

OUTLOOK  
FY2022

# FY 2021-22 OUTLOOK FOR BANKING SECTOR

**Moderation in asset quality pressures to drive credit and earnings growth in FY2022; Stable Outlook**

**December 28, 2020**

# Outlook for FY2022 for key metrics



## Credit and Deposit Growth

Bank credit growth likely to pick up to 6.0-7.0% in FY2022 as against estimated 3.9-5.2% in FY2021 and 6.1% in FY2020

Deposit growth to remain steady at 9.5-10.0% in FY2022 as against estimated 9.6-10.3% in FY2021 and 7.9% in FY2020



## Asset Quality

Net Non-performing advances to decline to 2.4-2.6% by March 2022 from estimated 3.0-3.2% as of March 2021 and 3.0% as of March 2020

Credit provisions to decline to 1.8-2.3% of advances in FY2022 as against estimated 1.9-2.6% in FY2021 and 3.1% in FY2020



## Capital Requirements

Incremental capital requirement estimated to be less than Rs 100 billion for private banks till FY2022

Public banks could require incremental capital of Rs 210-693 billion till FY2022 including pending allocation from recapitalization for FY2021



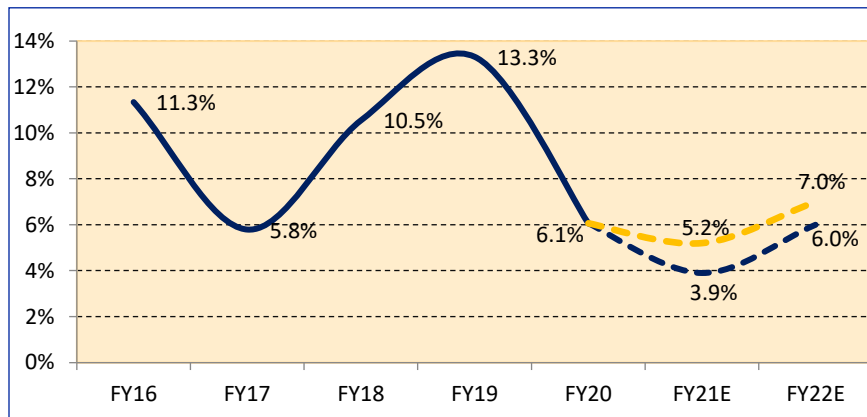
## Profitability

RoA and RoE for public banks to remain weak at 0.0-0.3% and 0.0-5.4% respectively in FY2022 (-0.1/+0.2% and -2.3%/+3.7% estimated in FY2021)

RoA and RoE for private banks to improve to 1.0-1.2% and 9.5-10.5% respectively in FY2022 (0.3~0.8% and 3.0~7.5% estimated in FY2021)

# Credit growth to improve in FY2022

Exhibit: Muted credit growth in FY2021, likely to recover in FY2022



Source: ICRA research

Exhibit: Segmental credit growth for FY2021



## Agriculture

6.6~7.2% : healthy kharif season and favorable outlook



## Industries

-1.6~- 2.2% of which MSME loans +3.0~4.0% driven by ECLGS



## Services

6.5~8.6% of which NBFCs +5.4~8.0%



## Retail

7.2~8.6% of which Housing +6.5~7.7%

- Sharp contraction in economic activity, risk aversion of lenders led to further slowdown in credit growth during FY2021
- Clarity on asset quality and consequent provisioning requirement will provide impetus to lenders and rejuvenate lending decisions
- Low interest rates, improved business volumes, better job and income prospects to stimulate credit demand
- Better competitive positioning vis a vis other lenders driven by steep decline in cost of deposits

# Asset Quality to improve in FY2022 after weak FY2021

Exhibit: Gross NPAs (Public and Private banks)

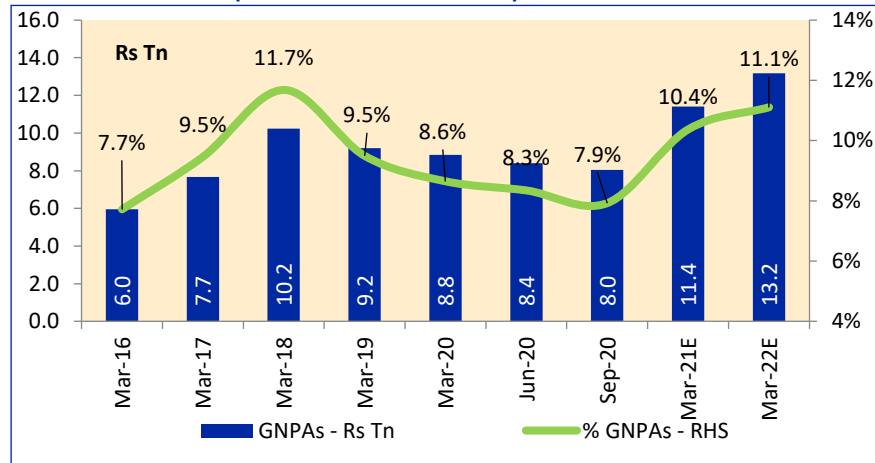
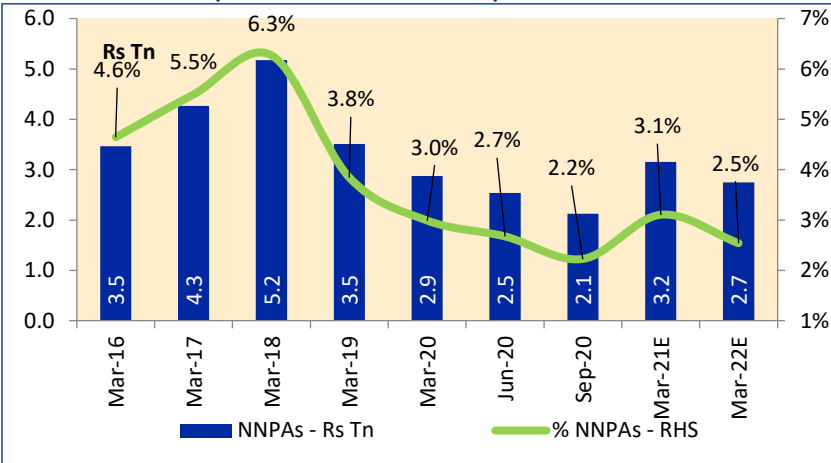


