Select Extracts of RBI's Financial Stability Report - July 2020

July 26, 2020 I BFSI Research

Contact:
Sanjay Agarwal
Senior Director
sanjay.agarwal@careratings.com
+91-22- 6754 3582
Mob.+91-810-800-7676

Saurabh Bhalerao
Associate Director
saurabh.bhalerao@careratings.com
+91-22-6754 3519
Mob. +91-900-495-2514

Mradul Mishra (Media Contact)
mradul.mishra@careratings.com
+91-22-6837 4424

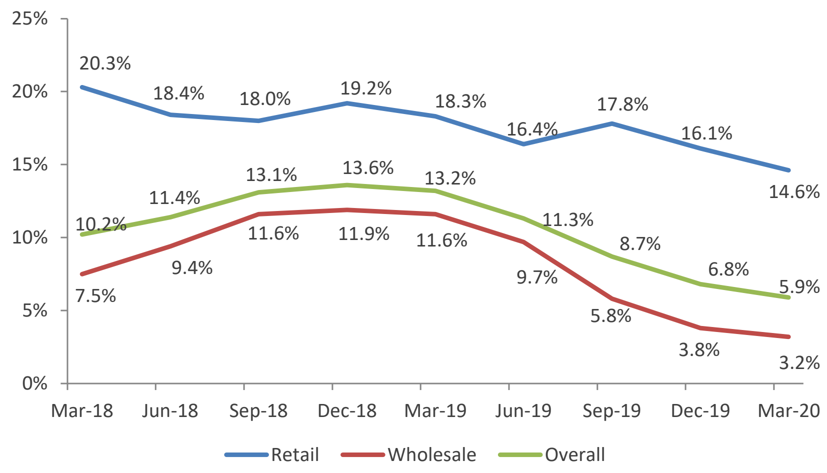
The Financial Stability Report of the RBI presents a contemporary picture of the Banking and Financial Services sector which is going through challenging times due to the Covid-19 pandemic and the consequential stressed economic environment.

Scheduled Commercial Banks

Credit growth (y-o-y) of scheduled commercial banks (SCBs), which had considerably weakened during the first half of 2019-20, slid down further to 5.9 per cent by March 2020 (vs. 13.2% in March 2019) and remained muted up to early June 2020. This moderation was broad-based across all bank groups.

Credit growth of public sector banks (PSBs) reduced to 3% (y-o-y) in March 2020 from 9.6% in March 2019. However, private sector banks (PVBs) reported double digit credit growth of 11.3%.

Figure 1: SCB - Credit Growth (% yoy)



Source: RBI

The corporate sector's credit offtake has slowed down; hence SCBs' credit growth has been due to a robust but slowing retail credit growth across bank groups, coupled with decelerating wholesale credit growth.

SCB deposit growth improved to 8.6% in March 2020 compared with 9.9% in March 2019. Deposit growth in both PSBs and PVBs outpaced their credit growth, although deposit growth in PSBs was comparatively slower at 6.9% y-o-y in March 2020 vs. 11.1% for PVBs.

Growth in net interest income (NII) dropped to 13% in March 2020 as compared with 16.5% in March 2019. PSBs' profitability metrics were subdued on account of the weak credit growth and PVBs' profitability ratios also declined, while foreign banks showed better profitability.

The Return on Assets (RoA) of PSBs continues to be negative at (-)0.2% as compared with 0.7% of PVBs as of March 2020. The RoA of SCBs overall stood at 0.2% for the same period.

The capital to risk-weighted assets ratio (CRAR) of SCBs edged down to 14.8% in March 2020 from 15.0% in September 2019; PVBs recorded a marginal rise in CRAR whereas the ratio weakened for PSBs and FBs.

