Bank Asset Quality Improves as Gross NPAs Fall to Six-year Low

July 05, 2022 | BFSI Research

Synopsis

- The GNPA (gross non-performing assets) ratio hit a six-year low of 5.9% in FY22 but remained above the pre-asset quality review (pre-AQR) in FY22. The overall provision coverage ratio (PCR) improved to 70.9%. Restructuring of loans by entities hurt from the second wave of Covid-19 under the Resolution Framework (RF) 2.0 stood at 1.6% of total advances in December 2021 vs. the restructuring under RF 1.0, which was limited to 1% of total advances
- As per the stress tests conducted by RBI, the SCBs GNPA ratio could improve from 5.9% in March 2022 to 5.3% by March 2023 under the baseline scenario driven by higher bank credit growth and a declining trend in the stock of GNPAs. However, the GNPA ratio may rise under the medium/severe stress scenarios, the GNPA ratio may rise to 6.2%/ 8.3%, respectively.

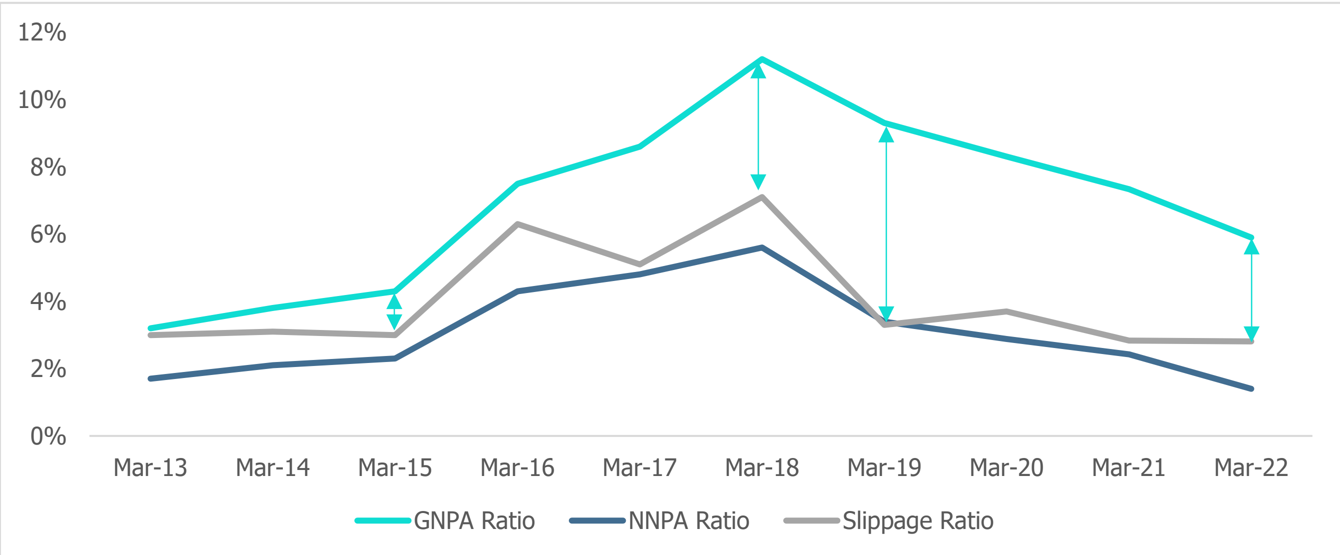
Bank Credit Growth on an Uptrend

As the Indian economy has navigated the pandemic-induced shocks, the bank credit growth by scheduled commercial banks (SCBs) improved post-August 2021 to reach 13.1% in early June 2022, a rate last recorded in March 2019. Apart from retail, the major driver of this growth has been the wholesale credit, which reported double-digit growth after witnessing a significant slowdown last year.

Asset Quality Looks Up

The RBI's Financial Stability Report released on June 30, 2022, presents a rather satisfactory picture of the Indian banking system and the GNPA ratio is one of the most important indicators to check the health of the banking system.

Figure 1: Movement in GNPA, NNPA and Slippage Ratios (in %)



Source: RBI

Post the asset quality review (AQR) in 2015-2016, the banks saw a spike in GNPAs from 3.8% in FY14 to 11.2% in FY18 (and NNPAs from 2.1% in FY14 to 5.6% in FY18) largely due to weakness in the wholesale advances which required banks to make a significant amount of provisioning and write-offs over the next four to five years. Accordingly, there was an overall risk aversion among the bankers as well as the credit demand from wholesale borrowers was low.

The asset quality deterioration in SCBs can be attributed to (1) regulatory challenges (2) shift in technology, (3) project delays and cost overruns; (4) absence of a strong bankruptcy regime, (5) wilful default/loan frauds/corruption in some cases, and (6) economic slowdown.

