Credit Growth Expected to be at 14.5% in FY25

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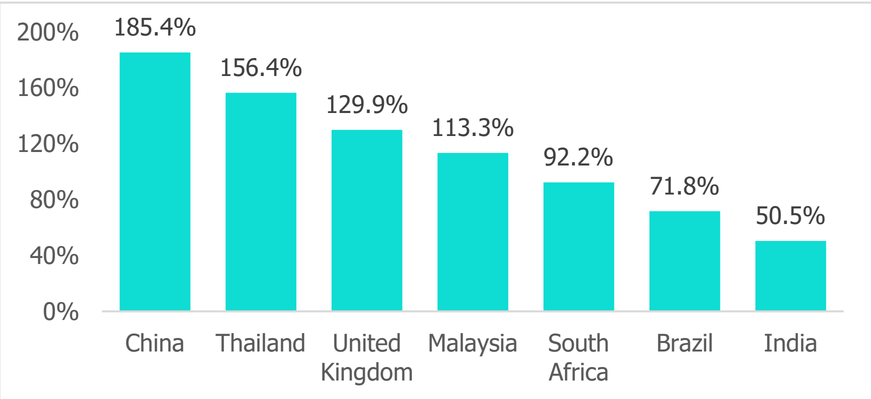
Synopsis

Bank credit growth maintained high growth and outpaced deposit growth significantly in FY24. The personal loans segment has remained the largest segment, along with NBFCs, while the industrial sector reported muted growth. The private sector banks (PVBs) have continued to outpace the public sector banks (PSBs). The medium-term prospects look promising with sustained personal loans along with the anticipated increase in capex spending especially by the private sector. Additionally, given that in FY24, credit offtake is anticipated to close with a growth of around 16% excluding the merger, it would be working off a higher base CareEdge estimates the credit growth to be in the range of 14%-14.5% at FY25 end. The effect of the HDFC merger would dissipate by the end of Q1FY25. However, elevated interest rates and global uncertainties could adversely impact credit growth.

Overall Credit Growth Has Remained Robust

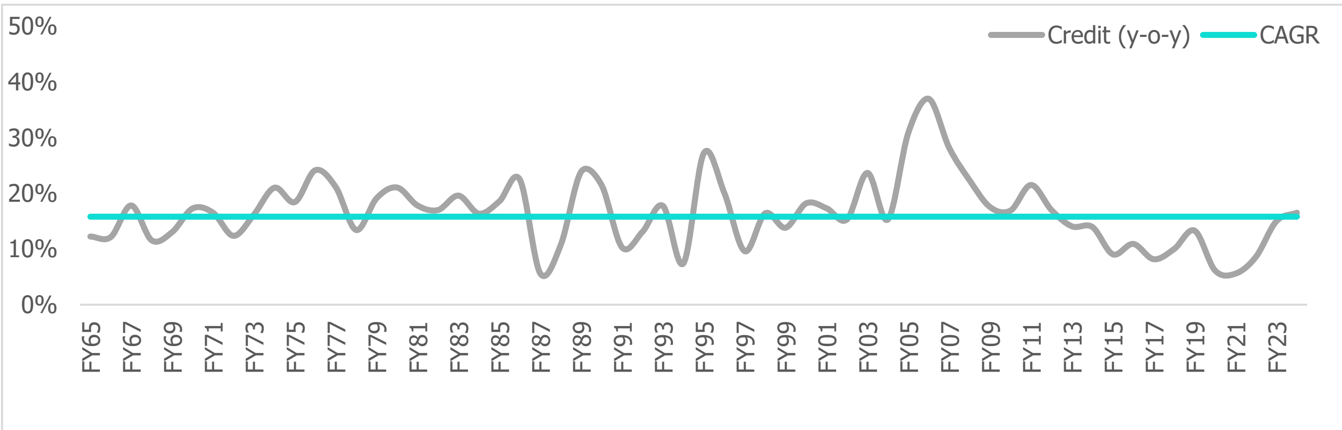
India has a relatively lower level of bank credit to GDP ratio when compared to other countries and to improve the same, access to credit and the cost of credit need to be addressed.

