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Building the NBFC of the future - A scalable and profitable model

Foreword

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India's NBFC sector continues to remain at the forefront in driving new credit disbursals for the country's underserved retail and MSME market. Over the last five years, the NBFC lending book has grown at nearly 18% driven by a deep understanding of target customer segments, use of technology advances, lean cost structures and differentiated business models to reach credit-starved segments.

Despite recording robust growth, the NBFC market share has been dominated by large players, while many small players have struggled to scale up operations profitably. Moreover, recently, the sector has taken a beating in the stock market with defaults and liquidity challenges, specifically related to one large NBFC. Although the problem seems isolated, it has concerned regulators due to the risk of contagion effect and the overall governance in the sector. Given the sector is fairly large now to impact the overall economy, this certainly entails some potential implications, including new compliance measures by the regulator, lending slowdown and potential consolidation by larger players.

Furthermore, the NBFC lending model is also under pressure as a result of increased internal and external forces such as:

1. Stiff competition from incumbents and the entry of Fintech players leveraging technology-based operating models to compete
2. Dynamic regulations that are increasing the cost to comply and restricting the ability to freely impose pricing
3. Technology advances (e.g., cloud computing, and big data analytics) that are enabling personalisation, real-time and social mobility, in addition to reducing cost-to-serve and an increased ability to launch new product and reach new customer segments
4. Rapidly increasing levels of customer expectation, driven by the need for a connected, 24X7 pervasive experience
5. Economic volatility, shrinking credit performance and pricing pressure as a result of eroding margins

Such disruptive forces necessitate another look at what are the building blocks of a robust, scalable and profitable NBFC business model that will sustain through similar stress cycles. Despite concerns surrounding the sector, we believe such NBFCs with robust business models, strong liquidity mechanism, governance and risk management standards are well positioned to take advantage of the market opportunity. Hence, it is even more critical for incumbent and new-to-market NBFCs to define and implement a balanced strategy that meets table-stakes across essential, core capabilities and differentiates across high value-adding capabilities. This report illustrates some key design imperatives across ten dimensions that NBFCs must consider to sustainably grow and operate in the future.

- First, NBFCs should formulate a segmentation strategy, defining target customer segments, product proposition, distribution channels and geographical locations for operations. The enterprise strategy must play on the NBFC lender's strengths and focus on right market opportunities that will enable differentiation and are likely to generate success.
- Second, NBFCs must offer customers personalised, seamless 24X7 sales and service interaction, with well-entrenched engagement programmes to attract and retain customers, while maximising lifetime value.
- Third, lenders should be willing to overhaul processes and transform operations instead of resorting to short-term, patchwork mechanism.
- Fourth, NBFCs must leverage technology-based tools to transform underwriting and decision making, thereby, helping drive competitive advantage and robust risk management.
- Fifth, overdue collections must adopt a customer-focused, data-driven, relationship-based approach to maximise recovery and minimise write-offs.

- Sixth, technology development must leverage agile methodologies and adopt a loosely coupled architecture to enable efficient scale-ups. Lenders must maintain focus on building tight information security controls to ensure insulation from rising threats.
- Seventh, as the toast of the financial services innovation space, Fintech alliances will allow lenders to add unique capabilities to boost their value proposition and compete stronger in a crowded market.
- Eighth, efficient risk detection, management and mitigation mechanisms will help NBFCs survive regulatory dynamics, market uncertainties and ensure lenders are well capitalised to operate.
- Ninth, the organisation design must align with enterprise goals to ensure optimal delivery that allows for sustained growth and continuous innovation.
- Lastly, lenders must build robust governance models to maintain stakeholder trust and improve resilience to survive in testing times.

NBFCs have played a critical role as a key contributor to the economy by providing a fillip to infrastructure, employment generation, wealth creation and access to financial services for the rural and weaker sections of society. The health and success of the NBFC sector has far-reaching implications on the inclusive development of the economy, financial inclusion of diverse population segments, capital formation and eventually the growth in GDP.

We congratulate the Associated Chambers of Commerce and Industry of India (ASSOCHAM) for engaging on a topic, which has gained attention from the mainstream, given the recent turn of events. I thank Sidharth Ravishankar, Pranav Jain, Bhawna Manocha, Vedika Gupta and Sutej Shekhar of the Financial Services team of PwC for researching and writing this report.

Message from **ASSOCHAM**

Uday Kumar Varma
Secretary General, ASSOCHAM

Raman Aggarwal
Chairman, ASSOCHAM National Council for NBFC; Chairman, FIDC and Sr. VP, SREI Equipment Finance Ltd

Of late, several new developments have significantly affected the functioning of NBFCs. For instance, FinTech companies are attempting to gain a share of the lucrative opportunity in the Indian lending market through their mastery of data and technology. Selecting the right segmentation strategy helps scope and focus efforts of the NBFC lender on opportunities that are likely to generate success. NBFCs must make a cultural shift in the manner they engage with the customer, in order to lay the foundation for a strong relationship and create a lasting impact. Large NBFCs must consider establishing a dedicated customer experience function. This can comprise focused resources or cross-function employee groups who are mandated to drive customer-centricity and buy-ins across functions.

Recently, India's non-banking financial companies (NBFC) sector is roiled by a series of defaults by the Infrastructure Leasing & Financial Services (IL&FS) group of companies. The IL&FS group defaulted on CP, which is an unsecured money market instrument issued in the form of a promissory note with a maximum validity of one year. Several corporates, mutual funds, and insurance companies have invested in CPs and NCDs of the IL&FS group, and there is fear that in the wake of the default, their funds could be locked in IL&FS debt instruments, leading to a liquidity crunch. The situation has created a liquidity shortage of close to 1 lakh crore INR in the system, and fears have intensified that the funding cost for NBFCs will zoom, and result in a sharp deterioration of their margins.

In this connection, several regulatory changes and government initiatives have altered the operating mechanism and necessitated changes in the risk management framework for NBFCs. Furthermore, these changes have differing implications for NBFCs, the basis for the target segment and geographical location of operation.

ASSOCHAM and PwC have come out with a knowledge report on imagining the NBFC of the future. We hope that this study will help regulators, market participants, government departments and other research scholars.

I would like to sincerely appreciate the ASSOCHAM-PwC team for sharing their thoughts, insights and experiences.

NBFCs have continued to be in limelight, recently, though, not for the right reasons. In spite of continued growth, coupled with improved asset quality and more than adequate capital adequacy, the stock markets have suddenly reacted negatively. With one of the important infrastructure financing NBFCs going down, the sentiment suddenly turned negative and as a result there has been a virtual blood bath at the stock markets, when it came to stocks of all the leading NBFCs. This recent development has once again highlighted the crying need to create a marked distinction between what is known as a 'typical NBFC model' focused on retail lending (primarily secured) with small ticket size and average tenure of two to four years. The NBFC facing the crisis today, is primarily engaged in long-term project financing and cannot be treated as a representative for the NBFC sector. Unfortunately, as has been the case in the past, it got clubbed with the other long-term financing, non-bank players such as the housing finance companies (HFCs). While all these long-term finance players may be exposed to an increased risk of asset liability mismatch, the same cannot be held true for retail lending NBFCs, which constitute more than 95% of the sector.

It has been heartening to note that the regulator has voiced the same feelings and have till date, refrained from any knee-jerk reactions.

With the timely intervention of the Government in resolving the crisis in the concerned NBFC, followed by the much needed clarifications and awareness messages given by the representative body FIDC and the leading industry players, the sudden panic seems to have died down. The NBFC sector have withstood such turbulent times even in the past, and have always come out stronger. Under these circumstances, this knowledge paper prepared by ASSOCHAM and PWC with valuable inputs from FIDC will be of immense help. The release of this Knowledge Paper at the 5th National Summit on NBFCs will provide the right information at the right time using the right platform.

Backed by strong financials, increased reach, better understanding of the market dynamics, down up to the local level, and ample growth opportunities, I am confident that NBFCs will not only continue but vastly enhance their role in providing credit to the unbanked, under banked and MSMEs including start-ups, which are the core focus areas in our Hon'ble Prime Minister's vision of a new India.

Amit Saxena
Co - Chairman, ASSOCHAM National Council for NBFCs

The NBFC sector in India has undergone a significant transformation over the past few years and has come to be recognised as systemically important components of the financial system and it is growing quite consistently year-on-year.

NBFCs are playing a critical role for development of core infrastructure, transport, employment generation, wealth creation, economic development, to finance economically weaker sections, and considerable contribution to the state exchequer.

ASSOCHAM, along with PwC, have come out with this Knowledge Paper with the objective to contemplate these issues and challenges being faced by NBFCs (specifically considering the revised regulatory framework) and suggest measures that can be taken to optimise their contribution thereto.

We hope that this study would help the regulators, market participants, government departments, and other research scholars to gain a better understanding on NBFCs' role in promoting 'Financial Inclusion' for our country. I would like to express my sincere appreciation to ASSOCHAM-PwC team for sharing their thoughts, insights and experiences.

