# Banking Credit Offtake Set to Improve in FY26

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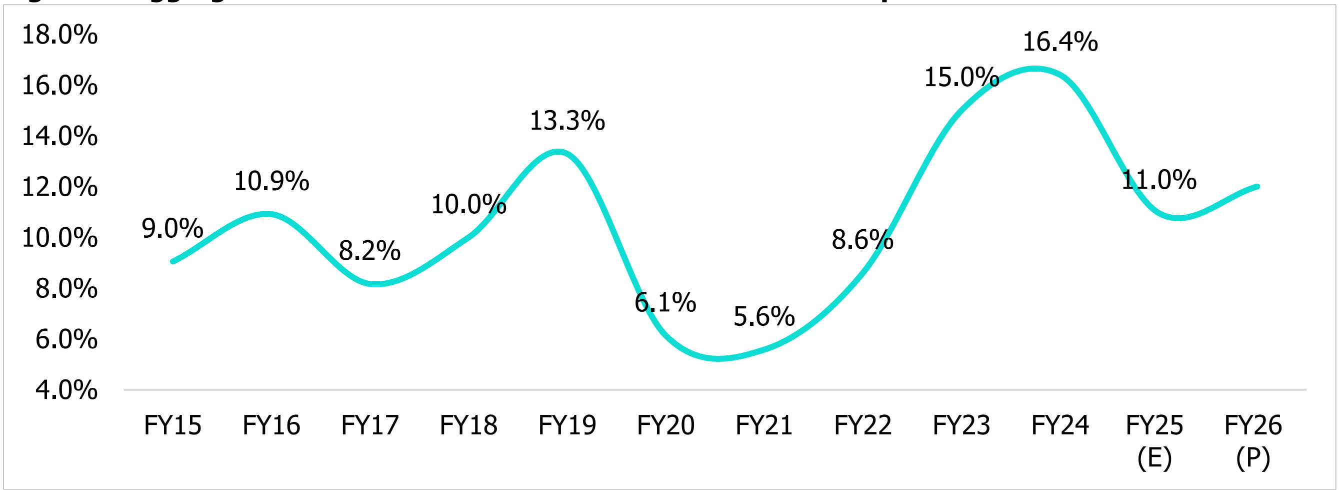
## Synopsis

Indian banks saw strong credit growth in FY24, achieving a credit growth of 16.4% (excluding the HDFC merger). However, in FY25, credit growth has slowed, primarily due to a deceleration in other personal loans and lending to non-banking financial companies (NBFCs). FY25 has closed with a growth of around 11%, with personal loans remaining the largest segment and industrial sector growth not showing significant improvement. CareEdge estimates credit growth to be **between 11.5% and 12.5% in FY26** as banks balance growth and margins while maintaining the credit-to-deposit (C/D) ratio.

## Banking Credit Offtake Set to Improve in FY26 due to Lower Base and Increased Demand

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, the growth in bank credit has slowed below the long-term growth rate and has converged towards deposit growth during FY25. The bank group-wise break-up shows a moderation in credit growth for both public sector banks (PSBs) and private sector banks (PVBs). Meanwhile, the elevated credit offtake numbers due to the HDFC-HDFC Bank merger have largely dissipated. Credit has continued to outpace deposit growth. A part of the funding gap was met through Certificates of Deposits (CDs), a reduction in surplus SLR investments, market borrowings, as well as avenues such as refinancing from financial institutions.

