Financials

Recovery in credit growth to go on; NIM to exhibit a positive bias

Traction in garnering deposits remains key; GNPA to moderate to decade lows

CRISIL Ratings hosted a webinar titled, 'Banking on a new note' to discuss growth and asset quality outlook, trends in overall earnings, and capital requirements. The webinar was followed by a panel discussion with Mr. Rakesh Jha (Executive Director of ICICI Bank), Mr. KVS Manian (Whole-Time Director and Group President of Kotak Mahindra Bank), Mr. Arun Khurana (Deputy CEO of IndusInd Bank), Mr. Sanjay Agarwal (MD and CEO of AU Small Finance Bank), and Mr. Pralay Mondal (MD and CEO of CSB Bank). Here are the key takeaways:

Buoyancy in credit growth to go on; Retail and MSME to be the key drivers

- After undergoing an elevated period of Balance Sheet fortification, the focus is now shifting towards expansion of credit growth. The credit profile of Banks across the industry has been stable, with an improvement across most parameters. While credit growth in the past few years has been largely driven by Retail, the same for the Corporate segment is seeing healthy signs of a pick-up. Corporate credit is largely driven by working capital requirements as private capex is still a few quarters away.
- While Corporate credit will pick-up gradually, the Retail and MSME segment will remain the key growth driver. Home and Unsecured loans will continue to keep Retail growth healthy. CRISIL expects overall loan growth to pick up to 14-15% CAGR over FY22-24, with the key risks being rising inflation and interest rates. Among segments, it expects Retail/MSME/Agri/Corporate to grow at 17-19%/16-18%/8-10%/10-12%.

Garnering deposits to be a challenge; competitive intensity to increase

Over the past few quarters, there was a faster growth in credit vis-à-vis deposit growth, given the excess liquidity and as Banks were focusing on a gradual deployment of the same. While the increase in deposit rates so far has been controlled, it is expected to rise at a faster pace in coming months. The panelists believe that deposit growth will be in focus over the next six months, given the RBI's stance on further rate hikes and tightening liquidity. As a result, deposits rates are likely to increase, which will intensify the competition to garner additional deposits to fund the increase in lending. This, in turn, will boost deposit growth.

Margin to exhibit a positive bias; a high mix of floating loans to aid margins

The mix of floating rate loans remains high ~80%, within which the mix of EBLR loans has increased to 44% in FY22 v/s a mere 2% in 1HFY20. This has resulted in faster re-pricing of the asset book in a rising interest rate environment, which, coupled with higher rates on incremental loans, will benefit yields. While deposit rates will see an increase, the same is likely to be lower than the rise in yields. Hence, margin is likely to exhibit a positive bias. CRISIL expects overall margin to improve to 3% in FY23 v/s 2.9% in FY22, with the key monitorable being the greater dependence on high-cost bulk deposits.

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Improving trend in asset quality; GNPA ratio to touch a decade low of 4%

- Over the past few years, the aggressive cleanup by Banks has resulted in a sharp decline in stressed assets. The mix of PSU and AA and above assets has risen to 77% in FY22 v/s 59% in FY17, while the mix of sub-investment grade assets have almost halved to 7% v/s 17%.
- Credit ratio witnessed an improvement in FY22 and is likely to continue its upward trajectory. However, rising inflation can impact cash flows of the corporates, primarily MSME, which remains a key monitorable.
- Total restructuring book for the system stood ~2% of loans, while the same for MSME stands elevated at 6%, of which 25% is expected to slip into NPA. However, the impact on overall asset quality is likely to be limited.
- Slippages are expected to moderate to 2% in FY23 v/s 2.5% in FY22. The GNPA ratio is expected to moderate to a decade low of sub-4% by FY24. The GNPA ratio for the Corporate/Retail/MSME/Agri segment is likely to moderate to sub-2%, 1.8-2%, 10-11%, and 9-10%.

