Treasury Gains Drive Operating Profits in Q1FY26 Amid Margin Pressures

August 01, 2025 | BFSI Research

Synopsis

- Pre-provision operating profit (PPOP) for select Scheduled Commercial Banks (SCBs) grew by 12.3% year-on-year (y-o-y) to reach Rs 1.12 lakh crore in Q1FY26, driven by growth in other income along with a slower rise in operating expenses. Furthermore, sequentially, PPOP increased marginally by 1.2%.
    - Public Sector Banks (PSBs) reported 9.4% y-o-y PPOP growth, supported by gains on treasury and forex income, recovery from written-off accounts, and controlled opex.
    - Private Sector Banks (PVBs) recorded a 14.1% y-o-y growth, outpacing PSBs, driven by a 22.2% y-o-y increase in non-interest income. This was largely supported by a significant rise in treasury incomes for PVBs, driven by the softening of bond yields following rate cuts.
- The cost-to-income ratio of SCBs improved, decreasing by 80 bps y-o-y to 46.0% in Q1FY26 from 46.8% over a year ago. Banks were able to partially offset NIM compression through higher earnings from non-interest income, along with slower y-o-y growth in operating expenses.

PPOP Rises q-o-q Marginally

Figure 1: PPOP Witnesses a Rise as Other Income Improves for SCBs (Rs Lakh Crore)

Group	Q1FY26	y-o-y (%)	q-o-q (%)
PVBs	0.71	14.1	4.9
PSBs	0.41	9.4	-4.6
SCBs	**1.12**	**12.3**	**1.2**

Source: Ace Equity, Bank Filings, CareEdge Calculations; Note: Includes 22 SCBs (11 PVBs and 11 PSBs)

Note: The Pre-Provision Operating Profit (PPOP) analysis for the quarter reflects a broad-based performance across Select commercial banks. However, the aggregate growth figures have been considered after adjusting for one-off gains reported by a large private sector bank due to the partial stake sale of its subsidiary.

- PPOP of SCBs grew significantly by 12.3% y-o-y to reach Rs 1.12 lakh crore in Q1FY26. PSBs grew at 9.4% y-o-y, slower than PVBs, which grew at 14.1% y-o-y. PSBs growth was supported primarily by improved treasury performance due to falling bond yields with rate cuts, leading to rising bond prices which enabled banks to generate MTM gains. Meanwhile, PVBs reported a stronger growth than PSBs, driven by credit growth, a higher share of repo-linked loans, and rising fee-based income.
- Sequentially, the PPOP of SCBs grew marginally by 1.2% supported by MTM gains from softening bond yields and growth in fee income. This was offset by subdued loan growth in select segments and rising deposit costs, which impacted NIMs

Figure 2: Cost-to-Income Ratio Improves

	FY24			FY25				FY26	Y-o-Y	Q-o-Q
Group	**1Q**	**2Q**	**3Q**	**1Q**	**2Q**	**3Q**	**4Q**	**1Q**	**(bps)**	**(bps)**
PVBs	46.6	46.2	46.5	45.9	45.5	45.5	45.4	44.4	150	100
PSBs	44.8	47.4	49.3	48.4	46.2	47.9	48.7	48.4	0	30
SCBs	**45.9**	**46.7**	**47.6**	**46.8**	**45.8**	**46.4**	**46.7**	**46.0**	**80**	**70**

Source: Ace Equity, Bank Filings, CareEdge Calculations; Note: Includes 22 SCBs (11 PVBs and 11 PSBs)

- The cost-to-income ratio of SCBs improved, decreasing significantly by 80 bps y-o-y reaching 46.0% in Q1FY26 from 46.8% in Q1FY25. This improvement was primarily driven by robust growth in non-interest income, which outpaced the 7.8% rise in operating expenses (compared to 14.0% growth a year ago).
- PSBs remained flat on a y-o-y basis, reaching 48.4% in Q1FY26. Meanwhile, PVBs experienced a notable improvement in their cost-to-income ratio, improving to 44.4% in Q1FY26 from 45.9% in Q1FY25.
  - Additionally, total operating expenses for PVBs grew by 6.3% on a y-o-y basis in Q1FY26, with this rise largely driven by a 7.4% increase in employee expenses due to the annual appraisal cycle. This is a significantly slower pace compared to the 15% increase in total operating expenses in the same period last year.
  - Improvement in SCBs was further supported by a significant 26.6% rise in non-interest income, up from 13.0% in the same period last year, contributing to the overall reduction in the cost-to-income ratio.

Income (Rs. Lakh, Cr.)

