

RBI Proposes Revised Risk-Weight Norms to Boost Credit Growth

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Synopsis

- The proposed changes in the Draft Reserve Bank of India (Scheduled Commercial Banks - Capital Charge for Credit Risk – Standardised Approach) Directions, 2025, are expected to help the minimum regulatory capital requirements for banks.
- Selecting high-quality segments could benefit from improved risk alignment across asset classes. Meanwhile, banks at the aggregate level already hold capital adequacy ratios that are significantly above regulatory requirements. These proposed regulations would likely have a limited immediate impact on the banking sector.

Overview

On October 07, 2025, RBI published the Draft Reserve Bank of India (Scheduled Commercial Banks - Capital Charge for Credit Risk – Standardised Approach) Directions, 2025. These draft guidelines aim to enhance the sensitivity of the banking system to risk and bring it into alignment with the revised Basel III standards. Starting April 1, 2027, the updated framework offers more detailed and consistent calculations of risk-weighted assets (RWA). This improvement involves refining sector-specific risk weights and tying them to borrower credit ratings, project development stages, and loan-to-value (LTV) ratios, thereby providing a more accurate assessment of credit risk across different assets classes.

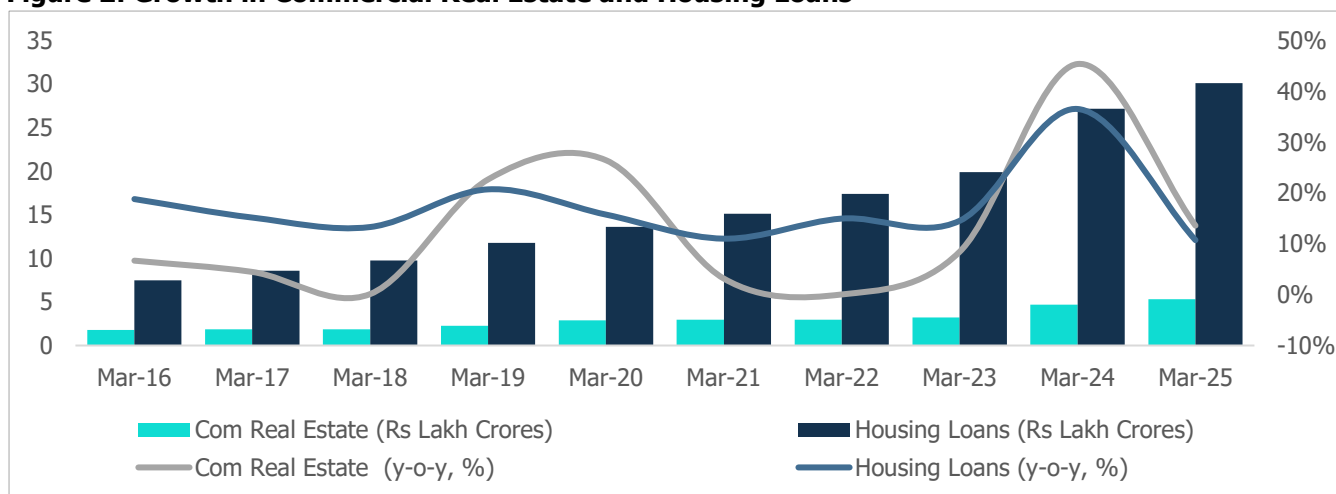
Real Estate

Figure 1: Comparison of Existing vs. Proposed Risk Weights

Real Estate exposure - LTV (%)			Existing	Proposed	Change	
CRE-RH (Residential Housing Project)			75%	100%	Increased by 25%	
Other CRE (ADC / Commercial)			100%	150%	Increased by 25%	
Housing Loans to individuals						
First and Second home				Third home		
LTV (%)	Existing	Proposed	Change	Existing	Proposed	Change
=<50%	35%	20%	Reduced by 15%	100%	30%	Reduced by 70%
>50-60%	35%	25%	Reduced by 10%	100%	35%	Reduced by 65%
> 60-80%	35%	30%	Reduced by 5%	100%	45%	Reduced by 55%
> 80-90%	50%	40%	Reduced by 10%	100%	60%	Reduced by 40%

Source: RBI, CareEdge

The proposed norms establish an LTV-based risk-weight framework for housing loans, reducing it to 20-40% for individual borrowers, given the low gross non-performing assets (GNPA) ratio of 1.0% as of March 2025. The framework also assigns a higher weight to third loans for individuals, reflecting their increased leverage. Meanwhile, risk weights for residential and commercial real estate have been increased to 100% and 150%, respectively. By prioritising capital allocation to retail housing, the policy aims to meet the rising demand for affordable homeownership. At the same time, it introduces safeguards to restrict credit flow to highly leveraged real estate developers, helping to mitigate systemic risks and ensure financial stability.