Figure 2: Performance of SCBs (%)

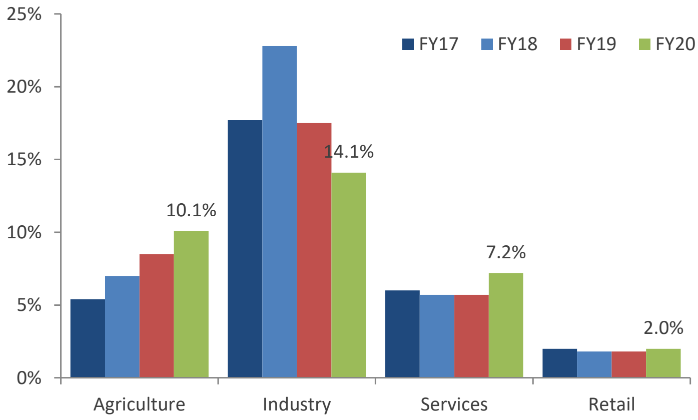
Financial Performance	Mar-18			Sep-18			Mar-19			Sep-19			Mar-20		
	PSB	PVB	SCB	PSB	PVB	SCB	PSB	PVB	SCB	PSB	PVB	SCB	PSB	PVB	SCB
Credit Growth (Y-o-Y)	6.3	21.3	**10.4**	9.1	22.5	**13.1**	9.6	21	**13.2**	4.8	16.5	**8.7**	3.0	11.3	**5.9**
Deposit Growth (Y-o-Y)	3.3	17.7	**6.9**	5.0	18.4	**8.7**	6.5	17.5	**9.9**	6.6	19.0	**10.2**	6.9	11.1	**8.6**
Ratios															
RoA	-0.9	1.3	**-0.2**	-0.7	1.2	**-0.004**	-0.9	1.2	**-0.1**	-0.1	1.0	**0.4**	-0.2	0.7	**0.2**
GNPA Ratio	15.6	4	**11.6**	14.8	3.8	**10.8**	12.6	3.7	**9.3**	12.7	3.9	**9.3**	11.3	4.2	**8.5**
PCR	47.1	51	**48.1**	51.4	56.2	**52.4**	60.8	57	**60.6**	61.7	58.5	**61.5**	64.8	67.5	**65.4**
CRAR	11.7	16.4	**13.8**	11.3	16.5	**13.7**	12.2	16.3	**14.3**	13.5	16.6	**15.1**	13.1	16.7	**14.8**

Source: RBI

Stressed Assets

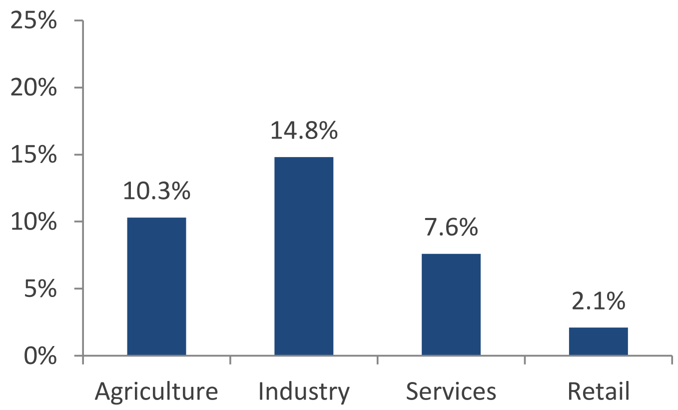
The gross nonperforming assets (GNPA) ratio fell to 8.5% from 9.3% and the overall provision coverage ratio (PCR) improved to 65.4% from 61.6% over this period. PCRs of both PSBs and PVBs increased March 2020.

Figure 3: Sector-wise GNPA Ratio



Source: RBI

Figure 4: Stressed assets ratio (FY20)



Source: RBI

Looking at sectoral GNPA, the agriculture sector GNPA stood at 10.1% on March 2020 as compared with 8.5% reported in March 2019. Industrial sector reported 14.1% GNPA Ratio in March 2020 as compared with 17.5% GNPA ratio in March 2019 and 22.8% of March 2018. Services and Retail sectors reported 7.2% and 2% GNPA in March 2020 as compared with 5.7% and 1.8% reported in March 2019, respectively.

