME loans

The MSME loans segment has been growing strongly with a four-year CAGR of 18% between Fiscals 2019 and 2023. Overall MSME portfolio is expected to grow at 12-14% CAGR between Fiscal 2023 and Fiscal 2025. Based on the value of overall MSME loans outstanding, the top 15 states accounted for 92% of the market size in this segment as of March 2023. Maharashtra tops the list with the highest share of 20%, followed by Gujarat (10%), Tamil Nadu (9%), Delhi (8%).

Top 15 states account for 92% of overall MSME loans portfolio (March 2023)



Note: Based on CRISIL MI&A estimates

Source: CRISIL MI&A.

MSME loans are expected to continue to grow at a strong pace

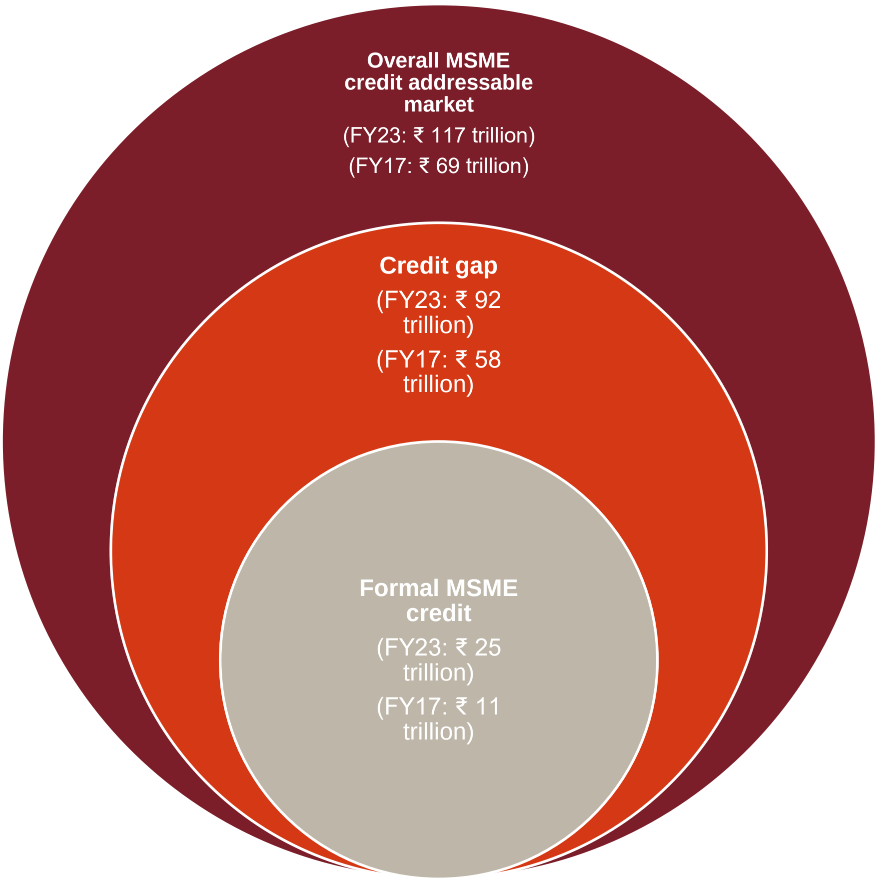
There is a huge demand supply gap in the MSME loan segment, especially in lower ticket size segments. With increasing presence of MSME lenders in smaller cities and rising focus of lenders on underserved target customer segment, loan portfolio is expected to see a strong growth in future. Going forward, CRISIL MI&A expects MSME loans with ticket size between ₹ 1 million to ₹ 10 million is expected to grow at 14-16% CAGR over Fiscals 2023 and 2025, aided by increasing lender focus and penetration of such loans, enhanced availability of data increasing lender comfort while underwriting such loans, enhanced use of technology, newer players entering the segment, and continued government support.

Growth drivers

High credit gap in the MSME segment

Less than 15% of approximately 70 million odd MSMEs have access to formal credit in any manner as of March 2022. High-risk perception and the prohibitive cost of delivering services physically have constrained traditional institutions' ability to provide credit to underserved or unserved MSMEs and self-employed individuals historically. As a result, they resort to credit from informal sources. This untapped market offers huge growth potential for financial institutions. As stated earlier, the credit gap was estimated at around ₹ 58.4 trillion as of 2017 *(Source: IFC report named Financing India's MSMEs released in November 2018, CRISIL MI&A)* and is estimated to have widened further to around ₹ 92 trillion as of Fiscal 2023.

Credit Gap estimated at ₹ 92 trillion as of Fiscal 2023



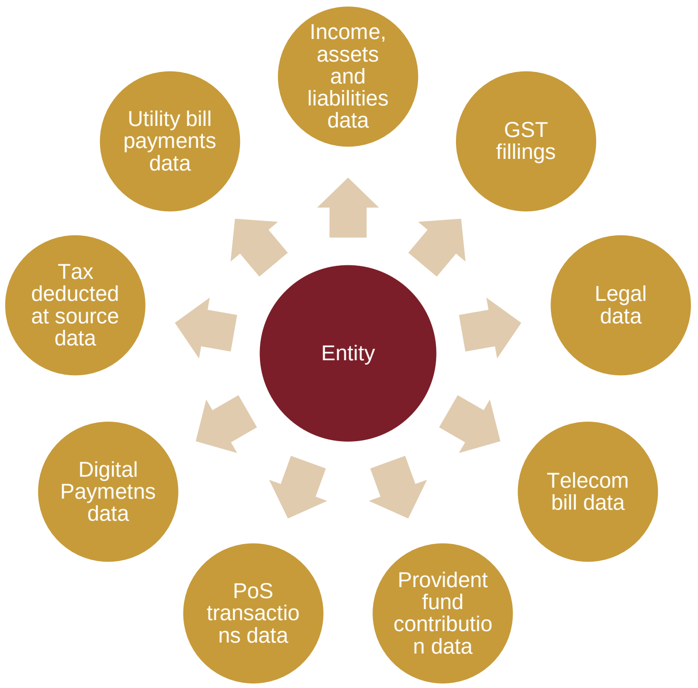
Note: Overall formal MSME credit given above includes all kinds of secured and unsecured loans given to MSMEs across ticket sizes by organised lenders.

Source: MSME Ministry Annual report for FY21, IFC report on Financing India's MSMEs dated November 2018, CRISIL MI&A

Increased data availability and transparency

With increased digital initiatives by the MSMEs, the shift towards their formalisation and digitisation has created a plethora of data points for lenders that would help improve the efficacy of credit assessment and gradually enable provision of credit to hitherto underserved customer segments. For example, the quantum of retail digital payments has catapulted from ₹ 140 trillion in fiscal 2017 to ₹ 606 trillion in fiscal 2023. Within UPI, the quantum of person-to-merchant payments has zoomed from ₹ 6.2 trillion in Fiscal 2021 to ₹ 30.7 trillion in Fiscal 2023. This increase has created a digital footprint of customers, which can be potentially used for credit decision making, along with other relevant parameters such as customer demographics, business details, credit score, and personal situation of the borrower.

Multiple data points can be used for credit assessment

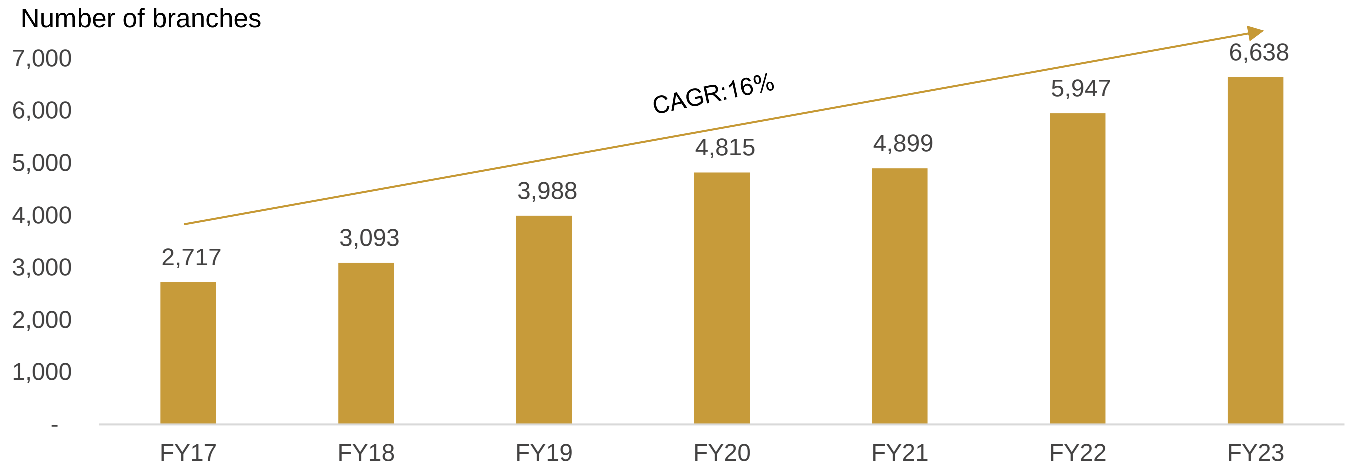


Source: CRISIL MI&A

Growth in branch network of players in MSME segment

Over past few years, players offering MSME loans have expanded their branch network with the intent to serve a larger customer base. In the future also, CRISIL MI&A expects lenders with a strong focus on MSME lending and healthy competitive positioning to continue to invest in branch expansion. With increasing branch network, customer acquisition and credit penetration of MSME loans is also expected to increase. To illustrate, the cumulative branch network of six MSME lenders (Fedbank Financial, Five Star Business Finance, Vistaar Finance, Veritas Finance, HDB Financial and IIFL Finance) has expanded at a 16% CAGR between Fiscals 2017 and 2023, even though the NBFC industry and the economy were impacted by the IL&FS crisis, a slowdown in growth in Fiscal 2020 and the COVID-19 pandemic.

Number of branches have grown at 16% CAGR over Fiscals 2017 and 2023



Note: The above data includes branches for Fedbank Financial Services, Five Star Business Finance, Vistaar Finance, Veritas Finance, HDB Finance and IIFL Finance

Source: Company Reports, CRISIL MI&A

Reduction in risk premiums due to information asymmetry

In the absence of reliable information about small businesses, it becomes difficult for lenders to assess the creditworthiness of the borrower. Hence, lenders often charge a credit risk premium from these customers, leading to higher interest rates. By leveraging technology and using a combination of traditional data (bureau data, financial statements, credit score), non-traditional data (payments, telecom, provident fund contribution and psychometric data), and government data (Aadhaar, GST), lenders would be able to gain greater insight into their customers' data, thereby increasing the accuracy of customer assessments. This would reduce the level of asymmetry in information and could lower the credit risk premium over a period of time.

Increasing competition with entry of new players and partnerships between them

More players in consumer-facing businesses with a repository of data (such as e-commerce companies and payment service providers) are expected to enter the lending business, intensifying competition. For example, In June 2018, Amazon India launched a platform for lenders and sellers, wherein sellers can choose loan offers from various lenders at competitive rates. In August 2021, Meta (earlier known as Facebook) partnered with Indifi Technologies to provide loans to small businesses that advertise on its platform. Incumbent traditional lenders are expected to increasingly leverage the network of their partners and/or digital ecosystem to cross-sell products to existing customers, tap customers of other lenders, and also cater to new-to-credit customers. This is expected to expand the market for MSME loans.

Reduction in turn-around-time ("TAT") and increased use of technology

With the availability of multiple data points and technological advancement, TAT for lending to MSMEs has been continuously declining. This too is expected to drive the demand for MSME loans.

Government initiatives

Relaxation in the threshold under SARFAESI Act from ₹ 5 million to ₹ 2 million for NBFCs

In the Union Budget 2021-2022, presented by the Finance Minister, for NBFCs with a minimum asset size of ₹100 crore, the minimum loan size eligible for debt recovery under the SARFAESI, 2002 was proposed to be reduced from the existing level of ₹ 5 million to ₹ 2 million. The objective of this move is to improve credit discipline while continuing to protect the interest of small borrowers. This relaxation is expected to facilitate recovery from stressed books, help the NBFCs to improve their ability to recover smaller loans and strengthen their overall financial health. More importantly, it acts as a deterrent to default and enhances the enforceability of collateral for players focused on the medium ticket size LAP segment with loans of ₹ 20-50 lakhs.

Inclusion of retail and wholesale trade under MSME category

In July 2021, the Ministry of Micro, Small and Medium enterprises decided to include Retail and Wholesale trade as MSMEs for the purpose of Priority Sector Lending and they would be allowed to be registered on UDYAM Registration Portal. The move is structurally positive from long-term perspective, as it is expected to enable entities operating in the segment to register on the Government of India's UDYAM portal, participate in government tenders and also avail financing options/ benefits available to the category. This move is expected to also aid in the formalisation of India's retail trade and enable financial support to small and mid-sized retail businesses. By widening the scope of MSME to cover wholesale as well as retail trade, this move also creates an additional opportunity for MSME lenders to increase their penetration and business.