Figure 2: Growth in Commercial Real Estate and Housing Loans

Source: RBI, CareEdge

Between FY16 and FY25, outstanding loans in the Commercial Real Estate and Housing segments have shown robust growth, significantly surpassing the overall banking credit growth. Commercial real estate grew at a compound annual growth rate (CAGR) of 13.0%, while housing loans experienced an even stronger CAGR of 16.8% during this period. This increase has led to the share of Commercial Real Estate and Housing segments rising from 2.4% and 10.3% in FY16 to 2.9% and 16.5% in FY25. This trend highlights the importance of real estate-related lending in the banking sector portfolio.

The rise in commercial real estate lending can be attributed to increased demand for office space, driven by expanding service sectors, urbanisation, and growing real estate investment trusts (REITs). In the housing sector, growth has occurred rapidly and organically, benefiting from the merger between HDFC Bank and HDFC Ltd. It has also maintained strong asset quality, with the GNPA ratio for housing loans remaining consistently low at around 1.0%. This low GNPA level further indicates that housing loans continue to be one of the safest segments of retail lending.

Corporates and NBFCs

Figure 3: Comparison of Existing vs. Proposed Risk Weights

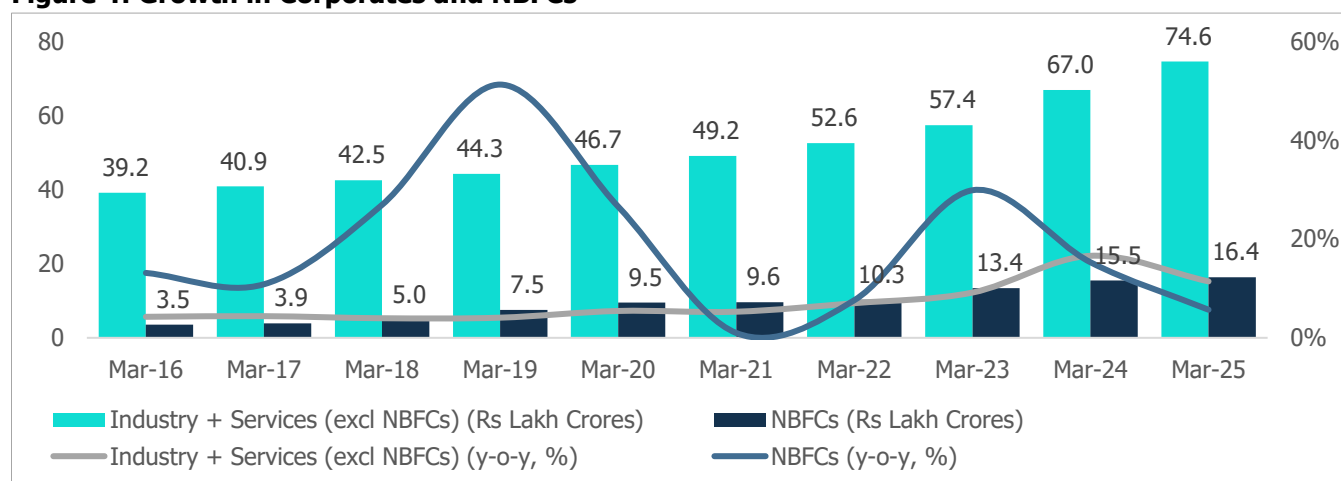
Corporates and NBFCs (Rating)	Existing	Proposed	Change
AA	30%	20%	Marginally eased with AA merged with AAA
A	50%	50%	No change
BBB	100%	75%	Reduced by 25%
BB	150%	100%	Reduced by 50%
Below BB	150%	150%	No change
Unrated	100%	100%	No change; however, a 150% threshold for greater than Rs 200 crore exposure

Source: RBI, CareEdge

The proposed norms lower risk weights for AA (merged with AAA), BBB and BB-rated corporates to 20%, 75%, and 100%, respectively, from 30%, 100%, and 150% earlier, while maintaining a higher charge for large unrated exposures (over Rs 200 crore), incentivising them to get rated. If we observe CareEdge Ratings, 1-Year average default rates (for FY21-25) for AAA and AA categories are the same at 0%, while 1-Year average default rates (for

FY21-25) for BBB and BB were 0.3% and 2.2%, respectively. Meanwhile, 1-Year weighted-average default rates – non-structured instruments (for FY11-15)- for the AAA, AA, BBB, and BB categories were 0.00%, 0.00%, 1.13%, and 3.97%, respectively. The rating-sensitive adjustments are designed to improve capital efficiency for well-rated corporates and large non-banking financial companies (NBFCs), aligning capital requirements more closely with credit quality.