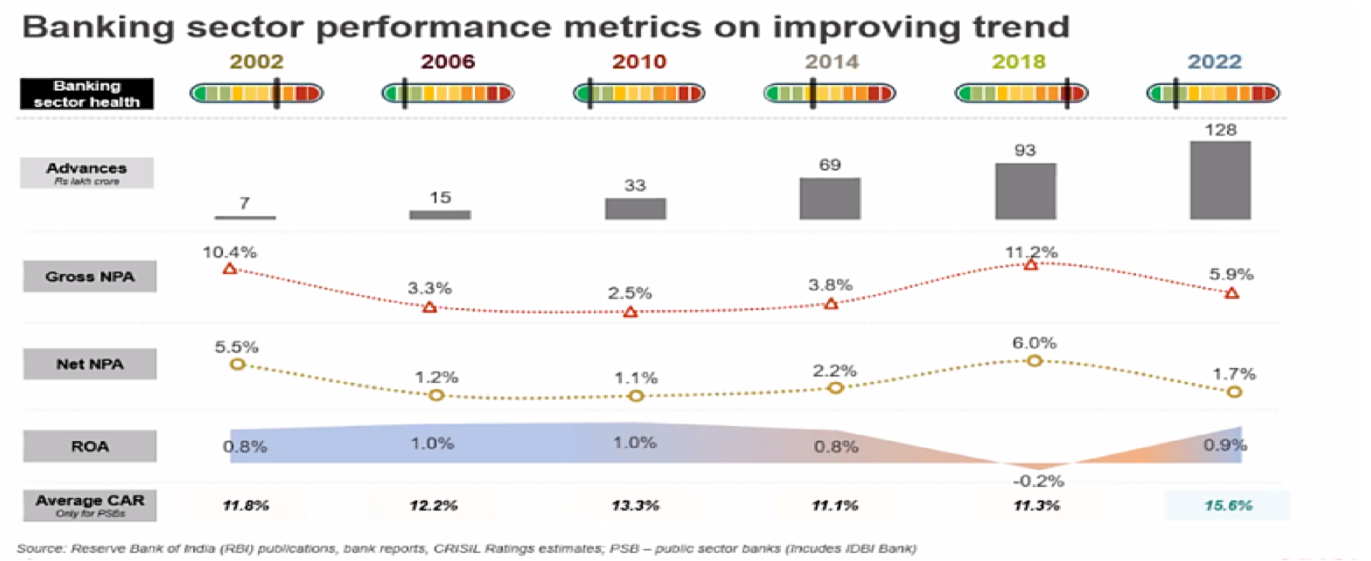
Credit cost continues to trend lower; return ratios to improve to 1% in FY23

Banks have significantly increased their PCR to 73% in FY22, which, coupled with a lower expectation of slippages, will keep the provisioning requirement controlled. As a result, credit cost will witness a downward trajectory, thereby aiding profitability. CRISIL believes that treasury losses have peaked in 1QFY23, which will further aid profitability. Credit cost is expected to moderate to 0.7% in FY23, while RoA is likely to improve to 1% in FY23. RoA is likely to improve to 0.7%/1.6% for PSBs/Private Sector Banks (v/s 0.3%/1.2% in FY21).

Capitalization levels have improved; incremental requirement to be lower

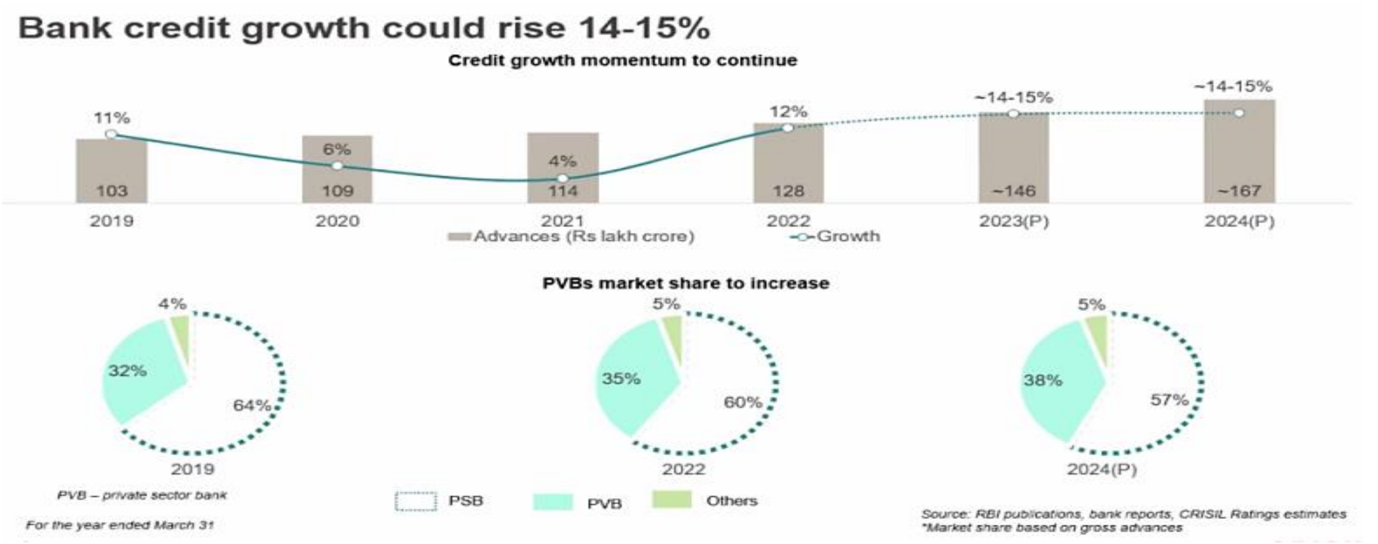
- Capitalization levels for the bank have improved significantly over the past few years and are well-paced at decade highs. As per CRISIL, all PSBs have a Tier I buffer of over 100bp v/s 24% in FY18. CAR currently stands at 15.6%, which has been the best in the past two decades.
- While the government has infused majority of the capital in PSBs, many Banks have been able to raise capital from the market in the past one-year, which is likely to pick up gradually as the earnings profile of the PSBs improves further. Over the past five-years, PSBs have raised ~INR3.5t (including government infusion) and Private Banks INR1.4t. CRISIL feels the incremental requirement for capital is likely to be lower in the coming years, given the improved levels.

