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THE ROLE OF NBFC IN DEVELOPMENT OF INDIAN ECONOMY: A CASE STUDY

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ABSTRACT

Though banking Sectors are affecting Indian Financial Market a lot, but now The Non Banking Financial Companies are playing a very vital role in Indian Financial markets and also competing with Banking Sectors by providing various Financial services and are playing a complementary role with other Financial institutions in Indian Economy. Here the Study has been made to know the role of NBFCs in Development of Indian Economy. In developing Country like India, For the access of finance in the economic development and For growth of Entrepreneurship is very difficult .now a days though various financial inclusion schemes like Pradhan Mantri Jan Dhan Yojana and many more have been implemented by the government through the help of Banking sectors, but banks cannot meet all the financial needs of all class peoples due to their rigid loan disbursement policies and credit worthiness policies, because households and small business man cannot access the financial services from banks due to the above reasons .So the needs of NBFCs for providing various financial services to the all segments people easily and more quickly for the development of Entrepreneurial activities in our Country. NBFCs are addressing the debt requirement of various sectors in the Economy like from large infrastructure financing to small micro finance, so playing a very vital role in fund mobilisation in our Economy. This Industry has responded positively to the regulatory efforts for the better understanding of risks and to identify such risks through the assistance of regulations in its Credit scenario. Over the time the Sector has been fragmented and accepts best management practices innovation, risk management, technology and governance. For above those points of view the research has been conducted to know the role of NBFCs in the development of Economy in our country and to know its present challenges.

Keywords: *Non-banking Finance Companies, Lease and Hire Purchase, Assets Growth.*

Introduction

In past few years India was known as bank dominated financial system but now a days the trend has totally been changed due to establishment of various alternative financial systems like Non Banking financial Companies which are known as the complementary to the banking sectors. Non Banking Financial Companies are companies which are registered under the companies act 2013 in India and engaged in the various business like loans and advances, acquisition of shares, stocks, bonds, insurance business, hire purchase business and chit fund business but do not include any institutions which are involved as their core business in agriculture Finance, industrial activities and other purchase, sale and construction of goods and any immovable property. The financial activities of NBFCs are strictly regulated and supervised by Reserve Bank of India under the RBI act.1934.Since past 20years the need

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and demand of NBFCs are very high due to the expansion of various industrial sectors and and the huge requirement of venture capital and also the need of working capital. These companies are providing the various financial services to those sector people who are not eligible and fulfilling the terms and conditions of banking sectors and due to their lack of credit worthiness. Those above sector people are generally belong to the rural and semi urban areas and are called unbanked customers. So NBFCs are known as the complementary to the banking sectors and are playing a very crucial role in development of Indian Financial System. NBFCs are now filling the gap between the financial demand of the society and financial institution's supply of such financial resources. These financial institutions mobilise the people's saving as deposit and are lending those funds to the needy sectors in our society.

Historical Background of NBFCS in India

NBFCs first started their operations from 1960 and were known as the alternative of banking sectors in India and at that time their demand were very low due to lack of awareness among the investors and borrowers but in now a days their demand are very high due to strict and rigid lending policies have been following by the banking sectors according to the strong guidelines are being followed by the instruction of RBI. In first the companies act regulates the financial operations of NBFCs but in later due to the complex and specialised nature of their operations the RBI decided to regulate and to supervise their operations. Between the 1980s to 1990s the NBFCs were recognised as reputed and customer friendly financial institutions and have retained a large volume of Industrial business customers and the number of companies have been increased from mere 7000 to approximately 30000 in 1992 as compare with 1981.Since then, activities Non Banking Financial Companies were monitored by RBI rules and regulations.

Review of Literature

Gurley and Shaw (1960) developed a financial concept that described the activities of financial intermediaries and the theoretical concept of financial institutions. They basically classified the intermediaries into two categories which are monetary and non monetary by nature. Monetary institutions like banks which help in generating money and thereon monetary sectors which do not help in generating money.

Goldsmith (1969) was the first author who realised and identified the need and role of financial institutions in development process. He has given priority in the role of such financial institutions in the process of mobilising the funds from the investors as deposit to the borrowers as loan for the productive and operational activities.

Shanker (1996) in his study described that the resources should be increased and efficiently allocated in the huge competitive scenario due to the large numbers of competitors and their financial soundness.

