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Indian Banking Sector

Credit growth and profitability to moderate; ICRA revises outlook to Stable from Positive

MARCH 2024

Agenda

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Key updates on banking sector

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Banking sector outlook for FY2025 revised to Stable from Positive due to expectation of moderation in credit growth and return indicators in FY2025

ICRA expects the asset quality of the banking sector to continue improving. While recoveries and upgrades are expected to slow down as a large chunk has already been covered, slippages are likely to inch up to some extent in FY2025. However, the same will remain under control. The corporate book's asset quality is expected to remain steady, while the collectability/recoverability in the retail book would keep net additions to non-performing advances (NPAs) in check. Controlled net additions to NPAs and growth in the loan book would lead to an improvement in the headline asset quality metrics.

The reported capital ratios of several banks have started reflecting the impact of the recent regulation regarding the increase in risk weights on lending to the retail unsecured and non-banking financial company (NBFC) segments. However, some impact is expected to be reflected in their reported results for Q4 FY2024 as well. The implementation of the expected credit loss (ECL) framework in the medium term would also be a monitorable, particularly for public sector banks (PSBs). Despite the impact of regulatory changes, the capital position of both public and private sector banks is expected to remain comfortable in the foreseeable future.

On the credit expansion front, the growth rate is expected to moderate in FY2025. This, along with the continuing compression of interest spreads, amid the upward repricing of the deposit base in FY2024 and the downward repricing of loans in FY2025 with likely cuts in monetary policy rates, would exert pressure on the profitability. Despite the moderation, the return indicators are expected to remain healthy and sufficient to meet most of the growth requirements of the sector. Accordingly, the outlook on the banking sector has been revised to Stable from Positive.

- The year-on-year (YoY) credit growth remained robust at 16.5% as on March 8, 2024 while deposits grew by 13.1% in the same period
- The headline asset quality metrics continued to improve with the gross NPA (GNPA) and net NPA (NNPA) at 3.0% and 0.7%, respectively, as on December 31, 2023 (4.0% and 1.0%, respectively, as on March 31, 2023)
- Profitability remains healthy on the back of benign credit costs, with the annualised return on assets (RoA) at 1.28% in 9M FY2024 (1.08% in FY2023)
- Most banks are comfortably placed on the capital front, with some raising growth capital in 9M FY2024
- The solvency (NNPAs/core equity capital) level improved to 6.1% as on December 31, 2023 (8.1% as on March 31, 2023)

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Thank You!