Figure 4: Growth in Corporates and NBFCs



Source: RBI, CareEdge

The growth of Industry and Services, excluding NBFCs, at 7.4% over FY16-FY25 has been lower than the overall bank credit growth, indicating corporates' deleveraging. Meanwhile, bank lending to NBFCs has increased substantially, with a CAGR of 18.6% during the same period. As a result, the share of Industry and Services growth excluding NBFCs and NBFCs has shifted from 54.1% and 4.9% in FY16 to 40.9% and 9.0% in FY25. However, the pace of bank credit to NBFCs has slowed considerably. By March 2025, banks' outstanding credit to NBFCs was ₹16.4 lakh crore, up 5.7% year-on-year, a sharp slowdown from the previous year. For over a year, advances to NBFCs have trailed overall bank credit growth due to regulatory changes, base effects, and high overseas and capital market activities borrowings.

MSME Exposure

Figure 5: Comparison of Existing vs. Proposed Risk Weights

MSME exposure	Existing	Proposed	Change
Rated MSMEs	Per corporate	Per corporate	Per the changes in the corporate mentioned above
Retail-qualifying MSMEs	75%	75%	No Change
Unrated MSMEs (non-retail)	100%	85%	Reduced by 15%; lower than unrated large corporates

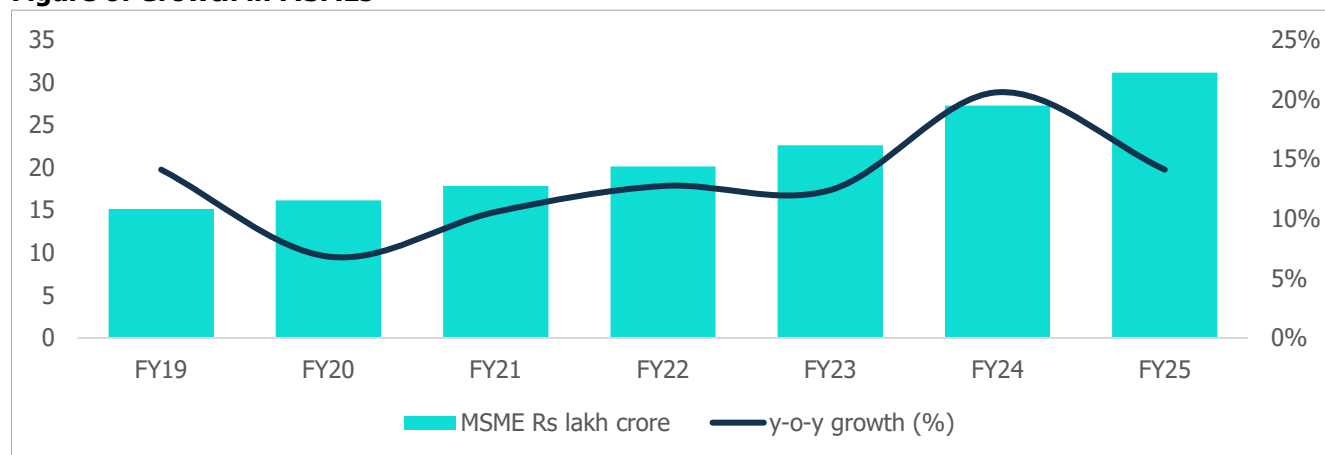
Source: RBI, CareEdge

In a significant move to enhance credit flow to small businesses, risk weights for unrated non-retail¹ MSME exposures have been reduced from 100% to 85%. Rated MSMEs have also benefited from a calibrated reduction

¹ If the MSME is part of a group and if the reported annual sales for the consolidated group of which the MSME is a part, is greater than ₹500 crore for the most recent financial year then it shall attract the risk weight which is applicable on corporate exposures

in risk weights, ranging from 10% to 50% based on their credit ratings. This adjustment provides capital relief, incentivising fresh lending to MSMEs. According to the RBI’s Financial Stability Report June 2025, ~₹6.28 lakh crore was guaranteed under two flagship schemes: the Credit Guarantee Fund for Micro Units (CGFMU) and the Emergency Credit Line Guarantee Scheme (ECLGS); and the GNPA ratio for SCBs was contained at 10.8% and 5.6%, respectively. Aggregate levels of GNPA and SMA-02 for the banking system to MSMEs have been on a downtrend, standing at 3.6% and 0.8%, respectively, as of March 2025.

