# Asset Finance Company: Role in an Emerging India

Newsletter

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SWARIT® ADVISORS

## Introduction

An Asset Finance Company is the one which provides finance for the physical assets, plant & machinery & equipment, involving a tremendous amount of investment.

Since India is considered one of the rapidly growing countries in terms of GDP, its infrastructure is developing at a considerable pace, the economy is growing faster and industrial development is taking place in almost all the sectors.

As far as the development is concerned, every business house requires big plants and machineries for expansion. In such cases, it may not be easy for them to pull out their existing funds for further development without affecting the flow of working capital.

For every capital expenditure, these business houses look out for such finance providers to cater the need of immediate funds without creating an internal clog in flow of funds. NBFCs have been more preferred options due to their reach, services and structured product offerings.

An Asset Finance Company, which is basically an NBFC categorized as an AFC, is the solution for such situations. These companies provide the funds as per the requirement of the borrower in comparatively lesser time-frame.

**Obligations for Asset Finance Companies (AFCs)**

-They should be a registered entity with RBI;

-They should follow the norms prescribed by RBI in terms of capital adequacy, credit/investment norms, Income recognition, Asset Classification, NPA provisioning, etc.;

-They should follow the KYC norms;

-They should adopt a Code of fair business practices.

**Market Overview of AFCs in the Indian Economy**

Current Indian economy is experiencing slowdown in a temporary phase and is anticipating huge demand of equipment in coming time from mining industries and infrastructure sector.

Therefore, NBFCs are restructuring and growing their network and products offering for robust growth. For the construction equipment which requires huge capital expenditure, financing is an appropriate alternate for the industry to spark demand and increase the customer base.

Financing accounts for approx. 80% of the total equipment purchased and in case of overseas purchase, it is even higher with about 90% of equipment purchased being financed.

According to the experts and sector insiders, the total size of the infrastructure equipment finance business in the country could be anything between Rs 25,000 crore and Rs 30,000 crore.

SREI claims to have a market share of about 30 per cent in the infrastructure equipment finance business and the positive outlook for the sector stems from the push given by the government to affordable housing and also roads construction.

**Market Segmentation:**


The equipment financing market has been divided into two parts on the basis of financers involved:

- Banks, and
- NBFCs.

NBFCs acquire the major portion of the market. The banks mainly provide funds to the needs of large players and are unwilling to cater the needs of the small and medium sized players whereas NBFCs fulfil the fund requirements at all levels of the market.

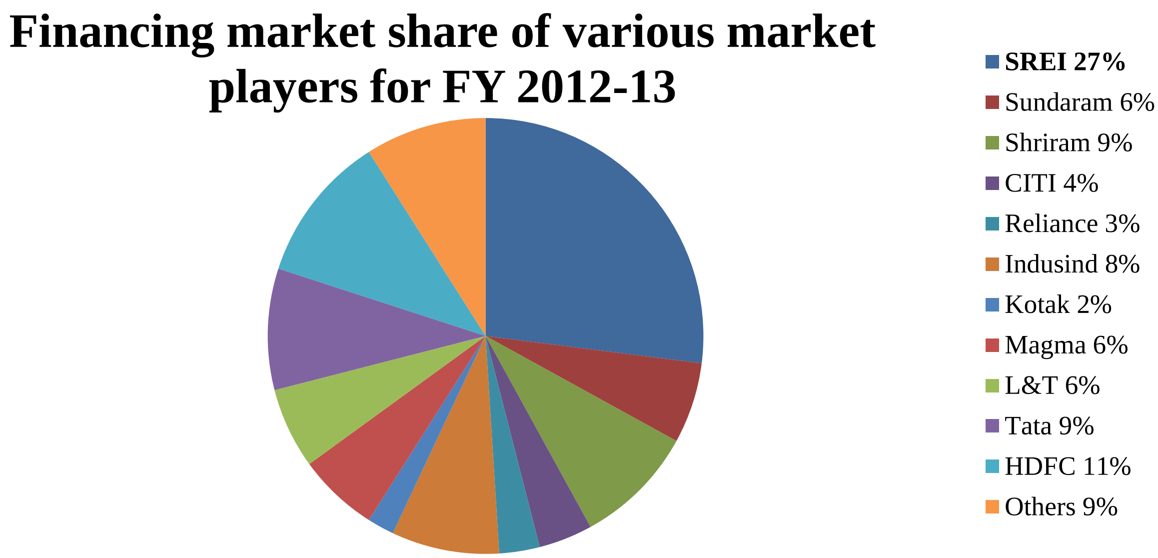
The MSME sector mainly approaches to the NBFCs to cater the requirement of funds for the equipment financing. NBFCs offer faster turn-around-time, doorstep services, tailor made schemes to suit individual requirement, higher loan to value, simple documentation process and various customer-friendly schemes. combination of these services makes the NBFCs leading players in the segment.