Exhibit: Net NPAs (Public and Private Banks)



Source: ICRA research. GNPA projections are excluding write-offs

- Headline asset quality number improved despite significant disruption in cash flows of borrowers during H1FY2021, because of moratorium on loan repayments and status-quo on asset classification ordered by Hon'ble Supreme Court. Expect slippages to rise to 3.1-3.7% for FY2021 and moderate to 2.4-2.9% in FY2022
- GNPA to rise to 13.3-13.7% by March 2021 and 14.1-14.8% by March 2022 for public banks (10-9-11.2% and 11.6-12.0% respectively after write offs)
- GNPA to rise to 6.5-7.3% by March 2021 and 7.5-8.4% by March 2022 for private banks (5.6-6.2% and 6.3-7.0% respectively after write offs)
- Net NPAs to decline below March 2020 levels by end of FY2022 for both public (3.1-3.4% by March 2022) and private banks (1.4-1.5% by March 2022)
- Lower Net NPAs to improve solvency profile for both public and private banks by March 2022

# Improved asset quality to translate in better profitability in FY2022

Exhibit: Return on Assets

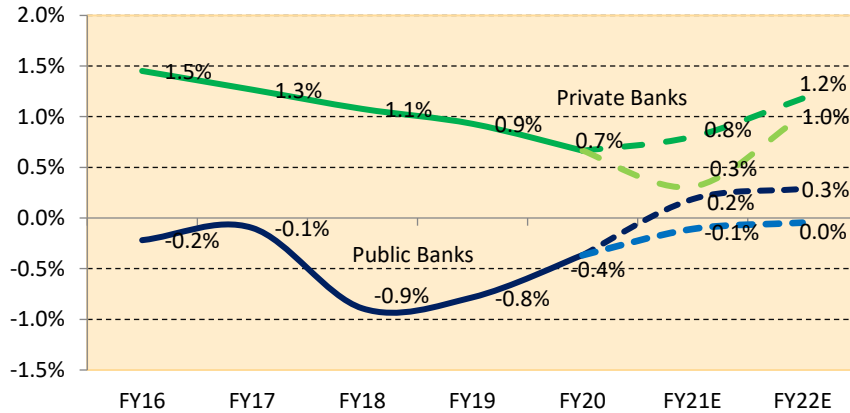
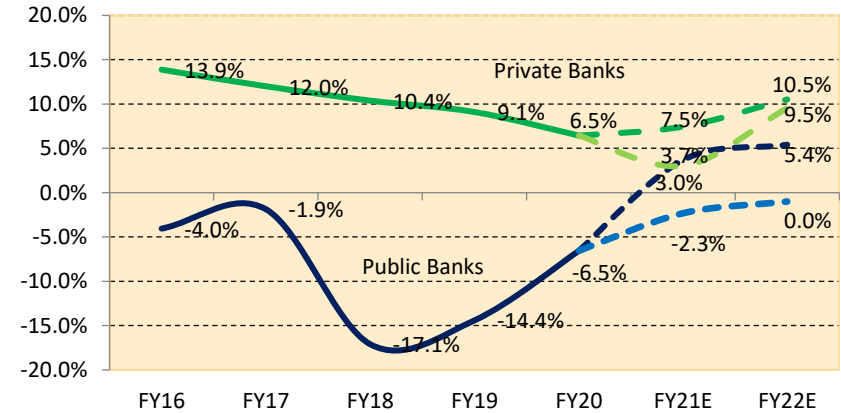