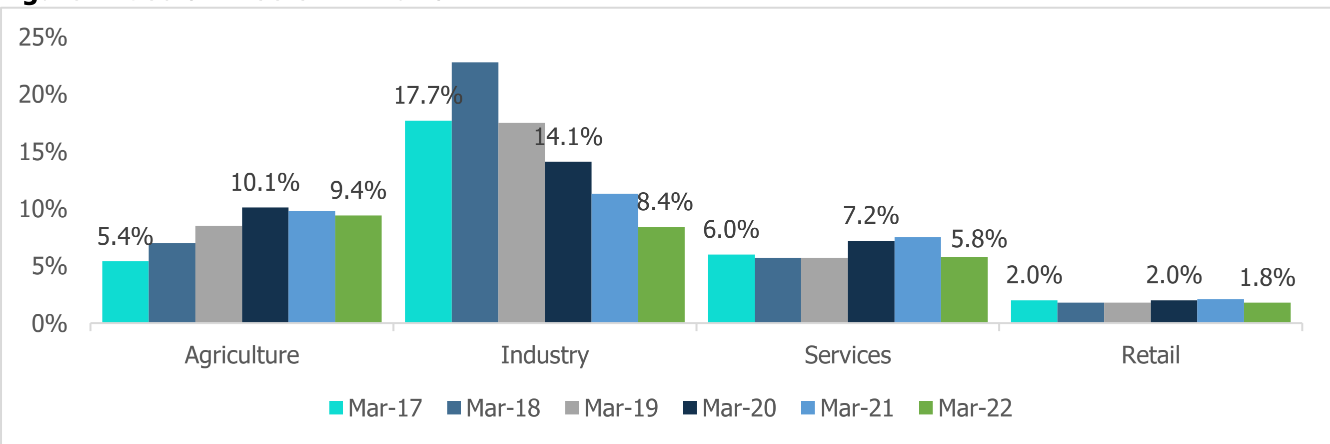
With the elevated provisions, the sharp rise in the GNPAs because of the AQR process led to a rise in the difference between GNPAs and NNPAs. This difference peaked in FY19 and has started to reduce given the write-offs and provisions.

Recovery from the sharp AQR-led deterioration of overall asset quality continued even during the pandemic period, led by increasing deleveraging and supported by regulatory intervention. These regulatory and government support schemes also helped borrowers to access liquidity and conserve cash flows. These schemes include (1) a moratorium on loan repayments for six months till August 30, 2020, (2) a covid-related restructuring scheme for large corporates, MSMEs, and personal loans (3) ECLGS to enable Banks and NBFCs to provide funding to MSMEs, (4) TLTROs, (5) Special refinance facilities to NABARD/SIDBI/NHB to address sectoral credit needs, and (6) Extended Partial Guarantee Scheme.

The GNPA ratio of SCBs had been on a downward trajectory since Mar-19. SCBs asset quality has seen some improvement (GNPA reduction) due to recoveries and higher write-offs by multiple banks, OTR schemes announced by RBI, etc. The PSB GNPA ratio continues to remain significantly higher than the private banks' NPA ratio.

In FY22, the GNPA ratio fell to 5.9%, a six-year low, however, continued to remain above the pre-asset quality review levels. The overall provision coverage ratio (PCR) improved to 70.9%. The PCRs of both PSBs and PVBs increased in March 2022. The slippage ratio and write-offs declined across bank groups in FY22 indicating lower accretion of fresh NPAs as well as the fact that older NPAs have already been written off.

