

Indian Banking Sector

**Performance update and outlook:
Asset quality of retail segment, a key
credit growth driver, holding up well**

SEPTEMBER 2023



1 Key Takeaways



2 ICRA's Outlook on Banking Sector



3 Overview of Banking Sector's Performance



4 Asset Quality Trends



5 Profitability



6 Capital Position and Requirement



7 Trends in Retail



8 ICRA's Coverage on Banking Sector



9 Sector Aggregates



The near-to-medium-term performance of the banking sector, in terms of the asset quality, is expected to witness a sustained improvement in FY2024, led by the controlled net non-performing advances (NPA) additions (net of recoveries and upgrades) as well as the reasonably strong credit growth. These factors continue to drive the benign outlook for credit costs in FY2024. Apart from this, banks remain comfortable on their solvency and capitalisation profiles while the earnings of most banks is expected to remain healthy, supporting their near-term growth requirements despite a relative moderation due to the repricing of liabilities. Accordingly, the outlook on the banking sector continues to remain Positive.

With the retail segment continuing to be one of the key drivers of credit expansion, its share in overall bank credit has increased in recent years. While there was some weakening in the asset quality levels following the onset of the Covid-19 pandemic, the same eased subsequently. Furthermore, the asset quality in the retail segment has remained on an improving trajectory while the potential vulnerable book/overdue book has declined, remaining largely at manageable levels. This is despite the higher interest rates and inflation, which have led to increased servicing burden and lower disposable income for retail borrowers at large. Going forward, while macro-economic conditions like poor monsoons, inflation, etc, may exert pressure on the servicing abilities of borrowers, banks are likely to be well positioned to manage higher slippages, if these were to rise, as they are expected to be much better placed to absorb the impact, if any. Moreover, given the granularity and better collectability of retail loans, the impact on profitability would remain lower if such a scenario were to play out.

- YoY credit growth remained robust at 14.4% as on August 11, 2023, despite a relative moderation
- The headline asset quality metrics for banking continued to improve with GNPA and NNPA at 3.7% and 0.9% as on June 30, 2023 (4.0% and 1.0% as on March 31, 2023)
- Profitability levels for the sector remain healthy, with the return on assets (RoA) at 1.32% in Q1 FY2024 (1.08% in FY2023), on the back of benign credit costs, even as net interest margins (NIMs) witnessed some compression
- Most banks are comfortably placed on capital, although few banks may need to raise growth capital
- The solvency level for the banking sector improved in Q1 FY2024 to 7.6% from 8.2% in March 2023



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