Exhibit: Return on Equity

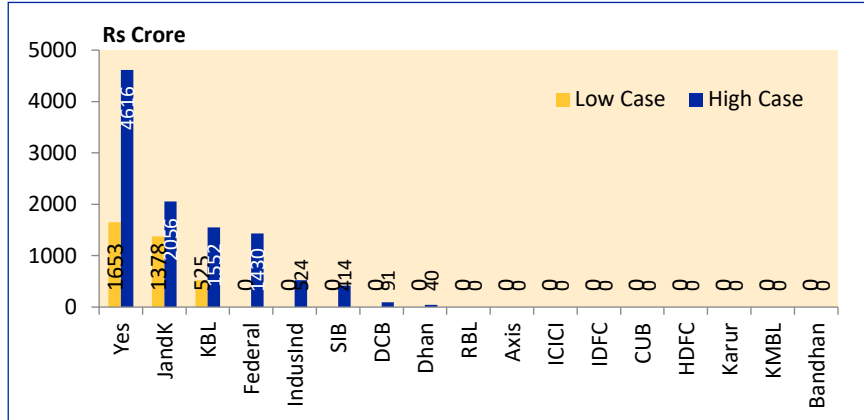


Source: ICRA research

- Private banks carrying higher Covid-19 provisions at 0.7% of advances as against 0.2% carried by public banks as of September 2020
- With estimated credit provisions of 2.4-3.6% for private banks and 2.1-2.8% for public banks for FY2021, reversal of Covid-19 provision seems unlikely in H2 FY2021
- Credit cost to moderate for private banks to 1.7-2.1% and 1.9-2.7% for public banks in FY2022
- Despite high credit losses, provisions for public banks are estimated to be lower than FY 2018-2020 leading to improved profitability/lower losses
- With upfront of provisions in Q4 FY2020 and FY2021, profitability for private banks to rebound in FY2022

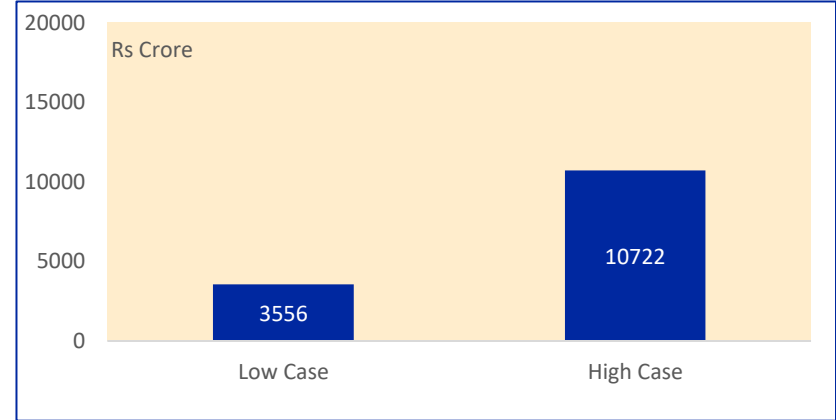
# Large private banks well placed on incremental capital requirements

Exhibit: Bank-wise Tier I capital requirement FY2021-2022



Source: ICRA research

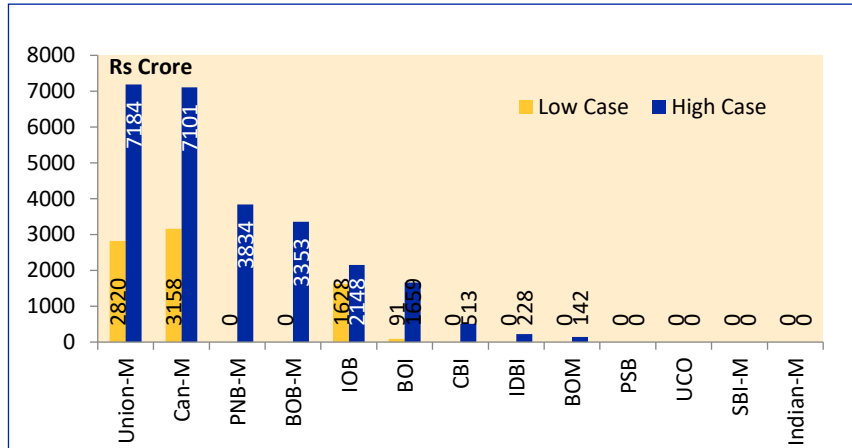
Exhibit: Capital Requirements for private banks FY2021-22



- Key assumption – RWA growth at 8-10% for FY2021 and 10-12% during FY2022 except for some banks which may consolidate or shrink balance sheets. Tier 1 capital cushion of 0.5-5.0% has been assumed depending on rating category of each bank. (AAA = 4-5%, AA = 3-4%, A = 2-3%, BBB = 1-2%). Above estimates includes the estimated profits / losses for FY2021-22 and includes any capital raisings done till December 2020
- Large private banks have raised equity capital of Rs 544 billion in 9M FY2021, which limits their incremental capital requirement
- Large private banks have call option falling due on their AT-I bonds totaling of ~[Rs 260 billion](#) during FY2022-2023, which shall not be a challenge
- Mid-sized and old private banks will however require further capital, and it could be a challenge for them, if the stress on asset quality increases

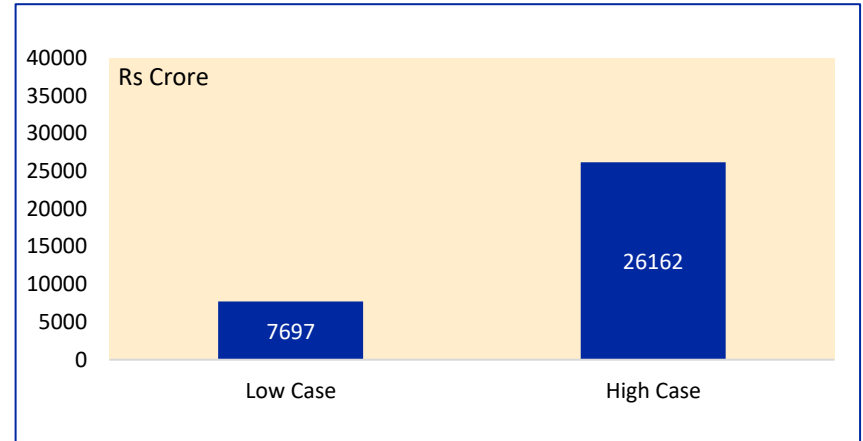
# Budgeted capital likely to be sufficient for public banks in FY2021