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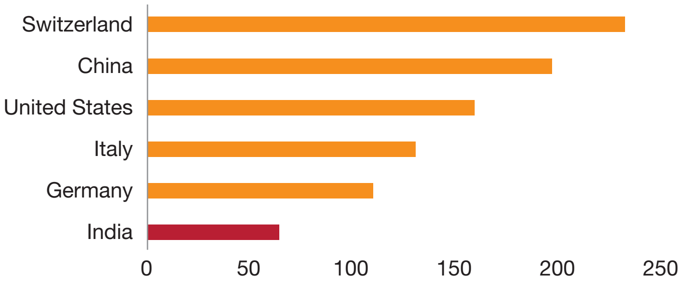
Introduction

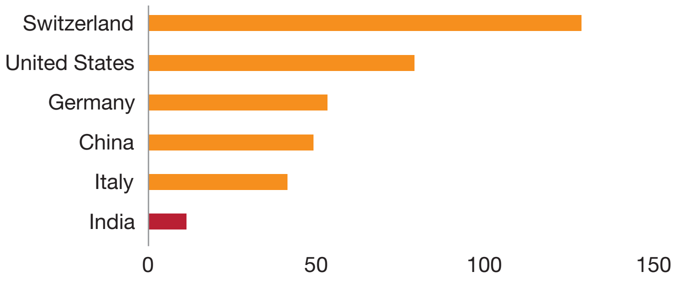
1.1. Indian lending market: an under-penetrated opportunity

The Indian economy has been on a positive trajectory in the amount of formal credit deployed, supplemented by rising consumer disposable income and ease of access to credit. Credit offtake has grown by 11% over the last 10 years[1], led by public and private sector banks. However, despite overall credit growth, India still remains under-penetrated in retail and MSME lending, with household credit to GDP[2] ratio lagging several major emerging and developed economies. The opportunity has driven several non-banks to enter the retail lending space, through the use of innovative lending models and product innovation.

Credit to GDP (%)



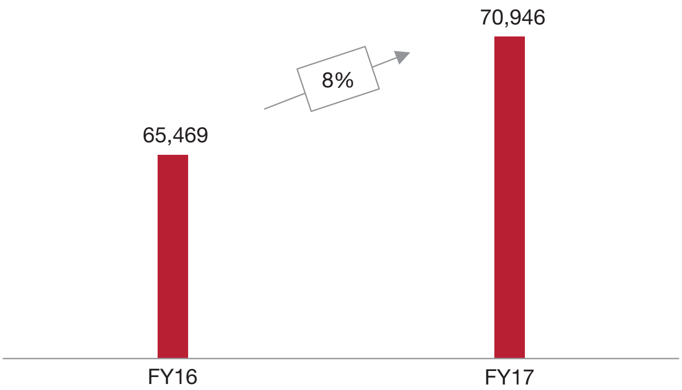
Household credit to GDP (%)



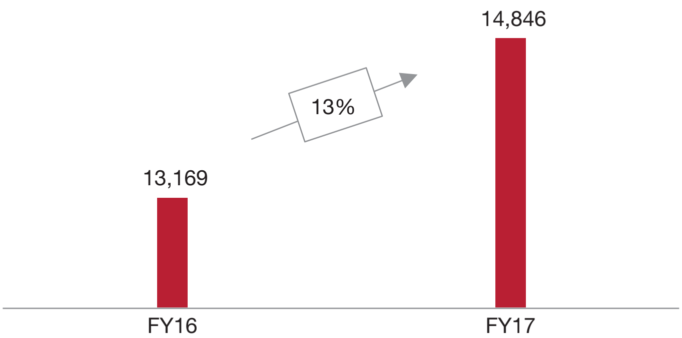
1.2. NBFCs leading the charge

In recent years, non-banks, particularly non-banking financial companies (NBFCs), have outperformed banks in new credit deployment. By leveraging technology to penetrate underserved segments, NBFCs have capitalised on the inability of banks to rapidly scale operations and customise rigid policies. NBFCs have seen a significant increase in their share of total new disbursals at the cost of public sector banks. This is witnessed in the form of their share in the total credit market going up from 13% in 2015 to 16% in 2017.[3]

Bank Credit Outstanding (INR bn.)



NBFC Credit Outstanding (INR bn.)



1. IBEF Banking report, 2018
2. BIS Statistics, September 2018
3. Non-banks share of credit pie to increase 300 bps in 3 years, CRISIL, September 2018

Retail and MSME segments have been key growth areas for NBFCs, with total credit outstanding of INR 7.5 trillion as on FY18.[4] NBFCs have disrupted these segments with a varied range of product offerings such as equipment financing, hire purchase and leasing, housing finance and gold loans in addition to carving out new segments such as consumer durable finance. Additionally, with Government initiatives such as GST and demonetisation moving individuals and enterprises gradually into the formal economy, NBFCs are well positioned to capture share and gain advantage in coming years.

Moreover, with the RBI enhancing scrutiny on corporate lending and NPA reporting by banks, the opportunity has opened up for NBFCs to grow their lending portfolio to a sector traditionally dominated by commercial banks.

Reasons for growth

- **Deep understanding of the customer segment:** Given their operations in unorganised and under-served segments of the economy, NBFCs have created a niche for themselves through a deep understanding of needs of their customer segments and ensuring last-mile delivery of products and services.
- **Customised product offerings:** Several NBFCs have focused on a limited line (or often mono-line set of products) to serve the target customer segment. Armed with a thorough comprehension of their target segment, NBFCs have customised product offerings to address unique characteristics of the customer segment and focus on meeting the right needs. Additionally, several NBFCs are also adopting non-standard pricing models for product lines, in-line with the customer profile and inherent risk of lending.
- **Wider and effective reach:** NBFCs are now reaching out to Tier-2, Tier-3 and Tier-4 markets, distributing the loan across several customer touch-points. Furthermore, they are also building a connected channel experience, that provides an omni-channel, seamless experience with 24/7 sales and service. With the consumer of today evolving and accessing digital media like never before, NBFCs have embarked on new and better ways to engage with the customer.
- **Leveraging technology advances for improved efficiency and enhanced experience:** The use of technology is helping NBFCs customise credit assessment models and optimise business processes, thereby reducing the time to market and helping improve customer experience. Select NBFCs are also investing in data analytics and artificial intelligence to build robust relationships with their target customer segments.
- **Co-lending arrangements:** NBFCs have been tying up with multiple alternative lenders with digital platforms and commercial banks as well, which has been adding to their targeted customer base.
- **Robust risk management:** Given their focus on lending to the sub-prime customer segment, and regulatory disadvantage (SARFEASI, DRT and capital adequacy requirements) in comparison to commercial bank lenders, NBFCs are ensuring enhanced governance through a pro-active, robust and agile risk management model.

4. ICRA. (2018)

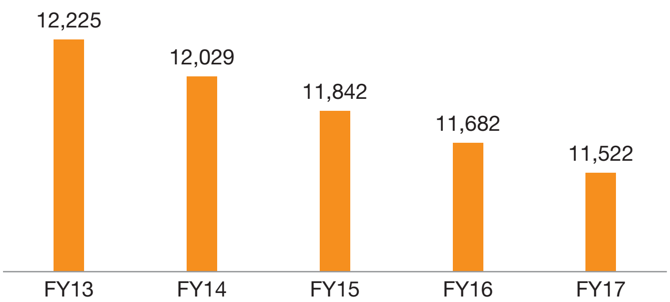
1.3. A fragmented market

As on FY17, there are a total of 11,522[5] NBFCs in the country. The under-penetrated nature of the market has driven multiple new entrants to set-up shop and attempt to capture market share. Data from year-on-year (YoY) new registrations[6] indicate an increased interest in setting up an NBFC business.

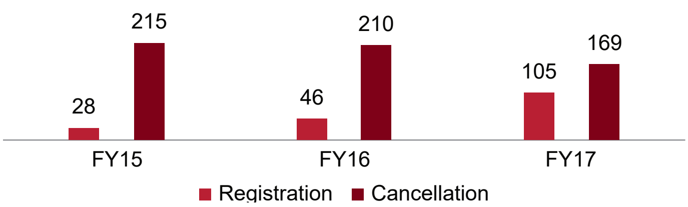
However, despite making rapid progress and capturing market share from commercial banks, the NBFC market has been largely dominated by prominent players, with small ones struggling to ramp-up operations and lend sustainably.

In the first half of 2018, the RBI pro-actively cancelled license of 368 NBFC lenders, deeming them economically non-viable for failing to meet the requirement of net owned fund (NOF) of INR 2 crore. This is more than double the number of cancellations in entire 2017. Recently, in the wake of the IL&FS crisis, news reports also indicate that the RBI may embark on a further clean-up of the sector, and resort to cancellation of NBFC licenses and making it difficult for new entities to obtain NBFC licenses.

Number of NBFCs in India



Number of registrations and cancellations



The emergence of new-age digital lenders has further intensified the competition for NBFCs in the market. Primarily FinTech companies, these digital lenders are attempting to gain a share of the lucrative opportunity in the Indian lending market through their mastery of data and technology. These start-ups conduct off-balance sheet and on-balance sheet lending, powered by innovative processes to deliver a captivating customer experience, quick turnaround time, reduced fees and increased transparency. The threat posed by such lenders is seen in the form of an estimated market share of nearly INR70 trillion over the next five years.[7]

The decline of NBFCs is being attributed to several reasons, key being taking up of significant credit risk and lack of effective monitoring and management of portfolio performance.

