FINANCIAL RISK OF NON BANKING HOUSING COMPANIES IN INDIA

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Abstract:

The Risk nourishes business but it could also kill it. There can be no business without risk. It is the returns that come from taking risk that keep the spirit of entrepreneurship alive and business going while it encourages and tempts business, risk could kill if not properly managed. It could just wipe out the company. Therefore, it would be very pertinent to understand what is the amount of operating risk, financial risk and business risk of Non Banking Housing Financial Companies. The business risk has two components.

Introduction:

The activities of non-banking financial companies (NBFCs) in India have undergone qualitative changes over the years through functional specialization. The role of NBFCs as effective financial intermediaries has been well recognized as they have inherent ability to take quicker decisions, assume greater risks, and customize their services and charges more according to the needs of the clients. While these features, as compared to the banks, have contributed to the proliferation of NBFCs, their flexible structures allow them to unbundle services provided by banks and market the components on a competitive basis. The distinction between banks and non-banks has been gradually getting blurred since both the segments of the financial system engage themselves in many similar types of activities. At present, NBFCs in India have become prominent in a wide range of activities like hire-purchase finance, equipment lease finance, loans, investments, etc.

Objective of the Study:

1. To identify the Operating Risk, Financial Risk, Business Risk & along with the return of respective companies.
2. To understand the Return per Unit of Risk (RPUR) of Select Non Banking Housing Financial companies in India.

Methodology:

The present study based on secondary data, the data has been gathered from various sources such as published books, journals, magazines, newspapers, websites and past records governments, private organization involved in housing finance operations as well as regulations. And also the data collected from RBI Bulletins also form part of the secondary data.: The present study sought to analyze and rank companies based on the following parameters risk and return of non banking housing financial companies in India

SCOPE OF THE STUDY

The present study expected to produce some important findings and conclusions/recommendations which may help the housing finance companies to formulate policies and programmes to manage minimization of risk & maximization of profit & value creation of Non- banking housing financial companies effectively. This will go in the improvement of better performance in the market.

Financial Risk

Another very important business risk of Non Banking Housing Financial Companies is financial risk which can be measured with the employment of degree of financial leverage. To define conceptually, it is the capacity of a firm to use fixed financial costs such as interest on loans, preference dividends on preference shares to magnify the effect of change in operating profit called EBIT on earnings available to shareholders which usually will be in Earnings Per Share (EPS) form. In other words, it is the relationship between proportionate changes in EPS due to proportionate change in operating profit. For Non Banking Housing Financial Companies the financial risk is presented in following table.

Table No – 6.02: Showing Financial Risk of Select Non Banking Housing Financial Companies in India for the study period 2004-05 to 2013-14 (In times)

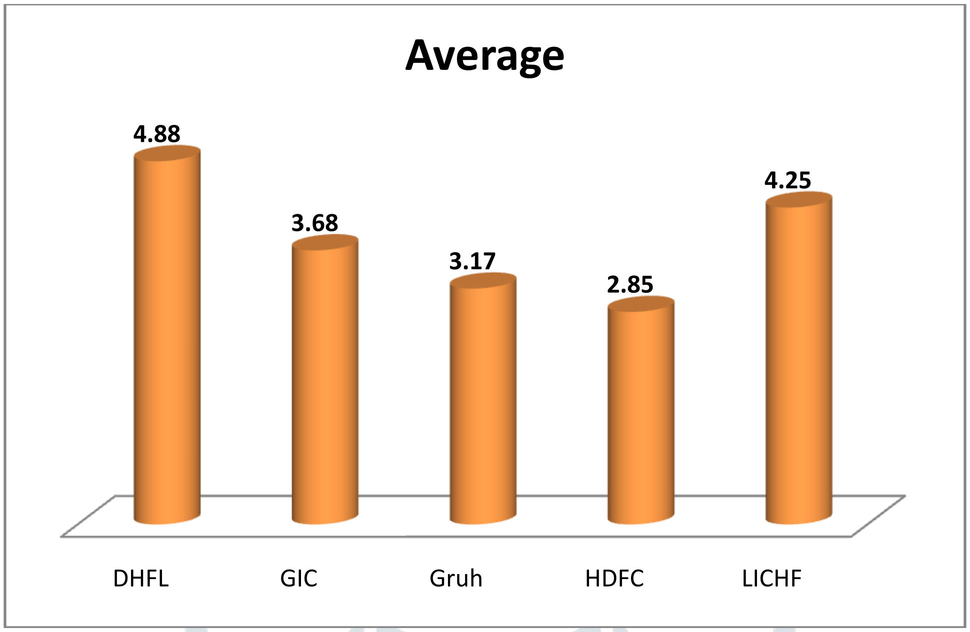
Year	DHFL	GIC	Gruh	HDFC	LICHF
2004-05	4.15	4.76	3.38	2.56	4.48
2005-06	4.00	3.33	3.35	2.60	4.32
2006-07	4.90	2.86	3.35	2.87	4.13
2007-08	4.46	3.22	3.05	2.54	3.81
2008-09	5.17	3.71	3.86	3.37	3.79
2009-10	4.41	3.05	2.90	2.80	3.65
2010-11	3.89	2.47	2.59	2.55	3.39
2011-12	5.52	4.94	2.90	2.97	4.73
2012-13	6.11	4.30	3.05	3.11	5.31
2013-14	6.15	4.15	3.23	3.15	4.93
Average	**4.88**	**3.68**	**3.17**	**2.85**	**4.25**