Exhibit: Bank-wise Tier I capital requirement FY2021



Source: ICRA research

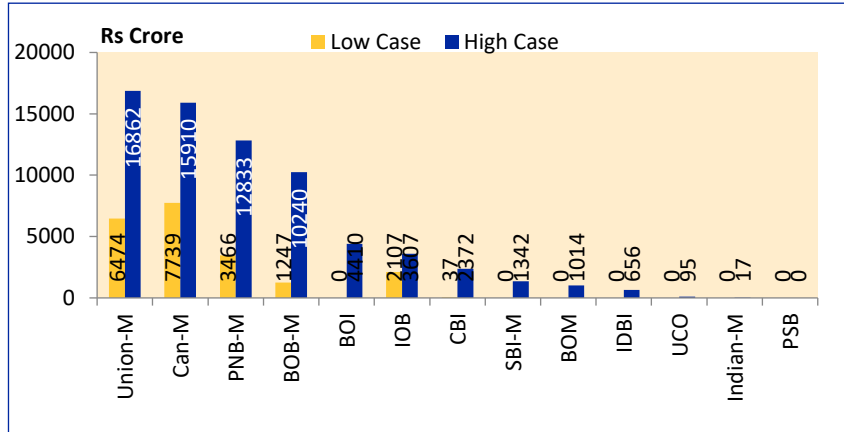
Exhibit: Capital Requirements for public banks FY2021



- Key assumptions – All PSBs (Excl PCA banks) to keep Net NPA <6% and all PSBs to maintain capital ratios with Tier 1 of minimum 9.5%. Non-PCA PSBs to have a RWA growth of 3-4% and PCA PSBs to reduce their RWA by 5-10%. Above estimates includes the estimated profits / losses for FY2021 and equity capital/Tier 1 bonds announced/raised till December 2020. Capital cushion have been assumed over regulatory levels for various banks varying from 0.5%-1.6% depending on rating levels and D-SIB requirements
- Govt has budgeted Rs 200 billion for FY2021 of which Rs 55 billion has been allocated to Punjab & Sind Bank
- Public banks have raised AT-I bonds totaling Rs 120 billion and equity capital of Rs 75 billion in 9MFY2021. With few more banks likely to raise capital from market, the capital budgeted by Govt appears to be sufficient for FY2021

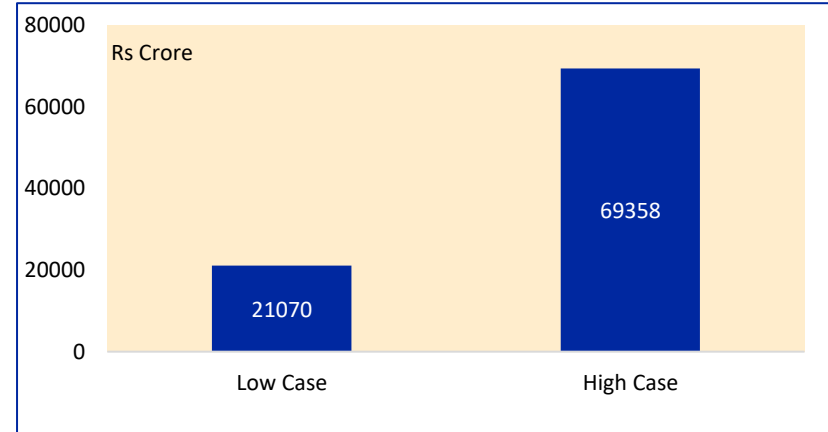
# Public banks to require upto Rs 430 billion of capital during FY2022

Exhibit: Bank-wise Tier I capital requirement FY2021 + FY2022



Source: ICRA research

Exhibit: Capital Requirements for public banks FY2021 + FY2022



- Key assumptions – Same as previous slide with RWA growth of 4-5% in FY2022 across all banks. Most PCA banks are likely to exit PCA framework in FY2022.
- Of the total estimated incremental capital of upto 700 billion for FY2021 + FY2022; Rs 145 billion is allocation pending from budgeted capital for FY2021
- Assuming banks were to raise the requisite capital of upto Rs 261 billion in FY2021 as outlined in previous slide, the incremental capital requirement will be ~Rs 432 billion for FY2022. Capital requirement has increased as banks have call option falling due on their AT-I bonds totaling [Rs 233 billion](#) in FY2022
- Incremental capital raise by public banks from market sources (equity / AT-I) will reduce their dependence on GoI.