Figure 1: Domestic Credit to the Private Sector (% of GDP, 2022)



Source: World Bank, CMIE

Figure 2: Bank Credit Growth Remains Robust (y-o-y, %)



Source: RBI, CMIE, CareEdge Estimates; YTDFY24 exclude merger impact

Apart from personal loans (driven by improved digitalisation), the major driver of this growth has been the NBFC segment. The recent period has been marked by a structural shift in the performance of India's banking sector with the sector seeing a substantial reduction in the overhang of stressed assets. On a y-o-y basis, credit growth generally began picking up in H2FY22 and since then it has continued the momentum with the HDFC-HDFC Bank merger bumping up the headline credit growth number. Credit has continued to outpace deposit growth by a significant margin significantly. A part of the funding gap was met via Certificates of Deposits (CDs), reduction in surplus SLR investments as well as avenues like refinance from financial institutions like SIDBI, NABARD, NHB, etc.

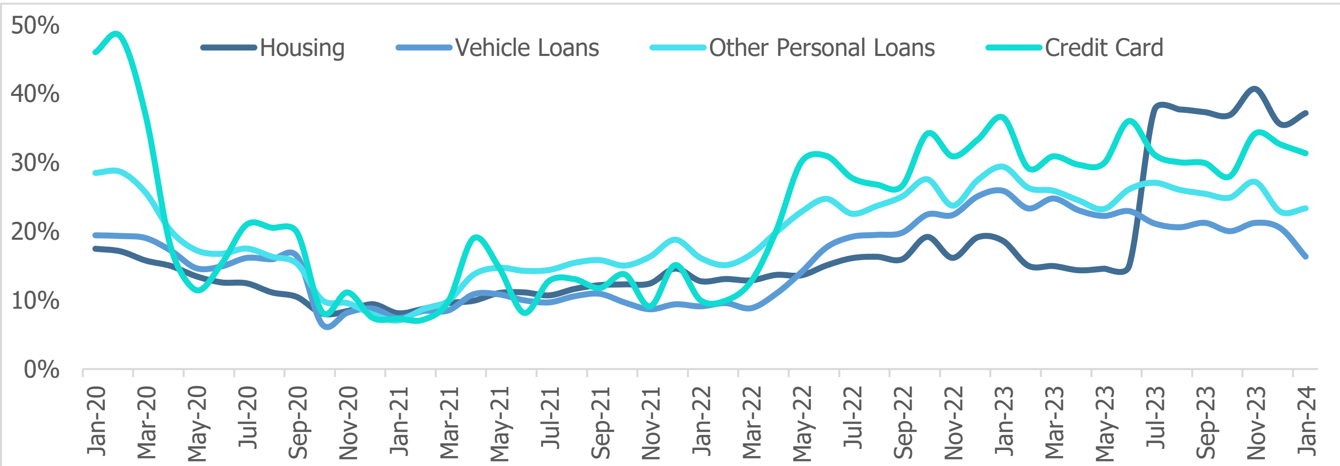
Figure 3: Movement in the Annual Growth Rates of Segments (%)

Seg.	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	FY22	FY23	10MFY24
Agri	13.7	7.9	12.9	15.0	15.3	12.4	3.8	7.9	8.3	**10.5**	9.9	15.5	22.9
Industry	**20.7**	**15.1**	12.8	5.6	2.7	-1.9	0.7	6.9	2.1	-0.5	7.5	5.8	11.1
Services	14.4	12.6	**16.1**	5.7	9.1	**16.9**	13.8	**17.8**	10.6	3.9	8.7	19.6	27.1
Personal	13.8	14.7	12.5	**15.5**	**19.4**	16.4	**17.8**	16.4	**22.8**	10.3	**12.6**	**20.7**	**31.8**
Overall	17.0	14.1	13.9	9.0	10.9	8.2	10.0	13.3	6.1	5.6	8.6	15.0	16.1*

Note: Negative in red, highest in the column in bold; * Excludes the merger impact; Source: RBI, CMIE

Personal loans and NBFCs have been the main growth drivers for the Indian banking sector, as corporate lending has been muted due to NPAs and deleveraging. The personal loan segment (largest segment with a 34.1% share) witnessed a robust growth of 31.8% y-o-y in January 2024 due to strong growth in unsecured loans, vehicle, and home loans. Credit growth in the personal loans space continues to be driven by significant digitalisation of the ecosystem with increased use of credit bureaus for faster decisions, data collation and validation and e-commerce transactions also leading to miniaturisation of credit. Within the personal loans segment, all major sub-segments witnessed robust demand during the month. This has resulted in the personal loans segment increasing its share and that is likely to continue to grow further given the focus on the segment.

