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SOURCES OF FINANCE II

NBCs are broadly divided into **two categories**:

Deposit taking (NBFC-D) and **non-deposit taking** (NBFC-ND). Among non-deposit taking NBCs, companies with an asset size of ₹500 crore or more have been further categorized as systemically important (NBFC-ND-SI).

PUBLIC DEPOSITS

Public deposits means a deposit as defined under **section 45-I(bb) of RBI Act, 1934,** excluding the following:

a) Any amount received from central government, state government or any other source, whose repayment is guaranteed by central govt., state govt., or any amount received from a local authority or a foreign govt., foreign citizen, authority or person;

b) Any amount received from IDBI, LIC, GIC, SIDBI, UTI, NABARD, Electricity Board, ICICI, IFCI, 1IBI, STC, REC, MMTC, AFC, ADB, IFC, Tamil Nadu Industrial Investment Corporation Ltd., SICOM, Gujarat Industrial Investment Corporation, or any other institution specified by the RBI;

c) Any amount received by a company from any other company;

d) Any amount received by way of subscriptions to any shares, stock, bonds, debentures pending allotment;

e) Any amount received from a person who at the time of receipt of the amount was a Director of the Company, or any amount received from its shareholders by a private company;

f) Any amount raised by the issue of bonds or debentures secured by the mortgage of any immovable property of the company or by any other asset;

g) Any amount brought in by the promoters by way of unsecured loan;

h) Any amount received from a mutual fund governed by SEBI;

i) Any amount received from a relative of a Director of a Company;

j) Any amount received by way of issuance of commercial paper as per RBI guidelines;

k) Any amount received by a Systemically important non-deposit taking NBCs by issuance of perpetual debt instruments:

l) Any amount raised by issuance of Infrastructure bonds, by an infrastructure finance company;

m) Any amount raised by issuance of non-convertible debentures with a maturity of more than one year and having a minimum subscription per investor at 1 crore and above;

n) Any amount received as hybrid debt or subordinated debt the minimum maturity period of which is not less than sixty months.

Acceptance of Public Deposits

Provisions contained in this direction shall not apply to a Mutual Benefit Financial Company or a Mutual Benefit Company.

Restrictions on acceptance of public deposits by NBFCs

a) Minimum Credit Rating :

- No NBFCs having net owned funds (NOF) of twenty five lakhs and above, shall accept public deposits unless **it has obtained a minimum investment grade or other specified credit rating for fixed deposits from any one of the approve credit rating agencies at least once a year** and copy of the **rating is sent to RBI along with the return on prudential norms.**

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- In the event of upgrading or downgrading of credit mating of any NBFC, it must inform to RBI in writing within 15 working days of it being rated so, about up grading or downgrading

b) Approved Credit Rating Agencies and Minimum Investment Grade Credit Rating:

Agency	Minimum investment grade rating
CRISIL	FA-
ICRA Led	MA-
CARE	CARERBE (FD)
Fitch Ratings	ta-(ind) (FD)
Brickwork	BWR FBBB
SMERA	SMERA A

c) Prohibition from accepting demand deposit:

No NBFCs shall accept or renew any public deposits which are repayable on demand.

d) Period of public deposit: No non-banking financial company shall accept or renew any public deposit, unless such deposit is **repayable after a period of 12 months but not later than 60 months from the date of acceptance** or renewal thereof.

e) Ceiling on quantum of deposit: An asset finance company or a loan company or an investment company, having minimum NOF and complying with all prudential norms, **may accept or renew public deposit, the total amount of such deposits accepted by them should not exceed one and one half times of its NOF**.

f) Downgrading of Credit Rating: In the event of the downgrading of credit rating below the minimum specified investment grade, an NBFC, being an asset finance company or an investment company or a loan company, shall regularize the excess deposit with immediate effect, by stopping accepting fresh public deposits and renewing excess deposits, by running off all existing deposits to maturity and reporting the position to RBI within 15 working days.

g) Ceiling on the rate of interest: No non-banking financial company shall invite or accept or renew public deposit at a rate of interest **exceeding twelve and half % per annum**.

h) Payment of Brokerage:

No non-banking financial company shall pay to any broker on public deposit collected by or through him,-

- brokerage, commission, incentive or any other benefit by whatever name called, in excess of 2% of the deposit so collected; and
- expenses by way of reimbursement on the basis of relative vouchers/bills produced by him, in excess of 0.5% of the deposit so collected.

i) Intimation of maturity of deposit to the depositors: It shall be the obligation of the NBFC to intimate the details of maturity of the deposit to the **depositor at least two months before the date of maturity of the deposit.**

j) Renewal of public deposit: Where an NBFC permits an existing depositor to **renew the deposit before maturity for availing of the benefit of higher rate of interest**, it will pay the depositor the increased rate of interest subject to:

- The deposit is renewed for a period **longer than remaining period of the original contract;**

k) Rate of interest on premature repayment of public deposits:

- After 3 months but before 6 months - No interest
- After 6 months but before the date of maturity -**interest payable shall be 2%** lower than the interest rate applicable to a public deposit for the period for which the public deposit has run or if no rate has been specified for that period, then 3% lower than the minimum rate at which public deposits are accepted by the non-

BANK FINANCE

In terms of section 45-IA of the RBI Act, 1934, all NBFCs have to mandatorily register with RBI.