Among major sub-sectors within industry, GNPA ratios of construction and gems and jewellery sectors increased in March 2020. On the other hand, the infrastructure sector (with a share of 36.2% in bank credit to the industrial sector), basic metals (11.3%) and electricity (17.5%) have shown a significant decline in GNPA ratios.

SCBs large borrowers accounted for 51.3% and 78.3% of the aggregate advances and GNPAs, respectively, in March 2020. Further, the top 100 borrowers accounted for 17.5% of gross advances, but only 12.6% of GNPAs of SCBs in March 2020.

Loan Moratorium and Bank Credit

Figure 5: Analysis of Loan Moratorium Availed as on April 30, 2020

Bank	Corporate		MSME		Individual		Others		Total	
	% of customer	% of total o/s	% of customer	% of total o/s	% of customer	% of total o/s	% of customer	% of total o/s	% of customer	% of total o/s
PSBs	28.8%	58.0%	73.9%	81.5%	80.3%	80.0%	48.8%	63.7%	66.6%	67.9%
PVBs	21.6%	19.6%	20.9%	42.5%	41.8%	33.6%	39.1%	40.9%	49.2%	31.1%
SCBs	24.7%	39.1%	43.1%	65.3%	52.1%	56.2%	45.7%	55.7%	55.1%	50.0%
NBFCs	39.7%	56.2%	60.7%	61.1%	32.5%	45.9%	37.3%	41.4%	29.0%	49.0%

Source: RBI

After the outbreak of COVID-19 pandemic in India, RBI announced several measures including a loan moratorium for all borrowers to mitigate the burden of debt servicing. Consequently, approximately 50% of the customers accounting for around half of outstanding bank loans opted for the moratorium. Further, a larger share of the MSMEs has opted for the moratorium, while PSBs accounted for the largest share of the moratorium by bank type.

Non-Banking Financial Services (NBFCs)

Over 9,600 NBFCs were registered with the RBI at end-March, 2020 of which 66 were deposit accepting (NBFCs-D) and 278 were systemically important non-deposit accepting NBFCs (NBFCs-ND-SI). Even as the combined balance sheet size of NBFCs is approximately one fifth when compared with the SCBs, NBFCs play a significant role in the in last mile credit delivery.

NBFCs continued to face asset quality stress in FY20. The gross NPA increased from 6.1% at March 2019 to 6.4% at March 2020, hover had witnessed a decline during FY20. However, the net NPA ratio, declined marginally from 3.3% in March 2019 to 3.2% as of March 2020. Furthermore, the CRAR dipped marginally to 19.6% in March 2020 versus with 20.1% in March 2019. The table below summarises the movement in these ratios.

- **Figure 6: Asset Quality and CRAR of NBFCs (in %)**

	GNPA Ratio	NNPA Ratio	CRAR
Mar-15	4.1	2.5	26.2
Mar-16	4.5	2.5	24.3
Mar-17	6.1	4.4	22.1
Mar-18	5.8	3.8	22.8
Mar-19	6.1	3.3	20.1
Sep-19	5.6	2.9	19.9
Dec-19	5.9	3.1	19.5
Mar-20	6.4	3.2	19.6