Figure 4: Movement in the Select Segments within Personal Loans (%)



Source: RBI, CMIE

Housing loans (share of 50.1% within personal loans) grew by 37.2% y-o-y in January 2024 compared to 15.7% a year ago mainly due to the merger (reclassification of HDFCs' advances), sales of high-value residencies, strong launch pipeline of residential projects and incentives and schemes offered by developers.

Vehicle loans (share of 11.1% within personal loans) registered a lower growth of 16.3% y-o-y in January 2024 as compared to 25.4% in the year-ago period. The continued growth, albeit slower compared to previous periods, can be attributed to higher sales of passenger vehicles and two-wheelers. Passenger vehicles and commercial vehicles are expected to drive demand.

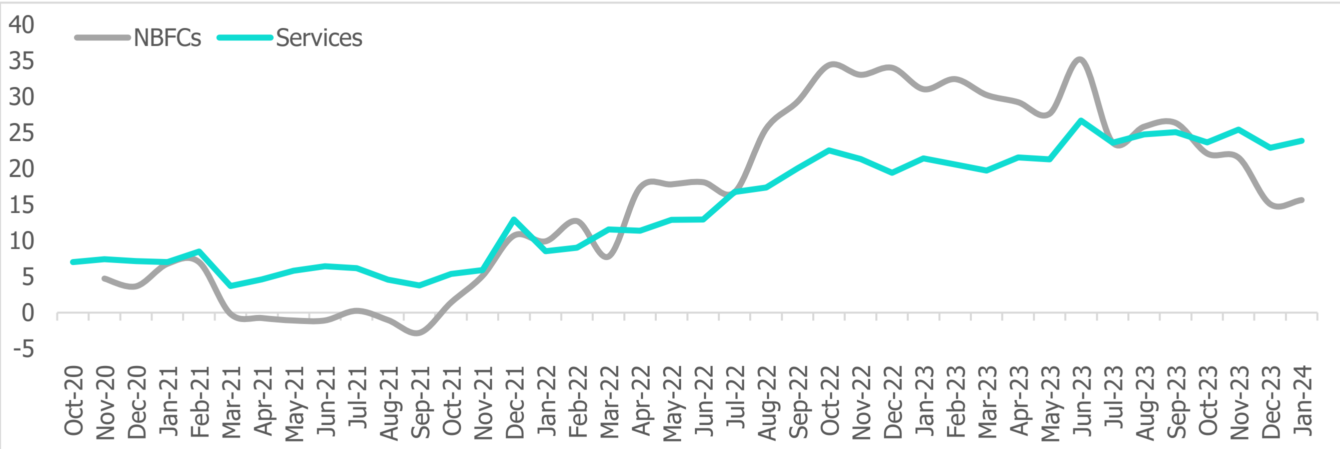
The other personal loans (share of 26.0% within personal loans) reached Rs 13.5 lakh crore and rose by 23.3% y-o-y due to the miniaturization of credit, digitalization of loans (faster loan turnaround and robust process), and preferences for premium consumer products. As corporate lending remained subdued, banks have focused on personal loans especially unsecured personal loans to drive growth. Another advantage has been that these loans typically carry relatively higher interest rates, thereby boosting margins. Meanwhile, this growth rate is slower than the average growth rate of the last twelve months. This deceleration can be attributed to RBI's action of increasing the risk weights on consumer loans.

