Co-Lending Model of Loan

Why in news?

The RBI tightened the norms for co-lending models since borrower's misuse the provision.

What is Co-lending?

- Co-lending is an arrangement where the loan origination is by one entity usually non-banking financial company (NBFC) but the risk is shared by two entities (NBFC and banks).
- NBFC is the originator while a bank is where the major portion of the loan rests.
- Co-lending model is developed by RBI to address the flow to credit to un served sectors of the economy.

What are the advantages of co-lending?

- **Multiple partners** - An NBFC can partner with multiple banks and a bank can partner with multiple NBFCs.
- **Wide range of loans** - It includes wide range of loans such as housing, affordable housing, gold, commercial vehicles, passenger vehicles or even microfinance loans.
- Basically it includes everything in retail.
- **Formulate its own policy** - The NBFC and banks can formulate their own policy on internal practices and risk management framework.
- **Risk sharing** - 80% of the loan risk is borne by the bank and the rest 20% by the NBFC.
- This ensures accountability on NBFC.
- **Financial inclusion** - This model allows banks to penetrate outside the urban and semi urban areas.
- It also accepts loans starting from Rs 3 to 5 lakhs and go up to Rs 1 crore.
- **Flow of credit** - This model improves the flow of credit to the un served and underserved sector of the economy.
- **Higher growth for NBFCs** - This model has helped the NBFCs to grow substantially during recent years.

What are the impacts of tighter regulations by RBI?

- Borrowers with not-so-good credit record may find it more difficult to get loans.
- The penetration of loans to areas outside metro zones may be reduced.
- The borrower gets a loan from a particular bank and under stress pulls out and gets a

new loan from different bank is addressed by RBI’s tighter norms.

Quick facts

Non-Banking Financial Company (NBFC)
• NBFC is a company registered under the ***Companies Act, 1956*** engaged in the business of loans and advances, acquisition of shares/stocks/bonds/debentures/securities issued by Government or local authority or other marketable securities of a like nature, leasing, hire-purchase, insurance business, and chit business. • NBFC does not include any institution whose principal business is that of agriculture activity, industrial activity, purchase or sale of any goods (other than securities) or providing any services and sale/purchase/construction of immovable property. • NBFC ***cannot accept demand deposits***. • NBFCs do not form part of the payment and settlement system and ***cannot issue cheques drawn on itself***. • Deposit insurance facility of Deposit Insurance and Credit Guarantee Corporation is not available to depositors of NBFCs.

References

1. The Hindu Business Line| About Co-Lending
2. RBI| Advantages Of Co-Lending
3. RBI| About NBFC