Levine et. al, (1999)pointed out that the growth of economy is very high where the financial institutions were developed. In this study he defined that the Non banking Financial Companies have increased their investment percentage in private sectors and which leads to enhancement real per capita GDP of about 0.6% points every year.

Shollapur (2005) realised that the NBFCs are playing a very adequate role in the system of finance and are known as the complimentary sectors of commercial banks of India. The healthy and productive financial services of NBFCs lead to retain large numbers of customers which also includes small borrowers.

Balachandran (2006) in his study he defined that the various financial products are available in the financial markets and which offer adequate credit and payment services and also helps in mobilising the funds of savers to the borrowers as investment of such financial companies and for those reasons NBFCs are playing a very major role in Indian financial markets.

Sundaram (2010) realised that NBFCs have been developed in their financial performance, profitability aspects. The researcher here advised that the RBI should fully regulate the NBFCs like commercial banks because these companies are developing rapidly and expanding their operational activities to the possible extent.

Khalil (2011) described the NBFC's performance in financial aspects which include the services like investment and leasing finance, management of asset, consulting services in case of investment which are not efficiently provided by the Banking sectors.

Research Gap

There are various studies have been done in NBFCs and Banking Sectors by describing its own financial Status, profitability and sustainability but there are no many researches have been done in role of NBFCs in Development of Indian Economy, So here we want to do research in this field.

Objectives of Study

- To study the contributions of NBFCs in Financial Services.
- To study the role of NBFCs in Economic Development of the Country.
- To study the role of NBFCs in Financial Inclusion in the Country.
- To study the role of NBFCs in Infrastructure Financing in India.

Research Methodology

Here the research is based on Secondary data which are collected from various websites, magazines and papers and considered from 2016 to 2018. Simple statistical tables and charts are used in this Research in order to analyse and interpret the data.

Definition and Meaning of NBFC

Under section 45-I(f) of the act, the NBFC is defined as:

- A company of financial institution.
- An NBFC is a company of finance which is basically engaged in accepting deposits under different policies and also giving loan in different schemes or policies.
- By the prior approval of government of India and by the notification published in government Gazette, non banking financial institutions are established and operated.

"The company will be called as a non-banking financial company (NBFC) if its financial assets are more than 50% of its total assets (netted off by intangible assets) and income from such financial assets is more than 50% of the gross income. Both of these tests are necessary to be satisfied as the factor determinant for the principal business of a company." The RBI amendment act 1997 defined that NBFC is known as the company and is a financial institution which has the core business of accepting of deposits under any policies and lending them in any manner or way. Such financial institutions which have the prime business to finance the agricultural sectors must be excluded from the above definition.

Classification of NBFCs

The NBFCs are classified as under:

- Loan Company
- Investment Company
- Asset Finance Company.
- Hire Purchase Company
- Mutual benefit Financial Company
- Residuary Non-banking Company.
- Chit Fund Company.

Role of NBFCs in Development of Indian Economy

NBFCs are playing a role of financial intermediaries between the rational depositors or savers and needy borrowers. These financial Companies provide a large numbers of economical services due to the presence of scale of Economies; the risk can be easily diversified in various units due to their ability and professional expertise services. Thus their operations and activities are giving both opportunities of getting more return of their investment and by taking lower risks. For the intermediation activities of such financial institutions the borrowers are getting a large and wide variety of financial service as loan and that ultimately helps in development of our economic position of nation. Commercial banking sectors are commonly providing and disbursing their capitals generally to the agricultural, industrial and commercial purpose and NBFCs are generally focusing for giving loans to small, rural and semi urban retail customers, giving loans for electronics, durable and consumable goods, purchase and renovation of home and for trading and transportation purpose. All the above activities are strictly supervised and regulated by the RBI like banking sectors. The main role of financial institutions is to mobilise the funds from savers to ultimate need of the borrowers. So they are playing a vital role in the growth and development of economic sectors of our nation. The RBI's export committee explored the essentiality of NBFCs in the mentioned areas:

- Growth and expansion of transport and infrastructure areas and many other important sectors
- Adequate and substantial employment generation
- Help in wealth creation
- Development of Economy
- Supplementary role of banking sectors in case of rural credit expansion.
- Knowing as trusty sector for rural, semi urban and fresh buyers
- Helps in providing credit to the weaker section of our economy
- Acting as huge amount of contributors to the central and state fund