Figure 5: Movement in the Share of Segments (%)

Seg.	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	FY22	FY23	10MFY24
Agri	12.7	12.1	12.0	12.8	13.5	14.0	13.4	12.9	12.6	13.2	13.3	13.3	13.1
Industry	45.2	45.8	45.5	44.3	41.7	37.8	35.1	33.4	30.9	29.2	28.6	26.2	23.9
Services	23.8	23.7	24.2	23.5	23.5	25.4	26.7	28.0	28.0	27.6	27.4	28.4	28.9
Personal	18.2	18.4	18.3	19.4	21.3	22.8	24.8	25.7	28.6	29.9	30.7	32.1	34.1

Source: RBI, CMIE

Figure 6: Movement in Services and NBFC (Growth, %)



Source: RBI

The services sector credit growth rose 28.9% y-o-y during January 2024 as compared to 21.4% for the same period of the last year due to growth in the major segments (NBFC and Trade) and the low base.

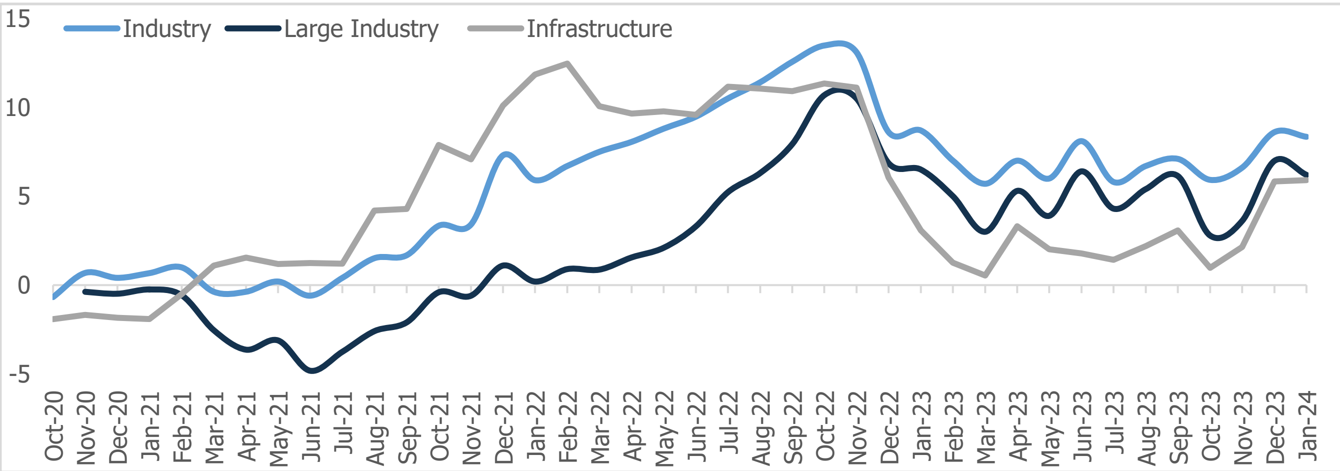
The credit exposure of banks to NBFCs stood at Rs 15.0 lakh crore in January 2024, indicating a 15.6% y-o-y growth which is nearly half of the growth rate reported in January 2023. However, the proportion of NBFC exposure in relation to aggregate credit has reduced from 9.7% in January 2023 to 9.4% in January 2024. In January 2024, the six-month average y-o-y expansion in bank advances to NBFCs reduced to around 21% levels compared to the approximately 28-30% average growth in the 12 months prior to the same. This could likely be attributed to the RBI's increasing risk weights and higher borrowings in the capital market. After the merger of HDFC Limited with

HDFC Bank, the quantum of outstanding exposure of banks to NBFCs reduced sequentially, albeit maintaining the y-o-y growth rate which has since moved past the pre-merger level.

Industry growth reduced to 8.3% y-o-y in January 2024 from 8.6% in December 2023 and 8.7% in January 2023. The moderation in growth was partially offset by the HDFC-HDFC Bank merger, if the merger impact had been excluded, growth would have been even slower at 7.8%.