Exhibit 1: Performance of key metrics over the past two decades



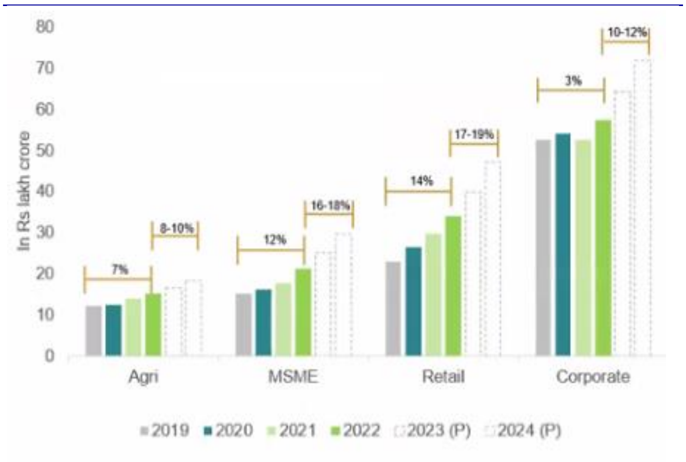
Source: MOFSL, CRISIL

Exhibit 2: Bank credit to grow at 14-15% CAGR over FY22-24



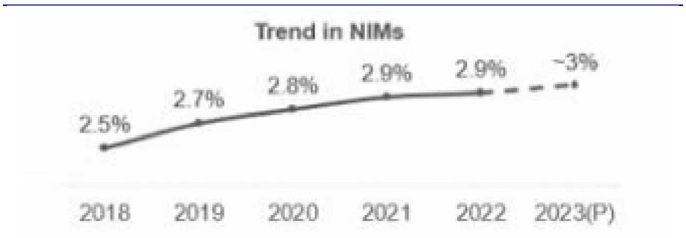
Source: MOFSL, CRISIL

Exhibit 3: Segmental growth trends



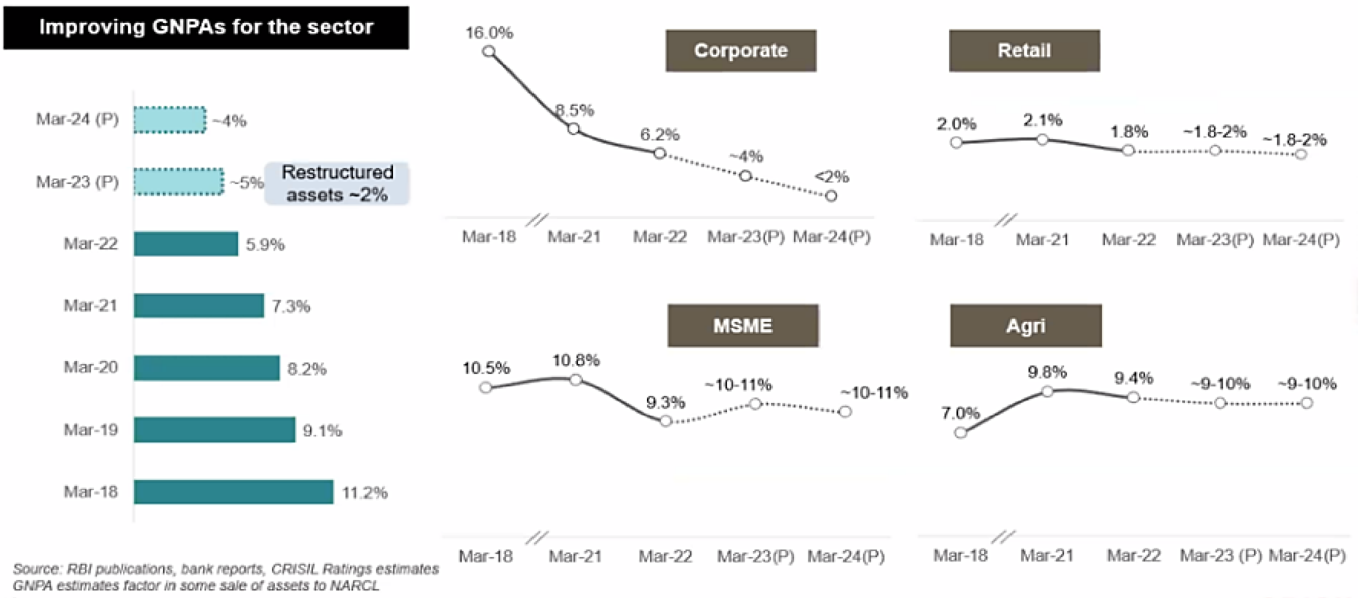