**Figure 1: Aggregate Bank Credit Offtake Slowed in FY25 set to improve in FY26**



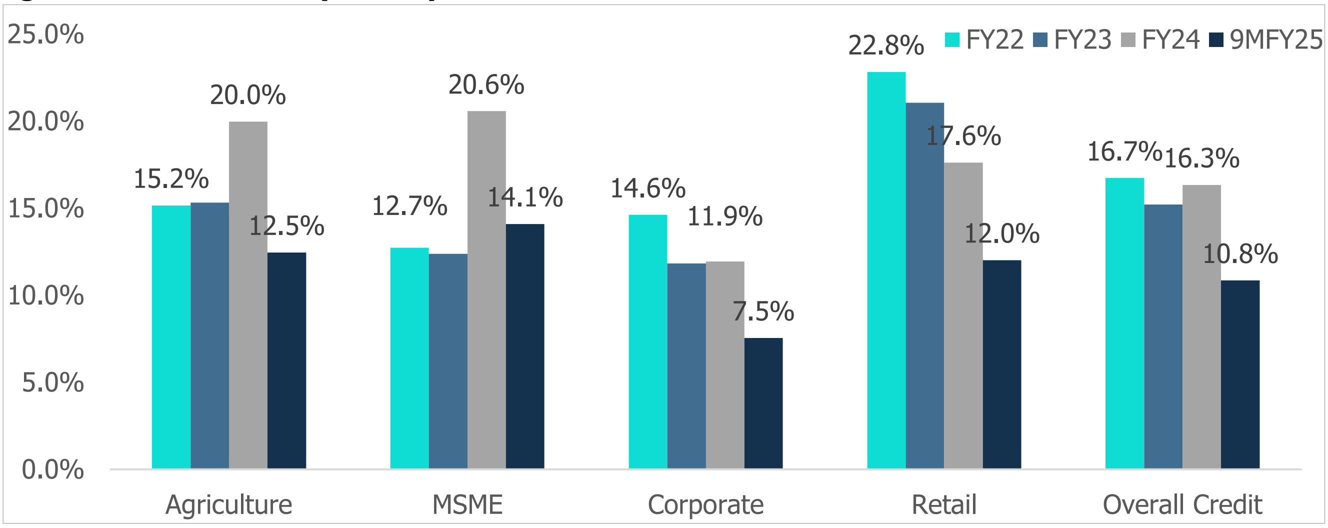

Source: RBI, CMIE, CareEdge Estimates

PSBs have gained market share by 28 bps year-on-year (y-o-y), reaching 53.5% in December 2024, slightly outpacing PVBs in credit growth during Q3 FY25, with a marginal difference of approximately 1-2%. This marginal outperformance can be understood as private banks have focused on managing their high C/D ratio.

### Credit Growth Has Decelerated Across Segments

Over the past decade, the overall composition of banking exposure has undergone significant changes. Credit growth is now led by the personal loan segment, largely retail, which holds the largest share in banking exposure. This segment, which constituted just about 18% in FY14, has increased to around 34% for FY24. In contrast, the industry segment, which accounted for 46% during the same period, has now decreased to 23%. This shift towards retail began after the Asset Quality Review days and has continued since then as banks have moved towards granularising their advances.

**Figure 2: Credit offtake (Growth)**




Source: RBI, CareEdge Calculations

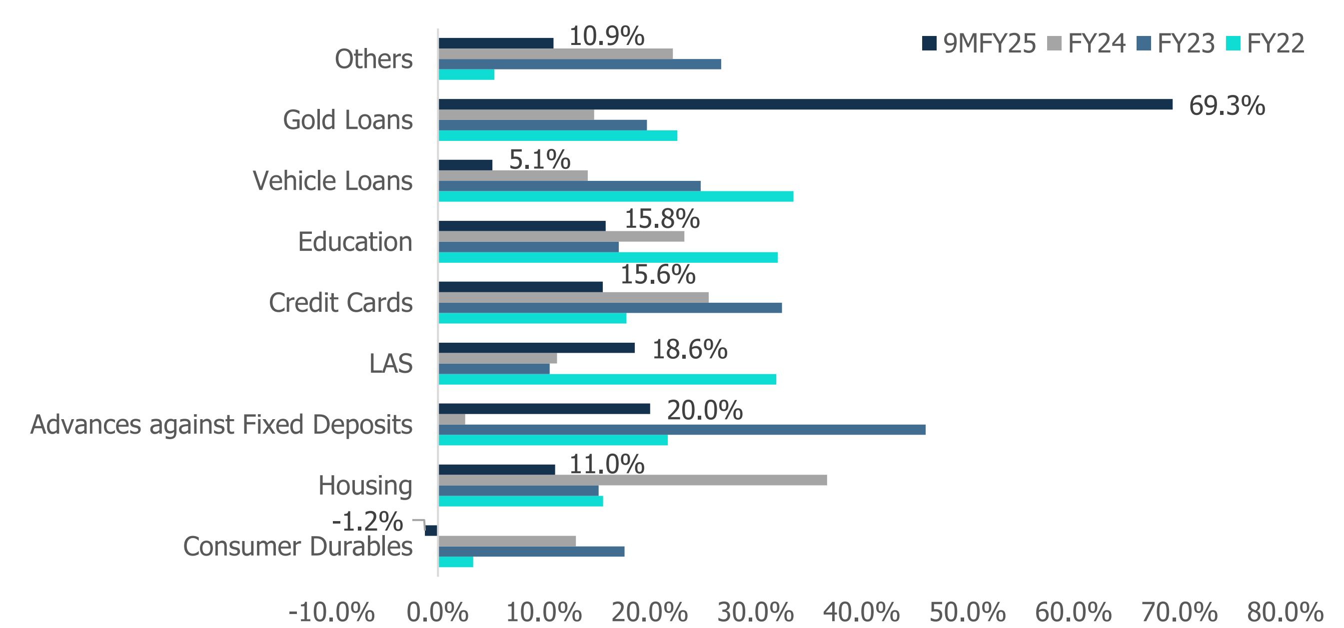
Industrial credit has been increasing from low levels but remains below the growth in loans to other major sectors, such as agriculture, services, and personal loan segments. Services and personal loans led the overall growth in credit. Within personal loans, credit card receivables continued to post robust growth over the last five years, despite the slowdown in unsecured lending in 9MFY25, due to concerns over asset quality and an increase in risk weights on unsecured personal loans.