The infrastructure (sub-segment, 35.0% share within the industry) witnessed a credit growth of 5.9% y-o-y in January 2024 vs. a rise of 3.1% over the year-ago period due to a drop in the ports, and airports, along with comparatively slow growth in power, and roads. Meanwhile, telecommunications, railways (excl. Indian Rail), and other infrastructure segments reported faster growth compared to the same period last year. The power segment (the largest segment of infrastructure, with a share of 50.0%) witnessed a growth of 3.2% in January 2024 vs. a rise of 4.3% in January 2023. Meanwhile, the credit offtake for roads stood at two-thirds of the rate last year. i.e. 6.0% y-o-y in January 2024 from 9.2% in January 2023. Over the past few years, while exposure of Banks to the power sector has remained largely range-bound, power-focused IFCs, supported by government schemes and improved financial position, have been consistently growing their loan book. The share of power-focused IFCs in exposure to the power sector vis-a-vis banks has gradually increased from 55% as of March 31, 2020, to 59%, as of March 31, 2023, and is expected to further increase to 63% by March 31, 2024.

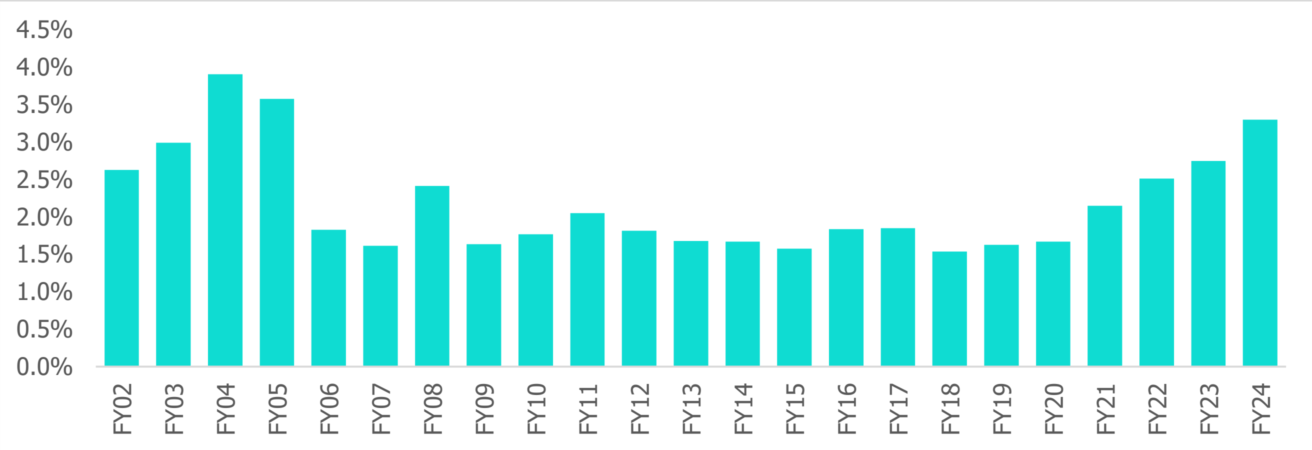
Figure 7: Movement in Industry (Growth, %)



Source: RBI

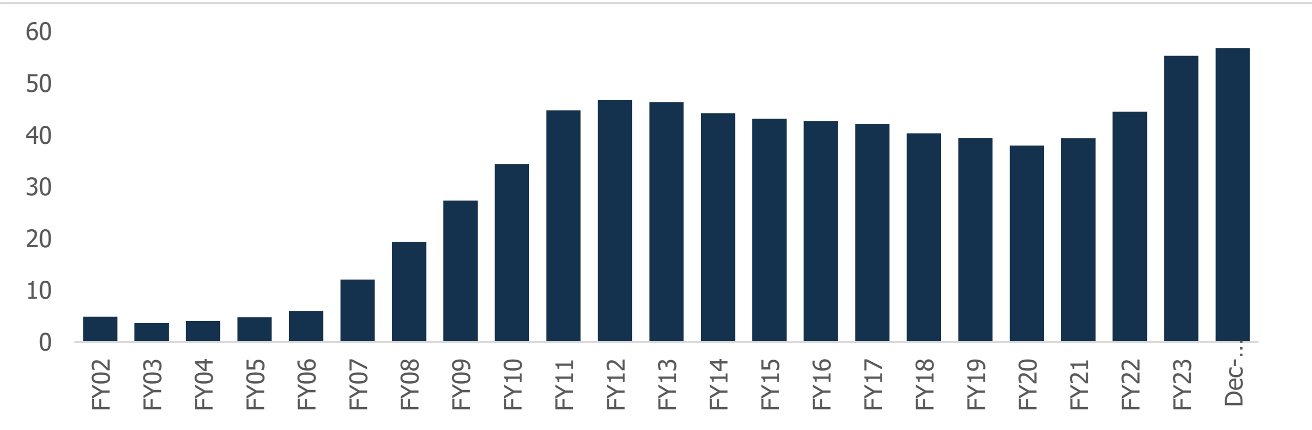
The retail and services segments have continued to keep the growth momentum going despite their growth rates moderating compared to the recent tear-away numbers. Given the planned capital expenditure by the government as well as the private sector, the industry segment is expected to increase its contribution to overall credit growth.

