

# SMALL FINANCE BANKS

Strategic shift in portfolio mix to drive growth; profitability to remain under pressure

December 2025



# List of abbreviations

<b>ARC</b>	Asset reconstruction company
<b>ATA</b>	Average total assets
<b>AUM</b>	Assets under management
<b>Bps</b>	Basis points
<b>CAGR</b>	Compound annual growth rate
<b>CASA</b>	Current account savings account
<b>CET</b>	Common equity Tier I capital
<b>CRAR</b>	Capital-to-risk weighted assets ratio
<b>GNPAs</b>	Gross non-performing assets
<b>LAP</b>	Loan against property
<b>NIM</b>	Net interest margin
<b>NNPAs</b>	Net non-performing assets
<b>NPAs</b>	Non-performing assets
<b>Opex</b>	Operating expenses
<b>RBI</b>	Reserve Bank of India
<b>RoA</b>	Return on assets
<b>SFBs</b>	Small finance banks

## 1 Portfolio Growth



## 2 Asset Quality Trends



## 3 Profitability and Capitalisation



## 4 Funding and Liquidity



## 5 Industry Outlook



## 6 Regulatory Updates, ICRA's Ratings in the Sector and Annexures





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*ICRA expects SFBs to report 18-20% growth in gross advances in FY2026 with secured products being primary growth drivers; adequate capital and liquidity support growth plans*

*Uptick in delinquencies in microfinance segment and limited seasoning of secured products would keep asset quality volatile; ICRA expects GNPA's of 3.7-3.9% as of March 2026*

*RoA projected to moderate to 1.0-1.2% in FY2026 amid margin compression and elevated credit costs; some improvement expected in FY2027*



- SFBs demonstrated a healthy portfolio growth of 17% year-on-year (YoY) in H1 FY2026 (21% in FY2025; 24% in FY2024) accompanied by a strategic shift in the portfolio mix. Given the asset quality challenges persisting in the microfinance segment, ICRA expects the portfolio growth of SFBs to moderate to 18-20% in FY2026, followed by an improvement to 22-25% in FY2027 with secured lending segments being the primary growth drivers.



- SFBs reported a ~120-bps increase in GNPA's to 3.6% as of March 2025, largely due to slippages in the microfinance segment; this inched up to 3.9% as of September 2025. ICRA expects the stress in the microfinance segment and limited seasoning of new products to keep the asset quality volatile and credit costs elevated in the near term.



- With SFBs strategically realigning their product mix towards relatively lower-yielding secured asset classes, portfolio yields declined in FY2025 and H1 FY2026, leading to a contraction in margins. Given the reduced NIMs and elevated credit costs, ICRA expects SFBs to report an RoA of 1.0-1.2% in FY2026 vis-à-vis 1.3% in FY2025, followed by some improvement in FY2027.



- In line with the trend seen for universal banks, depositors have moved towards term deposits, leading to a drop in the share of CASA deposits over the last few years. While deposit growth has remained healthy for SFBs, their CASA dropped to 27% as of September 2025 from 35% as of March 2022; increasing the share of CASA deposits remains a challenge for SFBs.



- As of September 2025, all SFBs were operating with adequate capital cushions over the regulatory levels. ICRA expects them to continue maintaining sufficient capital buffers in FY2026 with the Tier I ratio expected to be around 19% as of March 2026.



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