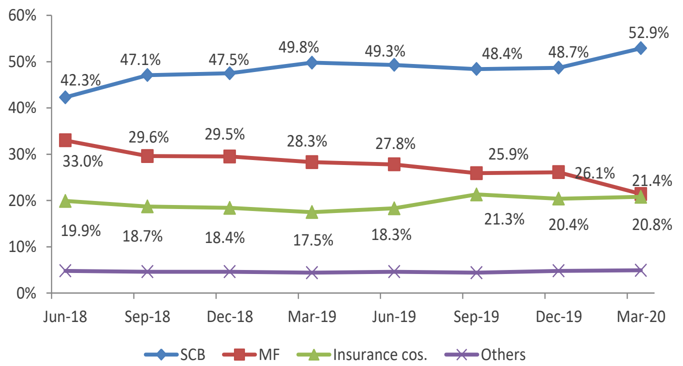
Source: RBI

Figure 7: Liability Structure of the NBFC Sector - December 2019

Particulars	Asset Size > Rs 5,000 cr		Asset size > Rs 500 cr but < Rs 5000 cr		Asset size < Rs 500 cr		Total	
	Rs cr	%	Rs cr	%	Rs cr	%	Rs cr	%
Number of NBFCs	102		220		9,289		9,611	
Outside liability	23,58,207		1,88,941		2,52,794		27,99,942	
Bank borrowing	5,78,193	24.5%	64,451	34.1%	1,03,914	41.1%	7,46,558	26.7%
Debenture	8,72,748	37.0%	34,661	18.3%	56,302	22.3%	9,63,711	34.4%
Inter Corp. Borrowing	91,846	3.9%	12,213	6.5%		0.0%	1,04,059	3.7%
CPs	95,116	4.0%	8,535	4.5%	13,603	5.4%	1,17,254	4.2%
Other Outside Liabilities	7,20,304	30.5%	69,082	36.6%	78,974	31.2%	8,68,360	31.0%
Total Liabilities	**29,81,471**		**3,61,395**		**3,77,868**		**37,20,734**	

Source: RBI

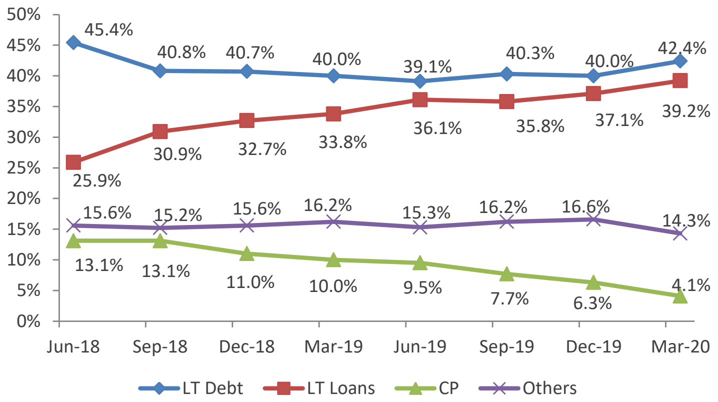
Figure 8: Share of lender groups



Source: RBI

NBFCs were the largest net borrowers of funds from the financial system. NBFCs owed 52.9% to SCBs followed by 21.4% to MFs and 20.8% to insurance companies. The share of SCBs which had increased in FY19 registered a moderate decline in H1FY20 however by the March 2020 end accounted for more than half of the funding source. A point to be noted is that with the rise of the bank funding, NBFCs have inherently lost a competitive pricing advantage to the banks. However, the share of MFs has been on a consistent declining trend for the last several quarters. Furthermore, if the funding mix is considered, the share of SCBs would be higher due to the significant loan asset sell down (direct assignment) as a funding source which is not included in the above computation (PSBs were significant acquirers of these assets).

