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Effect Of Demonetization On NBFCS & MFIS

Ms. PriyankaTanwar
Assistant Professor
IBMR, IPS Academy, Indore(M.P)

ABSTRACT

On November 2016,Indian government adopted demonetizationto tackle with black money and make India a cashless digital economy.Thepaper studies the effect of demonetization on NBFCs & MFIs.Non-banking financial companies (non-banking financial companies) are seeing healthy credit growth over the last few years due to high growth in domestic finance and consumer durables segment in the last financial year. Micro-finance institutions (MFIs) and non-banking financial companies (NBFCs) may have to face challenges in collecting monthly collection from their small retail customers to withdraw notes of Rs 500 and Rs.1000 .MFI can see some near-term difficulties in collection of lending to rural customers without access to branches and post offices. The RBI also given some suggestions or way out like Exchange of SBNs, Acceptance of SBNs and enhance the cash withdrawal limitto overcome with this demonetization effect on NBFCs and MFIs.The aim of mobility is to convert black money into white money, but consolidated development can only be achieved when these fundsare used for development purposes.

Keywords: Demonetization, Digital Economy, NBFC, MFIs, Government

INTRODUCTION

Demonetization has been an highly dynamic decision of the government of India in the last 50 years.When the economy was facing acute shortage of liquid currency it was feared that soon the Indian economy will face challenging recession in coming financial years.On one hand there was a problem of a huge amount of black money in the form of unaccounted cash in the hands of large numbers of peoples and the masses on the other hand where facing unemployment, poverty and poor living conditions.This was very fearsome threat to the economy because parallel economies having paradox of co-existence of extreme poverty and extreme richness have resulted in bankruptcy of advance nation in the world. The after affects of American & European recession upto 2009 are still visible & many nations are highly vigilant about the economic functioning.On this backdrop it will be interesting to study the effects of demonetization on NBFCs & MFIs.

OBJECTIVES

1) To discuss the effect of demonetization on Non-Banking Financing Companies (NBFCs) and micro financing institutions (MFIs).

NBFCS, MFIS & THEIR CUSTOMERS

India has a large number of Micro Financing Institutions (MFI), which caters to the financial needs of rural and semi-urban Indian populations. Customers, usually human beings (women, daily wagelabours/workers, farmers), small traders and retailers, mainly work on the basis of cash due to the informal and the trivial nature of the amounts involved in such transactions. Loan installments from some such clients/customers are typically collected on a daily basis and weekly. Due to demonetizationthe business transactions of these individuals are temporarily stopped which are running on a daily credit basis.There is a domino effect on institutions (NBFC-MFI) whose livelihood is based on cash payment, such customers do not have bank accounts and / or adequate resources to exchange currency in their possession, or make changes in cash without means of finance. This is adversely affecting their daily business / life, which in turn is affecting the reinsurance on the time taken by the NBFC&MFIs. These loan defaulters are moving towards the temporary increase in non-performing assets of NBFC-MFIs, which generally rely on borrowing from banks for further loans. The adverse impact of the NBFC-MFI's on the overall asset quality will eventually fall down into the banks and other financial institutions and hence it influencedthe Indian economy completely.

RBI figures show that in India 80 percent of monetary circulation is about Rs. 500 and Rs. 1000 notes. This demonetization is putting more than 80 percent of the country's monetary economy under the suspicion of black money. It creates confusion between " black money &unaccounted money". The aim of mobility is to convert black money into white money, but consolidated development can only be achieved when these fundsare used for development purposes. However, the government is withdrawing subsidy, and reducing expenditure on developmental areas. The development is in the spirit of smart cities and cashless economies but enough time and effort are needed to be a cashless and digital economy in India. Process can not be completed in the night or fortnight or months.

DEMONETIZATION EFFECT ON NBFCS & MFIs

Government has notified gazette notification no 2652 dated November8, 2016, to ban Rs.500 and Rs. 1000 notes(Specified Bank Notes or SBNs) as legally effect from November 9,2016, with an intention to eradicate smuggling,terrorism and circulation of counterfeit notes.This step, which aims at keeping the country's black money in jeopardy for years, can already have an impact on less organized / unorganized business and the financial sectors of the country.Micro-finance institutions (MFIs) and non-banking financial companies (NBFCs) may have to face challenges in collecting monthly collection from their small retail customers to withdraw notes of Rs 500 and 1,000 rupees. "MFIs can see the closest difficulty in the collection to lend the rural customers without access to bank branches and post offices.