Figure 2: Sector-wise GNPA Ratio



Source: RBI

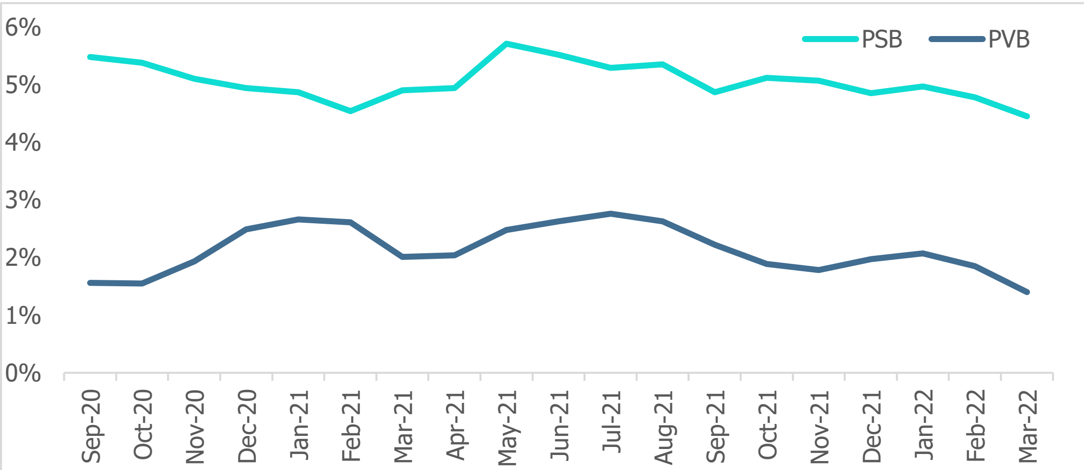
Looking at sectoral GNPA, the agriculture sector GNPA ratio stood at 9.4% in March 2022 as compared with 10.1% reported in March 2020 having increased from 5.4% in Mar-17. Agriculture GNPA generally rose due to droughts and elections - the anticipation of loan waivers).

The industrial sector reported an 8.4% GNPA ratio in March 2022 as compared with a 14.1% GNPA ratio in March 2020 and 22.8% in March 2018. Among major sub-sectors within industry, there was a broad-based improvement in the GNPA ratio, though it remained elevated for gems and jewellery and construction sub-sectors.

The services and retail sectors reported 5.8% and 1.8% GNPA in March 2022 as compared with 7.2% and 2.0% reported in March 2020, respectively. Retail NPAs can largely be attributed to the increased stress on unsecured loans. The asset quality of credit card receivables and education loans sub-sectors within the personal loans segment showed improvement.

The aggregate GNPA Ratio (PSBs and PVBs) in the MSME sector has moderated from 10.8% in March 2021 to 9.3% in March 2022 due to regulatory measures coupled with the continued flow of credit under ECLGS. However, compared to other segments in figure 8, they remain relatively high.

Figure 3: Delinquency Levels in Aggregate Consumer Credit

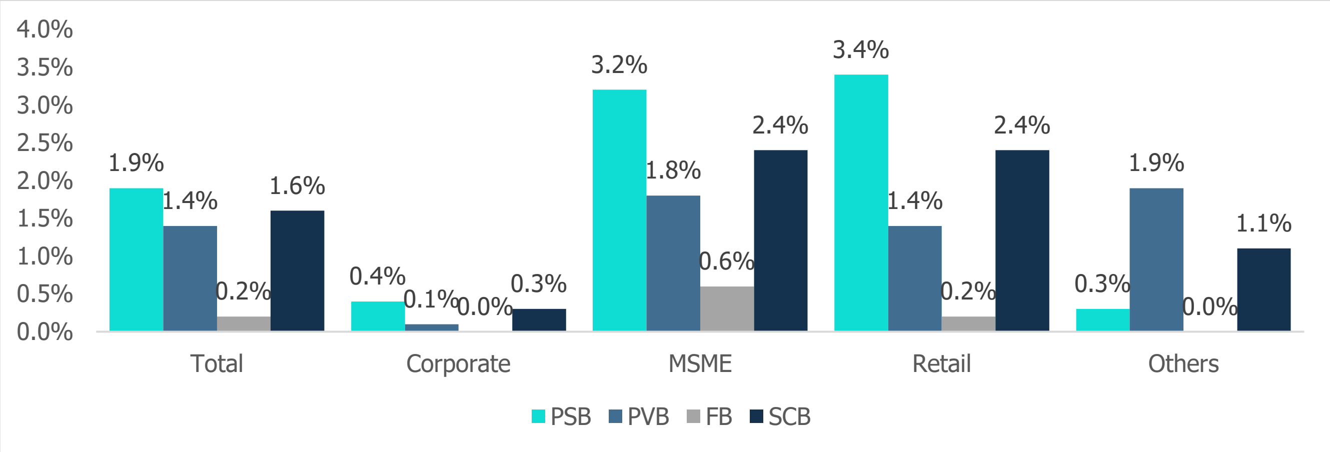


Source: RBI

Impairment in consumer credit, measured in terms of the proportion of the portfolio at 90 days past due or beyond, shows signs of stabilisation after the pandemic, but at a higher level for PSBs relative to PVBs.

Large borrowers have been witnessing a decline in their share of total credit which can be attributed to deleveraging and the rise of retail and diversification of borrowers. SCB large borrowers accounted for 47.7% and 62.3% of the aggregate advances and GNPAs, respectively, in March 2020. However, the top 100 borrowers accounted for 17.51% of gross advances, but only 6.9% of GNPAs of SCBs in March 2022.