Credit Guarantee Fund Scheme extended to cover NBFCs

One of the major reasons why MSMEs are credit-starved is the insistence by banks or financial institutions for the provision of collateral against loans. Collaterals are not easily available with such enterprises, leading to a high-risk perception and higher interest rates for these MSMEs. In order to address this issue, the Government of India launched the Credit Guarantee Fund Scheme under the aegis of the Credit Guarantee Fund Trust for Micro and Small Enterprises ("**CGTMSE**") in order to make collateral-free credit available to micro and small enterprises.

In January 2017, the scheme was extended to cover systemically important NBFCs as well. Key eligibility criteria for this scheme are:

1) NBFCs should be registered with RBI and meet specified prudential norms;

2) the NBFC should have made a profit for the three preceding fiscals at the time of enrolment;

3) the NBFC should be lending to micro and small enterprises with minimum 5 years of lending experience, minimum Rs 100 crore of MSE loan portfolio, NPA level below 5% for MSE portfolio and average recovery ratio of 90% for preceding three fiscals at the time of enrolment and

4) it should have long-term credit rating of at least BBB. The overall limit under the scheme was also been enhanced to ₹ 20 million.

Guarantees approved under CGTMSE

Year	Number of guarantees approved	Amount of guarantees approved (₹ billion)
FY19	435,520	302

Year	Number of guarantees approved	Amount of guarantees approved (₹ billion)
FY20	846,650	459
FY21	835592	369
FY22	717020	561
FY23	1165786	1,048

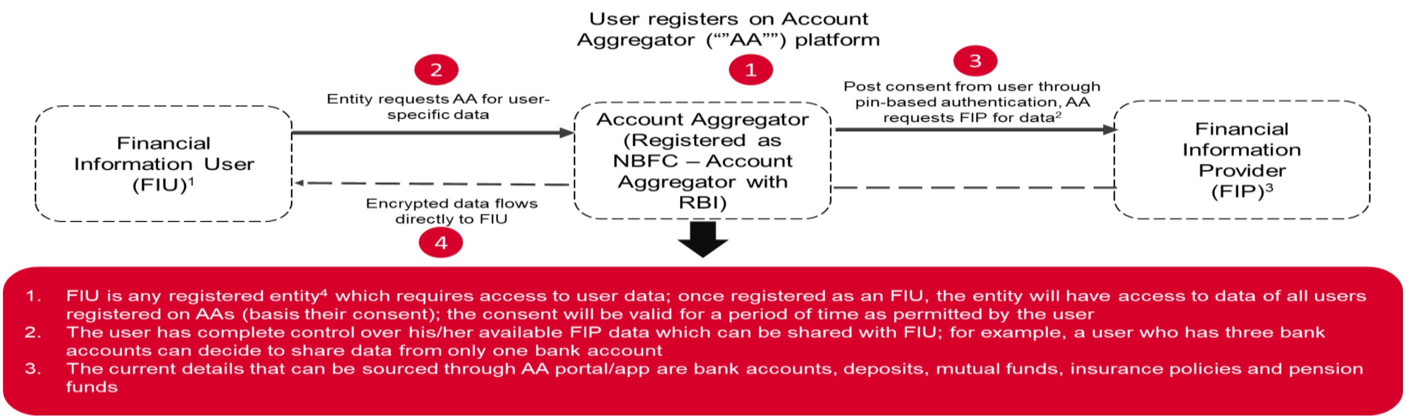
Source: CGTMSE, CRISIL MI&A

Government initiatives addressing structural issues in the MSME market

The Government of India has unveiled a number of initiatives aimed at addressing some of the structural issues plaguing small business lending segment. These include granting licenses to account aggregators, the Pradhan Mantri Mudra Yojana ("**PMMY**"), unveiling TReDS platforms and the implementation of GST.

Licensing account aggregators

RBI launched the account aggregator system on September 2, 2021, which has the potential to transform the MSME finance space once there is widespread adoption amongst the lending community. Four account aggregators also announced the launch of their apps on the same day which include OneMoney, FinVu, CAMSFinServ and NESL Asset Data Limited ("NADL"). Account aggregators are essentially NBFCs, licensed by RBI, that act as an intermediary to collect and consolidate data from all Financial Information Providers ("FIP") that hold users' personal financial data like banks and share that with Financial Information Users ("FIU") like lending agencies or wealth management companies that provide financial services. These account aggregators would provide granular insights to lenders into customers' financial assets and their borrowing history centrally, based on customer consent. Inclusion of additional data such as electricity bill payments and mobile recharges/bill payment data under the purview of account aggregators would further enhance its utility.



Note: [4] Registered with any one of the regulator – SEBI, RBI, IRDAI, PFRDA
Source: CRISIL MI&A

Some of the other government and regulatory initiatives are detailed below:

- UDYAM registration: Paperless and online registration process for MSMEs with an aim to promote ease of doing business.
- Stand-up India: It facilitates bank loans between ₹ 1 million and ₹ 10 million to at least one scheduled caste or

scheduled tribe borrower and at least one-woman borrower per bank branch for setting up a greenfield enterprise.

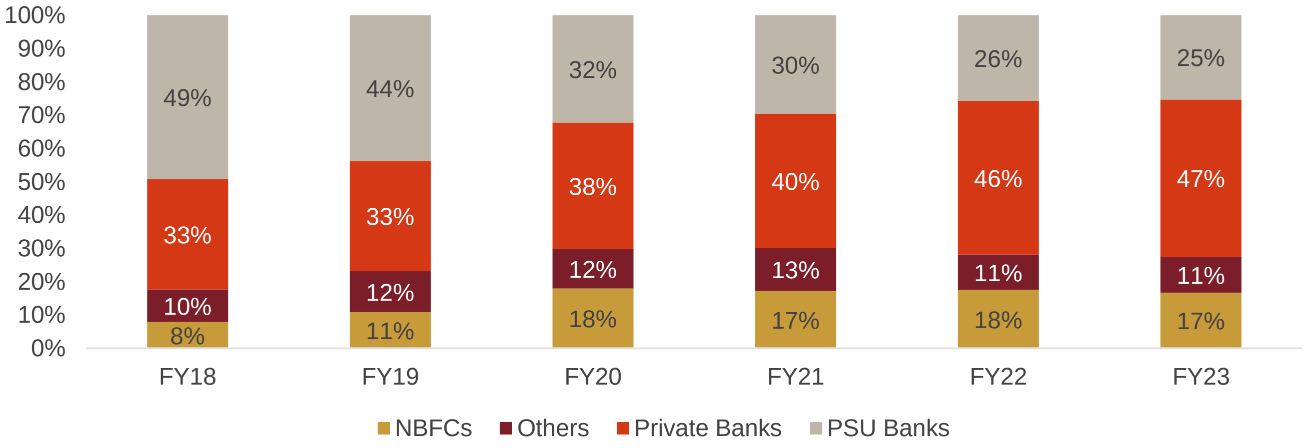
- Make in India: Launched with an intention to make India a global manufacturing hub, which in turn is expected to provide employment to numerous youths in India
- Mudra loans: To fulfil funding requirement of MSMEs who were earlier left out by financial institutions; credit guarantee support also offered to financiers.
- 59-minute loan: Online marketplace that provides in-principle approval to MSME loans up to ₹ 10 million in 59 minutes.
- Unified Payments Interface 2.0 (“**UPI 2.0**”): Real-time system for seamless money transfer from account
- TReDS: Institutional mechanism to facilitate financing of trade receivables of MSMEs from corporates and other buyers through multiple financiers.
- Factoring to support more participation from NBFCs: In an amendment to Factoring Regulation Act, 2011, the Lok Sabha passed the Factoring Regulation (Amendment) Bill in July 2021.

NBFCs increasing their presence in the overall MSME loans segment

NBFCs have managed to carve out a strong presence in MSME loans segment due to their focus on serving the needs of the customer segment, faster turnaround time, customer service provided and expansion in geographic reach. As of Fiscal 2023, the cumulative market share of NBFCs in MSME loans outstanding is estimated to be around 17%.

Over the years, the MSME book of NBFCs has grown at a similar rate compared with the portfolio at a systemic level, clocking a CAGR of 34% over Fiscals 2018 and 2023. Market share of NBFCs remained stable between Fiscal 2018 and 2019 due to demonetisation and the NBFC liquidity crisis but has increased subsequently. Going forward, CRISIL MI&A expects the market share of NBFCs in this segment is expected to continue to remain in the same range.

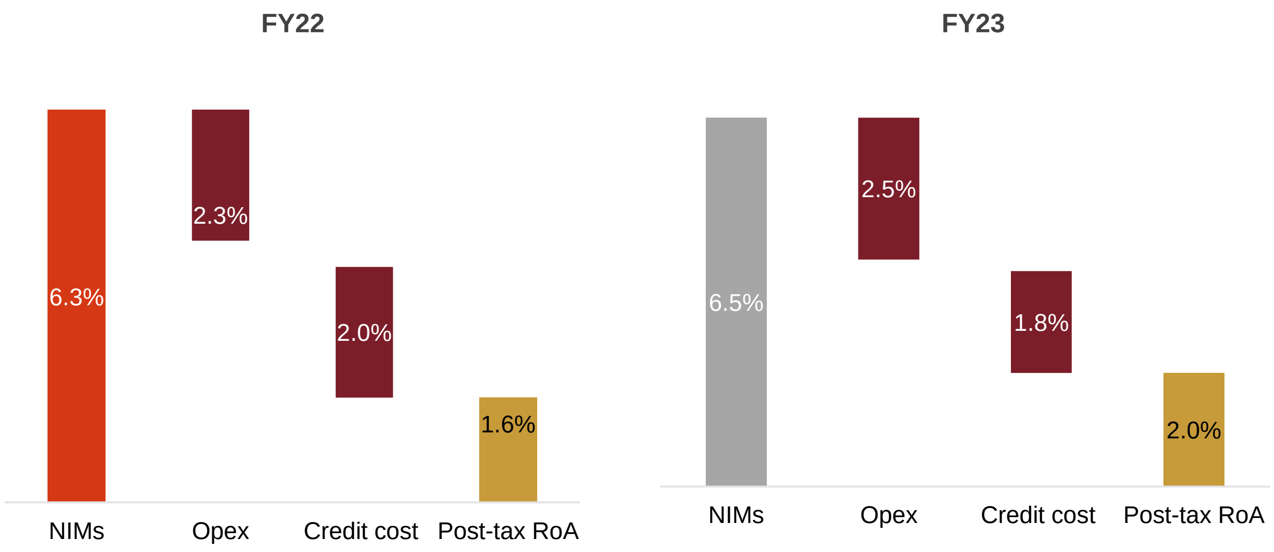
NBFCs share in overall MSME loans at 17% in Fiscal 2023



Source: CRISIL MI&A Estimates

NBFC profitability to improve going forward

NBFCs in MSME segment operate with yield in the range of 17-18%, on an average. With cost of funds being in the range of 10-11%, net interest margins (“**NIMs**”) for this segment are in the range of 6-7%. CRISIL MI&A estimates the profitability in this segment to have increased in Fiscal 2023 owing to better credit costs and increase in interest yields. Going forward, in Fiscal 2024, borrowing costs are expected to stabilise or marginally move upwards, and overall profitability of MSMEs loans is still expected to be sustained, on account of higher interest income. In addition, improvement in collections is expected to lead to aid profitability for the segment.



Source: CRISIL MI&A estimates

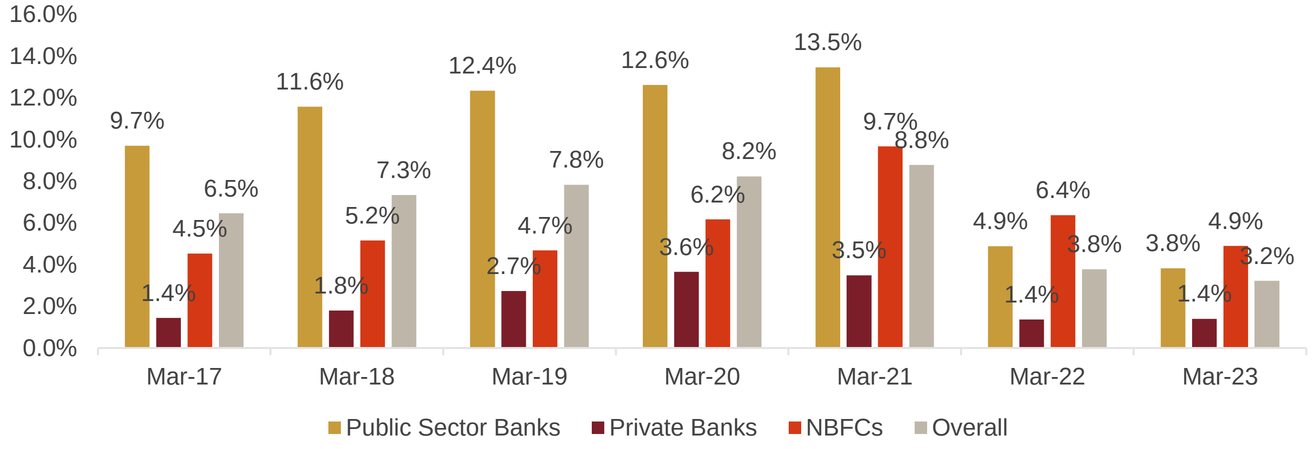
Asset quality for overall MSME at 3.2%; asset quality relatively better for private banks

Asset quality deteriorated as of March 2021 due to COVID-19 where income of the borrowers was impacted which led to rise in GNPA numbers. With continued improvement in economic activity, better collection efficiency and strong credit growth, GNPA level decreased as of March 2022. As of March 2023, the GNPA ratio for overall MSME loans stands at 3.2%.