Figure 9: Share of instruments



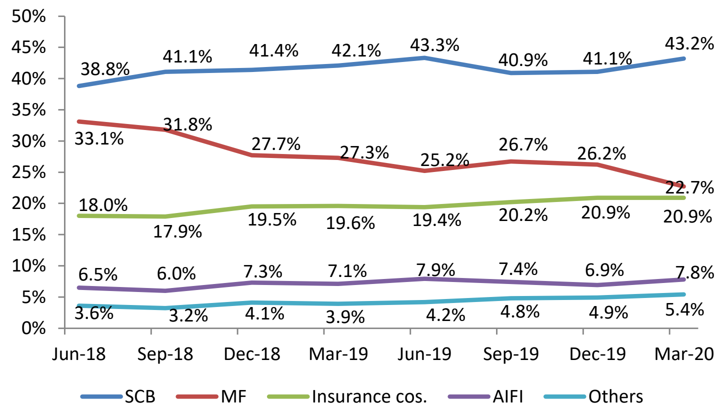
Source: RBI

The NBFC borrowing mix clearly highlights the increasing role of LT loans (provided by SCBs and AIFIs) and a declining share of CPs (primarily subscribed to by AMC-MFs and by SCBs)

LT debt is usually subscribed to by insurance companies and AMC-MFs.

Housing Finance Companies (HFCs)

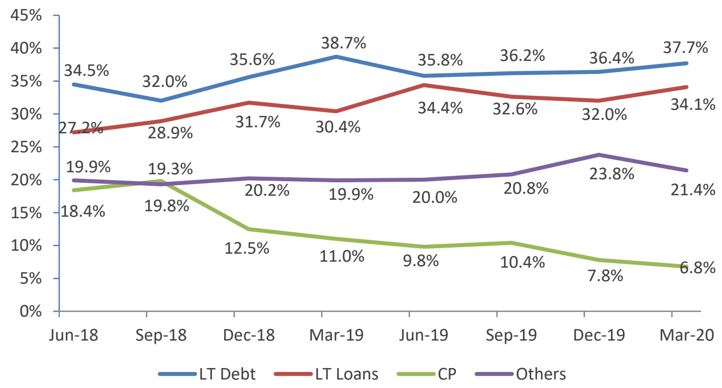
Figure 10: Share of lender groups



Source: RBI

HFCs were the second largest borrowers of funds from the financial system. HFCs have followed a borrowing pattern which is quite similar to that of the NBFCs, with AIFIs also accounting for a significant share. MFs as a funding source reduced significantly in December 2018; however, the same increased marginally in September 2019 and has declined for the next two quarters. In contrast, the relative share of SCBs showed an upward trend for the same period, but has dipped in September 2019, however the trend continued upwards for the next two quarters. Furthermore, certain HFCs resorted to sell-downs or securitisation of their retail assets in order to generate liquidity. Hence, the funding mix if these direct assignments are considered, the share of SCBs would be even higher as SCBs, especially PSBs, had acquired these assets.

Figure 11: Share of instruments



Source: RBI

The funding mix of the HFCs has been volatile for the last several quarters. Funding on CPs (subscribed primarily by MFs and followed by SCBs) continued to witness a sharp fall. This decrease has been offset by a significant rise in the share of LT loans (from banks and AIFIs) and LT debt. The borrowing mix has shifted from short term to a longer tenure.

Concluding remarks

Overall, growth in global GDP continues to remain uncertain, though financial markets have stabilised due to the multiple fiscal and monetary stimulus undertaken by various central banks and governments. As the interbank market is shrinking and financial entities have higher capital buffers, contagion risk through financial networks has moderated. However, the banking system would need to raise capital for catering to a post-COVID-19 economy by maintaining adequate buffers and dry powder. This has been evinced by several banks announcing capital raising plans.

According to the RBI's macro stress tests for credit risk, the GNPA ratio of SCBs may increase from 8.5% in March 2020 to 12.5% by March 2021 under the baseline scenario and if the macroeconomic environment worsens further, the ratio may escalate to 14.7% under very severe stress. Under the baseline scenario, PSBs' GNPA ratio of 11.3% in March 2020 may increase to 15.2% by March 2021, while PVBs' GNPA ratio may increase from 4.2% to 7.3%, over the same period. Further, SCBs capital to risk-weighted assets ratio (CRAR) could fall from 14.6% in March 2020 to 13.3% (11.8% in a very severe stress scenario) by March 2021.