# Summary



## FY2022 Outlook

Asset Quality	Capital	Solvency Net NPA / Core Capital	RoA	RoE
<p><b>Public Banks</b>  <b>Net NPAs = 3.1-3.4%</b>            Lower than 4.0%E for Mar 21 and Mar 20 level of 3.8%</p> <p><b>Private Banks</b>  <b>Net NPAs = 1.4-1.5%</b>            Lower than 1.5-1.6%E for Mar 21 and Similar to March 2020 level of 1.45%</p>	<p><b>Public Banks</b>  <b>Tier 1 = 9.3-10.8%</b>            Above estimate is with capital allocation/raise till Dec 2020</p> <p><b>Private Banks</b>  <b>Tier 1 = 15.2-16.5%</b>            No significant capital requirement for most of large banks</p>	<p><b>Public Banks</b>  <b>39-41%</b>            To improve from 46-49%E for Mar 21 and Mar 20 level of 46%</p> <p><b>Private Banks</b>  <b>8-9%</b>            To improve from ~10%E for Mar 21 but similar to Mar 20 levels of 9%</p>	<p><b>Public Banks</b>  <b>0.0% / + 0.3%</b>            Profitability to remain weak (-0.1/0.2%E for FY21 and -0.4% FY20)</p> <p><b>Private Banks</b>  <b>1.0-1.2%</b>            RoA to improve from FY2020 level of 0.7% and 0.3-0.8% for FY2021</p>	<p><b>Public Banks</b>  <b>0.0-5.4%</b>            Likely to break-even after six year of losses</p> <p><b>Private Banks</b>  <b>9.5-10.5%</b>            RoE to improve from FY 2020 level of 6.5% and 3.0-7.5% for FY2021</p>



ICRA

## RECENT TRENDS

Asset quality, Profitability and Capital ratios supported by moratorium and standstill on asset classification

# Fresh Slippages to rise in H2 FY2021

Exhibit: Fresh Gross Slippages – Public Banks

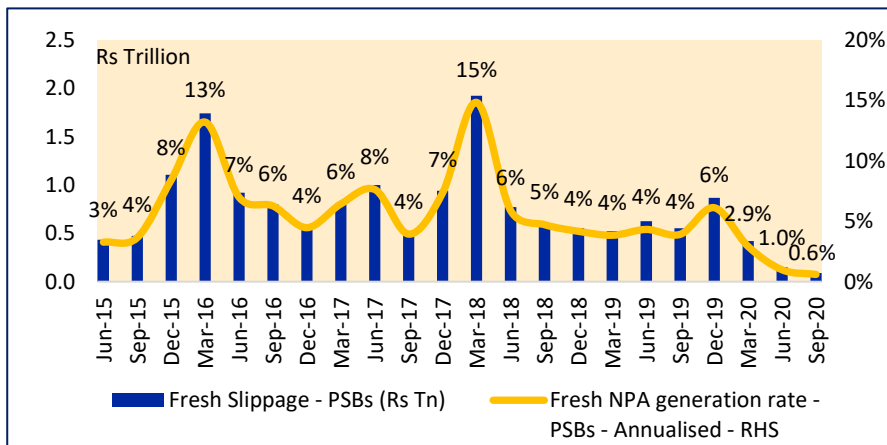
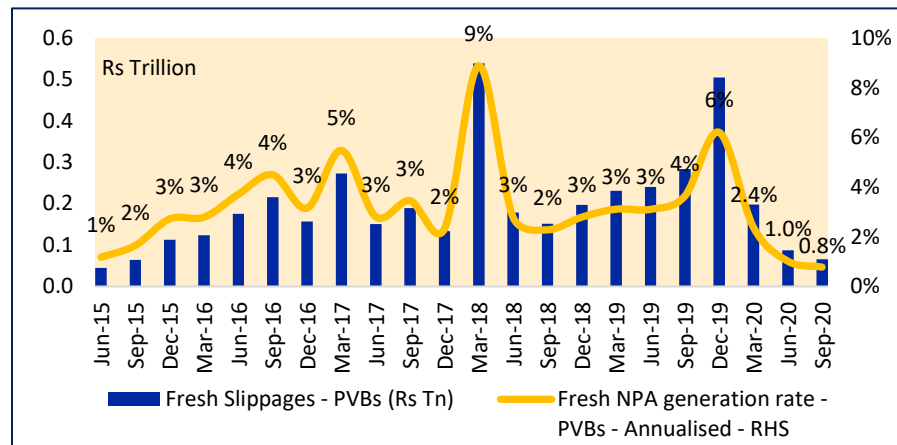


Exhibit: Fresh Gross Slippages – Private Banks



Source: ICRA research

- Moratorium on loan repayments coupled with stay on asset classification by Hon'ble Supreme Court resulted in steep decline in slippages during H1 FY2021
- Adjusted for stay order, the GNPA and NNPA are estimated to be higher by 0.4% and 0.3% respectively for banks which reported data as of September 2020
- Repayment by overdue borrowers during moratorium period corrected the overdue status of loans and could lead to lower slippages in near future also
- Emergency Credit Guarantee line scheme (ECLGS) of GoI also provided much needed liquidity to borrowers and reduced asset quality pressure and possible need for loan restructuring. Loan restructuring guidance by banks much lower than our [earlier estimates](#) and clarity to emerge in Q4 FY2021/Q1 FY2022.
- Expect gross fresh slippages of 3.1-3.6% for FY2021 and 2.5-3.0% for FY2022, apart from likely restructuring of 2.5-4.5% of advances