Asset quality across various players

Among various player groups, the asset quality is the best for private banks as of March 2023. Public Sector banks have the second best asset quality after private sector banks. Private sector banks have better asset quality because they serve relatively low risk customers compared to NBFCs, which also serve customers with no documented income.

Asset quality for overall MSME loans across various players



Source: CRISIL MI&A estimates

Key success factors for NBFCs offering MSME Loans

- **Strong branch network and deep understanding of the target customer segment and markets**: Players need to have a clear and deeper understanding of their target customer segment, the markets they operate in and develop a strong local network.
- **Strong underwriting capabilities**: MSMEs tend to generally be more impacted by vagaries of the business cycle given their limited financial wherewithal and/or reliance on larger buyers
- **On-the-ground presence to manage collections and maintain portfolio quality**: Additionally, given that players in the segment also cater to a relatively riskier profile, a strong focus on collections and monitoring risk of default at customer level is vital to manage asset quality.
- **Collateral risk management**: Properties that are used as collateral for MSME loans sometimes lack proper property titles, especially in the outskirts of large cities, semi-urban and rural areas.

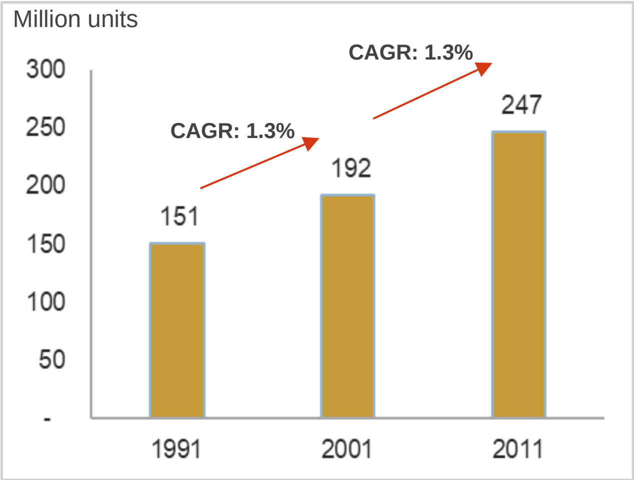
HOUSING LOANS (BELOW ₹ 5 MILLION TICKET SIZE)

Housing scenario in India

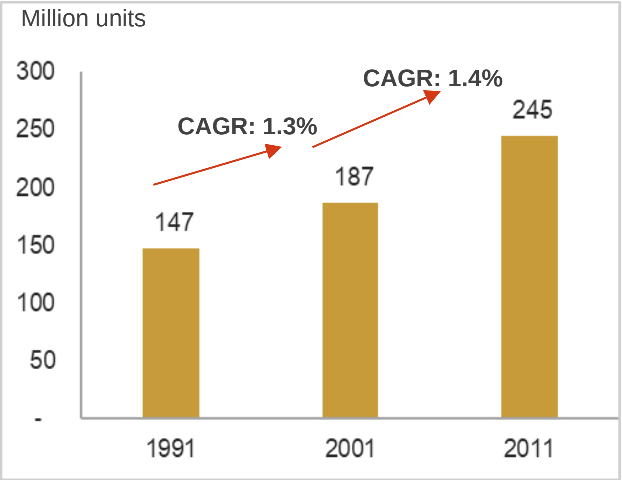
Housing stock

As per Census 2011, the number of households increased to 247 million as of 2011 from 192 million in 2001, at 1.3% CAGR. During the period, housing stock increased from to 245 million units from 187 million units. Of the 245 million units, about 61 million units are obsolete, congested or non-serviceable.

Increment in households



Increment in housing stock



Source: Census 2011, CRISIL MI&A

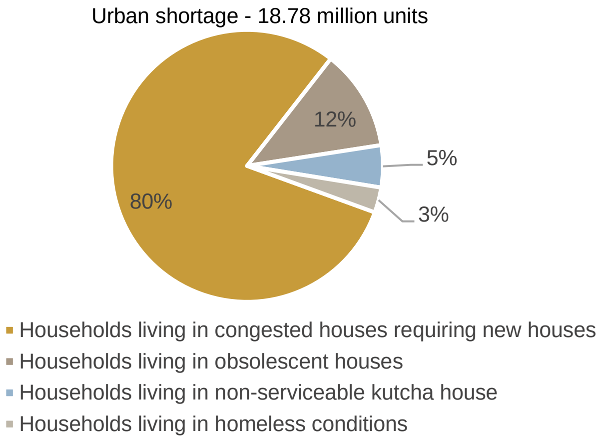
Housing shortage in India

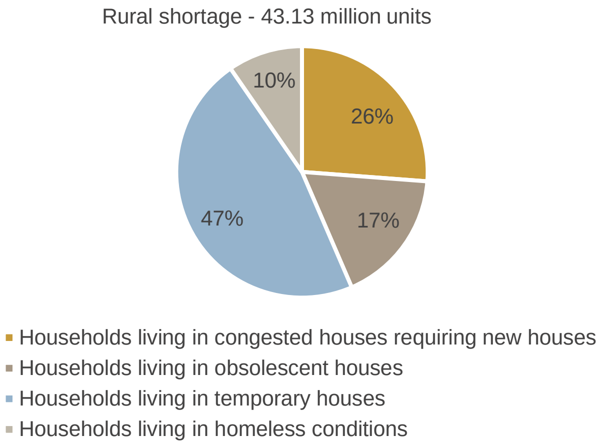
Despite the constant focus on the segment, housing in India is far from adequate. Shortage of housing is a perpetual problem, deterring the economic growth in India.

In the Twelfth Five Year Plan (2012-2017), the Government of India accorded this issue utmost importance and focused on increasing the amount of housing units available in both urban as well as rural areas. As per the estimates of the Twelfth Five Year Plan, housing shortage in the urban segment of the society stood at 18.78 million units. The EWS (Economically Weaker Section) accounts for three-fourths of the shortage and the low Income group ("**LIG**") nearly accounts for a quarter. In 2017, the housing shortage estimate was revised downwards to approximately 10 million units based on assessments carried out since 2011.

The erstwhile Planning Commission and the Ministry of Rural Development, Government of India, have official initiatives to assess the quantum of housing shortage in rural India. As per the estimates of the Twelfth Five Year Plan, housing shortage in the rural segment of society stood at 43.13 million.

Urban and rural housing shortage





Note: The above data is as per the estimates of the Twelfth Five Year Plan (2012-2017)

Source: NHB, CRISIL MI&A

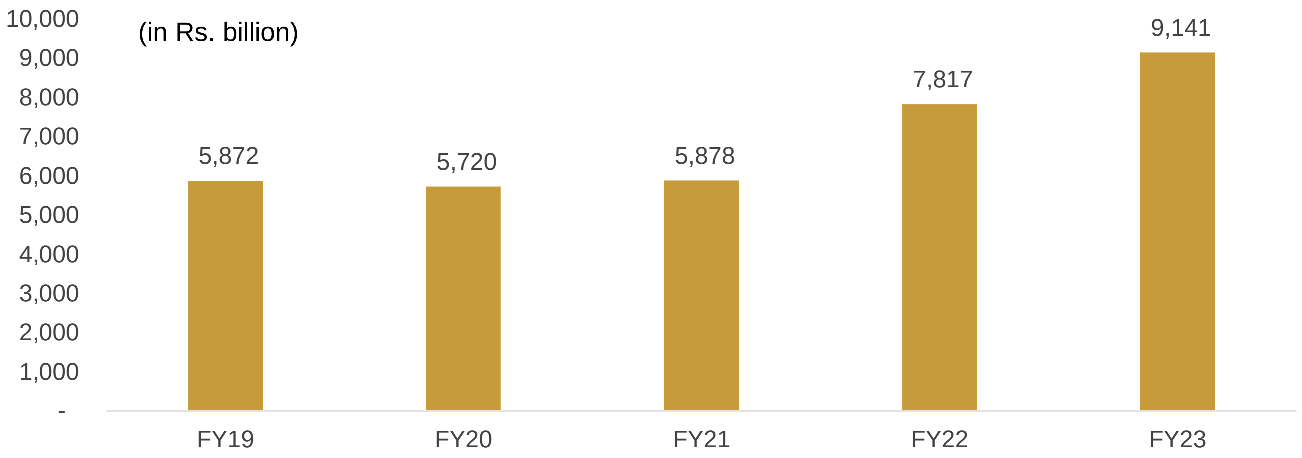
Indian housing finance market to log a CAGR of 13-15% between Fiscal 2023 and Fiscal 2026

The Indian housing finance market clocked a healthy growth in loan outstanding on account of a rise in disposable income, healthy demand emanating from smaller cities markets, attractive interest rates and government impetus on housing. In Fiscal 2021, credit growth for housing loans slowed down following the outbreak of COVID-19. While economy was significantly impacted in the first half of Fiscal 2021, there was a faster than envisaged revival in the second half of Fiscal 2021, with RBI, along with Centre and State governments, providing support. The first quarter of Fiscal 2022 witnessed the second wave of COVID-19 affecting credit growth. However, on account of improved affordability, pent-up demand and historically low interest rates, growth surged in the second half of the fiscal, leading to strong credit growth in Fiscal 2022.

In Fiscal 2020, disbursements remained more or less flat due to a slowdown in economic growth and challenges faced by some HFCs in availing funding post the IL&FS meltdown in September 2018. In March 2020, the industry was affected on account of COVID-19 pandemic induced lockdown, as a significant quantum of disbursements take place in the last month of the fiscal and in the last two weeks of March. In Fiscal 2021, the first quarter was a complete washout due to disruption caused by COVID-19 crisis and the resultant nation-wide lockdown. However, the latent demand for housing in India remained strong, given the vast housing shortage in India and the psychological comfort provided by owning a house post the uncertainty created by the COVID-19 pandemic.

In Fiscal 2023, RBI started increasing repo rates owing to concerns over increasing inflation and its impact on the macro economy amid geopolitical issues. Despite the aggressive rate hikes during the fiscal, credit growth remained intact, with healthy growth by both banks and HFCs/NBFCs. In Fiscal 2024, the credit growth momentum is expected to continue for HFCs/NBFCs, supported by pent-up demand, with affordable HFCs getting back on track, posting robust growth. Within NBFCs/HFCs, larger entities with strong funding profile, parentage and group support are expected to grow strongly and penetrated deeper as well as expand wider to diversify their portfolio, derive synergies and capitalize on operating leverage.

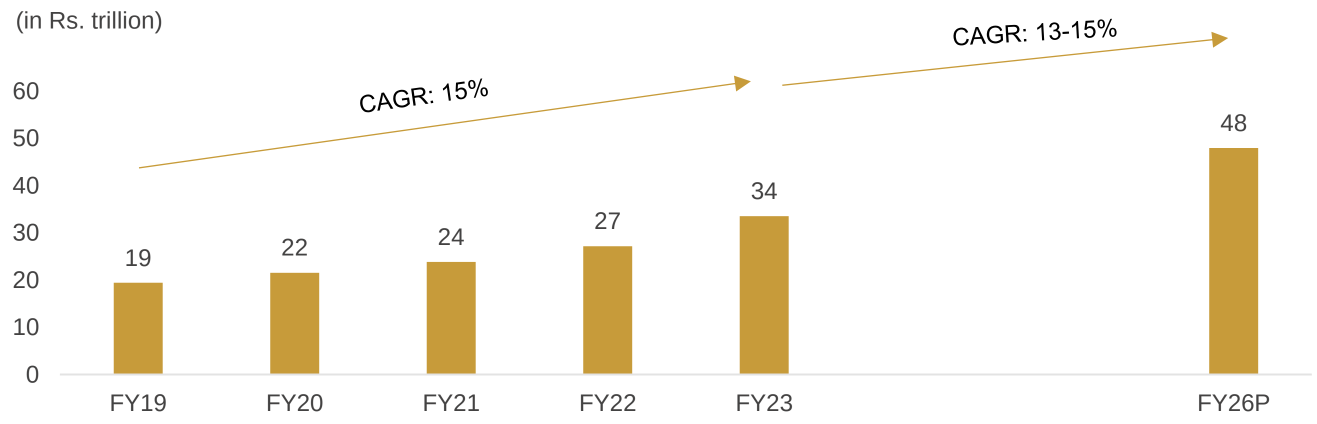
Disbursements of overall housing loans (in ₹ Billion)



Source: CRISIL MI&A Estimates

Between Fiscals 2023 and 2026, housing loan growth is projected to remain healthy at 13-15% CAGR. CRISIL MI&A believes that HFCs are expected to post high double-digit growth after a slowdown in Fiscals 2020 and 2021. In the past, demand for home loans rose due to higher demand from tier II and III cities, rising disposable incomes and government steps, such as interest rate subvention schemes and fiscal incentives. Similarly, the growth trend of housing loans with ticket size less than ₹ 5 million is expected to mimic that of overall housing loans as they constitute almost three-fourths of the overall market.