- **Leveraging an off-the-roll sales force with no direct ownership:** The absence of direct sales agents on NBFC payrolls has had a downward spiralling effect on the quality of sourcing. In addition to resulting in minimal accountability, the situation has also been exacerbated by agents looking to exploit gaps and loopholes with the existing underwriting model to on-board new customers.
- **Gaps in the underwriting model:** Given the focus on lending to the under-served segment, an approach to effective underwriting has required NBFC lenders to form personal relations with prospects and taking a credit call based on local context. The decline in asset quality for select NBFCs has stemmed from cases where underwriters are inexperienced, or with limited understanding of the local situation and dynamics that drive the demand for credit.
- **Misalignment in product offerings with customer needs:** Small NBFCs, in an effort to capture share, have expanded into new geographic locations and diversified their product portfolio. This has resulted in aggressive investment, increased cost of acquisition and operations.
- **Asset-liability mismatch:** Several NBFCs are faced with a liquidity crunch, liabilities maturing and coming up for payment faster than loans in the same tenure. With dynamic short-term rates, such lenders risk resorting to increased cost of funds to meet the shortfall, denting profitability. Additionally, this has also made it difficult for these NBFCs to raise capital for expansion in the market.

5. RBI Report on trend and progress of banking in India 2017
6. RBI Report on trend and progress of banking in India 2017
7. Digital Lending: A $1 trillion opportunity over the next 5 years, moneycontrol.com, July 2018

02

Ten considerations for building the NBFC of the future

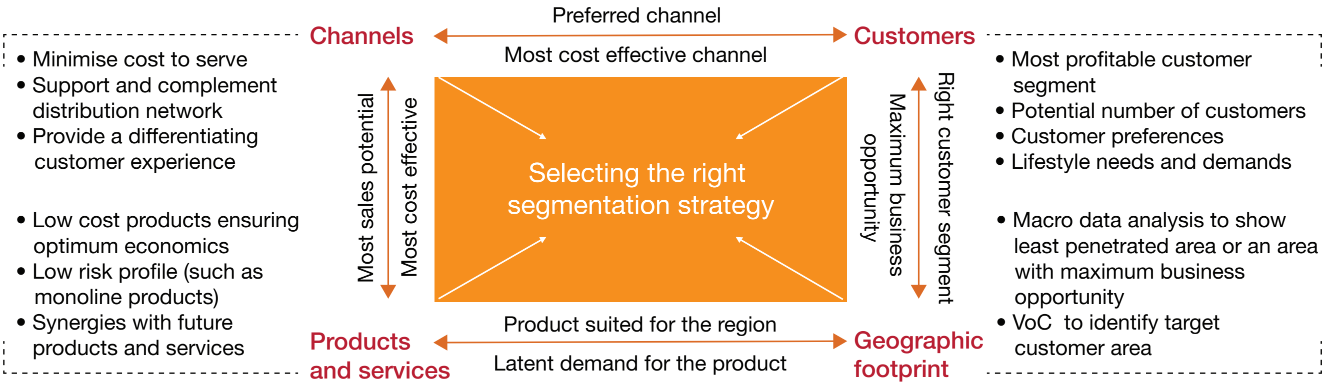
In the sections ahead, we have articulated ten considerations that will provide the foundation for NBFCs to sustainably grow and effectively operate in a dynamic and competitive lending marketplace. Existing incumbents and new-to-market entrants should benchmark their current strategy and future aspirations against these considerations to derive new opportunities to transform.

2.1. Select the right segmentation strategy and identify opportunities likely to generate success

Selecting the right segmentation strategy helps scope and focus efforts of the NBFC lender on opportunities that are likely to generate success. Through effective segmentation strategy, lenders can reap a host of benefits. These are listed below:

- Provide a source of advantage and help differentiate in a fragmented market
- Direct organisation-wide effort, investment and marketing effort in specific areas where success is more likely
- Derive sales, branding and distribution strategy
- Provide a pivotal opportunity to build a long-term customer relationship
- Enhance and accelerate downstream decisions

Selecting the right segmentation strategy requires lenders to make choices across target customer markets, product and service bouquet, channel offering and geographic footprint



Choosing the right segmentation strategy

Building the segmentation strategy requires shortlisting from several choices on a) customer segments that will be served b) product and services for offer c) physical and digital channels that will deliver the product and service d) geographies where the lender will create presence. Efforts to formulate the right segmentation strategy begins by building detailed insights on the product, market and competition; through primary surveys, deep market research and analysis.

Listed below are questions that will help NBFCs narrow down choices and finalise their segmentation strategy.

What is the size of your potential addressable market?

It is important to develop a fair estimate of the potential addressable market over a five year horizon. The estimate must include target customer segments that are likely to use or benefit from the lending product. Many organisations view market research and primary surveys as an unnecessary and expensive cost; however, these methods can provide critical insights on customer need and opportunities that can help build winning strategies for product design and deployment, and eventually pay-off in the long run.

What are key considerations for selecting the loan product?

There can be myriad reasons to select and offer a loan product. These include—intensity of competition, cost of risk, target customer base, size of market, yield rate, growth rate, operating efficiency, ability to bundle and cross-sell with existing products, among several others. It is important to identify considerations that fit the enterprise strategy and align with the short, medium and long-term goals of the NBFC.

If existing NBFCs are already selling the product (or variant), can your product (or variant) be superior, through customer experience, pricing, marketing or other value added benefits?

The design elements in the product, and supporting components (e.g., customer journey, target operating model, pricing etc.) account for the go-to-market proposition that will compete with other bank and NBFC lenders. It is important to consider if the lending product (and associated variants) help address an opportunity in the market. If yes, can the NBFC differentiate from competition when it comes to delivery of the product and service?

How adept is the distribution channel, to leverage for acquisition, on-boarding and servicing the loan product in selected geographies? Are there benefits from scale that can be achieved by using existing distribution channels for the new product?

Traditionally, lenders have relied on building a strong physical footprint across geographies to dominate markets and acquire share. The advent and proliferation of internet and smartphones has transformed lending today into an increasingly digital proposition. Customers are looking to access products, transactions and services digitally. As a result, digital-driven distribution models are increasingly gaining prominence for new-to-lender acquisition. However, it is important to note that no target customer segment is fully digital—the human touch-point will remain vital.

What are the potential sales, growth, profits, and time for payback?

Before commissioning product design and implementation, it is important to get a reasonable estimate of the numbers first. As a quantitative reflection of the strategy, a well prepared business plan will provide insights on the cost structure, sales required to break-even or even post a profit, and what the return on investment will be. The business plan can have significant downstream benefits during the implementation journey, and provide warning signals in case of significant deviation from the initial plan. More importantly, the business plan provides impetus to ancillary initiatives necessary to ensure a successful implementation (e.g., hiring plan, digital budget, marketing spend, branch rationalisation).

Does the organisation have deep-rooted capability to operationalise the product?

It is important for every NBFC to understand the extent of time and specialised resource availability for the product. Many organisations make the mistake of going ahead with operationalisation of the product, to only realise that they can't afford the specialised manpower required, or cannot commit to resources. It is important to evaluate at the onset, how the product can eventually be scaled up, if there is a demand flourish in the market. For example, an existing NBFC looking to launch a new lending product must consider the scalability of its existing distribution network (physical and digital) before embarking on additional investment.

Case Study: Marcus

Marcus, the consumer lending arm of Goldman Sachs took the market by storm when it launched a fixed-rate, no-fee personal loan. The product targeted credit card borrowers looking to consolidate their debt into one loan. Marcus' marketing was direct, and to the point—with banners proclaiming 'Debt happens. It's how you get out that matters'.

Despite joining a crowded field of online lending start-ups, chasing a market worth as much as 1 trillion US$, Marcus reached the 2 billion US$ origination mark in 13 years, with demand for the service growing at break-neck speed. The growth was achieved by three focus pillars—one, by selecting a strong, booming online consumer finance market. Two, by leveraging parent Goldman Sachs' strong balance sheet to fund its loans and therefore, reduce pricing. Three, by offering a high level of user experience through in-house technology development.