# Credit provisions to remain high despite lower slippages

Exhibit: Credit Provisions – Public Sector banks

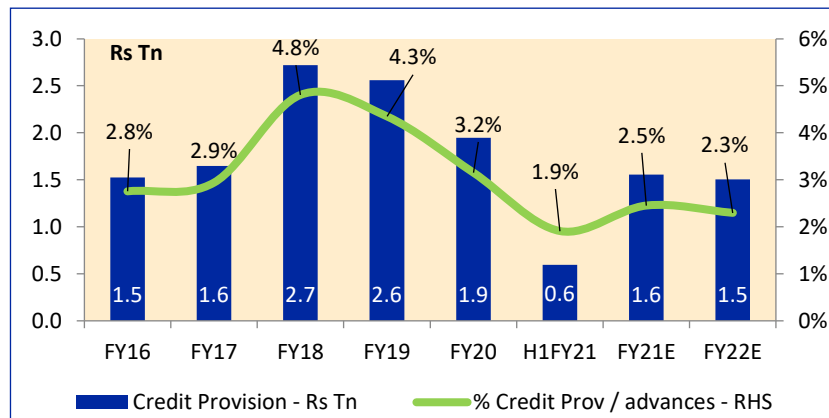
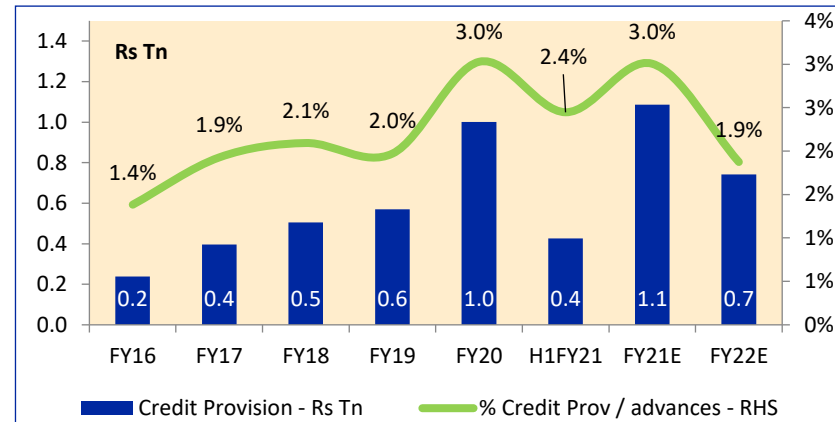


Exhibit: Credit Provisions – Private Sector Banks



Source: ICRA research

- Credit provisions remained high for both public and private banks despite lower slippages in H1 FY2021
- While public banks continued to make provisions on legacy NPAs leading to lower Net NPAs, Private banks made provisions for expected Covid-19 stress
- Private banks carrying Covid-19 provisions at 0.7% of advances as against 0.2% carried by public banks as of September 2020
- Reversal of Covid-19 provisions seems unlikely for most banks given our full year credit cost estimates for FY2021

# Gains on bond portfolios cushion bottom-line

Exhibit: Key profitability indicators – Public Banks

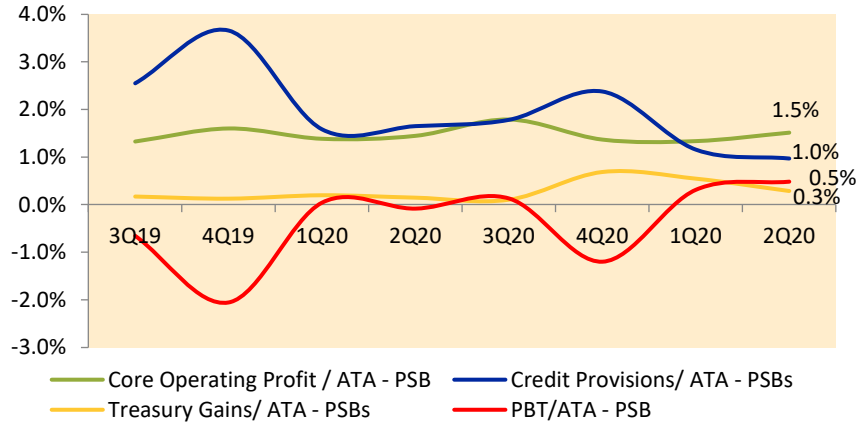
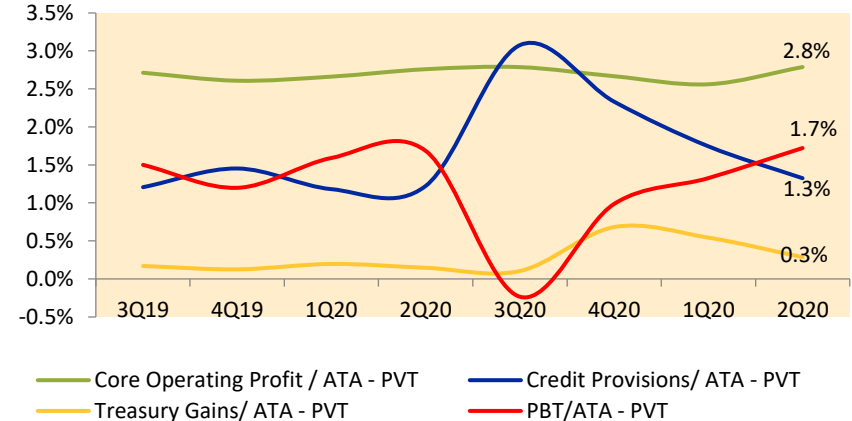