Figure 3: Interest Income

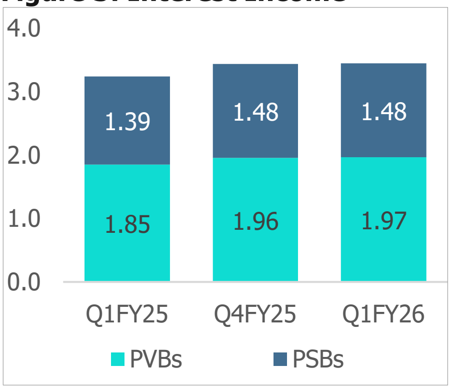


Figure 4: Non-Interest Income

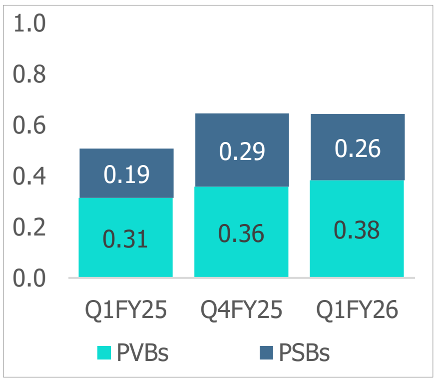
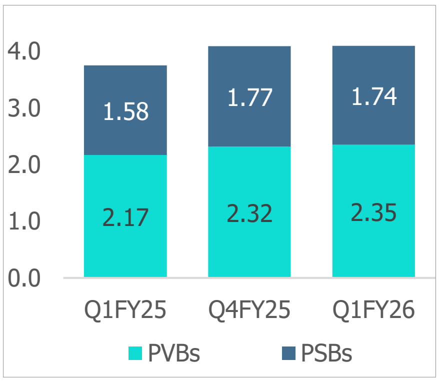


Figure 5: Total Income



Source: Ace Equity, Bank Filings, CareEdge Calculations; Note: Includes 22 SCBs (11 PVBs and 11 PSBs)

- SCBs total income grew by 9.2% y-o-y to Rs 4.09 lakh crore in Q1FY26, lower than the previous year's growth of 21.0%. This slower growth is attributed to the high base effect, lower yields on advances due to interest rate cuts, and a marginal reduction in the cost of funds.
  - Interest income of SCBs saw modest growth of 6.5% y-o-y, while other income recorded a strong expansion, supported by improved treasury performance and higher fee-based incomes.
- PSBs' total income grew by 10.2% y-o-y in Q1FY26. Sequentially, total income for PSBs declined marginally by 1.6%, primarily due to a shift in portfolio towards lower-yielding segments, which resulted in reduced interest income and margin compression compared to the previous quarter.

- Interest income for PSBs improved by 6.9% y-o-y alongside credit growth of 12.0% y-o-y, while Non-interest income benefited from favourable treasury gains and recoveries from written-off accounts.

- PVBs' total income grew by 8.5% y-o-y, outpacing PSBs in Q1FY26, driven by a 6.2% rise in interest income, based on a 9.1% rise in advances.

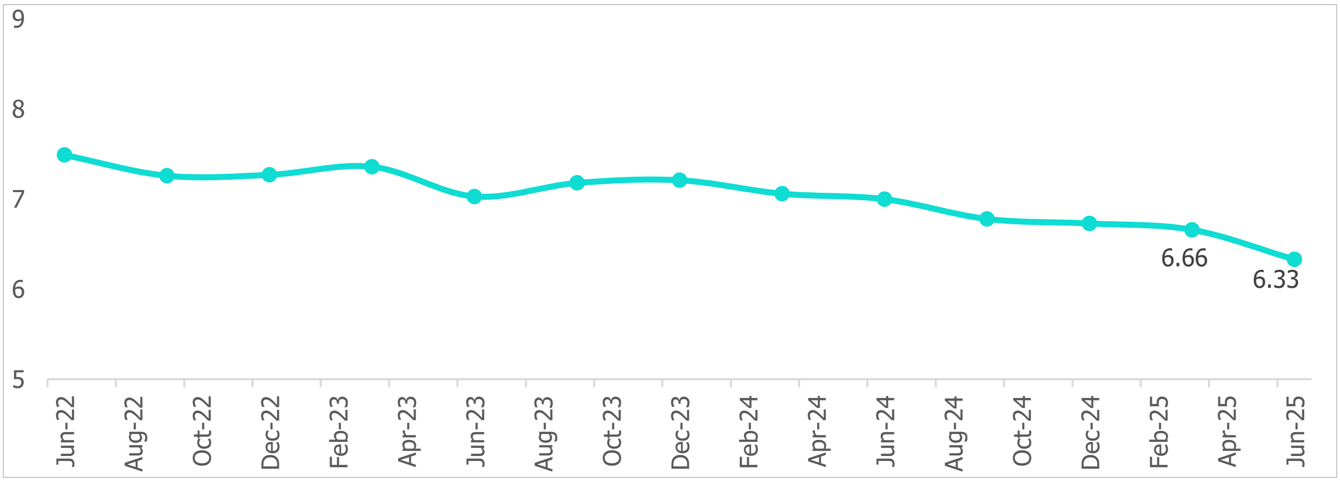
Figure 6: NIM Movement (%)