Source: Annual Reports of the Selected Companies.

By looking at the above table it is clear that the degree of financial leverage which is a proxy for financial risk measurement is ranging on an average from 2.85 times to 4.88 times which means financial risk of Non Banking Financial Companies for the study period financial risk is going around 2.85 to 4.88 times.

Compared to operating risk, financial risk of these companies is usually high as the nature of the business is the lending of finance to housing purpose. Out of the companies of the study, Dewan Housing Finance and LIC Housing Finance have exhibited higher amount of financial risk for the study period i.e, 4.88 and 4.25 times respectively. This offcourse is double edged sword. Suppose if there is proper management of risk these company will get maximum magnification in EPS due to change in operating profit before Interest and Tax. On the other hand, if there is no proper management of financial risk then in such situation it could produce maximum loss. Therefore, these two companies can be concluding as financially more risky compared to other firms in the pack. Whereas, the HDFC and Gruh Finance have revealed low financial risk for the study period. Their degree of financial leverage for the study period on an average stand at 2.85 and 3.17 times respectively, which means financially less risk companies for the study period. Moderate financial risk is exhibited by GIC housing finance.

Chart No-6.02 Showing Average Finance Risk of Select Non Banking Housing Financial Companies in India from 2004-05 to 2013-14 (In times)



Findings:

1. Average financial risk pertaining to Non Banking Housing Finance was going around 2.85% to 4.88%. The highest financial risk is exhibited by Dewan Housing Finance Ltd., (DHFL) and lowest is exhibited by Housing Development Finance Corporation (HDFC)

Suggestion:

1. Risk management must be undertaken in an optimum way. Hence Risk which produces more Return Per Unit of Risk (RPUR) should be taken as optimum risk. Accordingly risk should be identified, measured in terms of impact and to ensure this, strategy may be adopted.

Conclusion:

Banks and Non-Bank Financial Companies are both key elements of a sound and stable financial system. Banks usually dominate the financial system in most countries because business, households and the public sector all rely on the banking system for a wide range of financial products to meet their financial needs. However, by providing additional and alternative financial services, NBFC's have already gained considerable popularity both in developed and developing countries. In one hand these companies help to facilitate long-term investment and financing, which is often a challenge to the banking sector and on the other, the growth of Non-Banking Financial Companies widens the range of products available for individuals and institutions with resources to invest. Through their operation NBFC's can mobilize long-term funds necessary for the development of equity and corporate debt markets, housing financing factoring and venture capital. Another important role which NBFC's play in an economy is to act as a buffer, especially in the moments of economic distress. An efficient NBFC's sector also acts as a systemic risk mitigator and contributes to the overall goal of financial stability in the economy. NBFC's of India have already passed more than three and a half decades of operation. Despite several constraints, the industry has performed notably well and their role in the economy should be duly recognized. It is important to view Non-Banking Financial companies as a catalyst for economic growth and to provide necessary support for their development. A long term approach by all concerned for the development of NBFC's is necessary. Given appropriate support, NBFC's will be able to play a more significant role in the economic development of the developing country.

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