Figure 8: Govt Capex as % of GDP



As can be observed in Figure 8, the central government capex as a percentage of GDP has reached a near 20-year high and the government is expected to keep its capital expenditure spending elevated. Meanwhile, the private sector's investment projects under implementation have witnessed a rising trend (figure 9) with a significant proportion anticipated to be completed driving bank credit offtake.

Figure 9: Private Sector Invest. projects: Under Implementation (Rs lakh cr)

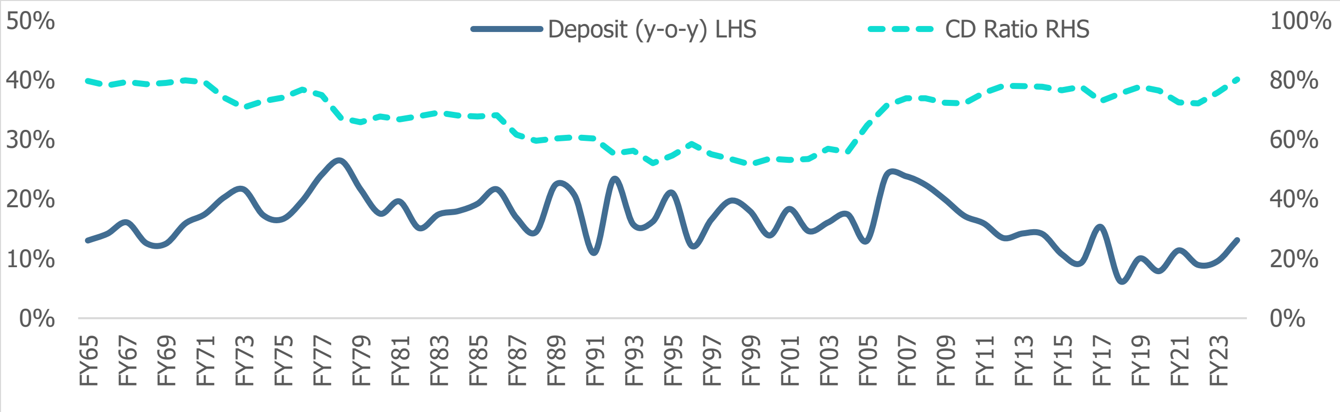


Source: CMIE

Growth in Deposit Franchise a Necessity to Sustain Credit Offtake

Deposits registered a growth of 13.1% y-o-y for February 24, 2024, with growth in time deposits outpacing growth in demand deposits. As a function of higher policy rates and supporting the credit growth, banks have raised rates on term deposits while holding on to savings rates, hence the deposit mix has changed with the CASA ratio declining for the banking system. The banking system's CASA franchise has gained more importance on account of the repricing of term deposits.