Group	NIM (Q1FY26) (%)	Y-o-Y (bps)	Q-o-Q (bps)
PVBs	3.60	-18	-11
PSBs	2.60	-26	-14
SCBs	**3.14**	**-22**	**-12**

Source: Ace Equity, Bank Filings, CareEdge Calculations; Note: Includes 22 SCBs (11 PVBs and 11 PSBs)

- NIM declined by 22 bps y-o-y in Q1FY26. PVBs and PSBs declined by 18 bps and 26 bps y-o-y, respectively, due to subdued credit growth primarily in the corporate and unsecured segments. Further, intensifying competition in the home loan market, driven by PSBs offering lower interest rates through faster transmission of EBLR-linked loans compared to PVBs, has further pressured lending margins, contributing to overall margin compression. Additionally, a quicker reduction in lending rates compared to deposit rates has weighed on banks' NIMs.

Figure 7: Yield on 10-year Residual Maturity of Government of India (%)



Source: CMIE; Note: Includes the Monthly weighted average 10-year residual maturity period.

- The yield on 10-year Government of India bonds, as of June 2025, reduced by 33 bps q-o-q and stood at 6.33% compared to 6.66%. This decline in bond yields in the current quarter due to rate cuts has driven up bond prices, resulting in higher treasury income.

Figure 8: Treasury Income as a % of Total assets (annualised)

Treasury Income as a % of Total Assets	Q1FY25	Q4FY25	Q1FY26
PVBs	0.16	0.13	0.41
PSBs	0.15	0.28	0.38
SCBs	**0.16**	**0.20**	**0.40**

Source: Ace Equity, Bank Filings, CareEdge Calculations; Note: Includes 22 SCBs (11 PVBs and 11 PSBs

- The treasury income of select SCBs, as a percentage of total assets, witnessed an increase of 20 bps, from 0.20% in Q4FY25 to 0.40% in Q1FY26. This sequential increase was primarily driven by MTM gains on government securities, particularly by Large PSBs, supported by softening bond yields.
- PSBs witnessed notable MTM gains during the quarter, benefiting from their relatively higher exposure to long-duration government securities amid easing bond yields. While SLR investments remained flat on a sequential basis, Non-SLR investments declined by 2%, leading to a 3% drop in total investment levels. However, the overall portfolio composition reflects a shift toward instruments yielding higher market-linked returns.
- Notably, HFT (Held for Trading) investments surged by 34% q-o-q, while AFS (Available for Sale) rose by 8%, indicating greater positioning in segments that benefit from MTM gains. Additionally, FVTPL (Fair Value Through Profit and Loss) increased by 6%. In contrast, HTM (Held to Maturity) holdings remained unchanged, suggesting that banks chose not to lock in funds into fixed-return securities during this rate cut cycle.

Operating Expenses (Rs. Lakh Cr.)