Growth in personal loans has halved in the 9MFY25 from high levels, driven by both a high base and lower originations. However, its expansion continued to be broad-based, with housing loans as the largest segment.

Meanwhile, the credit growth extended by banks to NBFCs has declined significantly. By January 2025, banks' outstanding credit exposure to NBFCs was Rs 16.2 lakh crore, reflecting a year-on-year growth of 7.7%, a sharp drop from the prior year. For over a year, advances to NBFCs have lagged behind overall bank credit growth due to regulatory changes (an increase in risk-weight on exposure to NBFCs in November 2023), base effects, and rising capital market borrowings by NBFCs.

The recent rollback of risk weights suggests that the RBI is comfortable with NBFCs in these asset classes. Although most banks have enough equity to meet additional capital requirements, the increased risk weight has made them more cautious about lending to NBFCs. Consequently, the growth in advances to NBFCs is unlikely to return to pre-circular levels in the near term, given the competitive intensity and favourable rates available in the capital markets compared to bank financing for top-rated NBFCs.

**Figure 3: Growth in Personal Loans Segments**




Source: RBI, CareEdge Calculations

Over here, we have attempted to dissect the personal loan growth story to identify the subsectors driving this strong expansion. While mortgages remain the dominant type, unsecured personal loans have seen a growth in market share. The share of housing loans within the personal loan space has decreased from over 50% to around 48%, while the share of unsecured loans has increased from less than 30% to 36% during the same period, highlighting the strong growth in this segment. The growth has been driven by the miniaturisation of credit, the digitalisation of loans (faster loan turnaround and robust process), and preferences for premium consumer products.

However, with the RBI's action in November 2023, the growth in the unsecured loans space has decelerated significantly from 21.3% in FY24 to 10.0% (y-o-y) in 9MFY25. Meanwhile, advances to individuals against gold rose by 76.9% in January 2025, a significant increase from the 17.4% growth reported in the same period last year. Based on discussions with bankers and disclosures, most of this growth can be attributed to the shift or reclassification of gold loans from agri-gold loans to retail loans due to higher eligible limits under retail loans compared to purely agricultural loans with gold as security.

Furthermore, a rise in gold prices of over 20% has also contributed to the substantial growth in retail gold during the period. CareEdge Ratings expects retail loans to remain the primary focus of banks, with mortgages continuing to dominate due to sustained demand for housing, expected rate cuts, historically better asset quality, and higher ticket sizes. Other higher-yielding retail segments (largely unsecured) would see some moderation as banks would continue to remain cautious in lending in these products.

**Deferral in Regulatory Tightening to Aid Credit Offtake**

**Figure 4: List of Planned Regulations**

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| Unsecured PL Lending - with incremental risk weights |
| Increase in risk weight for NBFC exposure (**now rolled back)** |
| Higher provisioning for project finance (draft guidelines) - **Implementation Deferred** |
| Investments in Alternative Investment Funds (AIFs) |
| Transition to the 'Expected Credit Loss (ECL)' framework (draft guidelines) **Implementation derferred** |
| Master Direction on IT Governance, R, C & A Practices |
| Fair Practices Code for Lenders on charging of Interest |
| Key Facts Statement (KFS) for all retail and MSME term loan products |
| RBI Circular on Forms of Business and Prudential Regulation for Investments (draft) |
| Modifications to the LCR Computations (draft guidelines) **Implementation deferred** |

Source: RBI, CareEdge

In 2023 and 2024, the RBI took proactive steps to tighten regulations. To ensure that there is no sectoral concentration towards a particular asset class, directions were issued to increase risk weights and maintain equilibrium. This was also to ensure that the system didn't accumulate any risk due to the interconnectedness of the financial system.

Additionally, with low credit costs and strong asset quality numbers, this appears to be a favorable time to introduce measures such as the proposed guidelines on increasing provisioning for financing long-term projects, which will ensure that lenders have sufficient cushion to handle unexpected losses. This is also an ideal time to take conscious steps towards ensuring the transition of the Indian banking system to globally accepted accounting practices. Furthermore, to promote transparency and encourage ethical lending practices, specific guidelines have been issued. The RBI also issued guidelines to strengthen IT governance and risk management practices, ensuring that the financial system keeps pace with the evolving digital landscape.

