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FIBAC | Risk Sharing / Co- Lending

MSME - Next Wave

DECEMBER 2021

Panelists



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Yes Bank



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Exec. Chairman
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Central thoughts

The aspiration of co-lending is risk sharing and to facilitate synergies between CASA funded balance sheets to NBFCs/FinTechs

- Banks bring cost of fund advantage
- NBFCs bring efficient last mile reach with asset class specialization

In theory, the economics of co-lending can be sound and attractive

- 400-600 bps of potential value unlock across funding cost and opex efficiency

In practice, scaling up has been a challenge

There are three central hurdles

- Asset class selection / prioritisation:
 - Banks and NBFCs lack financial / economic models that clearly establish cost-benefits
 - Missing prioritization of asset classes that are best suited for market expansion via co-origination
- Organizational:
 - Consequently, we don't see dedicated organizational resources with the right skills and KPIs
- Operational and technical:
 - Multiple wrinkles need to be ironed out - KYC, Common underwriting policies / score cards / rules, NPA recognition norms, statement-of-accounts synchronization, de-duping logic etc...

We need to create an industry standard open platform for co-lending

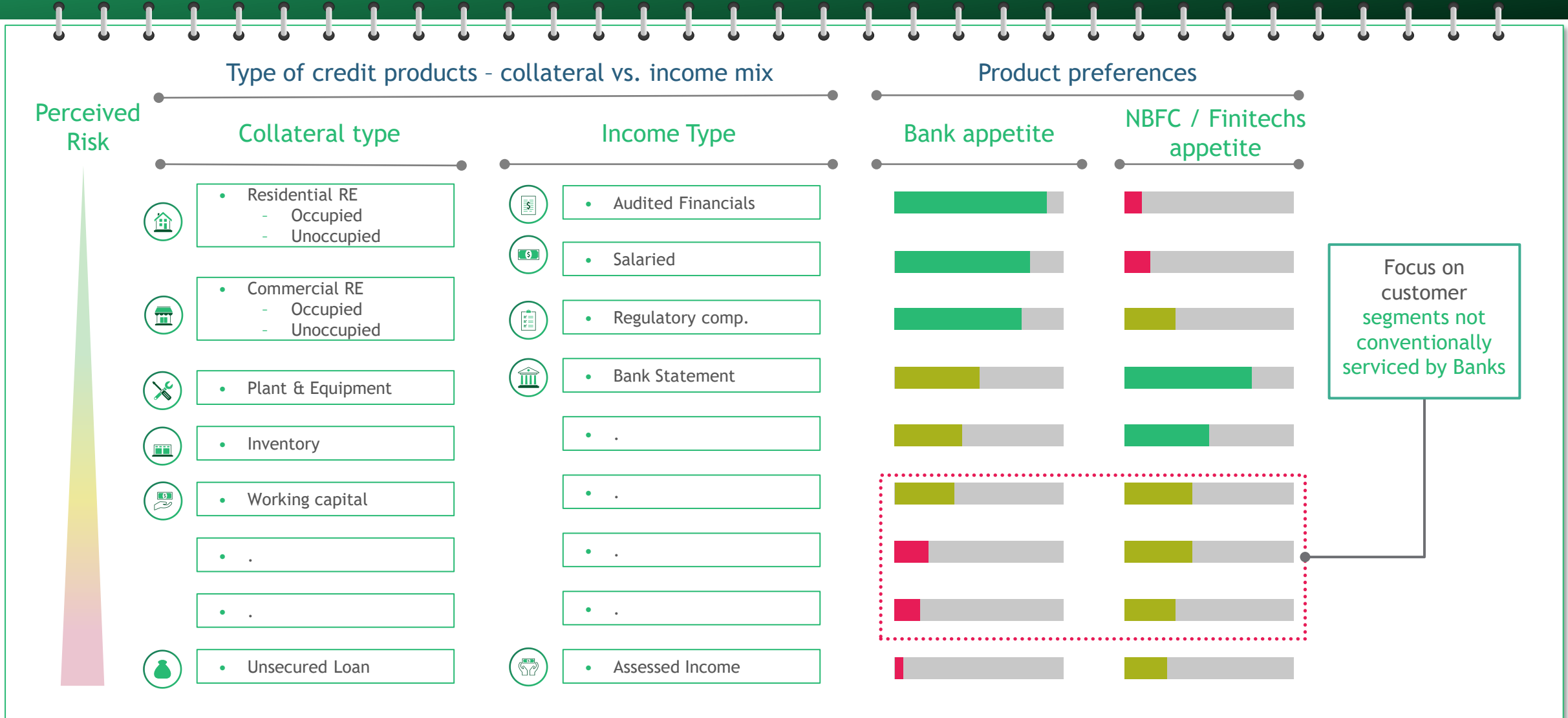
Our recommendation can address these problems at a banking system level in the near term