Figure 9: Employee Expenses

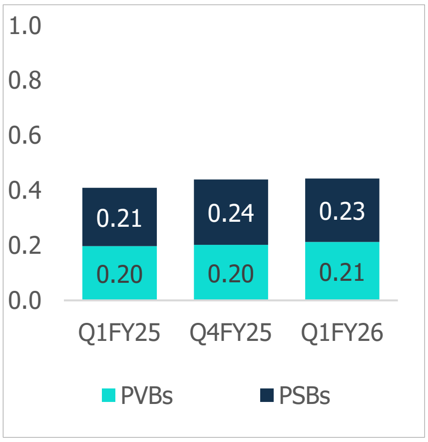


Figure 10: Other Op. Expenses

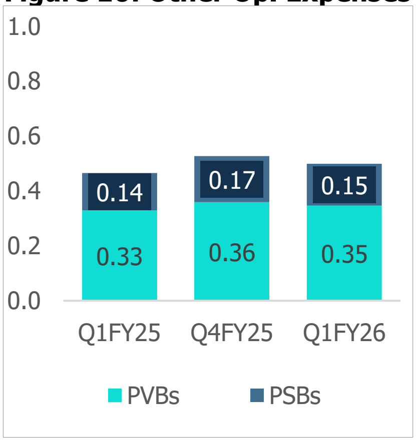
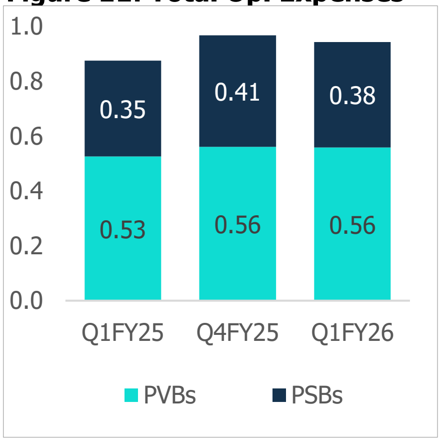


Figure 11: Total Op. Expenses



Source: Ace Equity, Bank Filings, CareEdge Calculations; Note: Includes 22 SCBs (11 PVBs and 11 PSBs)

- Operating expenses for SCBs rose by 7.8% y-o-y to Rs 0.94 lakh crore in Q1FY26, driven by an 8.3% rise in employee costs primarily due to the annual appraisal cycle for banks. Other operating expenses grew by 7.3% y-o-y, supported by investing in digital transformation, branch network expansion, and brand building. For PVBs, technology now consumes 8–11% of opex, largely reflective of recurring digital infrastructure and cybersecurity costs. PSBs are also scaling IT programs, though at slightly lower ratios, while expanding physical touchpoints to support broader financial inclusion. Additionally, the purchase of Priority Sector Lending Certificates (PSLCs) by a few banks has contributed to the increase in operating costs. Meanwhile, the growth in employee expenses slowed from 14.0% in Q1FY25 to 8.3% in Q1FY26, primarily due to reduced hiring activity and improved attrition rates by major commercial banks.
  - Employee expenses for PSBs increased by 9.1% y-o-y to Rs 0.23 lakh crore in Q1FY26, as compared to 12.0% growth seen in Q1FY25. While PVBs saw a 7.4% rise, this was down from 16% in Q1FY25.
  - Other expenses of SCBs are up by 7.3% in the quarter, standing at Rs 0.50 lakh crores, wherein PSBs grew at 11.3% and PVBs were up 5.6% y-o-y.

Figure 12: Yield on Advances (%)

Q1FY26	CBI	UCO	IDBI	RBL	Yes Bank
Yield on Advances	8.5	8.6	9.1	12.5	9.9
q-o-q (bps)	-16	-16	-71	-167	-30
y-o-y (bps)	4	-30	-83	-47	-20

Source: Data as per banks' presentations

Figure 13: Cost of Funds (%)

Q1FY26	CBI	UCO	IDBI	RBL	Yes Bank
Cost of Funds	4.9	4.7	4.9	6.5	6.5
q-o-q (bps)	17	6	-17	7	20
y-o-y (bps)	3	5	-11	4	10

Source: Data as per banks' presentations

Conclusion

In Q1FY26, banks continued to witness pressure on NIMs amid subdued business growth. NIMs are likely to remain subdued until the share of higher-yielding loans increases, or deposit costs are adjusted downward later in the year. Banks' profitability was supported by strong treasury gains, which helped cushion the impact of narrowing margins following the RBI's rate cuts. Although some banks reported lower net profits due to asset quality challenges, treasury income served as a vital offset. In the second half of FY26, improved liquidity conditions are expected to boost lending activity. However, due to the cumulative impact of rate cuts, banks' NIMs are expected to contract by 20– 25 bps over FY26. However, as bond yields are likely to stabilise in the upcoming quarters, the potential for additional treasury gains could taper off. As treasury support fades, a sharper focus on core earnings and asset quality will be critical to maintain profitability in the coming quarters.

Annexure

Note: Analysis based on 22 scheduled commercial banks (11 PSBs and 11 PVBs). Prior period numbers are not comparable to earlier reports due to the reclassification of select banks.

PSBs	Bank of Baroda	Canara Bank	Indian Bank	Jammu & Kashmir Bank	Punjab & Sind Bank	Bank Of Maharashtra	Central Bank of India
	Indian Overseas Bank	IDBI Bank	UCO Bank	Union Bank of India			
PVBs	HDFC Bank	ICICI Bank	Axis Bank	IDFC First Bank	Yes Bank	RBL Bank	Bandhan Bank
	Dhanlaxmi Bank	South Indian Bank	Kotak Mahindra Bank	Karur Vysya Bank			

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