Figure 10: Credit to Deposit (CD Ratio Trend)

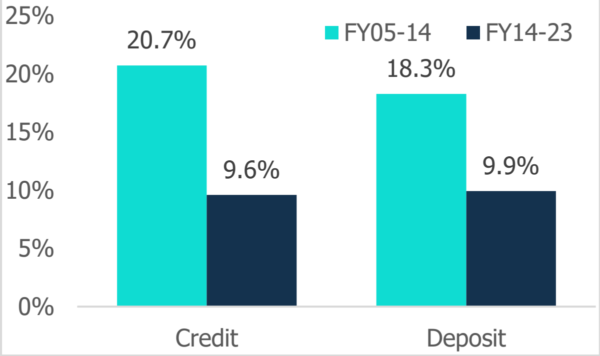


Source: RBI, CMIE, CareEdge

The Credit-to-deposit (CD) ratio has been generally trending upward since November 2021 and reached 80.2% by February 2024, due to continued faster growth in credit as compared to deposits. The CD Ratio continues to hover around the 80% mark.

Long-Term Growth: Credit and Deposit

Figure 11: Growth Over Two Decades (CAGR)



GDP Multiplier

1.38x	0.94x	1.22x	0.97x

Source: CMIE

In Figure 13, it can be observed that growth in the later decade (FY14-23) has been approximately half of the rate recorded in the earlier decade (FY05-14) for both credit as well as deposits. Credit offtake was significantly higher in the earlier period due to capacity building in several industries when banks underwrote several projects, while in the later decade, growth suffered as the AQR exercise was initiated in2015-2106 which led to banks turning risk-averse and slowed down lending, especially to the industry segment. Further, this has also resulted in the GDP multiplier (GDP at market prices) reducing by around 40 bps for credit and 25 bps for deposits.

Figure 12: Movement in CASA Share

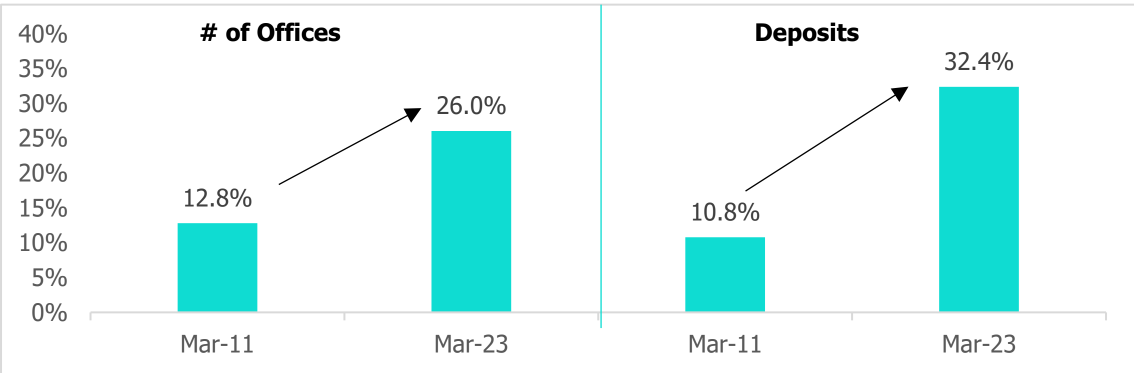
CASA (%)	FY18	FY19	FY20	FY21	FY22	FY23	Q3FY24
PSB	40.8%	41.7%	41.5%	43.2%	43.7%	42.1%	40.3%
PVB	44.4%	42.4%	42.3%	45.3%	47.0%	45.0%	39.9%
SCB	42.2%	42.2%	42.1%	44.1%	45.1%	43.1%	40.1%

Source: RBI

A higher CASA ratio means a higher portion of the deposits of the bank has come from current and savings deposits, which is generally a cheaper source of funds. Many banks don't pay interest on the current account deposits and money lying in the savings accounts attracts a limited interest rate. Hence, a higher CASA ratio means a better net interest margin, which means better profitability for the bank. The rising deposit rates have incentivised banking customers to increase their term deposits, thereby reducing the CASA share in the banking system. This reduction is also expected to increase the cost of deposits thereby pressuring NIMs.

Furthermore, private banks have stepped up their branch expansion and have increased their share of the branch network. This has had a knock-on effect on their deposit share which has also increased in tandem.