Contributions in Financial Services (NBFCS vs. Banks)

Financial institutions like NBFCs and Banking sectors in our country offer all or any of common basic features which are mentioned below:

- Some of them offer services of payment- with the help of claims which are utilised in the settlement of transactions. A claim must have a higher reliable and stable value in order to make effectiveness in payments and that must be widely get acceptance in the exchange market and should be linked with optimum and adequate settlement of value for arrangement purpose.
- The realisation of the asset's total market value can be possible under the process of liquidity if the decision for sell out the asset has been taken. Financial institutions in this way assist in expansion position of liquidity by taking help of scale and specialization.
- The assets can be traded in small denomination with the help of financial technique of Divisibility. Financial institutions helps in segregating the large denomination claims and also helps in aggregating the small claims of denomination in order to meet the requirement of divisibility in the society.
- Value of store under which a reliable store of purchasing power is provided by asset overtime – this is known as the fundamental concept of satisfying the saving preference.

Specific Roles of NBFCs

NBFCs perform certain types of activities which cannot be suitable for banking sectors:

- NBFCs help in expansion of promises of equity (by making addition of divisibility, liquidity, efficiencies of information's and services of pooling the risks). NBFCs help in spreading the existence of risks for the investors. In this process NBFCs are encouraging the saving and investment activities and also helps in increasing the efficiency of those saving and investment activities.
- NBFCs are raising their hands in promoting the risk management process and culture in doing encouragement to those who are not able or least able to take the risk and also decided to sell those risks and in that process they are helping in better and smooth management of risks.
- They are helping in the enhancement of resilience in the financial system to the Economic shock.
- NBFCs are providing competitive opportunities for banks with the help of financial services by making provision. NBFCs are providing the services of banking sectors to the great possible extent and trying to make competition with the banking sectors. NBFCs are export, professional and specialised in a particular sector and target to some particular segments or groups.

Role of NBFCs in Economic Development

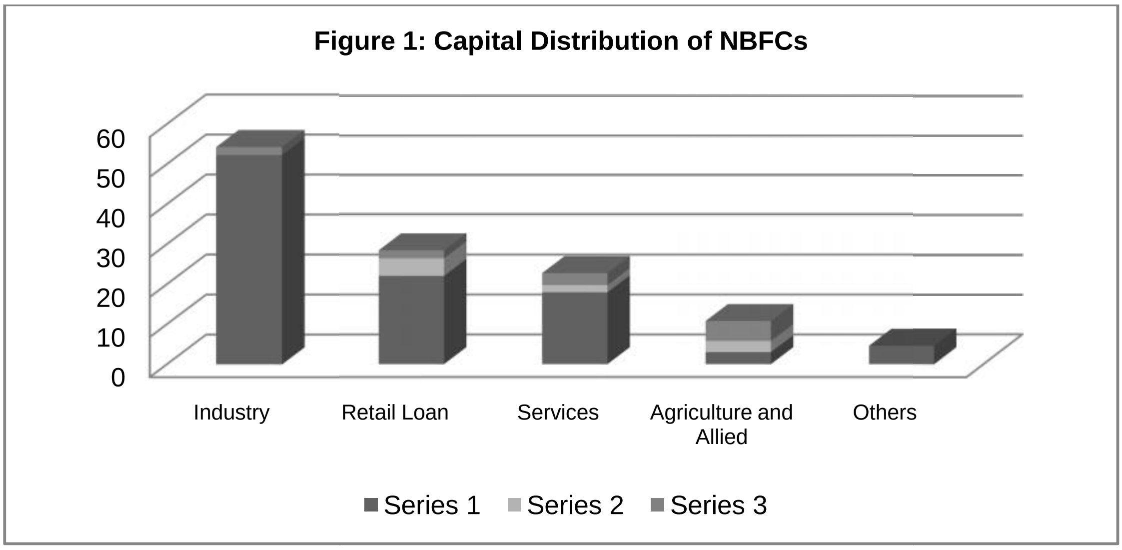
The development and sustainable growth of financial intermediaries contribute a lot for growth and development of economy of our nation. Due to the balanced growth of both banking sectors and NBFCs the developmental activities of economy have been increasing in a significant way. There are many major vital roles have been performing by NBFCs like making provision for the service of pooling the risks, liquidity and for divisibility which help in diversifying the quantum of risks and also help in promoting the concept of management of risks by motivating the customers who are unable to bear risks or able to take risks to some extent and also help in providing those financial services which are not adequately offered by the banking sectors in our country

The below table and chart shows the distribution of capital of NBFCs in the form of credit to the various sectors of the Economy.