In the long term the proposed solution could deepen co-lending market and drive even greater liquidity

- Current co-lending regulations (while not explicitly) but implicitly enable one Bank - NBFC pair
- Long term it is possible to have multiple banks partnering with one NBFC on the same transaction with risk sharing

Introduction to the panel

There is natural synergy between Bank and NBFCs/FinTechs



Co-lending can be a win-win proposition



Banks



ROE increased by **4-6%**



Improved cost to income ratio by **150 - 200 basis points**



Better reach to newer geographies



NBFCs / HFCs



Lower COF by **150-250 basis points** & additional fee income



Access to **new customer segments**



Off balance sheet leverage



Customers



ROI reduces by **100 -200 bps**



Quicker & more accessible loans



Access to **enhanced portfolio suite**

Question for panel

Do you feel co-lending is a real opportunity?

What has been your
experience?

Which Products are likely to work? Examples...

TL Secured
- LAP,
Home
Loan

TL Secured
- Plant &
Equip

WC
Secured -
invoice,
inventory

Unsecured

Question for panel

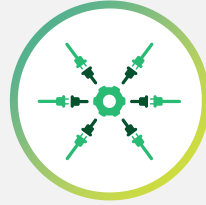
What are the hurdles?

Key hurdles to adoption of co-lending model



Identifying & onboarding the right NBFC Partner

- Incorrect risk-rewards sharing



IT systems integration

- Field mapping for Bank & NBFC LOS & LMS system



Alignment of operating model & ownership sharing

- Lack of clarity on ownership of customer



Alignment of accounting methodologies

- Interest calculation based on 360/365/actual days



Legal and compliance

- Misalignment in KYC standards & underwriting standards
- Ownership of NBFC's co-lending book in case of solvency

Question for panel

What will it take to sustain a
good partnership?

Key impediments to a co-lending partnership

1	Upfront risk assessment & alignment of strategic & financial arrangements	➤	<ul style="list-style-type: none"> • Banks not able to assess risk they are underwriting • Absence of FLDG impacts process design - increase in checks during sourcing • Bank and NBFC not able to align on product, geographies & target segments
2	Operating model alignment	➤	<ul style="list-style-type: none"> • Alignment on post disbursement asset inspection & hypothecation • Floating rate vs fixed rate loan • Design of credit policy/ process disrupting normal field operations e.g. FoS preferring normal sourcing over co-lending due to higher checks in co-lending
3	Lack of ownership from both entities	➤	<ul style="list-style-type: none"> • Lack of dedicated focus from internal teams leading to higher # of issues and resolution TAT
4	Difference in Accounting methodologies	➤	<ul style="list-style-type: none"> • Interest calculation method • Overdue's assignment order • IndAS vs IGAAP
5	Legal & compliance	➤	<ul style="list-style-type: none"> • Pari passu on assets • Right to initiate SARFAESI proceedings • Rights & procedure in case of bankruptcy of NBFC



IT implementation a major area of concern for Banks

Architecture & configuration alignment across systems



LOS integration challenges: Different mandatory fields, journey flow b/w Bank & NBFC

LMS integration challenges: Different charge masters, interest computation mechanism, holiday period treatment.

Breakage in integration due to poor testing



Multiple breaking points due to handovers across systems of both entities; Rigorous end to end testing required before launch