Exhibit: Key profitability indicators – Private banks

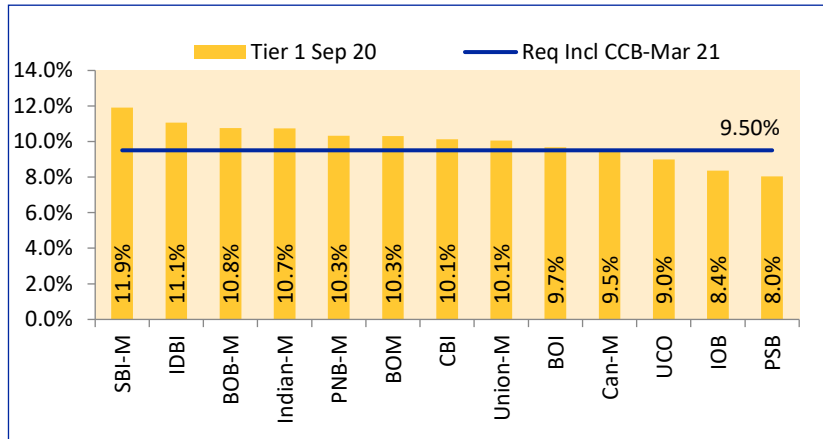


Source: ICRA research, ATA = Average total assets

- Public banks reported good profits during H1 FY2021 after many quarters, however this was supported by a) improved gains on bond portfolio after decline in bond yields and b) lower credit provisions as slippages were muted in H1 FY2021.
- Given the expectations of rise in provisions in H2 FY2021 and limited incremental gains on bond portfolio, profitability will be weak for public banks in H2 FY2021
- Private banks saw normalization of credit costs which coupled with gain on bond portfolios improved the bottom-line
- Private banks too likely to witness higher asset quality and provisioning pressure in H2 FY2021 and moderation in profitability from H1 FY2021 levels

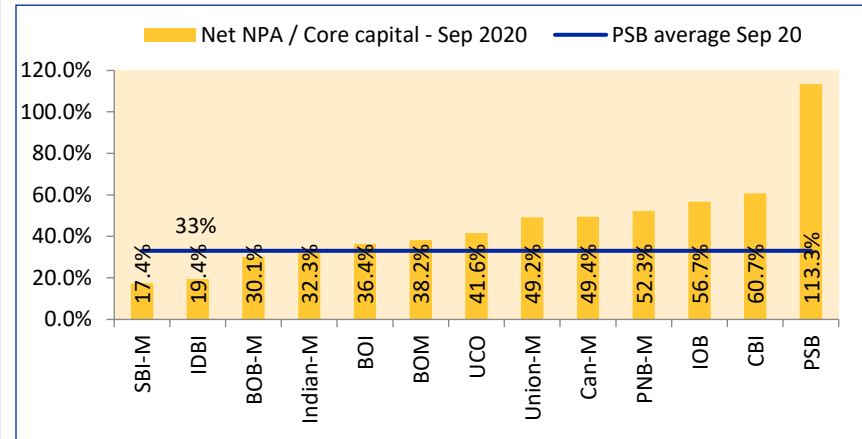
# Capital and solvency position of Public banks better than past

Exhibit: Tier I capital for public banks as on September 30, 2020



Source: ICRA research

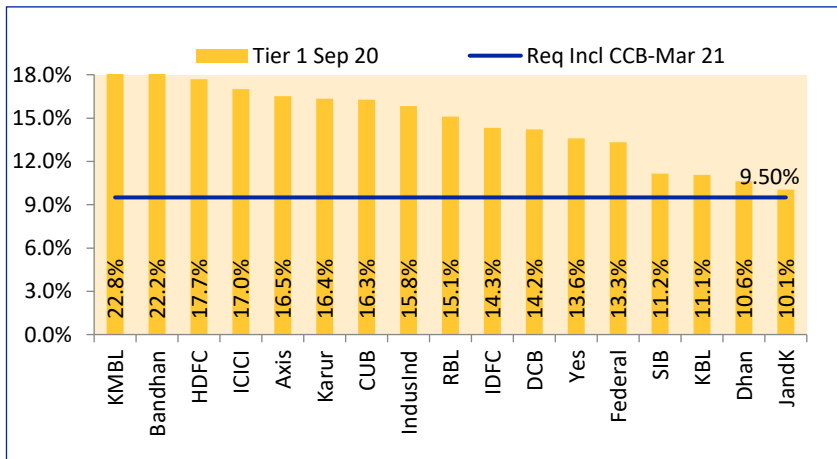
Exhibit: Solvency position for public banks as on September 30, 2020



- No meaningful equity capital raise by public banks in H1FY2021, however during Q3 FY2021, public banks raise equity capital of Rs 75 billion from markets
- Capital cushions for most PSBs weak and RBI also deferred the scheduled increase in regulatory Tier I requirements (9.5%) by 6 months to April 1, 2021
- GoI announced a capital allocation of Rs 200 billion during September 2020
- AT I bond issuances by public banks picked up. Indian Bank, Union Bank, Canara Bank, BoB and SBI raised Rs 123 billion in 9M FY2021 (Rs 103 billion in FY2020)
- Lower Net NPAs resulted in improved solvency position of 33% as on September 2020 as compared to 46% as of March 2020 and 61% as of March 2019