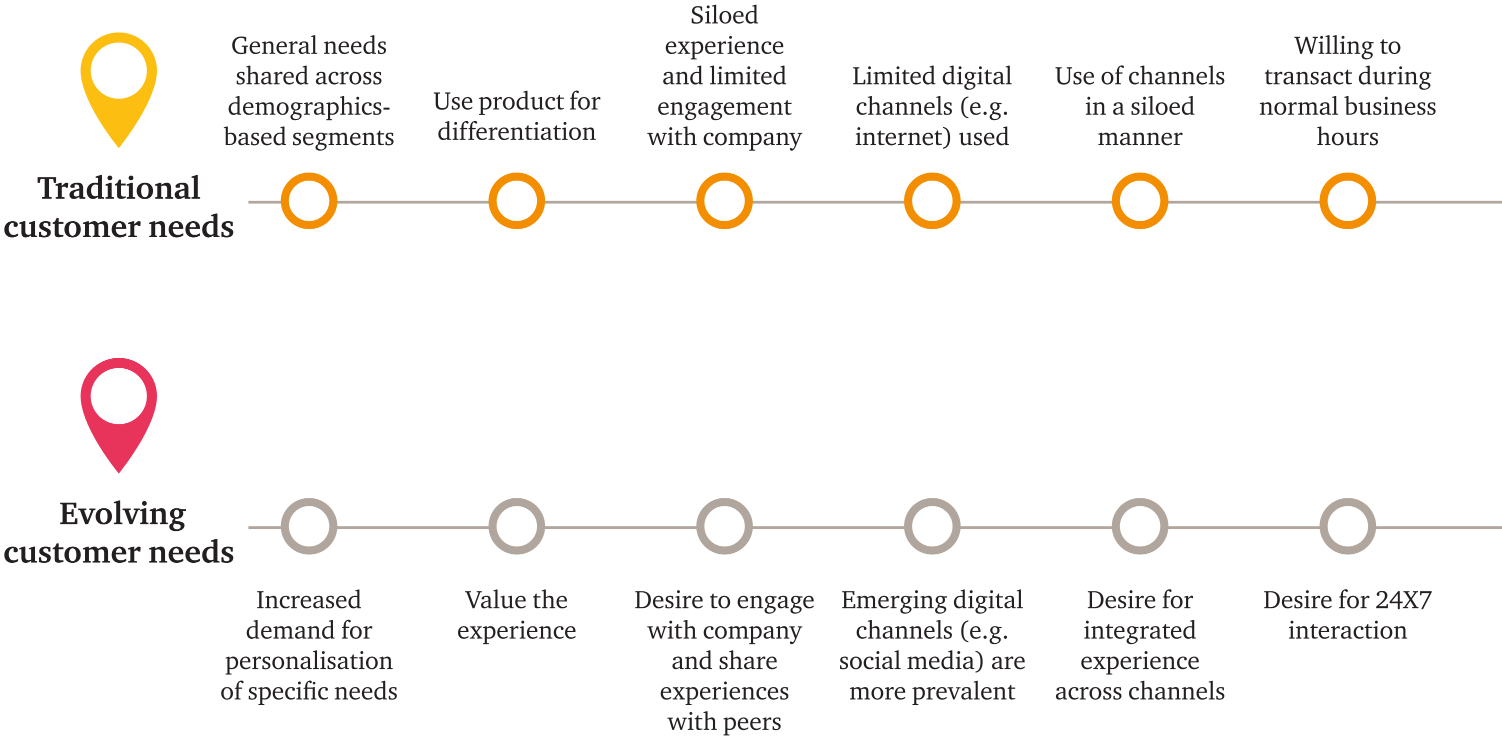
2.2. Embrace a new attitude to winning over the customer

'Customer is king' has never been more true than it is today. With lenders incorporating technology advances to penetrate underserved markets and differentiate in mature markets, customer expectations have evolved. The proliferation of new entrants with differentiated business models to serve customers is also increasing pressure on existing, incumbent NBFCs to increase customer focus.

Customers now demand seamless, personalised, 24X7 interaction across multiple touch-points, customised to their needs. This will require NBFCs to embrace techniques to derive customer insight, such as customer personas and journey maps, enhance their understanding of customer behaviour and subsequently drive-up meaningful outcome.

Winning the customer experience race will require much more than just technology; it also mandates a new attitude to winning the customer.

Customer expectations have evolved over time, resulting in several implications for lenders



Know your customer

Moving from segmentation to micro-segmentation

Personalisation of content has become ever important, especially in a time when customers are bombarded with a plethora of emails and SMS. Statistics show that more than 91% of people unsubscribe to email communications, 44% of direct emails go unopened and 60% opt out of mobile notifications.[8] The primary cause of this remains a glut of unrelated and irrelevant messages, which turn off the customer's interest. When flooded with choice, customers focus only on those products or services that are most relevant to them.

NBFCs must adopt a micro-segmentation approach in finding smaller sets of people to whom a specific product, service or a feature of a product could be vital. By incorporating marketing analytics, NBFCs can rapidly, dynamically, at massive scale, mine huge amounts of data, encompassing customer transactions, demographics and interactions as well as with data from external sources.

In addition to identifying lucrative micro-segments and probability of purchase, NBFCs will be able to communicate effectively with customers and price loan products better to minimise customer drop-outs. Over time, such tools will also help NBFCs capitalise on opportunities for up-sell, cross-sell and re-sell, thereby, boosting the customer lifetime value.

Additionally, lenders can use micro-segmentation to:

i. Identify customers potentially willing to pay a premium

ii. Scope to re-organise (and reduce) marketing spends

iii. Optimise sales and distribution strategy

8. Guidelines for messaging consumers, kahuna.com, September 2018

Creating a “WOW” experience

Map the customer journey

NBFCs must make a cultural shift in the manner they engage with the customer, in order to lay the foundation for a strong relationship and create a lasting impact.

Designing customer personas based on key attributes is the first step in creating a strong understanding of customers’ needs, motivations and tendencies. Developing customer journey maps for all scenarios will place design teams in the shoes of these personas to understand and enhance the design of the customer’s interaction with various facets of the NBFC. The visual representation of interactions through channels and decision paths will provide insights on potential bottlenecks that may hamper the customer experience.

Customer retention

Building customer loyalty

In chasing new markets and customers, NBFC lenders must not lose sight of existing customers. NBFCs must place equal focus on existing customers and reduce customer attrition, to better tap into the lifetime value of the relationship.

i. Efficient engagement of customers: NBFCs must distinguish between active and inactive customers to develop a focused engagement methodology and allocate resources efficiently.

ii. Building effective reward and loyalty programmes: NBFCs must increase customer retention by building a strong loyalty programme, with discount, cashback and air-mile benefits. The program must be customised according to the customer type and factor in right data variables to provide meaningful incentives and value for the customer

iii. Focus on customer satisfaction: A satisfied customer can be the NBFCs biggest ambassador, through word of mouth marketing. NBFCs must periodically review indicative metrics and develop remediation programmes to foster customer satisfaction.

2.3. Improve processes and transform operations to compete efficiently and effectively

Stiff competition has forced lenders to re-look current process workflows and operating models. Moreover, with regulatory adherence and compliance under intense scrutiny, lenders are building scalable models and agile processes to reduce investment costs to comply with current and future demands.

However, despite the situation in hand, some lenders have been unwilling to overhaul, given the associated investment cost, and have instead preferred to resort to patchwork workarounds. The issue with patchwork mechanism is that, while it bodes well in the short-term, it is not a sustainable, long-term solution.

Lenders without well-defined processes and operating models can face a host of challenges:

1. Heightened operating risk, from inconsistent and incorrect application of lending policies and processes to originate and onboard customers. The problem is compounded in the absence of knowledge repositories that serve as a handy guide to employees. As a downstream impact, this may affect new employee training and limit effective succession planning.
2. Operational inefficiencies, due to multiple handoffs between departments in the absence of clear accountabilities, roles and responsibilities. Furthermore, this can slow down decision making and negatively impact customer experience.
3. Affects customer experience, due to inconsistent treatment of customers. Furthermore, ambiguity within the organisation and limited interactions between functions and business lines can increase turnaround times to sell and service customers.

Improving processes to make them next-generation ready

Despite technology driving changes in customer-facing processes and applications, lenders have largely not extended benefits to the middle- and back-office. Such processes rely on people and paper, with a high error rate, manual data entry and high costs. Technology advances can provide solutions to a broad array of problem statements faced by lenders, including elimination of paper, enhanced process control, enhanced data integrity and operational efficiency.

Transitioning to the next generation model requires careful identification and mapping of the NBFCs' process universe. For the lending business, typical process classification covers customer acquisition, onboarding, underwriting, fulfilment, servicing, and collections, apart from universal and enterprise processes. Depending on the function involved, processes can range across criticality levels with differing implications for process transformation. Lenders must target process workflows for transformation that can provide a quick-win opportunity, and unlock the highest value.

- **Understand the potential for automation:** Gather information on automation capabilities (e.g., workflow tools, robotic process automation, intelligent automation, cognitive intelligence, and artificial intelligence) with potential for application.
- **Select the right automation capabilities:** Shortlist manual, non-value add, error-prone use-cases (e.g., data entry, financial ratio calculation, communication with sales etc.) where automation capabilities could be leveraged to provide potential benefits. It is useful to design proof-of-concept and test pilot implementation to determine go-ahead for a wider implementation of the automation program.
- **Document procedure exceptions:** While, digitisation and automation helps increase efficiency, it can act as a single point of failure if no alternative processes are defined. Identify manual alternatives to automated procedures such as automated verification and data input. Put into place alternate procedures to ensure business continuity in case of failures.

Prioritize processes whose transformation can unlock the largest benefit for the organization

From too many legacy processes… **… prioritise a few …** **… and address them in successive waves**

Business Processes

Universe Processes*

Enterprise Processes

Prioritisation: select one to three processes for each transformation wave

Criteria

- Client experience
- Efficiency opportunities
- Risk reduction
- Monetizing current investments and programs

Wave 1

- Card fulfilment and servicing
- Commercial lending
- Mortgage origination

Wave 2

- Consumer lending
- Lead management
- Treasury management
- On boarding and servicing

Wave 3

- Client problem resolution
- Real estate lending
- Others to be determined

illustrative

Transform lending operations in line with enterprise goals

There is no single, successful formula for transforming lending operations. A transformation exercise must align with NBFC goals—be it cost reduction, efficiency improvement or enhanced customer experience.

The best practices mentioned below can serve NBFC lenders effectively looking to transform their operations

Product and service simplification

- Lenders must minimise customisation of products and services, where customers do not see value or are regulatory mandated, with little or no impact on business.
- Align cost-versus-complexity of product and service features, to match the strategic direction communicated by the enterprise.

Digital advancement to improve front-end customer experience

- The use of digital technology has spawned several improvements in customer interactions and lenders must incorporate the same to remain relevant amongst competition, as well as match changing customer expectations.
- Implement straight-through-processing in middle and back-office functions to avoid manual processing for such front-end interactions.
- Form partnerships with niche and non-traditional service providers to build and deploy digital capabilities through operating model.

