ICRA

Indian Banking Sector

Retail and MSMEs drove credit growth in YTD FY2026; trend to continue in the medium term

DECEMBER 2025

Agenda

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1 Credit and Deposit Growth Revival

2 Trend in Advances – PSBs & PVBs

3 Asset Quality Trends

4 Profitability Trends

5 Capital Position and Requirements

6 ICRA's Outlook, Banking Sector Coverage and Sector Aggregates

Highlights

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ICRA expects the profitability to trend slightly downwards in FY2026; however, the return indicators are likely to remain comfortable, leading to ICRA's Stable outlook for the sector.

ICRA anticipates the credit growth to remain healthy and estimates credit expansion at 10.7-11.5% in FY2026 and 11.7-12.3% in FY2027.

The beginning of FY2026 witnessed slow credit offtake as the banks remained cautious towards the retail sector and non-banking financial companies (NBFCs), and the corporates preferred bond markets given the low yields. Nevertheless, bank credit picked up by end of H1 FY2026 and the trend continued thereafter, resulting in YoY credit growth of 11.4% as on November 28, 2025. Measures like goods and services tax (GST) rationalisation and liquidity boost via cash reserve ratio (CRR) cuts helped the sector achieve a healthy credit growth trajectory till November 2025. Factoring in the same, ICRA had recently revised its credit growth estimate for FY2026 upwards to Rs. 19.5-21.0 trillion (10.7–11.5%) from its earlier estimate of Rs. 19.0-20.5 trillion (10.4-11.3%). Going ahead as well, ICRA anticipates the credit growth to continue at a healthy pace with retail and micro, small and medium enterprises (MSMEs) as major growth drivers. In addition, private sector banks (PVBs) are likely to re-focus on growth after having reduced the credit–deposit (CD) ratio so far. Accordingly, ICRA estimates credit expansion of Rs. 23.50-25.00 trillion (11.7-12.3%) in FY2027.

The faster downward yield movement compared to deposit repricing has impacted the net interest margins (NIMs) of banks. The gradual downward repricing of deposits was expected to lead to NIMs improvement in H2 FY2026; however, the recent rate cut in December 2025 is likely to delay the improvement until Q1 FY2027. Overall, ICRA anticipates a slight moderation in the return indicators in FY2026, though the same would remain steady in FY2027. Further, these are likely to remain sufficient to meet the anticipated growth requirements of the sector.

Despite the expected improvement in economic activity and the outlook on credit growth, ICRA remains watchful of the asset quality, given the susceptibility to the uncertainties emerging from the evolving geopolitical conditions.

- The YoY credit growth bounced back to 11.4% as on November 28, 2025, from a low of 8.8% as on May 30, 2025 (10.9% as on March 21, 2025), while the YoY deposit growth stood at 10.2% as on the same date.
- The headline asset quality metrics improved further with the gross non-performing advances (GNPAs) and net NPAs (NNPAs) at 2.1% and 0.5%, respectively, as on September 30, 2025 (2.2% and 0.5%, respectively, as on March 31, 2025).
- Profitability remained healthy on the back of benign credit costs and healthy treasury income, with the annualised return on assets (RoA) at 1.3% in H1 FY2026 (1.3% in FY2025).
- The solvency (NNPAs/core equity capital) level stood at 3.6% as on September 30, 2025 (3.8% as on March 31, 2025).

Key takeaways

Stable outlook reflects ICRA's expectation of comfortable asset quality, capital position and earnings

Credit growth to pick up in H2 FY2026 and FY2027	▪ YoY credit growth rose to 11.4% as on November 28, 2025; ICRA had recently revised its credit growth estimate for FY2026 to 10.7-11.5% (earlier estimate of 10.4-11.3%) with growth picking up in H2 FY2026. The trend is expected to continue in FY2027 and ICRA estimates credit growth of 11.7-12.3% in FY2027.
Asset quality to stay comfortable despite uptick in slippages	▪ Absolute GNPAs and NNPAs expected to witness YoY uptick; however, with healthy credit growth GNPA% and NNPA% to remain steady ▪ Slippages are likely to be granular, unlike bulky corporate slippages in the past
Manageable credit costs to support profitability	▪ NIMs to start improving, going ahead, with deposits getting further repriced downwards; though the recent rate cut in December 2025 would slightly delay the margins recovery to Q1 FY2027 ▪ Treasury income supported RoA in H1 FY2026, amid pressure on NIMs ▪ Credit provisions to rise but remain benign, which would help keep RoA/return on equity (RoE) at heathy levels
Incremental improvement in capital and solvency position to remain limited	▪ Limited regulatory or growth-led fresh capital requirements for most banks in FY2026 and FY2027 ▪ Capital cushions to remain healthy as expected accruals would be sufficient to meet growth requirements ▪ Transition to expected credit loss (ECL) norms remains monitorable; though banks are estimated to have built-up capital cushions by the time ECL is implemented.

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Thank You!