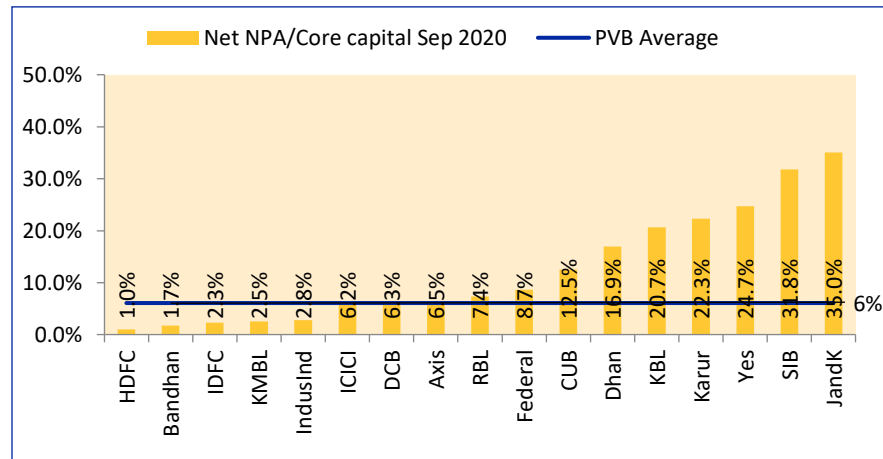
# Sizeable capital raise by private banks in H1 FY2021

Exhibit: Tier I capital for public banks as on September 30, 2020



Source: ICRA research

Exhibit: Solvency position for public banks as on September 30, 2020



- Private banks raised sizeable equity capital of Rs 543 billion (1.4% of risk weighted assets) in 9M FY2021, a large part of which was raised in H1 FY2021 prior to completion of moratorium and announcement of loan restructuring guidelines as the uncertainty on asset quality was high
- Notable capital raise included, ICICI = Rs 150 bn, Yes = Rs 150 bn, Axis – Rs 100 bn, Kotak = Rs 75 bn, Indusind = Rs 33 bn, IDFC = Rs 20 bn and RBL = 15.7 bn
- All large banks well placed to absorb asset quality shocks as they raised capital higher than our stress case estimates

# Rating actions FY 2021 YTD

Exhibit: Tier II bonds rating distribution of ICRA rated public banks (Incl IDBI)

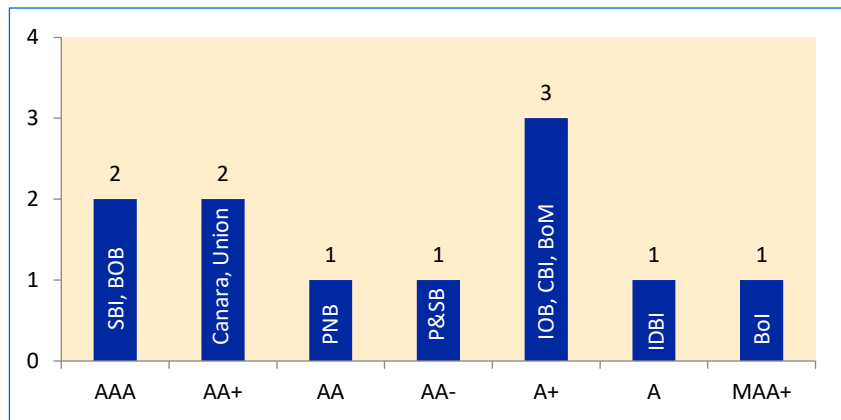
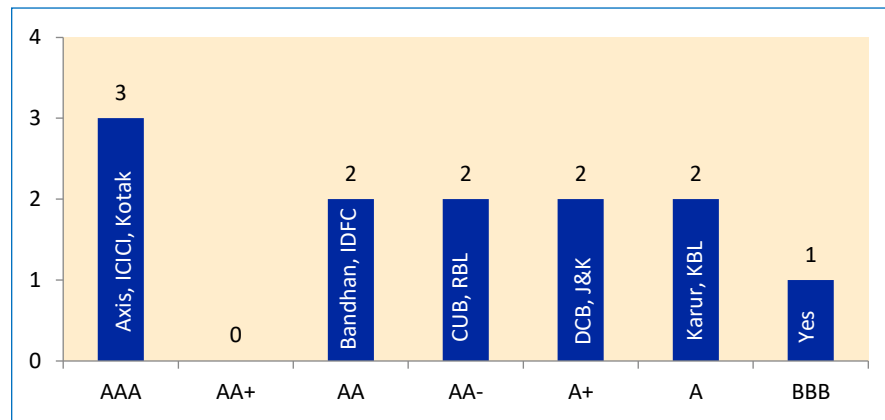


Exhibit: Tier II Rating distribution of ICRA rated private banks



Source: ICRA research, Rating for Bol is for fixed deposits

- ICRA rates 11 out of 13 Public Banks (incl IDBI). Rating on 4 banks is on negative outlook (P&SB, IOB, CBI and Union), while that of BoM is on positive outlook
- Rating downgrade in public banks included a) downgrade of Punjab and Sind Bank by 1 notch because of significant weakening of capital and solvency position
- Rating upgrade in public banks included a) Punjab National bank by 1 notch as capital and solvency profile improved and b) Canara Bank AT 1 by one notch to [ICRA] AA Stable as the coupon payment ability of the bank will improve as it proposed to set-off its accumulated losses against share premium account. In addition, the short-term rating of IDBI bank was upgraded to [ICRA] A1+ (from [ICRA] A1) as its liquidity position improved
- Among Private banks, ICRA upgraded the rating for lower Tier II bonds of Yes Bank to [ICRA] BBB Stable (from [ICRA]BB+) after the sizeable capital raise in Q2 FY2021. Prior to this, in July the rating on Upper Tier II bonds of Yes Bank was downgraded to [ICRA]D from [ICRA]BB because of regulatory breach in capital ratios

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