Bank Finance to NBFCs registered with RBI

Banks must develop a suitable loan policy, with the approval of their Board of Directors, for extending certain credit facilities in the form of working capital or term loans, within the prudential guidelines and exposure norms, subject to the condition that they are within the permissible activities of NBFCs (registered with the RBI), **engaged in infrastructure financing, equipment leasing, hire-purchase, loan, factoring, and investment activities.**

Bank Finance to NBCs not requiring Registration

- In respect of NBFCs which do not require to be registered with RBI, viz. **Insurance companies registered under section 3 of the Insurance Act, 1938**
- Nidhi Companies notified under **section 620A of the Companies Act, 1956**
- Chit fund companies carrying on **Chit Fund Business** as their principal business as per Explanation to clause (vii) of Section 45-I(bb) of RBI Act, 1934
- **Stock Broking Companies/Merchant Banking Companies registered under section 12 of the SEBI Act,**

Bank investment in Non-Convertible Debentures

Banks are permitted to **invest in Non-Convertible Debentures (NCDs) with original or initial maturity of up to 1 year** issued by NBCs subject to prudential guidelines and the issuer having disclosed the purpose in the disclosure documents, and such purpose being eligible for bank finance.

Activities not eligible for Bank Credit

Bills discounted/rediscounted by NBCs, except for rediscounting of bills discounted by NBFCs arising out of sale of-

a) Commercial vehicles (including light commercial vehicles) and
b) Two wheeler and three wheeler vehicles subject to the undernoted conditions:

- the bills should have been **drawn by the manufacturer on dealers** only.
- the bills must represent **genuine sales transaction as may be confirmed by chassis/engine number.**
- the banks should satisfy themselves **about the bona fides and track record of the NBFCs which have discounted the bills**.

c) Investments of NBFCs both **of current and long-term nature,** in any company/ entity by way' of shares, debentures. Stock broking companies may however be extended need based finance against shares and debentures held by them as stock in trade.
d) **Unsecured loans/inter corporate deposits** by NBFCs to/in any company.
e) **All types of loans and advances** by NBFCs to their **subsidiaries, group companies/entities.**
f) Finance to NBFCs for **further lending to individuals for subscribing to Initial Public Offerings (IPOs) and for purchase of shares from secondary market.**
g) Banks should not **grant bridge loans of any nature or interim finance against capital/debenture issues and/or in the form of loans** of abridge nature pending raising of long-term funds from the market by way of capital, deposits etc. to all categories of NBCs and RNBCs.
h) **Shares and Debentures cannot be accepted as collateral securities** for secured loans granted to NBCs for any purpose.

i) **Banks should not execute guarantees covering inter-company deposits/loans thereby guaranteeing refund of deposits/loans accepted** by NBFCs. Guarantees should not be issued for the purpose of indirectly enabling the placement of deposits with NBFCs

COMMERCIAL PAPER

Commercial Paper (CP) is an **unsecured money market instrument** issued **in the form of a promissory note**, was introduced in 1990 with the objective of providing highly rated corporate borrowers access to **money market by diversifying their source of short term borrowings**.

- unsecured promissory note issued by public or private sector companies
- maturity period 15 days to 1 year
- can be issued by companies with good reputation & creditworthiness
- banks & mutual funds are main investors

SHORT TERM AND LONG TERM BONDS

Bonds: Bonds are debt security where an **issuer is bound to pay a specific rate of interest as per the terms of payment and repay the principal amount at a later time.**

- Bond holders are **similar to creditors** in that interest is paid at an agreed-upon rate at an agreed-upon periodicity, and principal is paid at the end.
- Bonds are classified as **short term or long term based on their maturity length.**
- Bonds can be categorised as **variable rate or fixed rate depending on the coupon kind.**

- The various forms of ties can also be categorised according to their users. The different instruments can be classified as under two broad heads:

a) SLR securities
b) Non-SLR securities

COLLATERALIZED BORROWING AND LENDING OBLIGATION (CBLO)

- CBLO is a collateralized money market instrument that enables **borrowing and lending of funds between banks, primary dealers, and other financial institutions**.

- It is a **short-term instrument with a maturity period of 1 day to 1 year.**

- The interest rate on CBLO is market-determined and is based on the prevailing **market conditions, demand and supply of funds, and the creditworthiness of the parties involved.**

- CBLO transactions are **executed through the electronic trading platform of CCIL**, which acts as a central counterparty and provides clearing and settlement services for the transactions.

- The **underlying collateral for CBLO transactions is government securities,** which are pledged by the borrower and held by CCIL as collateral until the maturity of the CBLO.

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- The **minimum denomination for CBLO is Rs. 1 lakh and multiples** thereof.

- CBLO provides a **safe and secure way for financial institutions to borrow and lend funds in the money market**, with the underlying collateral providing a level of security for the lender.

CBLO is an **alternative to other money market instruments** such as treasury bills, commercial paper, and certificates of deposit, providing investors with greater flexibility and diversity in their short-term investments.