Optimisation of the delivery model

- Determine if tangible cost benefits can be realised by moving select activities to a shared-services or utility model, to maximise scale and reducing operating costs.
- Increase integration of third party providers into operations to improve cost efficiency and build capabilities.
- Successful transformation exercises can yield in significant benefits for lenders

Successful transformation exercises can yield in significant benefits for lenders

2.4. Leverage technology advances to reduce time to decision and pro-actively manage risk

Underwriting as a competitive advantage

As the focal pillar of NBFC lending, the underwriting function serves to detect, manage and mitigate credit risk. Viewed as a process bottleneck for higher turnaround times in the past, the function has managed to compress timelines, through transformative approaches to underwriting.

The NBFC lending space is witnessing rapid and deep changes, and this has necessitated transformation of the traditional underwriting model. By incorporating technology-based models, NBFC lenders are using underwriting to drive competitive advantage, provide customer friendly experience and pro-active risk management. Additionally, the transformation is also helping create an agile and scalable business, helping lenders expand into niche markets, roll-out new products, and in some cases even create a first-mover advantage.

Listed below are some key themes that can help NBFCs transform the underwriting model to provide a competitive advantage.

One size *does not* fit all

Traditionally, lenders have adopted a one-size fits all approach, evaluating all types of customers against a single credit policy, resulting in exclusion of a large population of creditworthy customers. Digital focused, disruptive NBFC lenders are now adopting a personalised approach to underwriting by incorporating segment-specific policies that leverage alternative data sources and apply scorecard-based credit decisions. The approach is helping broaden the customer funnel, allowing sales teams to target a large pool of prospective customers and offer relevant products.

Action Points:

- **Select target customer segments, products and geographies where customisation is possible and meaningful:** Customised underwriting has been useful when assessing low-income households and informal MSME enterprises, given the absence of data and financial history for the segment. However, applying customised underwriting to all segments may neither be meaningful nor be cost effective.
- **Pay careful attention to design, without compromising on risk standard:** A well-customised underwriting model makes changes to its design to factor in variability in customer type and situation. Customisation should create multiple customer journeys, alter data requirements and risk thresholds for decision-making and require additional checks and verifications. However, an attempt to personalise underwriting must not camouflage credit risk standards at the cost of new business.

- **Periodic evaluation of review and risk parameters:** Personalised underwriting models should be periodically assessed to determine effectiveness for the relevant target segment. Approval rates must be commensurate with risk lending standards to prevent deterioration of financials.

Continuous evaluation of the underwriting model

One of the mistakes lenders make when scaling up is to ignore periodic evaluation of the underwriting model. A periodic re-evaluation helps determine the efficiency and effectiveness (e.g., service delivery, risk management, cost efficiency etc.) in altered scenarios, and therefore, determines remediation steps to improve performance. For example, when underwriting a new portfolio, it becomes integral to set-up an upward feedback mechanism based on early trends in collections to alter credit assessment and decision making criteria.

Action points:

- Set up review committees at pre-set periodicity, with participants from impacted functions, including risk, underwriting, sales and collections to evaluate the model's altered relevance. A review must have access to the right data sets to enable development of effective remediation measures. Furthermore, measures must be percolated to relevant teams, and tracked for timely completion.

On-the-spot decision making

Several digital-focused NBFC disruptors have transformed the manual, time-consuming, human judgement-based underwriting process using technology advances to provide instant, real-time approvals. The transformation has helped NBFC lenders differentiate from competition, improve customer experience, ensure uniform application of credit policies and reduce cost. Despite most use-cases being currently restricted to full and in-principle approvals for unsecured loans, lenders are also providing conditional approvals for secured loans to engage the undecided customer.

Action points:

- Lenders operating in segments where instant, real-time approval is a competitive advantage must look to enhance current technology capabilities and partner with third-party players possessing specialised data analysis tools. New-age techniques (e.g., credit assessment scorecards, API integration with Fintech players) are helping NBFC lenders crunch approval timelines to seconds.
- Lenders must develop policy criteria that will need to be met to be eligible for real-time, in-principle or conditional approval. As a downstream impact, customer journeys and underwriting processes must be re-imagined to account for manual underwriting in exceptional scenarios (e.g., complex customer profiles, technology failure, customer not meeting instant approval criteria etc.).

2.5. Adopt a customer-focused, data-driven approach to collections

Building a collections set up for the digital age

Overdue collections, a generally well-regulated process for most lenders has gained spotlight recently, given the spate of rising bad debts. Led by PSU banks, the banking sector has seen fraud and loan default cases surge to more than INR 14 trillion and plague the INR 113 trillion formal banking sector.[9] Despite focusing on the low-risk retail segment, NBFCs has seen their non-performing assets also rise to more than 5% (742 billion INR) over the last five years.[10]

The rising difficulty in recovering money and enforcing contracts has increased the cost of risk, and cast a shadow on conducting business-as-usual. While regulations do provide opportunities for NBFCs to seek recourse through debt tribunals and SARFAESI, the recovery process largely remains slow and expensive. In such times, lenders are seeking recourse to better manage overdue customers across buckets, through a data-powered and digital approach.

Listed below are some key themes that can help NBFCs build efficient collections setup.

Do not let collections be an afterthought

1. Establish a functional collections set up early into the business

Most new launches underestimate the importance of setting up a fully functional collections set-up on go-live. Despite a limited 'collections-focused' role during the first few months of launch, a fully-fledged set up helps lenders test loan portfolio quality and iron-out teething issues that could affect credit risk management. Several lenders have witnessed an erosion in asset quality early on, by limiting technology investment and capability building in the collections function.

9. Scandals, bad debts at India banks threaten economic outlook, Economic times, September 2018
10. Reserve Bank of India, 2017

Streamline the collections operating structure

1. Segregate collection effort required across life-stages

Lenders must build process workflows, implement enabling infrastructure and partner with relevant third parties for capability building across five stages of collections. Actors and actions must be clearly identified for each stage of the cycle. Secured lending products will require local presence; however, automated processes and other processes, which do not require local knowledge should be managed centrally to drive economies of scale. Technology systems and third-party alliances should support the model for a holistic coverage. The priority of collections unit should be to prevent borrowers from advancing through these stages.

2. Identify accounts requiring special treatment

Lenders should clearly articulate parameters that may migrate a delinquent customer into a 'special treatment' situation. For example, special treatment could be necessitated by high value loans, high customer risk or customers in a delicate situation. On detecting a customer in a 'special situation', lenders must allocate a dedicated, experienced point of contact (PoC) capable of managing the customer's entire portfolio of accounts. Through specialised prior experience, the PoC can provide a focused, consistent treatment to manage collections for complex accounts with better recovery yields.

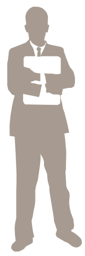
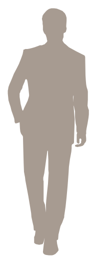
Advanced analytics powered collections decisions

1. Use wider data sets to derive collections strategy

Lenders have relied on customer account balances and credit scores to prioritise delinquent accounts and formulate collections strategy. With wider data sets and big-data processing ability, lenders should explore derivation of delinquent account strategy by looking at large sets of information.

The five stages of debt collection

1	2	3	4	5
Automated	Early stage collections	Mid-late stage collections	Specialists	Third party placement/sale

Exhibit:	**Borrower A** High-risk multiple prior delinquencies, large balance	**Borrower B** Low-risk first time delinquent, small balance	**Borrower C** Low-risk first time delinquent, small balance
			
Process:	Initially assigned to single point of contact ("SPOC") due to high risk	Early end to collections process because borrower pays/brings account current	Low-risk account becomes high risk due to change in borrower conditions and skips steps (sent to third party which handles bankruptcy
Outcome:	Repossessed	Cured, no longer in collections	Customer files for bankruptcy

2. Use third-party tools and data sources to build a 'complete' borrower profile

Lenders must build a holistic customer profile by incorporating alternative data from third party sources (e.g., mobile, utility bill payment records etc.) in addition to data elements gathered during on-boarding. Additional data elements will enable the lender to pro-actively manage risk by detecting early trends and patterns in customer behaviour.

Make collections more customer centric

Collections functions have historically focused on maximum recovery of the loan outstanding, with very little focus on maintaining customer experience. Such lack of focus may result in irreversible damage to any future customer lifetime value, and can have potential repercussions on the NBFC's brand image. By expanding focus from pure recovery maximisation to creating a good customer experience, NBFCs can paint a different strategy of debt management.

1. Take a relationship view towards development of systems and processes

Technology infrastructure with incumbent lenders largely consists of disconnected, disparate systems without any ability to provide a unified view of the customer's relationship with the lender. This leads to multiple collections groups engaging with the customers—leading to conflicting messages and inconsistent application of correction strategies and remediation tools.

2. Train and monitor agents to have appropriate behaviour

A significant percentage of the delinquent customer portfolio self-heals without reminders and improves in financial health over time. Collectors must treat all borrowers with respect, and as a valued customer, irrespective of the delinquency.

NBFCs should ensure that front-line collectors are trained to represent organisational values and maintain a customer-centric approach when dealing with the customer.