Table 1: Credit Distributions of NBFCs

Sectors	Percentage of Credit Distributions
Industry	52.30
Retail loans	22.10
Services	18.00
Agriculture and allied	03.00
Others	04.60

Source: RBI Website



Source: RBI Website

The above chart is showing the credit distribution of Non Banking Finance Companies to the various sectors of our Economy for development .the shares of contribution are calculated in cumulative manner, and out of total share of 100% NBFCs are giving loans to the industry sector is 52.3% and to the retail sectors is 22.1% and to the agriculture and allied activities is 3% and to service sectors is 18% and also to other sectors is 4.6%.

Table 2: Financial Parameters of the NBFC Sector

(Amount in Rs. Billion)

Items	2016-17 NBFCs	2017-18 NBFCs	2018-19 NBFCs
• Income	2310	2515	1395
• Expenditure	1822	1958	1069
• Net Profit	314	386	230
• Total Assets	19797	22760	26019
• Financial Ratios (As percent to total assets)			
▪ Income	11.7	11.00	5.4
▪ Expenditure	9.2	8.6	4.1
▪ Net Profit	1.6	1.7	0.9
• Cost to Income Ratio (Percent)	78.9	77.9	72.1

Source: RBI Website

The above table represents the financial parameter of NBFCs from 2016 to 2018.Here the cost to income ratio is calculated in percentage of NBFCs and observed that the Cost to Income ratio of NBFCs has been decreased in 2018-19 as compare with 2016-17 and it represents that the cost has been increasing and the profit has been increasing and that leads towards economic development of our Country.

Abridged Balance Sheet of NBFCS

(Amount in Rs. billion)

Items	At the End of 31.03.2017	At the End of 31.03.2018	At the End of 31.09.2018
• Share Capital and Reserves	4,527	5,153	5,595
• Public Deposits	306	319	326
• Debentures	6,481	7,155	7,551
• Bank Borrowing	3,134	4,039	4,936
• Commercial Papers	1,291	1,406	1,816
• Others	4,058	4,688	5,795
Total Liabilities	**19,798**	**22,760**	**26,019**
• Loans and Advances	14,800	17,643	19,842
• Investment	2,759	3,011	3,352
• Cash and Bank Balances	796	649	848
• Other Current Assets	1106	1168	1639
• Other Assets	336	288	337

Source: RBI Website

The above table shows the financial statement of NBFCs in 2017 and 2018 and that indicates, how the NBFCs are playing a very crucial role in our Country by contributing to the Economic Development by giving loans and advances and by in vesting its capital in various sectors of our Country and also in government bills and papers and by keeping its cash resources in various public sector and private sector banks and that also helps in Mobilization of financial resources.

Role of NBFCs in Financial Stability

The NBFCs sectors are comparatively less developed in the financial systems of India, banks will inevitably be required to assume risk that otherwise might be borne by the stock market, collective investments schemes or insurance companies. However, there is basic incompatibility between the kind's kinds of financial contracts offered by the banks and those offered by the financial institutions. Thus, banks are more likely to fail as a result. In order to minimise financial scarcity in our nation may leads to make promotion and to create awareness for making diversification of the institutions of finance and markets, and so for that reason all the rational investors can accept the risks beyond the banking sectors.

Role of NBFCs in Financial Inclusion

It is explained as the "provision of accessible and affordable financial services" for such customers who cannot access or less access by formal institutions of our traditional system of finance. These services include "payments and remittance facilities, savings, loan and insurance services". Microfinance is known as the very major part of financial inclusion of our country. It does not only gives small credit to the customers but also provides other many financial services in a lower quantities to the weaker section people. Financial inclusion in this way is targeting to offer credit and deposit facilities to the poor and weaker section people and also' helps in providing many other miscellaneous financial services like insurance and remittance services etc. We have given opportunities to the NBFCs to act as supplements of banking sectors for achieving the fundamental of financial inclusion to the great possible extent.