Source: MOFSL, CRISIL

Exhibit 4: Margin to improve by ~10bp to 3% in FY23



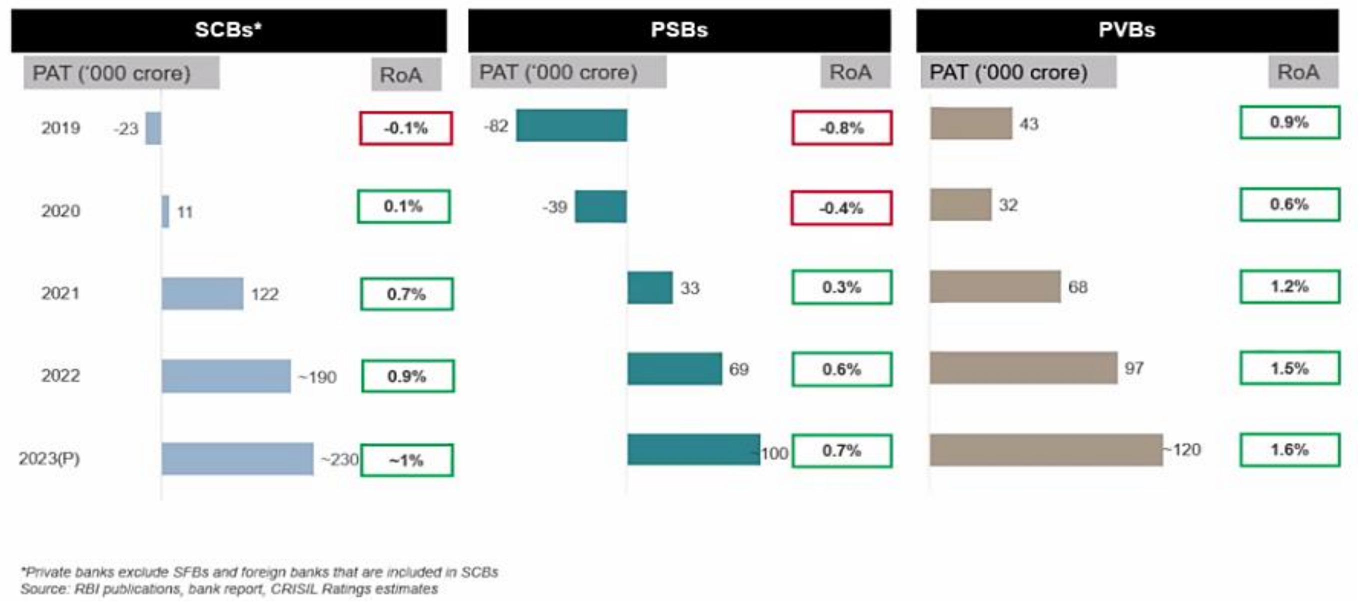
Source: MOFSL, CRISIL

Exhibit 5: GNPA to moderate to decade lows at 4% by FY24



Source: MOFSL, CRSIL

Exhibit 6: Expect RoA to improve to 1% in FY23



Source: MOFSL, MFIN

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