**Asset finance market players:**

**1. SREI Equipment Finance Ltd**

SREI Equipment Finance Ltd is a leading Equipment Finance Company in the Indian Market. As per the data, the Company was holding a market share of around 27% in FY 2012-13 followed by HDFC bank, Tata Capital and L&T.

The share of various market players for the FY 2012-13 can be depicted through the following figure:




Among the NBFCs, as stated above SREI Equipment Finance Ltd continues to grasp the largest share (about 30%) in the ECE financing market for the FY 2014-15 followed by Tata Capital and Sundaram Finance occupying 7% and 6% share of the market respectively.

**<u>2. Magma Fincorp Limited</u>**

Magma Fincorp Limited was incorporated in 1988 and registered with the Reserve Bank of India as an asset financing NBFC.

Magma today is one of the largest asset finance companies and has been one of the fastest growing asset financing companies in the country with a disbursement CAGR of over 26% in the past five years.

Several numbers of financial products and services offered by Magma as follows:

- Commercial Vehicle Finance

- Construction Equipment Finance
- Car and Utility Vehicle Finance
- Suvidha Loans (Refinance)
- Strategic Construction Equipment Finance
- Tractor Finance
- SME Loans

## Good Time Ahead for Financing Industry

The big developers usually sub-contract part of their work for execution to the small and medium scale entrepreneurs who constitute the bottom of the infrastructure pyramid in infrastructure projects. However, these players do not enjoy access to institutional financing (like banks).

Thus, it is the NBFCs that cater to the credit needs of such entrepreneurs. The NBFCs have in-depth knowledge of the credit requirements of these players and have a fair idea of their capability. NBFCs' decision-making process is also much faster than banks. NBFCs extend credit to these players on the basis of their track record, their order books, cash flow, etc. Credit intermediation has been the most preferred route for credit expansion and NBFCs have played this role for the past 30 odd years to near perfection.

Thus, NBFCs have a big role to play in rectifying the supply-demand imbalance at the bottom of the pyramid. RBI is also playing a positive role by re-classifying the various categories of NBFCs so that all NBFCs do not operate under a blanket regulatory framework.

This is the right approach by RBI to acknowledge the contribution of NBFCs like the Asset Finance Companies (AFCs) and the

Infrastructure Finance Companies (IFCs) to the process of nation-building. However, NBFCs like AFCs and IFCs need a level playing field vis-à-vis banks in order to perform their duties better.

**Conclusion**

In spite of various reforms made by the Government, NBFCs do not enjoy a level playing field vis-à-vis banks and other financial institutions, especially when it comes to issues like making provisions for bad loans, while recovering assets once a loan goes bad or paying taxes on sticky advances. With the regulatory framework tilted heavily in favour of borrowers, this creates incentives for wilful defaults. With most borrowers working in government/quasi-government projects, repossession of assets in case of defaults becomes even more challenging for NBFCs.

The only way forward to resolve this issue is to intensify the dialogue process with government authorities at various levels and make them realize that the faulty policies are costing India dear yet NBFCs have been preferred by customers due to their reach, services and structured product offerings. With RBI's decision to launch infra NBFCs, the NBFC's stand against banks have some strengths, however there is still a lot to come from the government in terms of NBFC support.

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