Figure 4: Restructured Advances Under RF 2.0: Segment-wise Amount Outstanding, December 2021



Source: RBI

Within standard assets, the share of restructured standard advances (RSA) increased from 0.4% in March 2020 to 0.8% in March 2021, largely due to the one-time restructuring scheme for standard advances announced by RBI in August 2020. The restructured assets further increased to 1.8% at end of September 2021 due to Resolution Framework (RF) 2.0 for retail and MSMEs which did not entail an asset classification downgrade.

Restructuring of loans by entities impacted by the second wave of COVID-19 under the RF 2.0 stood at 1.6% of total advances in December 2021. Restructured assets constituted 2.4% each of the advances under MSME and retail sectors. PSBs had a relatively larger share of restructured loan assets in their books. The restructuring under RF 2.0 was 50 bps higher than the restructuring under RF 1.0 which was limited to 1% of total advances indicative of the stress exerted by the second wave of the pandemic.

India Still has a higher NPA Ratio compared to other Nations

Despite the continued decline, India's NPA ratio is one of the highest among the comparable countries. Non-performing loans eased in advanced economies due to continued deleveraging, and institutional and government intervention.

Figure 5: Country-wise - Bank Non-performing Loans to Gross Loans (%)

Country Name	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
Russian Federation	6.6	6.1	6.0	6.8	8.4	9.2	9.7	9.7	8.8	8.3
South Africa	4.7	4.0	3.6	3.2	3.1	2.9	2.8	3.7	3.9	5.2
France	4.3	4.3	4.5	4.2	4.0	3.7	3.1	2.7	2.5	2.7
Indonesia	2.0	1.7	1.6	2.0	2.3	2.8	2.4	2.2	2.3	2.6
China	1.0	1.0	1.0	1.2	1.7	1.7	1.7	1.8	1.9	1.8
Malaysia	2.7	2.0	1.8	1.6	1.6	1.6	1.5	1.5	1.5	1.6
United Kingdom	4.0	3.6	3.1	1.7	1.0	0.9	0.7	1.1	1.1	1.2
United States	3.8	3.3	2.5	1.9	1.5	1.3	1.1	0.9	0.9	1.1

Source: World Bank

Conclusion

Financial entities have generally emerged resiliently from the pandemic and are expanding their business as the economic recovery takes hold. After a modest credit growth in recent years, the outlook for bank credit offtake is positive due to the economic expansion tracking nominal GDP growth, rise in government & private capital expenditure, rising commodity prices, implementation of the PLI scheme, the extension of ECLGS for MSME and retail credit push. The broad asset quality parameters are expected to remain stable due to moderation in slippages, and healthy PCR resulting in lower credit costs.

As per the stress tests conducted by RBI, the SCB GNPA ratio could improve from 5.9% in March 2022 to 5.3% by March 2023 under the baseline scenario driven by higher expected bank credit growth and a declining trend in the stock of GNPAs. This decline may be higher if several large accounts are transferred to the NARCL. However, under the medium/ severe stress scenarios, the GNPA ratio may rise to 6.2%/ 8.3%, respectively.

On the other hand, the possibility of increased slippages arising from sectors that were relatively more exposed to the pandemic continues as support measures are unwound along with rising interest rates. The performance of restructured accounts continues to be monitorable during the current fiscal.

Contact

Sanjay Agarwal	Senior Director	sanjay.agarwal@careedge.in	+91-22-6754 3582 / +91-81080 07676
Saurabh Bhalerao	Associate Director – BFSI Research	saurabh.bhalerao@careedge.in	+91-22-6754 3519 / +91-90049 52514
Mradul Mishra	Media Relations	mradul.mishra@careedge.in	+91-22-6754 3596

CARE Ratings Limited
Corporate Office: 4th Floor, Godrej Coliseum, Somaiya Hospital Road, Off Eastern Express Highway, Sion (East), Mumbai - 400 022
Phone : +91 - 22 - 6754 3456 I CIN: L67190MH1993PLC071691

Connect :

Locations: Ahmedabad I Andheri-Mumbai I Bengaluru I Chennai I Coimbatore I Hyderabad I Kolkata I New Delhi I Pune

About:

CareEdge (earlier known as CARE Group) is a knowledge-based analytical group that aims to provide superior insights based on technology, data analytics capability and detailed research methods. CareEdge Ratings is one of the leading credit rating agencies in India. It has an impressive track record of rating companies for almost three decades and has played a pivotal role in developing the corporate debt market in India. CareEdge provides near real time research on all domestic and global economic developments. The wholly owned subsidiaries include CareEdge Advisory & Research arm focused on providing advisory and consultancy services and CareEdge Risk solutions a platform that provides risk management solutions