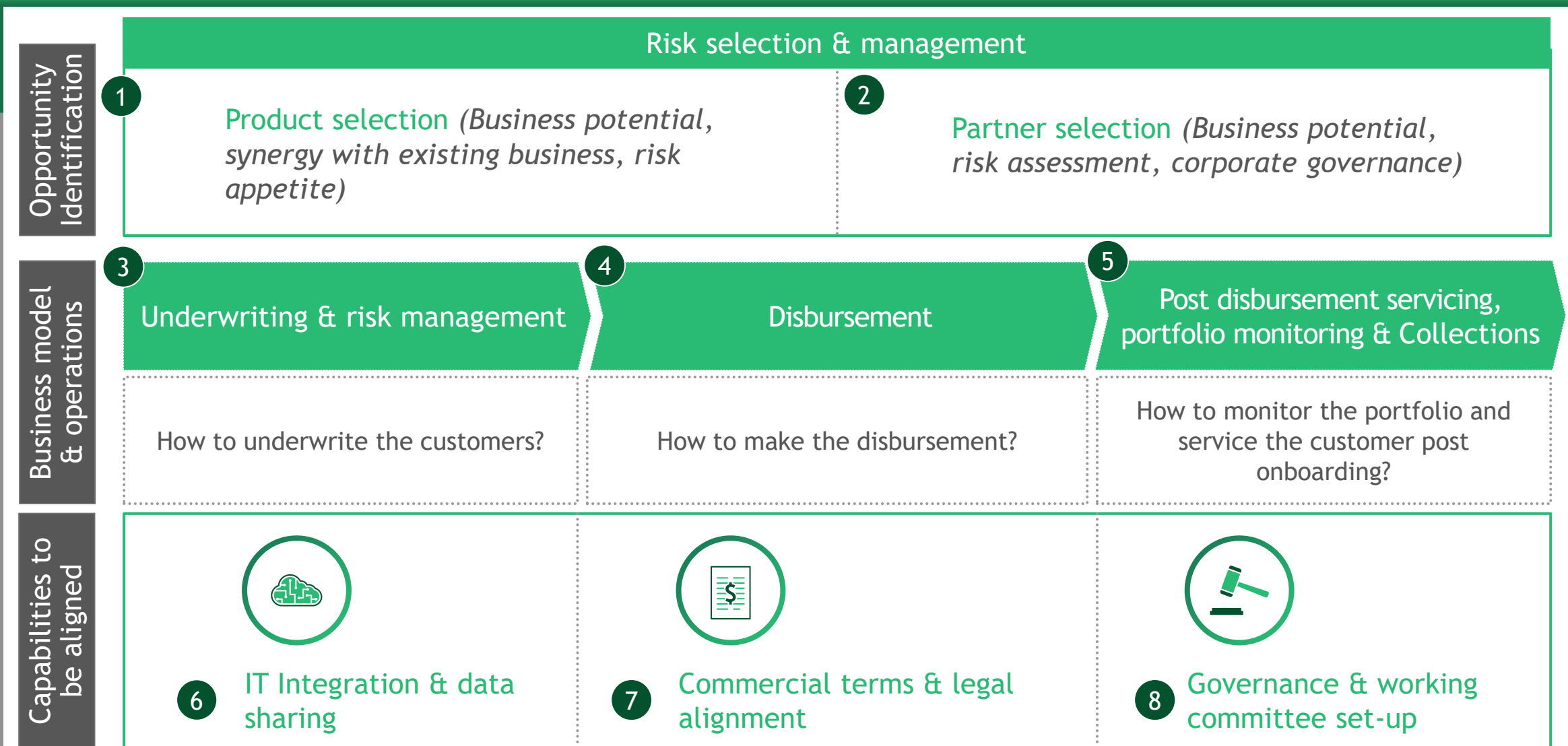
Field team not trained on new processes & journey



Significant effort required to onboard & train field team to adopt new process

- **Field inputs may be incorporated during design** to ensure seamless process flow

Eight key steps to define a successful co-lending strategy for banks



Question to panel

Can India set the standards via
an open CLM2.0 platform?

NBFC / FinTech

Co-lending enabled LOS
Leverage OCEN framework

Co-lending enabled LMS
RBI issued accounting norms, NPA recognition...

Customer Service APIs
Complains, Escalations, Service Requests, Joint Account Stmt....

Customer Data APIs
KYC, Demographics, Bureau...

Portfolio Data APIs
Access to loan-tape data from LMS...

CLM 2.0 Market Place

Credit Assessment Module
Standardized formats by asset class e.g. PL, CD, BIL, LAP...

Risk Scoring Module
Parameterized models by asset class

Portfolio X-Ray Module
Automated segmentation of portfolio into risk buckets

Program Management Module
Program KPI tracking dashboard - C-Sat, Credit parameters etc...

NBFC - Bank Onboarding Module
Standardized integration templates

Banks

Co-lending enabled LMS
PSL tagging, NBFC partner tagging, NPA recognition...

Operating Risk Management Module
De-dupe, AML, risk scrub etc...

Customer Data APIs
KYC, Demographics, Bureau...

Portfolio Data APIs
Access to loan-tape data from LMS...

Once 1 Bank to 1 NBFC format stabilizes, this platform can be extended to multiple Banks to NBFC format to deepen market

Takeaways

1. Deepen longer tenor products
2. Dedicated business model
3. Dedicated resources and org with new mindset
4. New products custom built for co-lending
5. Harmonization of policy
6. Advancements in origination but also collections and recovery
7. Raise credit standards overall
8. Use of tech critical
9. Journey - start with microcosm of CLM book...end state can be platform
10. Multi thousands crores of retail and MSME being targeted

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