Encourage customers to self-cure

1. Educate the borrower of his responsibilities

Prevention is the best cure. Lenders must work on educating customers about the detrimental effects of defaulting on loan repayments. To reinforce the same, lenders can implement practices of making welcome calls and awareness calls. The welcome call must be initiated after disbursal of the loan amount and should inform the customer about the payment schedule, repayment options and mode of payment. Awareness calls can be made before scheduled repayment to remind the customer of upcoming payment and ensure fund balances in the registered debit account. The frequency of calling, email and messages must be configurable and customisable basis the customer's previous credit behaviour and current financial situation.

2. Incentivise good behaviour

An approach that has gained popularity in recent times is incentivising customers to exhibit desired repayment behaviour. Good repayment practices can be inculcated by incentives such as late fee waiver on self-curing, discounted pricing on consecutive timely repayment.

2.6. Supplement technology build-up with agile development mind-set and relentless focus on information security controls

Techtonic shifts

The emergence of new technology advances (e.g., cloud computing, artificial intelligence, blockchain, API banking and digital wallets) have generated an opportunity for existing lenders and new entrants to transform traditional lending models through enhanced products, supplementary value-added services, efficient operations, pro-active risk management and leaner processes. Setting up a sound technology platform also enables NBFC lenders to expand rapidly through optimal resource utilisation and scalable operating models but with low investment cost. The need for a sound technology platform is further heightened in light of the present collaborative business environment requiring a close integration amongst various business and government players.

In the past, increased costs of adopting and implementing technology has deterred small lenders from innovating the middle and back-office. However, the ready availability of solutions at affordable prices, through on-demand models and emergence of pay-as-you-go models, is opening up opportunities for small lenders to reap technology benefits to optimally gain scale.

When starting out, companies face a dilemma in choices between selecting a big bang approach versus an approach of building systems incrementally. While the ideal situation will be to start in a big bang fashion, it is generally not practical in view of the time to market, constrained IT budget and the lack of understanding of all requirements at the initial stage. This is where a loosely coupled architecture with an agile mindset will come in handy, since it provides flexibility to scale, add or remove systems at appropriate time with a quick turnaround.

Leading technology practices

Create a loosely coupled architecture

In a tightly coupled architecture, system components have inter-dependent codes, and changes to any single component's behaviour necessitates changes across the system. Subsequently, these components require real-time synchronous communication to ensure data and control flow according to the initial design.

Lenders can achieve significant improvement in application scalability, resilience, maintainability, and extensibility by adopting a loosely coupled architecture. Unlike a tightly coupled architecture, the system components are independent and resistant to changes. Leveraging asynchronous communication channels, and loosely coupled architecture allows system components to process events and messages on their own terms without affecting the functionality of linked components that initiated the event or message.

For NBFCs, loosely coupled architecture helps connect legacy systems with new systems with minimal effort, and reduced bottlenecks. Additionally, NBFCs can also easily integrate with other internal group entity, government and third-party systems.

Achieve rapid prototyping by agile methodology

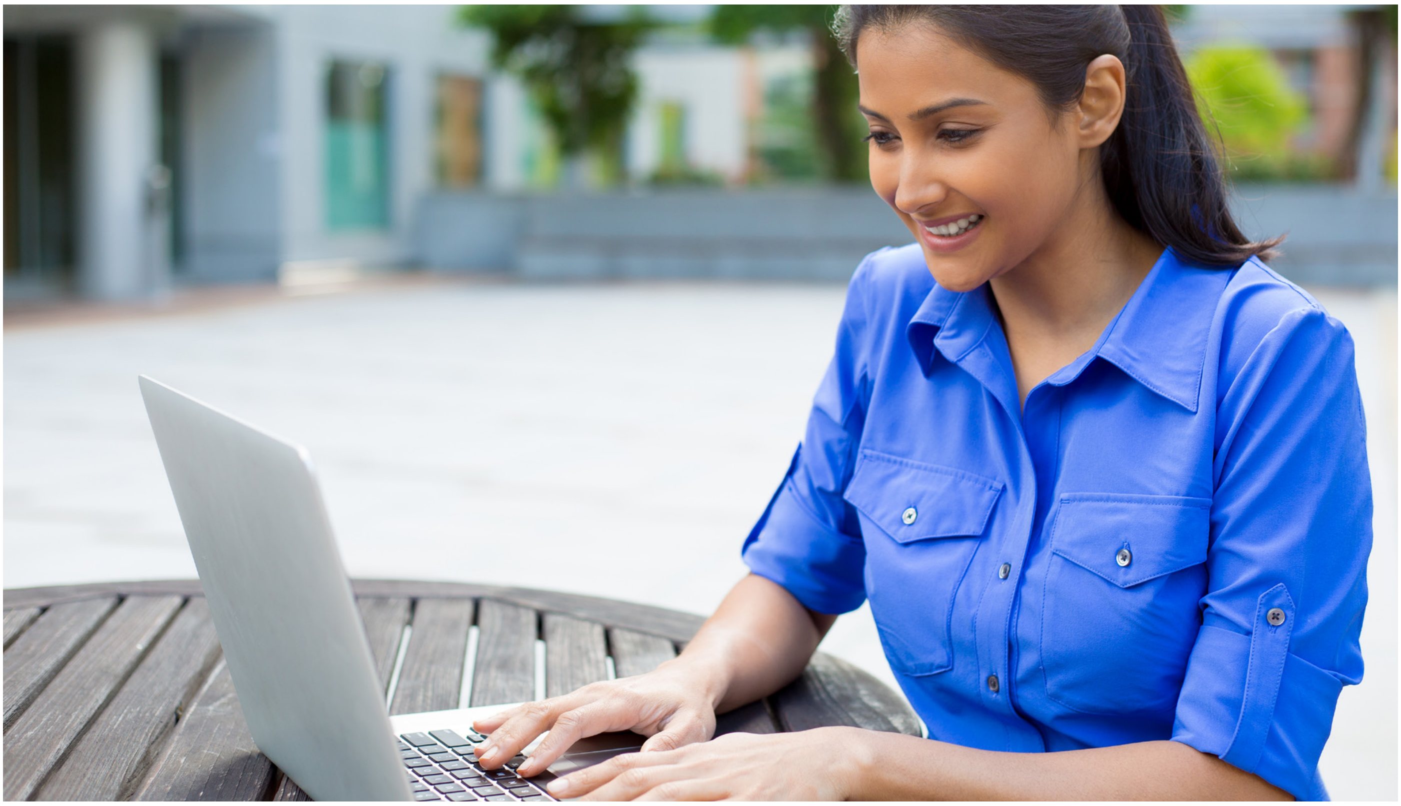
With the lending industry rapidly transforming, NBFC lenders must enable rapid prototyping capabilities to ascertain viability of the change hypothesis before making decisions on investment. Rapid prototyping capabilities allow lenders to create bare minimum working models to test the hypothesis, thereby enabling sound decision-making before going ahead with the necessary investment. Additionally, rapid prototyping also permits business users to deliver incremental value to customers frequently.

NBFC technology functions must transition into an agile development thought methodology to enable a shift towards flexible and robust architecture. This will require technology functions to look beyond traditional capabilities, train and hire resources with ability to apply the right solutions, establish alliance with partners who have a mind-set to work on agile, run iterative development cycles and work seamlessly with business and operations stakeholders..

Relentless focus on information security

Financial services firms have perennially been at the top of the list of targets for cyber-criminals. However, their vulnerability has only increased over the last few years. The propagation of smart devices, applications, IoT devices and an always-connected environment has provided hackers with increasing number of entry points to steal sensitive information and compromise systems.

A rising share of business through digital media has made it imperative for lenders to maintain a clear focus towards fulfilling information security standards in a comprehensive manner to ensure insulation from growing cybersecurity threats. The information security strategy must also be intertwined with the business strategy to avoid any disruption to business and reputation loss on this count. Information security teams must adopt approaches such as Governance-Risk-Compliance (GRC) framework towards setting and governing process and system controls to ensure complete protection. As companies grow, the scope of these controls and governance need to expand beyond internal systems and third-party partners as well. By conducting periodic re-evaluation of the framework, Information Security Officials must ensure that controls are in line with the organisation's ever-evolving needs and adhere to RBI guidelines.



2.7. Explore synergistic alliances with Fintech players

The emergence of Fintech players

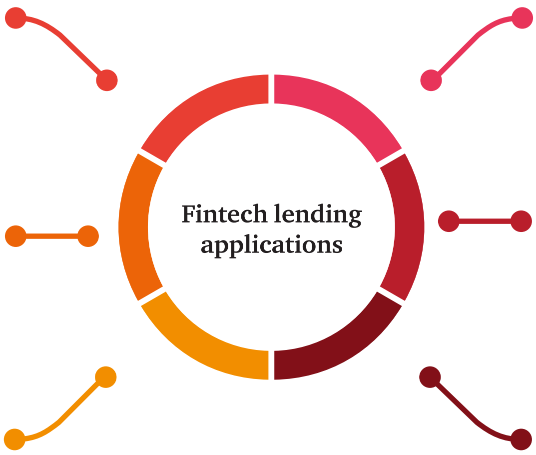
At the locus of technology innovation and financial services, Fintechs have been gaining prominence for promising opportunities and ability to supplement capabilities of the lender. The Fintech industry globally has received 17.4 billion US$[11] in investment in 2016-17. FinTech startups have developed offerings that are faster, better and cheaper across multiple domains—lending, payments, brokerage, credit scoring and personal finance. More than 225 alternative lending based FinTechs (including direct lending, P2P lending, invoice trading, crowdfunding, marketplace platforms and credit scoring) were founded in India in 2017.