Role of NBFCs in Capital Market

Non Banking Financial companies are playing a very major role in terms of Investment activity of their total assets. These types of financial institutions broadly contribute their major capital in investing in the capital market. There are some specialised and expertise NBFCs that are purely and professionally involved in trading securities with the help of capital market. In this way NBFCs are helping to give opportunity of liquidity in the capital market. Further, these institutions also help to the investors to invest in the capital market by providing lending facilities to such investors and that also leads to growth and development of capital market in India.

Role of NBFCs in Factoring

Under factor regulation act, 2011 factoring is defined as engagement in acquisition of receivables by a factor and for that activity it claims undivided interest on such debt receivables or helps in financing against interest of security over any debt receivables but it exclude loan giving facilities by banks against securities of receivables which is performed by banks as ordinary business transactions.

Under the new regulation of Indian Factoring act, Reserve bank of India has just introduced new variety of Non Banking Financial companies which is known as NBFC factors and are regulating and supervising to those categories of NBFCs. These types of NBFCs are basically involved in giving factoring services. In this way NBFCs are just playing the complimentary role of bank finance and fulfil the needs of working capital requirements of small and medium scale enterprises who have adequate quantity of receivables but cannot get finance from any other financial institutions due to lack of eligible profile or collateral securities. Factoring helps those sectors by giving freedom of their resources and also known as the contributors of all types of financial needs of the business under one roof and without any more hesitations and which can be addressed through the help of appropriate regulatory authorities.

Role of NBFCs in Infrastructure Financing

There are some specific types of NBFCs like infrastructure debt funds and infrastructure finance companies which are professionally deals with infrastructure financing in our country in a significant way. Such types of finance companies are professionally very export for financing long term project. Reserve bank of India have provided dispensation in the way of extending the credit of banks, high rate of exposure for norm ceiling and also for making provision of ECB under the way of automatic lending to the sectors of infrastructure. In case of those IFCs who are giving long term credit against short term liabilities, the position of assets and liabilities are definitely the matter of concern for them.

Problems and Challenges of NBFCs in India

According to the newly updated policies and rules of Reserve Bank of India, some of regulations will be appreciable and acceptable due to its capital adequacy rules and better and smooth funds management, but here there is some ambiguity in today's thinking how can such Non Banking financial institutions should mobilise the funds and to expand its leasing and hire purchase business in a significant way. In present scenario by taking many factors into consideration it was concluded that the NBFCs should allocate and mobilise its financial resources by not taking the help from banking sectors and other financial institutions in form of receive credit but have to utilise and mobilise their own financial resources without depending upon any other complementary institutions of finance. The proportion of deposits acceptance from people for not depending upon the Banks were liberally conceived and in the recent time only the AAA companies are authorised to receive the deposits from the people or to fix the rate of interest without any limitations.

Conclusion

NBFCs are now known as the important part of our system of finance. Those institutions have been offering credit to the retail customers who are not eligible to get loan from banks and other complementary financial institutions due to their low credit worthiness and poor or lack in documentations and for that reason they are called undeserved customers in banks point of view. They are very efficient in introducing innovative financial products for filling the gap between the customer's needs and banks and other financial institution's supply of financial services. They have been playing very important role in contributing towards major sectors like infrastructure, road transport which are known as the heart of the country for economic development and growth. Due to the establishment of export committee and taskforce by the help of regulatory bodies like Reserve Bank of India the above role has been strongly exhibited by the NBFCs. Now these financial institutions are also known as the essential part of financial systems in India and also have significant roles and contributions towards strategic government decisions like Financial Inclusion and many more other decisions. they are also filling the gap between the financial requirements of the retail and rural undeveloped customers and bank's contributions to such customers for providing credit. The relevance of the findings of the study states that in NBFC's activities and performances, the risks play a very important role. Management of such risks must be supervised by the efficient risk managers and by the Country's central bank. The findings of the study suggest that in case of NBFCs sector, practices of management for risks or lower risk taking incentives which leads to better and significant performance of its financial activities in India. Further it is suggested that the regulatory bodies should analyse, realise and supervise the effect of activities of risk taking of NBFCs on their performance of finance and should also inspect or verify rigidly and enforce new rules and regulations for its better and efficient performance and which can leads to development of our Economic sectors in a healthy and prosperous way. The above steps should be taken in a continuous process for the better management of financial performance of NBFCs and which will help in strengthening the financial systems of our Country and for Development of Economic sector,

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