Figure 13: Private Banks Have Stepped Up Branch Expansion Leading to Increasing Share

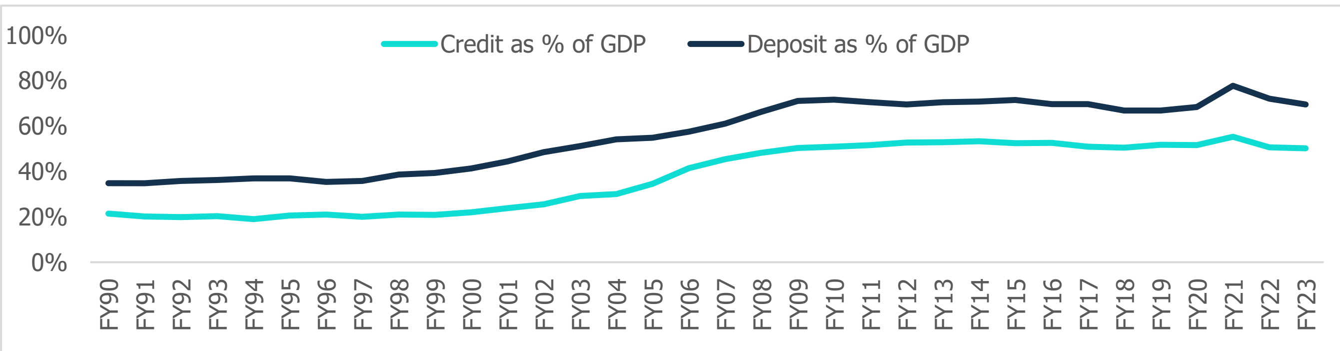


Source: RBI

CareEdge View

CareEdge Economics expects the GDP growth to reach 7.6% in FY24 and around 7% in FY25. The growth in the current financial year was supported by a strong growth in the investment demand led by public capex. While the agriculture growth is currently subdued, the manufacturing and services sectors are contributing to the overall growth momentum. Private consumption demand also remained muted in Q3FY24 despite some sequential improvement. The sustainability of investment growth in the medium-term hinges significantly on the imperative need to strengthen consumption growth. The escalation of global geopolitical tensions and slowing external demand can further add to the downside risks to the external sector. Going forward, the most critical aspect to watch out for will be a broad-based improvement in consumption growth. The other critical aspect would be a significant expansion in private investment. Overall robust GDP growth will be sustainable only when there is a meaningful improvement in consumption and private investment.

Figure 14: Credit and Deposit as a % of GDP



Source: RBI, CMIE

The outlook for bank credit offtake continued to be positive due to the economic expansion, rise in capital expenditure, growth in retail credit and the anticipated expansion in capex spending especially by the private sector. The growth is anticipated to be broad-based across the segments. The personal loan segment is expected to continue doing well compared with the industry and service segments. The medium-term prospects look promising with diminished corporate stress and a substantial buffer for provisions. This growth would be coming off a high base in FY24 which would impinge marginally on the growth rate. Further, the HDFC merger effect is anticipated to dissipate by the end of Q1FY25 and the headline numbers would show the removal of the base effect. Hence, based on GDP forecasts, sectoral credit growth expectations, and management expectations, CareEdge estimates the credit growth to be in the range of 14%-14.5% during FY25. However, elevated interest rates and global uncertainties could adversely impact credit growth. Further ebbing inflation could also reduce the working capital demand.

Deposit growth although improving has lagged credit growth for FY24 and consequently is anticipated to play a leading role in FY25 as banks take further efforts to shore up their liability franchise and ensure that lagging deposit growth does not constrain the credit offtake. Further with rate cuts anticipated in the later part of FY25, some amounts might flow back into the banking system thereby improving the CASA ratios to a certain extent. Hence, based on GDP forecasts and management expectations, CareEdge estimates the deposit growth to be in the range of 13%-13.5% during FY25.

Further, as the credit offtake moderates compared to the last year but remains higher compared to the increasing deposit growth, the credit-to-deposit ratio is also slated to continue to remain elevated at above 81% in FY25. PSBs continue to have a lower CD ratio compared to PVBs leaving some headroom for credit growth in the near term, hence PSBs could catch up to a certain extent with the PVBs in the near term. However, branch expansion to source retail deposits would be a key source of competitive strength.

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