Indian Banking Sector

Credit slowdown to pull down profitability, though the same would remain healthy

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Agenda

ICRA

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2 Advances - PSBs Gained Market Share

3 Asset Quality and Profitability Trends

4 Capital Position and Requirements

5 ICRA's Outlook on Banking Sector

6 ICRA's Coverage on Banking Sector and Sector Aggregates

Highlights

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Though ICRA expects the credit growth to remain moderate and profitability to trend downwards in FY2025 and FY2026, the return indicators are expected to remain comfortable leading to ICRA's Stable outlook for the sector.

The overall credit growth has moderated in the past few months with banks focusing on reducing their credit-to-deposit (CD) ratio and reducing their exposures to unsecured retail and non-banking financial companies (NBFCs). Consequently, the credit and deposit growth has almost merged and ICRA expects the trend to continue. Accordingly, ICRA has revised its credit growth downwards to 10.5-11.0% for FY2025 from its earlier estimate of 11.6-12.5% in FY2025. For FY2026, ICRA expects the credit growth to further reduce to 9.7-10.3% as the persisting high CD ratio and implementation of the proposed changes in the liquidity coverage ratio (LCR) framework, would weigh on the credit growth.

Fresh non-performing advances (NPAs) generation rate is expected to rise in H2 FY2025 and FY2026, while the recoveries and upgrades are likely to moderate. Consequently, the quantum of gross NPAs (GNPAs) would rise; although the GNPA ratio is estimated to trend rangebound by March 2025. Thereafter, even the GNPA ratio is likely to rise in FY2026. The capital ratios of several banks remain comfortable, and no major growth-related capital requirement has been seen in FY2025 and FY2026. Nevertheless, the implementation of the expected credit loss (ECL) framework and increased provisioning for project finance in the medium term is likely to be monitorable.

ICRA expects the persisting high interest rates and the slowdown in credit growth (especially towards high yielding advances) to impact margins. In addition, the rate transmission on yields is estimated to be faster as and when the rate cut begins, which would further compress the margins. Nevertheless, the return indicators are likely to remain healthy and sufficient to meet most of the growth requirements.

- The YoY credit growth moderated to 10.6% as on November 29, 2024, while deposits grew by 10.7% in the same period.
- The headline asset quality metrics continued to improve with the GNPA and net NPA (NNPA) at 2.6% and 0.6%, respectively, as on September 30, 2024 (2.8% and 0.6%, respectively, as on March 31, 2024).
- Profitability remained healthy on the back of benign credit costs, with return on assets (RoA) at 1.36% in H1 FY2025 (1.32% in FY2024).
- Most banks are comfortably placed on the capital front.
- The solvency (NNPAs/core equity capital) level stood at 4.6% as on September 30, 2024 (5.1% as on March 31, 2024).

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Thank You!