Fintech lending start-ups offer differentiated capabilities

Credit Scoring
Many companies have taken up the role of an enabler in the industry, using alternative data sources to build credit scores of the 350 million credit invisible people without a documented credit history.

Marketplace and Comparison Platform
Digital marketplaces connect borrowers and lenders. They reduce the loan processing time and match borrowers to the best fit lender.

Crowdfunding
Crowdfunding entails raising external finance from a large group of investors. The investors can interact with the investees and view their ideas on a crowdfunding platform



Direct Lending
Direct Lending includes platforms that have a lending license. The digitisation of sub-processes, allow reduced costs and gives these NBFCs an edge over banks

P2P Lending
P2P lending involves building a marketplace to bring together individual borrowers and lenders through tech-enabled platforms.

Invoice Trading
Invoice trading assists MSMEs that often struggle with working capital and cash flows due to delayed payments

While previously seen as competition, lenders have now begun to find synergies in collaborating with Fintechs to differentiate or improve their businesses. This has led to several banks and NBFCs to leverage capabilities of Fintech partners to overcome challenges in distribution, underwriting, risk management, etc., and increase their access to underserved and financially excluded customers.

Partnering with Fintech players can help lenders significantly boost capabilities and drive competitive advantage in a crowded market:

- **Creation of new product offerings:** NBFCs are introducing new product offerings by partnering with Fintechs to leverage technology-based tools to access previously unavailable data, and build real-time underwriting models. The partnership is helping NBFCs launch innovative product offerings such as invoice financing, POS financing, payday loans, consumer durable loans and more.
- **Enhanced distribution through digital acquisition:** The capabilities offered by Fintechs have enabled lenders to re-look at their existing processes, to replace their existing manual processes with completely digital and paper-less processes. Enablement of digital onboarding and verifications has led to significant reductions in the cost of acquiring customers, and subsequently allowed lenders to reach out to geographies previously considered unviable.
- **Widening of customer database:** Fintech platforms not only enhance the distribution reach but are also able to comprehensively source and analyse customer data from internet-enabled applications. By incorporating predictive modelling and present customer insights offered by Fintech platforms, lenders can make personalised offers and communications to drive up the probability of lead conversion. At the same time, the data can also be used to understand the riskiness of financing applications.
- **Higher operational efficiency:** The landscape around internal productivity and external simplicity, right from secured loan applications delivered on mobile devices to on-tap P2P payments, has been altered by Fintechs. This has allowed lenders to look beyond cost benefits provided by digital technologies to completely revamp their operational back-office. This has resulted in streamlined delivery and product development with reduced operating costs and increased productivity.

11. Everything you've always wanted to know about financial technology, www.cnbc.com, October 2017

- **Superior customer experience:** A strong customer experience is one of the key reasons for the growth in adoption of digital lenders. Traditional lenders need to play catch-up and rethink their customer experience to provide an omni-channel user-friendly interaction. NBFCs have started to borrow the expertise of these start-ups in attracting new customers, while they manage their core business of managing the loan portfolio.

Ensuring a fruitful engagement

As organisation go about seeking the right partner, they need to bear in mind a few important things to ensure a fruitful engagement.

- The objectives and terms of engagement between the two organisations should be well established to ensure an alignment between the expected goals and capabilities
- Lenders need to make certain that their platforms are at the sufficient level of digital maturity to integrate with the capabilities of the partners
- The cultural nuances of the two organisations should be able to complement each other in the long run

2.8. Develop pro-active and robust risk detection, management and mitigation mechanisms

Despite disrupting the market through technology advances and innovative business models, NBFCs operate at a disadvantage vis-à-vis commercial banks in the form of increased cost of funds and subsequently reduced balance sheet sizes. Additionally, NBFCs have been pursuing an aggressive growth strategy by advancing unsecured credit to new, underpenetrated markets and targeting 'thin file' borrowers, with limited credit history. The strategy has resulted in NBFCs requiring to manage increased risk, across all types—credit risk, interest rate risk, liquidity risk, operational risk, and even reputational risk.

Risk management is paramount for NBFCs, given downstream implications on the ability to successfully raise funds from the market in the short-term and potentially enlist on secondary markets through an IPO in the medium to long term. Additionally, recent regulatory changes and government initiatives have altered the operating mechanism and necessitated changes in the risk management framework for NBFCs. Furthermore, the changes have differing implications for NBFCs, basis the target segment and geographical location of operation. Some key changes include:

- Implementation of new accounting standards (Ind AS/IFRS)
- New FDI norms introduced by the Government to support NBFC funding
- Increased scrutiny by the RBI on NPA reporting, provisioning norms and capital adequacy ratio requirements

NBFC lenders must develop and implement risk management frameworks to pro-actively detect, manage and mitigate internal and external risk types. Listed below are key risks faced by NBFCs, and leading risk management practices that lenders can adopt to remain relevant:

- **Managing credit risk:** As the most common risk faced, NBFCs must develop, formalise and periodically review standard operating procedures and policy guidelines covering majority scenarios. Furthermore, enforcing a robust credit line management for loan approvals, over-withdrawals, exception approvals and inactive or delinquent account closure will help mitigate credit risk. Additionally, due diligence, concurrent and internal audit mechanisms must be formulated and periodically conducted to review and track enforcement and adherence of pre-set policy guidelines.
- **Managing vendor risk:** NBFC lenders often outsource non-value add activities across the loan lifecycle (e.g., field verification, data entry, document scanning and upload, marketing, data analytics etc.) to third-party players with specialised capabilities. The model can potentially expose lenders to a plethora of risks stemming from the vendor's inability to meet service levels or failure in the vendor's operating model. NBFC lenders must consider set-up of a specialised vendor management office to supervise vendor services, ensure periodic audits to ensure commensurate quality, enforce SLAs and penalties. In addition, by monitoring vendor selection and on-boarding, the approach can help NBFCs ensure an unbiased approach to selecting the most qualified vendor.
- **Conducting periodic compliance reviews:** The dynamic nature of regulations requires NBFC lenders to conduct periodic compliance reviews to ensure adherence. Lenders must define a review mechanism and framework, scope of coverage and periodicity to ensure that the organisation remains compliant at all times with prescribed guidelines.
- **Performing quality control checks to ensure process adherence:** NBFC lenders operate with multiple controls to ensure process and data integrity, minimal default and effective delivery of products and services. Conducting periodic quality control checks with reasonable samples ensures functions adhere to stipulated processes.
- **Ensuring information integrity:** NBFC lenders must guard against information leaks, which could potentially jeopardise the customer's financial security as well as tarnish the lender's image. Lenders must incorporate and periodically review IT checks and controls responsible for maintaining information integrity. Moreover, application development cycles must be adhered to and systems periodically audited to minimise leakages. Systems should be developed to incorporate access control, record audit trail, maintain back-up and recovery. Lenders should clearly articulate a data archival policy and ensure that systems are configured according to policy requirements.

2.9. Align the organisation structure with enterprise strategy to maximise productivity and ensure optimal delivery

Ineffective organisation structure design can hamper strategy objectives

Symptoms of ineffective organisation structure	Potential diagnosis areas
Delay in implementation of strategic projects, organisation does not respond quickly to changes in the macro-scenario	Can business and service delivery be enhanced by building new people capabilities and teams?
Poor inter-departmental communication, friction between departments	How should tasks be divided between the corporate centre (group) and the local (region) in a rapidly expanding organization?
Gap in skill-set of employees versus role requirements; underutilised skills and resources; poor employee morale	How do we ensure the right roles are being performed by the right people?
Low net promoter score, high customer attrition, rise in customer complaints	How can the organisation be realigned to drive customer centric behaviour?
Disruptions and cumbersome processes; quality control issues due to deterioration of checks and balances	How do we ensure ease of data flow and access to information across key people?
Deterioration of risk standards, particularly operation risk and credit risk	How do we ensure decision making within the organisation is being performed the right roles, and people with right skillsets?

Lenders are evolving in trying to pursue a complex strategy, entering new geographies, catering to dynamic customer segments and attempting to thrive in intense competition. As organisations attempt to deal with external uncertainties and align with internal strategy, they transform organisation structures through an addition of new positions and departments. Often this results in overlooking roles, responsibilities and creating chaos. An outdated organisation structure can create ambiguity and lack of accountability.

Similarly, poorly designed organisation structures could hinder growth and create risk and control failures.

With an understated ability to foster effective communication, workforce collaboration, effective decision-making and smooth operations, organisation design has emerged as a top priority for leadership in recent years. Lenders who can design effective organisation models and manage complex strategy will sustain and compete better.

