FOR IMMEDIATE RELEASE
May 25, 2012

RBI measures a credit positive for Gold Loan companies; though could impact profitability

Gold loan companies, are estimated to have grown by a CAGR over 100% over last three years, with the portfolio of top three companies reaching over Rs. 41,000 crore as on December 31, 2011. Given the rapid pace business growth and risks involved (concentration risk and market risk due to adverse movement of gold prices), RBI introduced prudential measures on March 22, 2012 for NBFC's with over 50 percent of their financial assets in Gold loans.

These measures are likely be credit positive in the long term for the gold loan companies as they introduce stringent LTVs and require them to maintain higher level of superior capital (Tier 1 capital of 12% by April 1, 2014 as against around 10% current requirement). However, over the short term, fresh disbursements could reduce because of lower LTVs; additionally delinquencies may build up as the loan eligibility of the borrowers, who want to refinance, would come down. Further, the regulations are likely to impact the competitive positioning of Gold Loan companies vis a vis banks (as the regulation is applicable to only NBFC's).

Highlights of the key measures and likely impact are as follows:

Key Measures

- Loan-to-Value(LTV) ratio not to exceed 60 percent for loans granted against the collateral of gold jewelry
- Disclose the percentage of Gold loans to their total assets in the balance sheets
- Not to grant loans against bullion / primary gold/ gold coins
- Higher Tier 1 capital requirement of 12% (against 10% currently) by April 1, 2014 for NBFC's engaged in lending against gold jewelry

Impact

As per ICRA estimates, relatively a small proportion of the lending is at 60% or lower LTVs, therefore disbursements volumes are bound to reduce. However, current LTVs are typically applied after taking haircuts for making changes, precious stones etc, if we were to gross these up and then compute loan eligibility based on overall cost to the borrower, impact on the disbursement volumes may not be so severe. Further, lower LTVs could lower the yield of the gold loan portfolio of NBFCs (typically lending yields reduce as LTVs go down) impacting their return on equity. Currently rates offered on 60% LTV scheme by a leading Gold loan company are lower than weighted average yields by 5-6%, therefore, the way value of collateral value is computed, would have a significant bearing on the profitability of Gold Loan Companies. In case value is based on customer acquisition price, impact on profitability is unlikely to be significant; else significant repricing or cost rationalization would required to offset pressure on profitability. Pressure on lending yields and disbursement volumes, could get more pronounced as the competing banks do not need to abide by the 60% LTV norms. Apart from growth prospects and profitability, RBI's new measures could also impact asset quality of the Gold loan companies adversely in the short term, as the borrowers who want to refinance their loans would end up, getting eligible for a lower amount of loan than the existing loans availed before RBI's new guidelines.

As for capitalization, most of ICRA rated NBFCs have Tier 1 in excess of 12%, therefore would not need external capital to meet the regulatory norm. At the same time, it would require these growth oriented players to maintain superior Tier 1 capital in future, which is a credit positive. Moreover, with return on equity expected to reduce, reliance on external equity for Gold loan NBFCs, would go up in case these were to maintain high growth trajectory. The regulation also increases the gap between banks and Gold loan NBFCs as far Tier 1 capital is concerned. Tier 1 capital for a bank for gold loan portfolio at 60% LTV would be negligible, while it would be as low as 1.5% for as high an LTV as 80%. Although bank balance sheets are more diversified, credit and market risk on Gold loan portfolio may be similar (to that of NBFCs), there may be some merit in increasing Tier 1 capital requirement for banks as well to bridge the whopping current gap in Tier 1 capital adequacy requirement on the Gold loan portfolio.

For further details please contact:

Analyst Contacts:
Ms. Vibha Batra, (Tel. No. +91-11-4545 302)
vibha@icraindia.com

Registered Office
ICRA Limited
195, Kailash Building, 11th Floor, 96, Kasturba Gandhi Marg, New Delhi 19001
Tel: +91-11-93357940-50, Fax: +91-11-93357014

Corporate Office
Mr. Vivek Mathur
Mobile: **9871221122**
Email: vivek@icraindia.com

Building No. 8, 2nd Floor, Tower A, DLF Cyber City, Phase II, Gurgaon 199009
Ph: +91-124-4545310 (D), 4545300 / 4545800 (B) Fax; +91- 124-4050424

Mumbai **Mr. L. Shivakumar** Mobile: **9821086490** Email: shivakumar@icraindia.com 3rd Floor, Electric Mansion, Appasaheb Marathe Marg, Prabhadevi, Mumbai - 400 095 Ph : +91-99-9433 946/ 953/ 969/ 974/ 986/ 987 Fax : +91-99-9433 1390	**Kolkata** **Mr. Jayanta Chatterjee** Mobile: **9845099459** Email: jayantac@icraindia.com 5th Floor, Karumuttu Centre, 498 Anna Salai, Nandanam, Chennai-600035. Tel + (91 44) 45964300, Fax + (91 44) 9434 3663
Chennai **Mr. Jayanta Chatterjee** Mobile: **9845099459** Email: jayantac@icraindia.com 5th Floor, Karumuttu Centre, 498 Anna Salai, Nandanam, Chennai-600035. Tel + (91 44) 45964300, Fax + (91 44) 9434 3663	**Bangalore** **Mr. Jayanta Chatterjee** Mobile: **9845099459** Email: jayantac@icraindia.com 'The Millenia', Tower B, Unit No. 904, 9th Floor, Level 9, 19-14, 1 & 9, Murphy Road, Bangalore - 560 008 Tel:91-80- 43396400 Fax:91-80-43396409
Ahmedabad **Mr. L. Shivakumar** Mobile: **989986490** Email: shivakumar@icraindia.com 907 & 908 Sakar -II, Ellisbridge, Ahmedabad- 380006 Tel: +91-79-96585494, 96589008,96585049, 96584994 TeleFax:+91-79- 9648 4994	**Pune** **Mr. L. Shivakumar** Mobile: **989986490** Email: shivakumar@icraindia.com 5A, 5th Floor, Symphony, S.No. 99, CTS 3909, Range Hills Road, Shivajinagar,Pune-411 090 Tel : (91 90) 9556 1194 -96; Fax : (91 90) 9556 1931
Hyderabad **Mr. M.S.K. Aditya** Mobile: **9963953777** Email: adityamsk@icraindia.com 301, CONCOURSE, 3rd Floor, No. 7-1-58, Ameerpet, Hyderabad 500 016. Tel: +91-40-9373 5061 /7951 Fax: +91-40- 9373 5159	

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in