NBFC-MFI generally relies on borrowing additional loans from banks. Due to limited capital, defaults from customers can not only be done by limited NBFC-MFI business but also by limiting their liquid resources, and force them to stop distribution of further loans.

According to various circulars issued in November 2016, the exchange of SBNs on the counter has been effectively limited to Rs. 2,000 / - and can be done only once per person from November 18, 2016. In addition, cash withdrawal from bank accounts on the bank counter has been restricted to 24,000 / - per week, upto 24th November, 2016. RBI has clarified its circular dated November 10, 2016, that the upper limits on withdrawal are not applicable to cash withdrawal from the bank account- (i) a bank from any other bank; (ii) post office; (iii) Currency converter that operates at international airports; and (iv) Operators of White Label Automatic Teller Machines ("ATMs") without specifying that these limitations were only for saving accounts or for any other bank accounts. After this, through the circular of November 14, 2016 and November 21, 2016, the RBI clarified that the maximum amount of Rs. 50,000 per week can be withdrawn from current / overdraft (excluding individual overdraft accounts) and cash accountwhich has been operated for the last 3 months or more. As mentioned above, NBFC-MFI usually lends to small customers by borrowing from banks. Therefore, by placing a limit on withdrawal by NBFC-MFIs, they will be severely restrained from withdrawing money from their existing accounts to lend them ahead of their customers.

SUGGESTIONS/WAY OUT

According to December 2015, the report of the Reserve Bank of India titled "Report of the Committee on Medium –term path on financial inclusion", the number of branches population of per 100,000 in rural and semi-urban areas is less than that in urban and metropolitan areas.

The presence of ATMs in rural areas is very low. However, NBFC-MFI has very strong reach in rural areas and semi-urban areas where there is very little entry in the banks. Therefore, in order to reduce the difficulty and financial crisis faced by NBFC-MFIs and the rural and semi-urban communities, Government / RBI may consider the following:

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1. **Exchange of SBNs :-**

   The government can take advantage of the comprehensive infrastructure and allow NBFC-MFI to be eligible for exchange of SBNs against valid compliance documents in rural and semi-urban areas.

2. **Acceptance of SBNs :-**

   NBFCs-MFIs act as facilitators and up to December 30,2016 through SBNs,the repayment of the loan from its customers can be allowed while complying with all the other control and KYC requirements in compliance with the prescribed by the Reserve Bank of India in this regard. This loan will inadvertently help in reducing cases of default and also to ensure that the overall asset quality of the NBFC-MFI sector does not get eroded.

3. **Enhance the withdrawal limits :-**

   In order to provide necessary operational flexibility and as well as being aware of increasing business needs, the Government / Reserve Bank of India may consider restoring the daily / weekly clearance limit for the companies involved in Micro-financing sector. The decision to make SBNs political is to prevent anti-national activities, it is a welcome move, a person should consider adopting the above measures to reduce the plight of informal cash-operated sectors and resolve the infection.

CONCLUSION

"In the near term, financial sector companies, such as microfinance institutions (MFIs) and non-banking financial companies (NBFCs) are working in cash-intensive businesses, due to insufficient lines of credit from banks and liquid assets, liquidity. If normalcy is restored in the next few weeks, then the NBFC intervention will be able to absorb. "

"We believe that given the cash flow of the borrower segment NBFC-MFIs and small finance banks (SFBs) cannot be significantly affected in the long run, usually occur in small communities. However, obstacles to the near-term collection cycle also, the outstanding amount can increase, so that their liquidity can be distribution cycle under force and pressure. "" NBFCs can be self-employed, SMEsand other small businesses are catering to the cash, which may experience some delays in payments due to the difficulty in converting their holdings within the time prescribed by the customers." Housing Finance Companies (HFCs) catering for self-employed segments, especially in small ticket loans, may experience late delays.

Similarly, due to the aggressive credit practices of many banks and non-banking financial companies (NBFCs), loans against property (LAP) face business asset quality risk. In this case, while deciding on income eligibility and loan amount for the borrower, unaccounted income is kept in mind. Especially NBFCs asset quality of retail asset fixers, have developed expertise in the credit rating of the informal segment and have created models around it to come under pressure in the short term. For long, implications for NBFCs can be a risk profile change, because strong borrower profiles can potentially migrate to banks.

In the medium term, especially in the secondary market and tier II cities where the cash component is important as the proportion of real estate demand, the trickle-down effect can be confronting the entire region. This NBFC and housing financiers have been created with large-scale risks (LAP / mortgages) with self-employed customer profiles.

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