Growth in housing loans outstanding (₹ trillion)



Source: CRISIL MI&A Estimates

Gold loan lenders have performed well in scenarios of credit squeeze in the economy, while MSME lenders typically witness faster growth in the converse situation. For instance, gold loan market grew faster than the MSME loan market between Fiscal 2019 and 2022 when the economy was impacted by the NBFC liquidity crisis and COVID-19 pandemic. The following table sets forth details of gold and MSME lending for the respective periods:

	FY17	FY18	FY19	FY20	FY21	FY22	FY23E
Gold Loan Market (₹ billion)	2,315	2,508	2,875	3,262	4,709	5,524	6,100
Year-on-year growth (%)	-	8	15	13	44	17	10
MSME Loan Market (₹ trillion)	14	16	17	18	19	21	24
Year-on-year growth (%)	-	14	6	6	6	11	13

Note: E: Estimated, Source: CRISIL MI&A

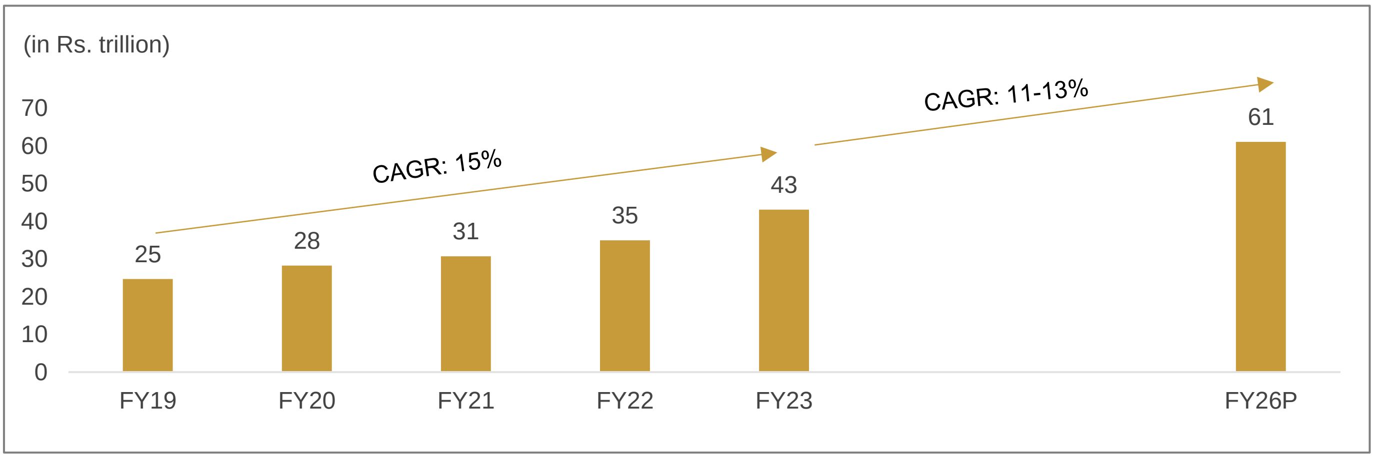
INDIAN MORTGAGE MARKET

Indian mortgage market to witness a CAGR of 11-13% between Fiscal 2023 and Fiscal 2026

The Indian mortgage market (comprising of housing loans and loans against property) logged a steady growth of ~15% over Fiscal 2019 to Fiscal 2023 on account of higher affordability led by rising disposable income, growing urbanisation & nuclearization of families, government measures to push housing sector (including "Housing for all", impetus packages to tackle the pandemic, NHB Refinance scheme etc.), emergence of tier-II and tier-III cities, ease of financing, and widening reach of financiers.

Going forward, CRISIL MI&A expects the mortgage market to witness a healthy 11-13% CAGR between Fiscal 2023 and 2026, propelled by rapid urbanisation, increasing demand from tier-II and tier-III cities, tax and interest rate incentives and government initiatives.

Growth in mortgage market (housing loans and loans against property) (₹ trillion)



Note: Overall mortgage market include Housing and LAP Loans, P- Projected

Source: CRISIL MI&A Estimates

PEER COMPARISON

In this section, CRISIL MI&A has compared the financial and operating performance of NBFCs operating in segments such as gold loans, secured property backed MSME loans and Housing loans in India based on the latest available data for Q1 Fiscal 2024. The players considered for the peer comparison are Aptus Value Housing Finance, Fedbank Financial, HDB Financial Services, IIFL Finance, Manappuram Finance, Muthoot Finance, Repco Home Finance, Five Star Business Finance, SBFC Finance, Veritas Finance, and Vistaar Finance. For analysis, we have classified these peers into segments with Aptus Value Housing Finance and Repco Home Finance in Housing Finance segment, Five Star Business Finance, Veritas Finance, and Vistaar Finance in MSME segment, Fedbank Financial and SBFC Finance in MSME and Gold segment, Manappuram Finance and Muthoot Finance in Gold loans segment and HDB Financial Services and IIFL Finance in Diversified segment.

Fedbank Financial is the fourth fastest NBFC in terms of year on year growth of AUM amongst the peer set as of Q1 Fiscal 2024

Segment	Player	AUM (in Rs billion)			Disbursement (in Rs billion)		
		Q1FY23	Q1FY24	Y-o-Y growth (%)	Q1FY23	Q1FY24	Y-o-Y growth (%)
Housing Finance	Aptus Value Housing	55	71	29%	5	6	23%
	Repco Home Finance	119	127	7%	6	7	7%
MSME	Five-Star Business Finance	53	76	43%	6	11	99%
	Veritas Finance	24	39	61%	NA	NA	-
	Vistaar Finance	NA	NA	NA	NA	NA	-
MSME and Gold	**Fedbank Financial Services**	**67**	**94**	**42%**	**25**	**30**	**16%**
	SBFC Finance	36	53	47%	5	7	32%
Gold loan	Manappuram Finance	308	371	21%	NA	NA	-
	Muthoot Finance	567	676	19%	NA	NA	-
Diversified	HDB Financial Services	NA	736	-	NA	NA	-
	IIFL Finance	528	682	29%	NA	NA	-

Note: NA: Not Available, Source: Company Reports, CRISIL MI&A

Fedbank Financial is the third fastest NBFC in terms of 3-year AUM growth amongst the peer set

Fedbank Financial has the third fastest AUM growth among NBFCs in the peer set in India with three year CAGR of 33% during Fiscals 2020-2023. SBFC Finance and Veritas Finance grew at a faster pace of 44% and 40% respectively during the same time period. In terms of size, however, HDB Financial Services, Muthoot Finance and IIFL Finance are among the largest players in the peer set analysed with each of them having AUM in excess of ₹ 500 billion as of March 2023.

Segment	AUM (Rs billion)	FY16	FY17	FY18	FY19	FY20	FY21	FY22	FY23	CAGR (FY20-23)
Housing Finance	Aptus Value Housing	5	8	14	22	32	41	52	67	28%
	Repco Home Finance	77	89	99	110	118	121	118	124	2%

Segment	AUM (Rs billion)	FY16	FY17	FY18	FY19	FY20	FY21	FY22	FY23	CAGR (FY20-23)
MSME	Five-Star Business Finance	2	5	10	21	39	44	51	69	21%
	Veritas Finance	0.1	1	3	7	13	16	22	35	40%
	Vistaar Finance	8	11	13	14	19	21	24	31	19%
MSME and Gold	**Fedbank Financial Services**	**6**	**10**	**14**	**20**	**38**	**49**	**62**	**91**	**33%**
	SBFC Finance	NA	NA	8	12	16	22	32	49	44%
Gold loan	Manappuram Finance	101	137	158	194	252	272	303	355	12%
	Muthoot Finance	244	273	291	342	416	526	580	632	15%
Diversified	HDB Financial Services	259	343	445	554	588	616	614	701	6%
	IIFL Finance	195	223	311	349	380	447	512	646	19%

Note: NA: Not Available, Source: Company Reports, CRISIL MI&A

Fedbank Financial held a share of 0.26% in the total NBFC credit outstanding as of Fiscal 2023. According to CRISIL MI&A estimates, total NBFC credit as of Fiscal 2023 stood at Rs 35,164 billion. Loans provided by NBFCs typically include mortgage loans, vehicle loans, business loans, gold loans etc.

Segment	Player	Market Share as of FY23
Housing Finance	Aptus Value Housing	0.19%
	Repco Home Finance	0.35%
MSME	Five-Star Business Finance	0.20%
	Veritas Finance	0.10%
	Vistaar Finance	0.09%
MSME and Gold	**Fedbank Financial Services**	**0.26%**
	SBFC Finance	0.14%
Gold loan	Manappuram Finance	1.01%
	Muthoot Finance	1.80%
Diversified	HDB Financial Services	1.99%
	IIFL Finance	1.84%

Note: Market Share calculated on total NBFC credit as of Fiscal 2023; Source: CRISIL MI&A

Fedbank Financial is the third fastest NBFC in terms of 3-year disbursement growth amongst the peer set

Fedbank Financial has the third fastest disbursement growth among the peer set with 3-year CAGR of 35% during Fiscals 2020-2023. SBFC Finance and Veritas Finance witnessed the first and second highest disbursement growth among the peer set with 3-year CAGR of 42% and 39% respectively during Fiscals 2020-2023.

Trend in disbursements for players

Segment	Disbursement (₹ billion)	FY16	FY17	FY18	FY19	FY20	FY21	FY22	FY23	CAGR (FY20-23)

Housing Finance	Aptus Value Housing	3	4	8	11	13	13	16	24	23%
	Repco Home Finance	29	26	28	31	26	18	18	29	4%
MSME	Five-Star Business Finance	1	4	15	15	24	12	18	34	12%
	Veritas Finance	0.1	1	3	6	8	6	12	22	39%
	Vistaar Finance	6	7	7	8	9	6	9	14	15%
MSME and Gold	**Fedbank Financial Services**	**NA**	**NA**	**16**	**20**	**44**	**59**	**75**	**107**	**35%**
	SBFC Finance	NA	NA	3	10	13	15	26	36	42%
Gold loan	Manappuram Finance	NA	NA	NA	NA	NA	NA	NA	NA	NA
	Muthoot Finance	516	576	660	732	966	1,239	1,059	NA	5%*
Diversified	HDB Financial Services	148	192	253	317	299	250	290	NA	-1%*
	IIFL Finance	NA	NA	NA	NA	240	275	383	560	33%

Note: NA = Not available, (*) CAGR is calculated for 2 years from FY20 to FY22.

Source: Company Reports, CRISIL MI&A

Fedbank Financial has the highest Disbursement to AUM ratio amongst the peer set as of Fiscal 2023 and Q1 Fiscal 2024

Fedbank Financial has the highest disbursement to AUM ratio amongst the peer set at 118.5% for Fiscal 2023. Fedbank Financial also has the highest disbursement to AUM ratio amongst the peer set at 31.4% for Q1 Fiscal 2024. Fedbank Financial has the second highest average disbursement to AUM ratio from Fiscal 2020 to Fiscal 2023. This disbursements-to-AUM ratio reflects the focus of the company on expanding its branch network and disbursements over the last few years. Muthoot Finance has the highest average disbursement to AUM ratio from Fiscal 2020 to Fiscal 2023 at 216.8%.