Guiding principles for effective organisation design	
Agility	1. **Ensure simplicity** in the organisation design • Promote a simple and easy to understand structure that is transparent to all LOBs and functional stakeholders • Ensure the structure and mandates define clear accountabilities and ownership through concise role definition across the value chain in delivery of the lender's strategy • Optimise structure (e.g., layers and spans) in order to accelerate efficiency in decision-making
	2. Promote **scalability in the design** • Ensure that the lender can scale its design to align with new market conditions and competitive environment • Explore opportunities to leverage alternative service delivery (e.g., sourcing strategies or partnerships) • Design positions to make the most of the strengths of people occupying them
Scalability	3. Drive **"one spirit and culture" mindset** in the design • Drive for increased enterprise-wide or shared capabilities, but respect fundamental differences in business models • Maintain commercial separation only where good governance and contractual terms dictate and only where capabilities are truly unique/critical to delivering value within various lines of business—otherwise identify and address duplication of activities
	5. Design an organisation that promotes **cost effectiveness** • Minimise layers, reduce spans of control • Identify synergies—both exits and reallocation of identified capacity
	6. Bolster **operating model delivery** • Ensure the new structure makes significant enhancements to how the operating model is delivered (e.g., reduction of hand-offs, clear ownership, less duplication, pooling of functions) • Make sure that decision rights are clear and that information flows rapidly and clearly from the executive committee to business units, functions, and departments.
Execution	7. Focus on **customer centricity** to drive for an unparalleled member, client, customer and partner experience • Emphasise design choices that create single points of accountability for core customer interactions (to drive speed of delivery, minimise 'client collisions' and to ensure that it is easy to bring the best of Canara Bank to every customer interaction) • Ensure roles or capabilities, which are closest to the customer are empowered to make decisions without needless hand-offs or escalation
	8. Foster **product or process or service innovation and continuous improvement** • Dedicated, focused investment in product, customer experience and partnership innovation • Build incremental innovation into day-to-day operations and promote a continuous improvement mindset

2.10. Establish a robust governance mechanism to build stakeholders trust in the business

The default of a systemically important NBFC, has thrust corporate governance for the sector into the spotlight. Concerns of a contagion risk for the sector prompted the Government to take swift action and replace the board of the company. Findings from a report prepared by the Ministry of Finance (MoF) has highlighted critical lapses in the management and governance of NBFCs, including the absence of periodic sittings by the risk management committee.

Corporate governance for NBFCs is emerging a vital mechanism especially in trying times where trust in the business is at a premium, and scrutiny from stakeholders is more intense. A strong framework ensures that the workforce is aligned to the lender's purpose and principles, and that corporate goals and value translate into decisions and actions. Given reduced regulatory oversight for the NBFC sector, inadequate governance standards can have downstream implications on the ability of the lender to continue raising funds to support growth and sustain current operations. NBFC organisations must establish a strong, pro-active governance framework to ensure detection, management and mitigation of breaches such as asset misappropriation, money laundering, accounting frauds, bribery, corruption

Recent events surrounding a systemically important NBFC have implications for key players and their lending operations:

- Re-evaluation of credit ratings expected, leading to a probable increase in the cost of borrowing
- Higher borrowing costs may require NBFCs to pass on the costs to the customer, affecting their competitiveness
- Calls for a stronger Asset-Liability Management function to limit interest and liquidity risks
- Tightened regulatory norms and increased scrutiny by the regulator
- Consolidation of NBFCs expected with better capitalized firms likely to takeover smaller rivals

and regulatory non-compliance. Strong governance can be enforced through five pillars:

- Leadership strategy and culture: Described as the ‘tone from the top’, this defines the way business leaders conduct themselves and the ethics and values demonstrated in doing so
- Structure and performance oversight: Required to be infused and embedded across all levels in the organisation, this ensures corporate governance is translated into daily behaviour
- Risk: As the heart of corporate governance, the pillar ensures components of the framework are designed to reflect the overall NBFC risk appetite and ensure accountability
- Management information and controls: Encompassing information systems responsible for data collection and dissemination, this pillar mandates clear, accurate and timely reporting to responsible management and non-management stakeholders, to ensure financial and non-financial impact can be detected, measured and monitored
- Transparency and reporting: Requires open, accurate and timely communication with all stakeholders across shareholders, regulators and employees to ensure a clear understanding of the business situation at hand

Benefits of effective governance models

03

Conclusion

Rising customer expectations and the proliferation of digital business models have accelerated the need for existing NBFC incumbents to transform their operations, while forcing new NBFC entrants to rethink their entry strategy. With recent events increasing the scrutiny on NBFCs and their operations, it is imperative for players to build robust risk and governance models as they grow their lending businesses. Through this paper, we have discussed ten themes that NBFCs should bake into their thinking around long-term, sustainable growth. The leaders in NBFC lending are customer-centric, tech-savvy and, most importantly, are continuously changing to deliver best results. A never-ending exercise, a successful transformation can result in several financial and non-financial benefits and build the NBFC of the future.

	Benefit levers								
	Enhance revenue	Reduce cost	Support sustainable growth	Improve operational efficiency	Enhance customer experience	Meet regulatory compliance	Ensure sound asset quality	Improve access to liquidity	Improve organization capability
Select the right segmentation strategy	D	I	D	D	D	I	D	I	I
Embrace a new attitude to winning over the customer	D	D	I	I	D	I	I	I	I
Improve processes and transform operations	D	D	D	D	D	D	D	D	D
Transform underwriting through technology tools	D	D	D	D	D	I	D	I	I
Adopt a customer-focused, data driven approach to collections	I	I	D	D	I	D	D	I	I
Ensure technology build-up with agile methodology and information security controls	D	D	D	D	D	D	D	D	D
Explore synergistic relationships with fintech players	D	D	D	D	D	I	D	I	D
Develop pro-active and robust risk mechanisms	I	D	D	D	I	D	D	I	D
Align the organization structure with enterprise strategy	D	D	D	D	D	I	D	I	D

D: Direct benefit I: Indirect benefit

04

About ASSOCHAM

ASSOCHAM

THE KNOWLEDGE ARCHITECT OF CORPORATE INDIA

Evolution of Value Creator

ASSOCHAM initiated its endeavour of value creation for Indian industry in 1920. Having in its fold more than 400 Chambers and Trade Associations, and serving more than 4,50,000 members from all over India. It has witnessed upswings as well as upheavals of Indian Economy, and contributed significantly by playing a catalytic role in shaping up the Trade, Commerce and Industrial environment of the country.

Today, ASSOCHAM has emerged as the fountainhead of Knowledge for Indian industry, which is all set to redefine the dynamics of growth and development in the technology driven cyber age of 'Knowledge Based Economy'.

ASSOCHAM is seen as a forceful, proactive, forward looking institution equipping itself to meet the aspirations of corporate India in the new world of business. ASSOCHAM is working towards creating a conducive environment of India business to compete globally.

ASSOCHAM derives its strength from its Promoter Chambers and other Industry/Regional

Chambers/Associations spread all over the country.

Vision

Empower Indian enterprise by inculcating knowledge that will be the catalyst of growth in the barrierless technology driven global market and help them upscale, align and emerge as formidable player in respective business segments.

Mission

As a representative organ of Corporate India, ASSOCHAM articulates the genuine, legitimate needs and interests of its members. Its mission is to impact the policy and legislative environment so as to foster balanced economic, industrial and social development. We believe education, IT, BT, Health, Corporate Social responsibility and environment to be the critical success factors.

Members – Our Strength

ASSOCHAM represents the interests of more than 4,50,000 direct and indirect members across the country. Through its heterogeneous membership, ASSOCHAM combines the entrepreneurial spirit and business acumen of owners with management skills and expertise of professionals to set itself apart as a Chamber with a difference. Currently, ASSOCHAM has more than 100 National Councils covering the entire gamut of economic activities in India. It has been especially acknowledged as a significant voice of Indian industry in the field of Corporate Social Responsibility, Environment & Safety, HR & Labour Affairs, Corporate Governance, Information Technology, Biotechnology, Telecom, Banking & Finance, Company Law, Corporate Finance, Economic and International Affairs, Mergers & Acquisitions, Tourism, Civil Aviation, Infrastructure, Energy & Power, Education, Legal Reforms, Real Estate and Rural Development, Competency Building & Skill Development to mention a few.

Insight into 'New Business Models '

ASSOCHAM has been a significant contributory factor in the emergence of new-age Indian Corporates, characterized by a new mindset and global ambition for dominating the international business. The Chamber has addressed itself to the key areas like India as Investment Destination,

Achieving International Competitiveness, Promoting International Trade, Corporate Strategies for Enhancing Stakeholders Value, Government Policies in sustaining India's Development, Infrastructure Development for enhancing India's Competitiveness, Building Indian MNCs, Role of Financial Sector the Catalyst for India's Transformation.

ASSOCHAM derives its strengths from the following Promoter Chambers: Bombay Chamber of Commerce & Industry, Mumbai; Cochin Chambers of Commerce & Industry, Cochin: Indian Merchant's Chamber, Mumbai; The Madras Chamber of Commerce and Industry, Chennai; PHD Chamber of Commerce and Industry, New Delhi. Together, we can make a significant difference to the burden that our nation carries and bring in a bright, new tomorrow for our nation.

Uday Kumar Varma
Secretary General

The Associated Chambers of Commerce and Industry of India

As a representative organ of corporate India, ASSOCHAM articulates the genuine, legitimate needs and interests of its members. Its mission is to impact the policy and legislative environment to foster a balanced economic, industrial and social development. We believe education, IT, BT, health, corporate social responsibility (CSR) and environment to be the critical success factors.

ASSOCHAM represents the interests of more than 450,000 direct and indirect members across the country. Through its heterogeneous membership, ASSOCHAM combines the entrepreneurial spirit and business acumen of owners with management skills and expertise of professionals to set itself apart as a chamber with a difference.

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About PwC

At PwC, our purpose is to build trust in society and solve important problems. We're a network of firms in 158 countries with over 250,000 people who are committed to delivering quality in assurance, advisory and tax services. Find out more and tell us what matters to you by visiting us at www.pwc.com.

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