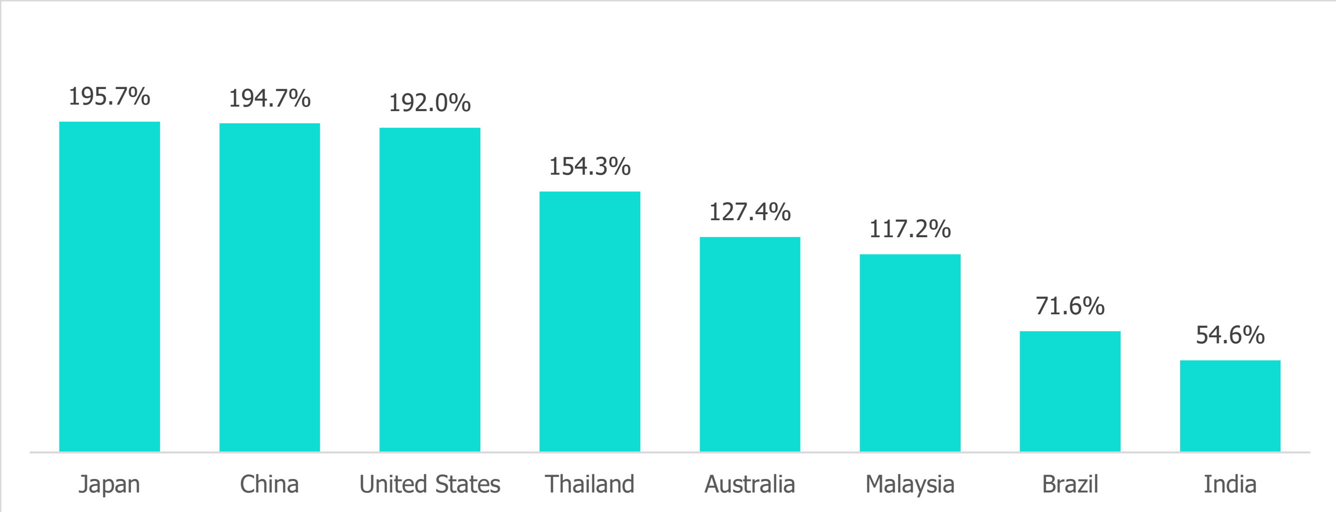
The RBI appears to have modified its stance slightly, as evidenced by the deferral of changes to the Liquidity Coverage Ratio (LCR) norms and provisions on project financing. It has also rolled back risk weights on microfinance loans and bank loans to NBFCs while undertaking measures to infuse liquidity and address the liquidity deficit.

**Outlook**

CareEdge Economics expects the economic growth momentum to be supported by domestic factors even though external headwinds remain high. Factors such as recovering rural demand, a lower tax burden, policy rate cuts, falling food inflation, and a recovery in public capital expenditure are expected to support an improvement in economic activity. Private consumption demand has shown improvement led by rural demand. Festivities during the 'Maha-Kumbh' celebrations in Q4 should also support consumption demand and sectors such as trade, hotels, and transport. Going ahead, we expect consumption demand to strengthen further as inflationary pressures ease and the benefits of a lower tax burden take effect in the next financial year. A sustained recovery in consumption will be crucial to driving a meaningful increase in corporate capital expenditures. The RBI has already reduced the policy repo rate by 25 bps in the February policy meeting and has implemented measures to support liquidity conditions. We expect additional rate cuts of 50-75 basis points in FY26, contingent on the growth-inflation dynamics. A lower borrowing rate should further support an uptick in private capex and demand conditions.

However, rising global policy uncertainty, especially on the trade front, as well as geopolitical tensions and weather events, remain key monitorable. The risk of reciprocal tariffs from the US and the global trade war could dampen business sentiments, even though the overall direct impact is likely to be limited (0.2-0.3% of GDP). However, there could be more severe indirect impact as global growth slows amidst heightened uncertainties.

**Figure 5: Domestic Credit to the Private Sector (% of GDP, 2023)**




Source: World Bank, CMIE

India has a relatively low bank credit-to-GDP ratio compared to other countries and, hence, continues to present significant headroom for growth on an aggregate basis. Credit offtake has moderated in FY25. This slowdown has been primarily driven by a decrease in unsecured retail lending and slower advances to NBFCs. Recently, RBI rolled back the risk weights, which is likely to result in more funds being made available to banks to on-lend to NBFCs and is expected to lead to lower borrowing costs for NBFCs.

This change, along with the deferral of the LCR framework, is expected to improve the bank credit growth in FY26 compared to FY25. The outlook for bank credit off-take remained positive due to economic expansion, a rise in capital expenditure, growth in retail credit, and the anticipated expansion in capital expenditure 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 low base in FY25, which would marginally impinge on the growth rate. **Hence, based on GDP forecasts, sectoral credit growth expectations, and management expectations, CareEdge Ratings estimates credit growth to be in the range of 11.5% to 12.5% during FY26.** However, elevated interest rates and global uncertainties could adversely impact credit growth. Further reducing inflation could also reduce the working capital demand.

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