Trend in disbursement to AUM ratio for players

Segment	Player	Disbursement to AUM ratio						
		FY19	FY20	FY21	FY22	FY23	Q1FY24	Avg (FY20-23)
Housing Finance	Aptus Value Housing	50.0%	40.6%	31.7%	30.9%	35.5%	9.1%	34.7%
	Repco Home Finance	28.2%	22.0%	14.9%	15.3%	23.4%	5.4%	18.9%
MSME	Five-Star Business Finance	71.4%	61.5%	27.3%	34.7%	49.0%	14.9%	43.1%
	Veritas Finance	85.7%	61.5%	37.5%	54.5%	63.5%	NA	54.3%
	Vistaar Finance	57.1%	47.4%	28.6%	37.2%	44.2%	NA	39.4%
MSME and Gold	**Fedbank Financial Services**	**100.0%**	**115.8%**	**121.2%**	**120.7%**	**118.5%**	**31.4%**	**119.5%**
	SBFC Finance	82.0%	76.9%	67.6%	80.5%	73.5%	12.3%	74.6%
Gold loan	Manappuram Finance	NA	NA	NA	NA	NA	NA	NA
	Muthoot Finance	214.0%	232.2%	235.6%	182.6%	NA	NA	216.8%*
Diversified	HDB Financial Services	57.2%	50.9%	40.6%	47.2%	NA	NA	46.2%*
	IIFL Finance	NA	63.2%	61.5%	74.8%	86.6%	NA	71.5%

Note: NA = Not available, (*) Average calculated from FY20-FY22.

Source: Company Reports, CRISIL MI&A

Operational analysis

Fedbank Financial has the fastest growth in terms of branches amongst the peer set

Fedbank Financial has been in expansionary mode and has increased its branch network from 300 branches to 575 branches over the course of Fiscals 2020-2023, registering the fastest CAGR in branches amongst the peers analysed over this timeframe. It is followed by IIFL Finance and Five Star Business Finance, which grew at a pace of 21% and 14% annually, respectively, during the same time period. As of Fiscal 2023, Manappuram Finance had the highest number of branches at 5,232.

Trend in number of branches for players

Segment	Branches	FY16	FY17	FY18	FY19	FY20	FY21	FY22	FY23	Q1FY24	CAGR (FY20-23)
Housing Finance	Aptus Value Housing	70	80	115	143	175	190	208	231	231	10%
	Repco Home Finance	150	156	160	170	177	177	179	192	193	3%
MSME	Five-Star Business Finance	73	103	130	173	252	262	300	373	386	14%
	Veritas Finance	17	43	72	147	202	204	229	287	NA	12%
	Vistaar Finance	198	201	225	220	216	191	193	211	205	-1%
MSME and Gold	**Fedbank Financial Services**	**112**	**107**	**123**	**152**	**300**	**359**	**516**	**575**	**584**	**24%**
	SBFC Finance	NA	NA	65	91	96	124	135	152	162	17%
Gold loan	Manappuram Finance	3,293	4,152	4,197	4,351	4,622	4,637	5,057	5,232	5,281	4%
	Muthoot Finance	4,275	4,307	4,325	4,480	4,567	4,632	4,617	4,739	4,742	1%
Diversified	HDB Financial Services	929	1,151	1,165	1,349	1,468	1,319	1,374	1,492	1,581	1%
	IIFL Finance	1,000	1,112	1,378	1,947	2,377	2,563	3,296	4,200	NA	21%

Note: NA: Not Available, Source: Company Reports, CRISIL MI&A

Fedbank Financial has the fourth fastest growth in terms of employees amongst the peer set

Fedbank Financial has increased its employee strength from 1,890 to 3,570 over the course of Fiscals 2020-2023, registering the fourth fastest CAGR of 24% in employee growth amongst the peers analysed over this timeframe. SBFC Finance, Veritas Finance and Five Star Business Finance have employee CAGR growth of 35%, 34% and 25% respectively over the same time, thereby growing at a faster rate than Fedbank Financial. As of Fiscal 2023, HDB Financial Services recorded the highest number of employees at 117,162.

Trend in number of employees for players

Segment	Employees	FY16	FY17	FY18	FY19	FY20	FY21	FY22	FY23	Q1FY24	CAGR (FY20-23)
Housing Finance	Aptus Value Housing	401	650	1,000	1,300	1,702	1,913	2,271	2,405	NA	12%
	Repco Home Finance	619	670	785	929	994	977	925	951	954	-1%
MSME	Five-Star Business Finance	293	691	1,290	1,971	3,734	3,938	5,675	7,347	7,538	25%
	Veritas Finance	NA	NA	719	1,422	1,850	2,333	2,727	4,432	NA	34%
	Vistaar Finance	2,125	2,337	2,107	2,188	1,847	1,660	2,024	2,446	NA	5%
MSME and Gold	**Fedbank Financial Services**	**NA**	**484**	**590**	**964**	**1,890**	**2,130**	**2,852**	**3,570**	**3,732**	**24%**
	SBFC Finance	NA	NA	585	802	1,153	1,471	2,048	2,822	3,136	35%

Segment	Employees	FY16	FY17	FY18	FY19	FY20	FY21	FY22	FY23	Q1FY24	CAGR (FY20-23)
Gold loan	Manappuram Finance	16,693	18,933	24,886	25,610	27,726	30,522	26,970	30,612	NA	3%
	Muthoot Finance	22,781	24,205	23,455	24,224	25,554	25,911	26,716	27,273	27,701	2%
Diversified	HDB Financial Services	16,508	65,906	74,049	93,373	109,167	104,960	121,595	117,162	NA	2%
	IIFL Finance	12,000	11,432	15,000	16,799	18,569	19,825	28,325	33,910	NA	24%

Note: NA = Not available.

Source: Company Reports, CRISIL MI&A

Operational Efficiency of the peer set

Repco Home Finance is the most efficient NBFC amongst the peer set with AUM per branch of ₹ 656 million as of June 2023 followed by HDB Financial Services (₹ 465 million) and SBFC Finance (₹ 329 million). Fedbank Financial has an AUM per branch of ₹ 162 million as of June 2023. The AUM per branch has, however, to be viewed in the context of the vintage of branches. Fedfina, for example, has more than tripled its branch network from 152 branches as of March 2019 to 584 branches by June 2023, and hence, most of its branches have still not reached the mature stage.

Operational efficiency for players (Q1 Fiscal 2024)

Segment	Player	AUM per branch(1) (₹ million)							Disbursement per branch(2) (₹ million)						
		FY19	FY20	FY21	FY22	FY23	Q1FY24	Avg (FY 20-23)	FY19	FY20	FY21	FY22	FY23	Q1FY24	Avg (FY 20-23)
Housing Finance	Aptus Value Housing	157	182	214	249	292	308	234	83	73	68	79	104	28	81
	Repco Home Finance	649	668	685	657	648	656	665	182	148	104	99	152	35	126
MSME	Five-Star Business Finance	122	154	170	169	185	196	170	87	95	48	59	91	29	73
	Veritas Finance	51	64	77	96	123	NA	90	41	40	30	52	78	NA	50
	Vistaar Finance	66	87	108	125	148	NA	117	36	42	30	47	66	NA	46
MSME and Gold	**Fedbank Financial Services**	**132**	**128**	**135**	**120**	**158**	**162**	**135**	**132**	**146**	**164**	**145**	**187**	**51**	**160**
	SBFC Finance	127	172	179	236	325	329	237	104	132	121	190	239	40	171
Gold loan	Manappuram Finance	45	55	59	60	68	70	80	NA	NA	NA	NA	NA	NA	NA
	Muthoot Finance	76	91	114	126	133	143	116	163	212	267	229	NA	NA	236*
Diversified	HDB Financial Services	411	401	467	447	470	465	446	235	203	189	211	NA	NA	201*
	IIFL Finance	179	160	174	155	154	NA	161	NA	101	107	116	133	NA	114

*Note: NA = Not available, * Average is calculated for 3 years from FY19 to FY22, (1) AUM per branch: AUM at the end of the financial year divided by number of branches at the end of the financial year, (2) Disbursement per branch: Disbursement at the end of the financial year divided by number of branches at the end of the financial year.*

Source: Company Reports, CRISIL MI&A

Fedbank Financial is the second most efficient NBFC in terms of average AUM per employee amongst the peer set

Repco Home Finance is the most efficient NBFC amongst the peer set with AUM per employee of ₹ 133 million as of June 2023 followed by Fedbank Financial (₹ 25 million) and Muthoot Finance (₹ 24 million).

Operational efficiency for players (Q1 Fiscal 2024)

Segment	Player	AUM per employee[1] (₹ million)							Disbursement per employee[2] (₹ million)						
		FY19	FY20	FY21	FY22	FY23	Q1FY24	Avg (FY 20-23)	FY19	FY20	FY21	FY22	FY23	Q1FY24	Avg (FY 20-23)
Housing Finance	Aptus Value Housing	17	19	21	23	28	NA	23	9	8	7	7	10	NA	8
	Repco Home Finance	118	119	124	127	131	133	125	33	26	19	19	31	7	24
MSME	Five-Star Business Finance	11	10	11	9	9	10	10	8	6	3	3	5	1	4
	Veritas Finance	5	7	7	8	8	NA	7	4	5	3	4	5	NA	4
	Vistaar Finance	7	10	12	12	13	NA	12	3	5	3	4	6	NA	5
MSME and Gold	**Fedbank Financial Services**	**21**	**20**	**23**	**22**	**25**	**25**	**23**	**21**	**23**	**28**	**26**	**30**	**8**	**27**
	SBFC Finance	14	14	15	16	18	17	16	12	11	10	13	NA	2	11
Gold loan	Manappuram Finance	8	9	9	11	12	NA	10	NA	NA	NA	NA	NA	NA	NA
	Muthoot Finance	14	16	20	22	23	24	20	30	38	48	40	NA	NA	42*
Diversified	HDB Financial Services	6	5	6	5	6	NA	6	3	3	2	2	NA	NA	3*
	IIFL Finance	21	20	23	18	19	NA	20	NA	13	14	13	17	NA	14

*Note: NA = Not available, * Average is calculated for 3 years from FY20 to FY22, (1) AUM per employee: AUM at the end of the financial year divided by number of employees at the end of the financial year, (2) Disbursement per employee: Disbursement at the end of the financial year divided by number of employees at the end of the financial year.*

Source: Company Reports, CRISIL MI&A

Fedbank Financial has the second highest disbursements per employee amongst the peer set in Fiscal 2023

Repco Home Finance has the highest disbursement per employee of ₹ 31 million followed by Fedbank Financial at ₹ 30 million in Fiscal 2023.

Fedbank Financial's cost to income ratio reflects it is in process of expansion

Fedbank Financial's cost-to-income ratio of 58.6% is much higher than the peers analysed. This can be attributed to Fedbank being in expansionary mode and adding several branches in the last few years. Consequently, its opex is also relatively higher at 5.6% as of Fiscal 2023. HDB Financial Services and Veritas Finance has a relatively higher opex of 7.5% and 6.9% respectively, as compared to Fedbank Financial.

Operational efficiency for players (Q1 Fiscal 2024)

Segment	Player	Cost to income ratio[1]							Opex to total assets[2] (%)						
		FY19	FY20	FY21	FY22	FY23	Q1 FY24	Avg (FY 20-23)	FY19	FY20	FY21	FY22	FY23	Q1 FY24	Avg (FY 20-23)
Housing Finance	Aptus Value Housing	30.4%	26.1%	21.8%	18.5%	19.4%	15.6%	21.6%	3.6%	2.9%	2.4%	2.3%	2.6%	0.6%	2.6%
	Repco Home Finance	20.7%	20.2%	19.6%	20.1%	24.4%	23.9%	21.1%	1.0%	0.9%	0.9%	1.0%	1.2%	NA	1.0%
MSME	Five-Star Business Finance	32.1%	30.1%	29.5%	32.0%	34.7%	32.6%	31.6%	6.1%	5.1%	4.2%	5.0%	5.8%	1.4%	5.1%
	Veritas Finance	67.1%	65.2%	49.0%	48.9%	45.5%	50.0%	52.2%	8.8%	7.6%	5.8%	6.4%	6.9%	2.0%	6.7%
	Vistaar Finance	57.3%	53.1%	43.8%	50.8%	51.2%	49.9%	49.7%	8.8%	7.5%	5.2%	5.5%	5.6%	NA	6.0%

Segment	Player	Cost to income ratio[1]							Opex to total assets[2] (%)						
		FY19	FY20	FY21	FY22	FY23	Q1 FY24	Avg (FY 20-23)	FY19	FY20	FY21	FY22	FY23	Q1 FY24	Avg (FY 20-23)
MSME and Gold	**Fedbank Financial Services**	**61.8%**	**70.6%**	**61.1%**	**58.3%**	**58.6%**	**59.5%**	**62.2%**	**4.8%**	**6.0%**	**4.9%**	**5.2%**	**5.6%**	**1.3%**	**5.4%**
	SBFC Finance	72.3%	54.7%	45.9%	57.0%	49.7%	48.4%	51.8%	5.8%	3.7%	3.0%	4.0%	4.5%	1.2%	3.8%
Gold loan	Manappuram Finance	47.6%	39.6%	30.3%	42.7%	47.4%	45.1%	40.0%	7.1%	5.7%	4.3%	5.1%	5.6%	NA	5.2%
	Muthoot Finance	33.2%	30.0%	25.9%	24.6%	30.9%	28.6%	27.9%	4.5%	4.0%	3.1%	2.7%	3.0%	0.8%	3.2%
Diversified	HDB Financial Services	56.2%	56.5%	49.5%	52.2%	55.5%	55.6%	53.4%	6.0%	6.5%	5.7%	6.7%	7.5%	1.8%	6.6%
	IIFL Finance	49.7%	63.6%	39.3%	40.7%	49.5%	52.9%	48.3%	8.1%	4.9%	3.6%	4.4%	5.5%	NA	4.6%

Note: (1) Cost to income ratio: operating expenses for the relevant fiscal year to the sum of net interest income (interest earned minus interest expended) and other income for the relevant fiscal year, expressed as a percentage, (2) Opex to total assets: operating expenses for the relevant fiscal year to the average total assets for the relevant fiscal year, expressed as a percentage

Source: Company Reports, CRISIL MI&A

Fedbank Financial has the lowest opex to disbursement ratio as of Fiscal 2023 amongst MSME peers considered

IIFL Finance had the lowest opex to disbursement ratio for Fiscal 2023 at 2.3% within the peer set considered. When compared to peers engaged in MSME lending, Fedbank Financial had the second lowest opex to AUM ratio of 4.8% for Fiscal 2023 after SBFC Finance (4.7%). In addition, the ratio for Fedbank Financial was also lower in comparison to housing finance peers.

