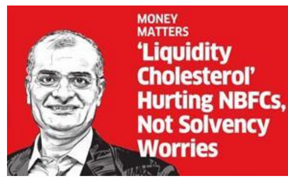
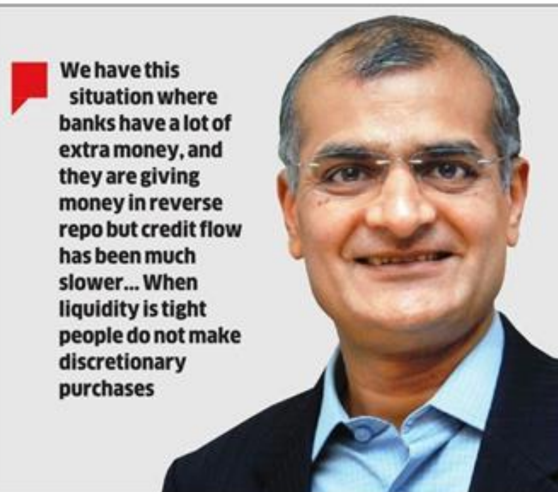


ET Q&A

RASHESH SHAH
Chairman, Edelweiss Group

'Liquidity Cholesterol' Hurting NBFCs, Not Solvency Worries

Liquidity, the crucial financial grease for running an economy, appears to be in short supply at the moment, Rashesh Shah, chairman, Edelweiss Group, told **Saikat Das**. But that shortage of immediate liquidity in certain consuming sectors is not indicative of a solvency problem. Liquidity fuels optimism in the broader economy, said Shah, drawing an analogy that links India's savings dynamics with automotive purchases. If people have some extra money, they would go and buy a new car. Otherwise, they would go to a mechanic and repair the existing vehicle, Shah said, to drive home the impact of inadequate liquidity on certain discretionary purchases. Edited excerpts:



We have this situation where banks have a lot of extra money, and they are giving money in reverse repo but credit flow has been much slower... When liquidity is tight people do not make discretionary purchases

Is fear keeping investment away from the NBFC sector?

There will be fear when there are sporadic events. There was fear when certain corporate groups defaulted. But, in my assessment, October to December was very challenging where even I didn't know who is in what shape even in the industry. However, after March, I feel confident that all these are all manageable accounts. This is a liquidity problem and not a solvency problem as there is value in the asset. The asset is not a broken asset, it is a good asset.

What is your take on tight market liquidity?

Our hypothesis is that one catalyst of the economic slowdown clearly is liquidity, because somewhere liquidity has got jammed. This is what I call as 'liquidity cholesterol'.

So, we have this situation where banks have a lot of extra money, and they are giving money in reverse repo but credit flow has been much slower. Partly because flow to NBFCs, which finance a significant chunk of car loans, home loans, gold loans and other discretionary spends, has slowed. When liquidity is tight people do not make discretionary purchases. Liquidity fuels optimism. If one has a little extra money, he will go and buy a new car otherwise he will go to a mechanic and repair his existing car and pull through.

Will it impact growth?

In the near term, it will, yes. But there are three underlying reasons that should hopefully open up soon enough. First, recent liquidity infusion by RBI into the banking system is yet to move into the economy. Second, because of elections, cash in circulation is much higher than normal, which should stabilise soon enough. Third, government spending has been limited in this transitional phase, which should open up once the new government takes charge. So discretionary spending will be limited like in recent times – especially automobiles.

Fortunately, home sales are strong enough. Home sales have not slowed down in last five years. Commercial real estate has always been solid in last three years and is still doing well and that's the reason Embassy REITs formed such a good acceptance. But the housing market also remains strong in the past five-six months. What happened in cars and FMCG has not happened in housing.

What is your assessment of the real estate sector?

Home sales are strong as the inventory has fallen last eight quarters. I think it will take another one and a half years or two to clean the excess inventory. People complain that prices have not fallen despite slowdown in sales. However, given that eight years prices have not gone up and there is inflation In India, in real term the correction has already happened.

There is still inventory, so supply is slightly more than demand. However, financing of projects is not yet normalised and project launches have almost come to a standstill, which means the gap between supply and demand will quickly decline. Good projects will continue to do well, especially in the sub-₹1-crore unit range where the demand is high and continues to rise.

Will bonds issued by real estate companies pose default threats?

Unlikely. I think everybody has stable asset-liability management and liquidity, which is fairly solid. See, the risk of this was the highest in October, November and December because commercial papers were maturing then. Select NBFCs have obtained enough access to long-term borrowing, if you see borrowing profiles. People are able to raise funds in the current market. Even the debt to equity ratios are fairly okay.

During H2-FY19, Edelweiss has raised ₹7,800 crore of long-term money. And this is after the market dislocation happened. This is actually higher than the money we raised in H1. So, things have not changed and I'm not talking about commercial papers, which have changed, but this is non-commercial papers like NCDs.

Are you still borrowing from mutual funds at the same levels?

We are focused on long-term borrowing primarily and the same holds true for our borrowing from MFs as well. While the level is mostly the same long-term, it requires a bit of more effort. Earlier, if you had to do a ₹100-200-crore deal, it was easily available. But now for the same amount of fund we have to provide more data and statistics, but money is available. Yes, industry borrowing costs have gone up, but we are passing on the increases as well. Our cost has also gone up by 100 basis points in the last six months.

But what happens in total borrowings through bonds is that only a third is getting renewed. So, when 100 basis point cost is increased, the average is only 33 basis points, because of the ₹45,000 crore borrowing, only ₹15,000 crore is getting renewed every year, for instance.

So, what is getting repriced?

It is only about a third of your total borrowing that is getting repriced, and if your total cost increases by 120 basis points for the new borrowing, your average is only 40 basis points. Half of which we are also able to pass on. So if you look at our yields and spreads, they have not changed much. On the credit book if you see, if you look at what you call NIMs (net interest margins), they have not changed much.

How much is your borrowing now from commercial papers?

If you look at commercial paper for us now, it is actually less than 2%. It used to be 29% at one point last August.

Did the share of NCDs and bank loans jump?

NCDs and bank loans are now almost 90%, which are tenured. In FY17, 42% of our borrowing was mutual fund. Last year, we had brought it down to 30% and now they are down to 15%. So banks and retail...which is retail NCD, is now 23%.

Is the worst over for NBFCs?

I think now also overall liquidity is tight, not just for NBFCs, for everybody. Even today, general lending is about 50-60% of what it was a year ago. Like I said, liquidity is tight because of three major reasons and I see all three improving in the near future. So things should hopefully only improve from here.

What is your prescription for running Edelweiss now?

There are three-four things that are really paramount to building a business, which can tackle any risk events.

At least, this is what we believe and follow in Edelweiss religiously. First is ALM (Asset Liability Management) – as long as cash flows are matched positively, there will never be a problem of liquidity even in tough times.

So even today, we hold more than ₹10,000 crore in short-term liquidity, which is more than sufficient to pay off any near-term liabilities.

Second is gearing and capital adequacy – if you look at the US during the Global Financial Crisis, most of the banks were highly over-levered.

At Edelweiss, we always worry about building the equity cushion first and then think about growth. So our Ex-Treasury debt-equity ratio usually will never cross 5.5 since we will raise equity capital before that. In fact, we now have a debt-equity of less than 4 after receiving the first tranche of equity infusion from CDPQ. Finally, we have seen in India that good governance always pays in the long term. And we repeatedly emphasise on it, both internally and externally.