Opex to AUM and opex to disbursement ratio for players (Q1 Fiscal 2024)

Segment	Player	Opex to AUM ratio[1]							Opex to Disbursement ratio[2]						
		FY19	FY20	FY21	FY22	FY23	Q1FY24	Avg (FY 20-23)	FY19	FY20	FY21	FY22	FY23	Q1FY24	Avg (FY20-23)
Housing Finance	Aptus Value Housing	3.0%	2.8%	2.4%	2.3%	2.5%	0.6%	2.5%	6.1%	6.9%	7.5%	7.1%	6.9%	6.8%	7.2%
	Repco Home Finance	0.9%	0.9%	0.9%	1.1%	1.2%	0.3%	1.0%	3.2%	4.1%	6.2%	7.0%	5.0%	5.7%	5.6%
MSME	Five-Star Business Finance	5.1%	4.4%	4.8%	6.0%	6.3%	1.7%	5.4%	7.2%	7.1%	17.2%	17.4%	12.9%	11.2%	13.7%
	Veritas Finance	9.1%	8.5%	7.5%	7.0%	6.6%	2.1%	7.4%	12.1%	13.2%	19.1%	13.0%	10.4%	NA	13.9%
	Vistaar Finance	8.8%	7.0%	5.4%	5.8%	5.5%	NA	5.9%	16.7%	14.6%	19.4%	15.6%	12.5%	NA	15.5%
MSME and Gold	**Fedbank Financial Services**	**4.1%**	**4.6%**	**4.8%**	**5.1%**	**4.8%**	**1.3%**	**4.8%**	**4.4%**	**4.3%**	**4.0%**	**4.2%**	**4.0%**	**4.1%**	**4.1%**
	SBFC Finance	7.9%	6.7%	5.6%	5.5%	4.7%	1.3%	5.6%	9.6%	8.7%	8.3%	6.9%	6.3%	10.4%	7.6%
Gold loan	Manappuram Finance	5.9%	4.7%	3.9%	4.5%	4.4%	NA	4.4%	NA	NA	NA	NA	NA	NA	NA
	Muthoot Finance	4.5%	4.3%	3.4%	3.1%	3.4%	0.8%	3.5%	2.1%	1.8%	1.4%	1.7%	NA	NA	1.7%*
Diversified	HDB Financial Services	5.5%	6.4%	5.7%	6.8%	7.0%	1.7%	6.5%	9.6%	12.6%	14.0%	14.4%	NA	NA	13.7%*
	IIFL Finance	2.3%	2.4%	1.7%	2.0%	2.0%	0.5%	2.0%	NA	3.4%	2.7%	2.6%	2.3%	NA	2.9%

*Note: NA = Not available, 1) Opex to AUM ratio is calculated as operating expenses for the fiscal year divided by AUM as of end of fiscal year, 2) Opex to Disbursement ratio is calculated as operating expenses for the fiscal year divided by disbursements for the fiscal year, 3) *: Average is calculated for 3 years from FY20 to FY22*

Source: Company Reports, CRISIL MI&A

Fedbank Financial's share of new to credit customers low as compared to peers

Fedbank Financial's share of new to credit customers (7%) is low as compared to peers. The average ticket size is typically low for MSME and gold loan focused players. Granularity of the book provides competitive advantage to the businesses since it minimizes the unit risk.

Average ticket size for peers (as of June 2023)

Segment	FY23	Average ticket size (₹ Million)	Average LTV	Share of New to credit
Housing Finance	Aptus Value Housing Finance	1.00	<50%**	38%
	Repco Home Finance	1.20	<70%	NA
MSME	Five-Star Business Finance	0.34	38%	NA
	Veritas Finance	0.20^	45%	NA
	Vistaar Finance$	0.68	45%	NA
MSME and Gold	**Fedbank Financial Services**	**0.13**	**59%**	**7%**
	SBFC Finance$$	0.98	42%	8%
Gold loan	Manappuram Finance^	0.06	64%	NA
	Muthoot Finance	0.07*	68%	NA
Diversified	HDB Financial Services	NA	NA	NA
	IIFL Finance^^	0.73	70%*	NA

Note: NA = Not available, (*) for fiscal 2023;; (^) for Gold Loan; (^^) For LAP loans; (**) As of September 2022, ($) Data as for Vistaar Saral Business Loan as of Fiscal 2023, ($$) Data for secured MSME loans
Source: Company Reports, CRISIL MI&A

Many players tend to have geographically concentrated portfolios; Fedbank Financial has the second lowest share of top state amongst the peer set

It is observed that most of the players in the considered peer set have a significant portion of their portfolio (between 37-56%) emanating from the largest state in their respective portfolios. Fedbank Financial had the second lowest proportion of AUM emanating from the largest state in its portfolio (19% from Karnataka as of June 2023), next to SBFC (17% from Karnataka as of March 2023) amongst the peers analysed.

State-wise distribution of AUM (as of June 2023)

Segment	FY23	Share of top state	Name of top 5 states
Housing Finance	Aptus Value Housing Finance	42%	Tamil Nadu (42%), Andhra Pradesh (36%), Telangana (14%), Karnataka (8%), Odisha (0%)
	Repco Home Finance	57%	Tamil Nadu (57%), Karnataka (13%), Maharashtra (9%), Andhra Pradesh (6%) and Telangana (5%)
MSME	Five-Star Business Finance	34%	Tamil Nadu (34%), Andhra Pradesh (30%), Telangana (20%), Karnataka (7%) and Madhya Pradesh (5%)
	Veritas Finance*	42%	Tamil Nadu (42%), West Bengal (17%), Telangana (10%), Andhra Pradesh (10%) and Karnataka (7%).
	Vistaar Finance**	37%	Tamil Nadu (37%), Karnataka (23%), Andhra Pradesh (11%), Maharashtra (7%)
MSME and Gold	**Fedbank Financial Services**	**19%**	**Maharashtra (19%), Karnataka (18%), Tamil Nadu (16%), Delhi (12%), Gujarat (12%)**
	SBFC Finance*	17%	Karnataka (17%), Uttar Pradesh (16%), Telangana (13%), Maharashtra (11%), Madhya Pradesh (7%)

Segment	FY23	Share of top state	Name of top 5 states
Gold loan	Manappuram Finance	NA	NA
	Muthoot Finance	NA	South (48%), North (23%), West (19%), East (10%)
Diversified	HDB Financial Services	NA	NA
	IIFL Finance*^^	NA	West (39%), North (35%), South (21%), East (5%)

*Note: NA = Not available; * For Fiscal 2023, ** For Fiscal 2022, ^^ For LAP loan.*

Source: Company Reports, CRISIL MI&A

Profitability analysis

Five Star Business Finance and Veritas Finance have the highest NIMs compared to its peers as of Q1FY24

Five Star Business Finance and Veritas Finance have the highest NIMs of 16.6% and 14.8%, respectively as compared to the peers analysed, while Fedbank Financial Services has a NIMs of 7.7%, as of Q1FY24.

Muthoot Finance has the lowest cost of borrowings amongst the peer set analysed as of Q1FY24

Muthoot Finance has the lowest cost of borrowings of 8.4% as of Q1FY24 amongst the peer set followed by Manappuram Finance at 8.5%. Fedbank Financial Services incurs 8.9% as cost of borrowings as of Q1FY24.

HDB Financial Services and Muthoot Finance have the highest RoE as of Q1FY24

HDB Financial Services has the highest RoE of 19.4% as of Q1FY24 amongst the peer set followed by Muthoot Finance at 18.5%. Fedbank Financial Services reported RoE of 15.6% as of Q1FY24.

Yield on advances, Net Interest Margins, Cost of borrowings, Return on assets and Return on equity for players (Q1FY24)

Segment	Player	Q1FY24^				
		Yield on advances (%)	NIMs (%)	Cost of borrowings (%)	RoA (%)	RoE (%)
Housing Finance	Aptus Value Housing	17.5%	11.5%	8.6%	7.7%	16.9%
	Repco Home Finance	NA	NA	NA	NA	NA
MSME	Five-Star Business Finance	25.9%	16.6%	9.0%	8.3%	16.6%
	Veritas Finance	NA	14.8%	NA	4.4%	NA
	Vistaar Finance	NA	NA	NA	NA	NA
MSME and Gold	**Fedbank Financial Services**	**15.7%**	**7.7%**	**8.9%**	**2.3%**	**15.6%**
	SBFC Finance	16.5%	7.8%	9.3%	3.2%	10.3%
Gold loan	Manappuram Finance	NA	NA	8.5%	NA	16.7%
	Muthoot Finance	18.2%*	10.3%	8.4%	5.3%	18.5%
Diversified	HDB Financial Services	19.9%*	8.3%	NA	3.1%	19.4%
	IIFL Finance	NA	NA	NA	NA	NA

*Note: ^Q1FY24 figures have been annualised; *Yield on advances calculated on total interest income; NA = Not available*

Source: Company Reports, CRISIL MI&A

Five Star Business Finance and Veritas Finance have the highest NIMs compared to its peers

Five Star Business Finance and Veritas Finance have the highest NIMs of 16.4% and 14.4%, respectively, in Fiscal 2023 as compared to the peers analysed. Fedbank Financial has the fourth lowest NIMs of 8.4%, reflecting the relatively lower yields given the customer profile catered to.

Yield on advances and Net Interest Margins for players (Fiscal 2023)

Segment	Player	Yield on advances (%)							NIMs (%)				
		FY19	FY20	FY21	FY22	FY23	Avg (FY 20-23)	FY19	FY20	FY21	FY22	FY23	Avg (FY 20-23)
Housing Finance	Aptus Value Housing	17.2%	17.6%	17.2%	17.2%	17.7%	17.5%	10.3%	9.9%	10.2%	11.4%	12.2%	10.9%
	Repco Home Finance	11.4%	11.7%	11.5%	10.9%	10.8%	11.2%	4.3%	4.3%	4.5%	4.7%	4.5%	4.5%
MSME	Five-Star Business Finance	24.3%	24.2%	24.3%	24.7%	24.5%	24.6%	18.0%	15.8%	13.6%	14.9%	16.4%	15.2%
	Veritas Finance	22.1%	24.9%	23.4%	22.4%	22.6%	23.3%	10.2%	10.5%	11.3%	12.3%	14.4%	12.1%
	Vistaar Finance	21.6%	20.7%	19.2%	18.6%	18.1%	19.2%	14.0%	12.2%	10.0%	9.5%	9.1%	10.2%
MSME and Gold	Fedbank Financial Services	13.6%	14.9%	15.5%	15.6%	15.2%	15.3%	6.5%	7.2%	7.2%	7.9%	8.4%	7.7%
	SBFC Finance	15.7%	15.9%	15.3%	15.1%	16.1%	15.6%	6.5%	5.5%	5.3%	5.8%	7.4%	6.0%
Gold loan	Manappuram Finance	24.2%	25.0%	25.1%	20.6%	19.7%	22.7%	14.6%	14.0%	13.8%	12.0%	11.5%	12.8%
	Muthoot Finance	21.0%	22.1%	21.2%	19.0%	16.4%	19.8%	13.1%	13.0%	11.6%	10.6%	9.3%	11.2%
Diversified	HDB Financial Services	13.7%	14.8%	14.5%	14.3%	14.3%	14.5%	6.7%	7.1%	7.5%	8.1%	8.2%	7.7%
	IIFL Finance	44.3%	17.7%	20.0%	23.8%	24.4%	21.7%	15.0%	6.8%	7.3%	8.6%	8.5%	7.8%

Source: Company Reports, CRISIL MI&A

Fedbank Financial has the second lowest cost of borrowings amongst the MSME, Gold loan and MSME & Gold loan peer set in fiscal 2023

Fedbank Financial has the second lowest cost of borrowings of 7.8% in Fiscal 2023 amongst the MSME, gold loan and MSME & Gold loan peer set, after Muthoot Finance at 7.4%. Amongst the overall peer set, Fedbank Financial has the fourth lowest cost of borrowing among overall NBFC peer set in India in Fiscal 2023.

Cost of Borrowings for players (Fiscal 2023)

Segment	Cost of borrowings (%)	FY19	FY20	FY21	FY22	FY23	Average (FY20-23)
Housing Finance	Aptus Value Housing	9.5%	10.2%	9.1%	8.0%	8.5%	9.0%
	Repco Home Finance	8.2%	8.5%	8.0%	6.9%	7.1%	7.6%
MSME	Five-Star Business Finance	10.1%	13.1%	11.2%	10.0%	7.8%	10.5%
	Veritas Finance	9.0%	13.2%	10.7%	10.5%	9.3%	11.0%
	Vistaar Finance	11.0%	10.8%	10.2%	9.2%	9.3%	9.9%
MSME and Gold	**Fedbank Financial Services**	**8.3%**	**8.3%**	**8.3%**	**7.4%**	**7.8%**	**8.0%**
	SBFC Finance	7.8%	12.5%	8.2%	7.7%	8.3%	9.2%
Gold loan	Manappuram Finance	8.9%	9.2%	9.7%	7.8%	8.1%	8.7%
	Muthoot Finance	9.3%	8.7%	8.9%	8.0%	7.4%	8.3%
Diversified	HDB Financial Services	8.2%	8.6%	7.8%	6.7%	6.8%	7.5%

Segment	Cost of borrowings (%)	FY19	FY20	FY21	FY22	FY23	Average (FY20-23)
	IIFL Finance	8.9%	9.1%	10.1%	9.9%	8.7%	9.5%

Source: Company Reports, CRISIL MI&A

Repco Home Finance and Fedbank Financial are the only long term AA rated players amongst the peer set which have cost of borrowings less than 8.5% between Fiscal 2019 to Fiscal 2023

Repco Home Finance and Fedbank Financial are the only long term AA rated players amongst the peer set which have cost of borrowings less than 8.5% between Fiscal 2019 to Fiscal 2023. Repco Home Finance (7.1%) was followed by Muthoot Finance (7.4%), Fedbank Financial (7.8%) and Five-Star Business Finance (7.8%) in terms of cost of borrowings amongst long term AA rated peer set as of fiscal 2023. As of Fiscal 2023, other long term AA rated players like Manappuram Finance (8.1%), Aptus Value Housing (8.5%) and IIFL Finance (8.7%) had relatively higher cost of borrowings.

Short-term and long-term credit ratings of players (as of September 2023)

Segment	Player	Short-term credit rating	Long term credit rating
Housing Finance	Aptus Value Housing Finance	NA	ICRA AA-, CARE AA-
	Repco Home Finance	CARE A1+, ICRA A1+	CARE AA-, ICRA AA-
MSME	Five-Star Business Finance	CARE A1+	ICRA AA-, IND AA-, CARE AA-
	Veritas Finance	CARE A1+	CARE A
	Vistaar Finance	ICRA A1	ICRA A, IND A
MSME and Gold	**Fedbank Financial Services**	**CRISIL A1+, ICRA A1+, CARE A1+**	**CARE AA, IND AA-,**
	SBFC Finance	NA	IND A+, ICRA A+, CARE A+
Gold loan	Manappuram Finance	CRISIL A1+, CARE A1+	CRISIL AA, CARE AA
	Muthoot Finance	CRISIL A1+, ICRA A1+	CRISIL PPMLD AA+, /CRISIL AA+/, ICRA AA+
Diversified	HDB Financial Services	CRISIL A1+, CARE A1+	CRISIL AAA/CRISIL PPMLD AAA, CARE AAA
	IIFL Finance	ICRA A1+, CRISIL A1+	ICRA AA, CARE AA, BWR AA+, CRISIL AA/CRISIL PPMLD AA

Note: NA = Not available.

Source: Company Reports, CRISIL MI&A

Comparison of RoA and RoE amongst peer set as of Fiscal 2023

HDB Financial Services has the highest RoE of approximately 18.7% in Fiscal 2023 followed by IIFL finance at 16.9% and Aptus Value Housing at 16.1%. In terms of RoA, Five-Star ranks the highest with RoA of 8.0% as of Fiscal 2023.

RoE and RoA for players (Fiscal 2023)

Segment	Player	RoA (%)						RoE (%)					
		FY19	FY20	FY21	FY22	FY23	Avg (FY20-23)	FY19	FY20	FY21	FY22	FY23	Avg (FY20-23)
Housing Finance	Aptus Value Housing	5.9%	7.0%	6.5%	7.3%	7.8%	7.1%	17.4%	17.5%	14.5%	15.1%	16.1%	15.8%
	Repco Home Finance	2.3%	2.4%	2.4%	1.6%	2.4%	2.2%	16.5%	16.9%	15.0%	8.9%	12.5%	13.3%
MSME	Five-Star Business Finance	8.9%	7.8%	7.1%	7.5%	8.0%	7.6%	16.0%	15.8%	16.8%	15.0%	15.0%	15.7%
	Veritas Finance	2.7%	2.3%	3.1%	3.1%	5.2%	3.4%	6.7%	5.3%	7.3%	6.6%	11.8%	7.7%
	Vistaar Finance	2.3%	2.5%	3.0%	2.9%	3.2%	2.9%	5.8%	7.3%	9.6%	10.0%	12.0%	9.7%
MSME and Gold	Fedbank Financial Services	2.0%	1.3%	1.3%	1.7%	2.3%	1.6%	10.1%	6.8%	8.1%	10.4%	14.4%	9.9%
	SBFC Finance	1.5%	1.2%	2.0%	1.5%	2.9%	1.9%	2.8%	3.8%	7.7%	5.2%	9.9%	6.6%
Gold loan	Manappuram Finance	4.9%	5.9%	6.9%	5.0%	4.5%	5.6%	19.3%	25.2%	27.7%	17.6%	15.0%	21.4%
	Muthoot Finance	5.7%	6.8%	6.5%	5.9%	4.9%	6.0%	22.4%	28.3%	27.8%	23.5%	17.6%	24.3%
Diversified	HDB Financial Services	2.3%	1.7%	0.6%	1.6%	3.0%	1.7%	17.4%	13.2%	4.8%	11.2%	18.7%	12.0%
	IIFL Finance	4.7%	0.8%	1.6%	3.3%	3.4%	2.3%	18.0%	4.2%	9.2%	18.1%	16.9%	12.1%

Source: Company Reports, CRISIL MI&A

Fedbank Financial had the sixth lowest GNPA and eighth lowest NNPA amongst the peer set as of Q1FY24

At the end of Q1FY24, Five Star Business Finance has the best asset quality with net NPA of 0.8% followed by HDB Financial Services (~0.8%), Aptus Value Housing (1.0%). In terms of GNPA, Aptus Value Housing has the lowest GNPA as of Fiscal 2023 at 1.3% followed by Manappuram Finance (1.4%) and Five Star Business Finance (1.4%). In addition, Fedbank Financial has the sixth lowest GNPA and eighth lowest NNPA among the peer set as of Q1FY24.

Segment	Player	Q1FY24		
		GNPA	NNPA	Credit Cost
Housing Finance	Aptus Value Housing	1.3%	1.0%	0.0%
	Repco Home Finance	5.5%	2.8%	NA
MSME	Five-Star Business Finance	1.4%	0.8%	0.2%
	Veritas Finance	2.2%	1.3%	0.5%
	Vistaar Finance	3.5%	2.2%	NA
MSME and Gold	Fedbank Financial Services	2.3%	1.8%	0.1%
	SBFC Finance	2.5%	1.6%	0.2%
Gold loan	Manappuram Finance	1.4%	1.2%	NA
	Muthoot Finance	4.3%	3.8%	0.1%
Diversified	HDB Financial Services	2.5%	0.8%	0.4%
	IIFL Finance	1.8%	1.1%	0.4%

Note: NA = Not available.

Source: Company Reports, CRISIL MI&A

Fedbank Financial had the fifth lowest GNPA and eighth lowest NNPA amongst the peer set as of Fiscal 2023

At end of Fiscal 2023, Five Star Business Finance has the best asset quality with net NPA of 0.7% followed by Aptus Value Housing (0.9%). In terms of GNPA, Aptus Value Housing has the lowest GNPA as of Fiscal 2023 at 1.2% followed by Manappuram Finance (1.3%) and Five Star Business Finance (1.4%). In addition, Fedbank Financial has the fifth lowest GNPA and eighth lowest NNPA among the peer set as of Fiscal 2023.

Segment	GNPA	FY19	FY20	FY21	FY22	FY23	Average (FY20-23)
Housing Finance	Aptus Value Housing	0.4%	0.7%	0.7%	1.2%	1.2%	1.0%
	Repco Home Finance	3.0%	4.3%	3.7%	7.0%	5.8%	5.2%
MSME	Five-Star Business Finance	0.9%	1.4%	1.0%	1.1%	1.4%	1.2%
	Veritas Finance	0.9%	1.9%	2.7%	3.9%	2.2%	2.7%
	Vistaar Finance	3.4%	3.7%	3.3%	2.7%	3.8%	3.4%
MSME and Gold	**Fedbank Financial Services**	**2.3%**	**1.5%**	**1.0%**	**2.2%**	**2.0%**	**1.7%**
	SBFC Finance	0.4%	2.3%	3.2%	2.7%	2.4%	2.7%
Gold loan	Manappuram Finance	0.6%	0.9%	1.9%	3.0%	1.3%	1.8%
	Muthoot Finance	2.7%	2.2%	0.9%	3.0%	3.8%	2.5%
Diversified	HDB Financial Services	1.8%	3.9%	4.5%	5.0%	2.7%	4.0%
	IIFL Finance	1.7%	2.0%	2.0%	3.2%	1.8%	2.1%

Source: Company Reports, CRISIL MI&A

Segment	NNPA	FY19	FY20	FY21	FY22	FY23	Average (FY20-23)
Housing Finance	Aptus Value Housing	0.3%	0.6%	0.5%	0.9%	0.9%	0.7%
	Repco Home Finance	1.4%	1.9%	2.3%	4.9%	3.0%	3.2%
MSME	Five-Star Business Finance	0.7%	1.1%	0.8%	0.7%	0.7%	0.8%
	Veritas Finance	0.8%	1.3%	1.4%	2.3%	1.3%	1.6%
	Vistaar Finance	2.6%	2.5%	2.2%	1.9%	2.5%	2.3%
MSME and Gold	**Fedbank Financial Services**	**1.9%**	**1.1%**	**0.7%**	**1.8%**	**1.6%**	**1.3%**
	SBFC Finance	0.3%	1.6%	2.0%	1.6%	1.4%	1.6%
Gold loan	Manappuram Finance	0.3%	0.5%	1.4%	2.7%	1.2%	1.5%
	Muthoot Finance	2.4%	2.0%	0.8%	2.7%	3.4%	2.2%
Diversified	HDB Financial Services	1.3%	3.3%	3.2%	2.5%	1.0%	2.5%
	IIFL Finance	0.5%	0.8%	0.9%	1.8%	1.1%	1.2%

Source: Company Reports, CRISIL MI&A

Fedbank Financial had the third lowest average credit cost from Fiscals 2020 to 2023 amongst MSME peer set

Muthoot Finance has the lowest credit cost of 0.1% in Fiscal 2023. Credit cost in Fiscal 2023 for Fedbank Financial is at 0.6%, however, it had the third lowest average credit cost from Fiscals 2020 to 2023 amongst MSME peer set.

Segment	Player	Credit cost (%)						Stage 1 provisions to Stage 1 assets	Stage 2 provisions to Stage 2 assets	Stage 3 provisions to Stage 3 assets	Total provision to AUM ratio	Restructured book (%)		
		FY19	FY20	FY21	FY22	FY23	Avg (FY20-23)	FY23	FY23	FY23	FY23	FY21	FY22	FY23
Housing Finance	Aptus Value Housing	0.1%	0.1%	0.1%	0.7%	0.5%	0.4%	0.4%	8.0%	25.0%	1.1%	0.0%	1.5%^	NA
	Repco Home Finance	0.2%	0.5%	0.7%	1.9%	0.4%	0.9%	NA	NA	49.6%	4.2%	NA	NA	NA
MSME	Five-Star Business Finance	0.4%	1.5%	0.7%	0.8%	0.3%	0.8%	0.3%	7.0%	49.3%	1.6%	0.0%	1.4%	NA
	Veritas Finance	0.6%	1.0%	2.0%	2.5%	1.4%	1.7%	0.4%	12.9%	42.8%	1.6%	0.2%	3.6%	1.6%
	Vistaar Finance	3.0%	3.0%	2.4%	1.4%	1.0%	1.9%	0.4%	8.2%	36.2%	1.8%	6.2%	4.3%	NA
MSME and Gold	**Fedbank Financial Services**	**0.2%**	**0.7%**	**1.5%**	**1.4%**	**0.6%**	**1.1%**	**0.4%**	**11.2%**	**22.2%**	**1.2%**	**1.9%**	**4.6%**	**2.2%**
	SBFC Finance	0.01%	1.1%	0.8%	1.1%	0.6%	0.9%	0.6%	7.0%	39.3%	1.7%	1.5%**	3.8%	2.3%^^
Gold loan	Manappuram Finance	0.2%	0.4%	0.5%	0.3%	0.2%	0.4%	0.5%	1.4%	13.5%	0.5%	0.3%	NA	NA
	Muthoot Finance	0.1%	0.2%	0.2%	0.2%	0.1%	0.2%	0.8%	1.0%	10.3%	1.2%	NA	NA	NA
Diversified	HDB Financial Services	1.3%	2.5%	5.0%	4.0%	2.0%	3.4%	3.0%	28.3%	65.1%	5.2%	5.9%	NA	NA
	IIFL Finance	3.1%	1.5%	3.7%	2.2%	1.2%	2.2%	2.1%	6.4%	41.3%	0.6%	1.7%	0.7%	NA

*Note: NA = Not Available, ^ Data as of September 2021, ** Data as of December 2020, ^^ Data as of December 2022*

Source: Company Reports, CRISIL MI&A

Segment	Player	Q1FY24	
		Leverage (times)	Capital Adequacy Ratio (%)
Housing Finance	Aptus Value Housing	1.2	75.4%
	Repco Home Finance	NA	36.1%
MSME	Five-Star Business Finance	1.0	60.3%
	Veritas Finance	NA	41.8%
	Vistaar Finance	NA	36.1%
MSME and Gold	Fedbank Financial Services	5.4	19.7%
	SBFC Finance	2.0	33.6%
Gold loan	Manappuram Finance	2.1	30.0%
	Muthoot Finance	2.4	30.0%
Diversified	HDB Financial Services	NA	19.8%
	IIFL Finance	NA	20.6%

Note: NA = Not available.

Source: Company Reports, CRISIL MI&A

Segment	Player	Leverage (times)						Capital adequacy ratio (%)					
		FY19	FY20	FY21	FY22	FY23	Avg (FY20-23)	FY19	FY20	FY21	FY22	FY23	Avg (FY20-23)
Housing Finance	Aptus Value Housing	2.3	1.2	1.3	0.9	1.1	1.1	43.6%	82.5%	73.6%	85.6%	80.8%	80.6%
	Repco Home Finance	6.1	5.7	5.0	4.3	3.9	4.7	24.1%	25.9%	30.7%	33.6%	35.8%	31.5%
MSME	Five-Star Business Finance	0.7	1.2	1.5	0.7	1.0	1.1	64.8%	52.9%	58.9%	75.2%	67.2%	63.6%
	Veritas Finance	1.3	1.2	1.4	0.8	1.5	1.3	48.0%	59.3%	50.7%	64.4%	45.0%	54.9%
	Vistaar Finance	1.5	2.0	2.1	2.4	2.7	2.3	40.3%	37.6%	36.5%	30.0%	26.4%	32.6%
MSME and Gold	Fedbank Financial Services	3.5	4.7	5.2	4.4	5.3	4.9	21.6%	17.9%	23.5%	23.0%	17.9%	20.6%
	SBFC Finance	1.0	3.0	2.3	2.3	2.2	2.4	44.8%	21.9%	26.3%	26.2%	31.8%	26.5%

Segment	Player	Leverage (times)						Capital adequacy ratio (%)					
		FY19	FY20	FY21	FY22	FY23	Avg (FY20-23)	FY19	FY20	FY21	FY22	FY23	Avg (FY20-23)
Gold loan	Manappuram Finance	2.9	3.3	2.6	2.3	2.1	2.6	23.3%	21.4%	29.0%	31.3%	31.7%	28.3%
	Muthoot Finance	2.7	3.2	3.0	2.7	2.4	2.8	26.1%	25.5%	27.4%	30.0%	31.8%	28.7%
Diversified	HDB Financial Services	6.3	6.2	6.0	5.1	4.8	5.5	17.9%	19.4%	18.9%	20.2%	20.1%	19.7%
	IIFL Finance	3.7	4.0	4.3	3.7	3.4	3.8	18.3%	16.6%	25.4%	23.9%	20.4%	21.6%

Source: Company Reports, CRISIL MI&A

ALM position of various players as of Q1 Fiscal 2024

Amongst the peer set analysed, Muthoot Finance has highest ALM surplus (₹ 332.7 billion) within 12 months bucket followed by Manappuram Finance (₹ 111.6 billion) and IIFL Finance (₹ 82.3 billion). In addition, Fedbank Financial has assets to liability ratio of 184% within 12-month bucket. In the after 12 months bucket, HDB Financial Services has highest ALM surplus (₹ 75.6 billion) followed by Aptus Value Housing Finance (₹ 59.8 billion).

ALM position of various peers

Segment	Q1FY24 (In ₹ Bn)	Assets		Liability		Net		Assets to Liabilities ratio@	
		Within 12 months	After 12 months	Within 12 months	After 12 months	Within 12 months	After 12 months	Within 12 months	After 12 months
Housing Finance	Aptus Value Housing Finance	27.3	109.3	16.1	52.0	11.3	57.4	170%	210%
	Repco Home Finance**	26.4	98.8	26.3	73.8	0.1	25.1	100%	134%
MSME	Five-Star Business Finance**	26.1	60.9	15.3	28.3	10.8	32.6	171%	215%
	Veritas Finance**	13.3	27.6	8.2	16.8	5.0	10.9	161%	165%
	Vistaar Finance*	7.9	19.7	6.3	14.4	1.7	5.4	126%	137%
MSME and Gold	Fedbank Financial Services**	57.6	43.2	31.3	60.4	26.2	-17.2	184%	71%
	SBFC Finance	54.9	162.4	30.5	139.2	24.4	23.2	180%	117%
Gold loan	Manappuram Finance**	231.7	61.7	120.1	83.5	111.6	-21.8	193%	74%
	Muthoot Finance**	671.4	55.1	338.8	177.1	332.7	-122.0	198%	31%
Diversified	HDB Financial Services**	266.2	434.3	227.4	358.7	38.8	75.6	117%	121%
	IIFL Finance	258.5	288.0	180.4	366.1	78.1	-78.1	143%	79%

*Note: * Data for fiscal 2022, ** Data for fiscal 2023, @ Asset to liabilities ratio is calculated by dividing the percentage of assets maturing in the specified time period by percentage of liabilities maturing in the same time period.*

Source: Company Reports, CRISIL MI&A

List of formulaes

Parameters	Formula
Disbursement to AUM	Disbursement at the end of the financial year divided by AUM at the end of the financial year
AUM per Branch	AUM at the end of the financial year divided by number of branches at the end of the financial year
Disbursement per Branch	Disbursement at the end of the financial year divided by number of branches at the end of the financial year
AUM per employee	AUM at the end of the financial year divided by number of employees at the end of the financial year
Disbursement per employee	Disbursement at the end of the financial year divided by number of employees at the end of the financial year
Cost to Income Ratio	Operating expenses for the relevant fiscal year divided by the sum of net interest income (interest earned minus interest expended) and other income for the relevant fiscal year
Operating Expense	Operating Expenditure (Employee Expenses + Depreciation and amortization expense + Fees and commission expense+ Other expenses)
Opex to total assets	Operating expenses divided by total average assets at the end of the financial year
Opex to AUM	Operating expenses divided AUM at the end of the financial year
Opex to Disbursement	Operating expenses divided by Disbursements at the end of the financial year
RoA	Profit after tax / average of total assets on book
RoE	Profit after tax / average net worth
NIMs	(Interest income – interest paid) / average of total assets on book
Yield on advances	Interest earned on loans and advances / average of total advances on book
Cost to income	Operating expenses / (net interest income + other income)
Cost of borrowings	Interest paid / (average of deposits and borrowings)
Credit cost	Provisions / average total assets on book
Leverage	Total Borrowings / Total shareholder equity of the same fiscal

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ADDENDUM NO. 3 TO THE AGREEMENT FOR SERVICES

This Addendum No. 3 ("Addendum") dated 14th June 2023 amends the Agreement for Services effective October 22, 2021 (Reference number: SS/BD/FEDFS/DRHP/2021/CH1211) as may have been amended previously, (“Agreement”), executed between FedBank Financial Services Limited

AND

CRISIL Limited, a company incorporated under the laws of India whose registered office is at CRISIL House, Central Avenue, Hiranandani Business Park, Powai, Mumbai – 400 076 (“**Supplier**”)

“**Fedfina**” and “**Supplier**” shall wherever the context permits be individually referred to as “**Party**” and collectively referred to as “**Parties**”.

RECITALS:

A. The Parties have entered into the Agreement where the Supplier has agreed to an update to Services (Industry Report) to Fedfina according to the terms and conditions contained in the Agreement. The update would be as per the below mentioned details:

- One-time DRHP Industry Report update (to be commenced immediately in June 2023)
- One-time RHP update (basis not later than December 2023 numbers, executed and Consent letter delivered not later than Jan/Feb 2024).

B. Unless repugnant to the context, any capitalized term not otherwise defined herein shall have the meaning ascribed to it in the Agreement.

OPERATIVE CLAUSES:

1. Except as otherwise modified under this Addendum, all other terms and conditions of the Agreement shall remain unchanged for the term of the Agreement, including the term extended by this Addendum.

2. The Parties hereby agree that this Addendum shall be read in conjunction with the Agreement and all terms and conditions as mentioned in the Agreement shall apply *mutatis mutandis* to this Addendum.

3. The Recitals under this Addendum form an integral part of the Agreement and are binding on both the Parties.

IN WITNESS WHEREOF, the Parties have executed this Addendum on and as of the date first mentioned above.

FedBank Financial Services Limited	CRISIL Limited
Signature:	Signature:
Printed Name: C. V. Ganesh	Printed Name: Dinesh Agarwal
Title: CFO	Title: Director - Business Development, CRISIL Market Intelligence & Analytics
Date:	Date: July 06, 2023

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ADDENDUM NO. 4 TO THE AGREEMENT FOR SERVICES

This Addendum No. 4 ("Addendum") dated 9th oct 2023 amends the Agreement and Addendum No 3 for Services effective October 22, 2021 (Reference number: SS/BD/FEDFS/DRHP/2021/CH1211) as may have been amended previously, ("Agreement"), executed between FedBank Financial Services Limited

AND

CRISIL Limited, a company incorporated under the laws of India whose registered office is at CRISIL House, Central Avenue, Hiranandani Business Park, Powai, Mumbai – 400 076 ("**Supplier**")

"**Fedfina**" and "**Supplier**" shall wherever the context permits be individually referred to as "**Party**" and collectively referred to as "**Parties**".

RECITALS:

A. The Parties have entered into the Agreement where the Supplier has agreed to an update to Services (Industry Report) to Fedfina according to the terms and conditions contained in the Agreement.
The update would be as per the below mentioned details:

- One-time RHP update for updating June 2023 nos
- In case of any further update additional fees would be applicable as agreed earlier (not later than December 2023 numbers, executed and Consent letter delivered not later than Jan/Feb 2024).

B. Unless repugnant to the context, any capitalized term not otherwise defined herein shall have the meaning ascribed to it in the Agreement.

OPERATIVE CLAUSES:

1. Except as otherwise modified under this Addendum, all other terms and conditions of the Agreement shall remain unchanged for the term of the Agreement, including the term extended by this Addendum.

2. The Parties hereby agree that this Addendum shall be read in conjunction with the Agreement and all terms and conditions as mentioned in the Agreement shall apply *mutatis mutandis* to this Addendum.

3. The Recitals under this Addendum form an integral part of the Agreement and are binding on both the Parties.

IN WITNESS WHEREOF, the Parties have executed this Addendum on and as of the date first mentioned above.

FedBank Financial Services Limited	**CRISIL Limited**
Signature:	Signature:
Printed Name:	Printed Name: Dinesh Agarwal
Title:	Title: Director, Business Development, CRISIL MI&A
Date:	Date: 9th October 2023

Disclaimer

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