Figure 6: Growth in MSMEs



Source: RBI, CareEdge

As per RBI’s Financial Stability Report (June 2025), share of credit to the MSME sector within total non-food bank credit has continued to grow steadily, even amid a broader deceleration in overall bank credit growth. Notably, credit expansion in the MSME segment outpaced that of other sectors in FY25. This has resulted in the MSME share reaching 17.0% in FY25. However, within the MSME category, micro enterprises—which accounted for 49.0% of total MSME credit—experienced slower incremental growth than small and medium enterprises.

Specialised Lending

Figure 7: Comparison of Existing vs. Proposed Risk Weights

Specialised Lending (Project/ Object/ Commodity Finance)	Existing	Proposed	Change
Project Finance (High Quality Operational)	100%	80%	Reduced for high-quality projects that meet post-COD and covenant conditions

Source: RBI, CareEdge

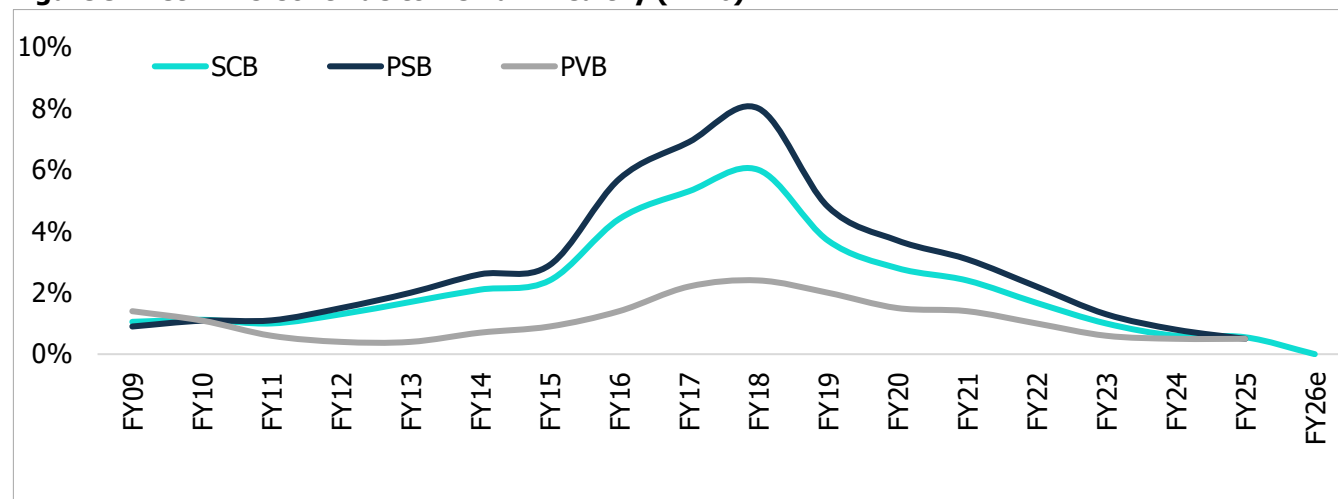
To strengthen the quality and timeliness of infrastructure development, risk weights for post-commissioning project finance exposures have been revised to 80% from 100% for unrated projects (for rated projects, risk weights in Figure 3 would apply), depending on the project’s operational performance. This approach creates a clear incentive for developers to complete projects on schedule and maintain stable cash flows. By linking capital requirements to operational quality, the proposal encourages better project execution and risk management. This proposal would be beneficial to sponsors with moderate credit quality, as higher-quality sponsors would achieve a better rating.

Figure 8: Comparison of Existing vs. Proposed Risk Weights

Others	Existing	Proposed	Change
Personal Loans	125%	125%	No Change
Credit cards (transactor)	125%	100%	Reduced by 25% accepting a lower credit risk for transactors who clear dues in full in the previous 12 months

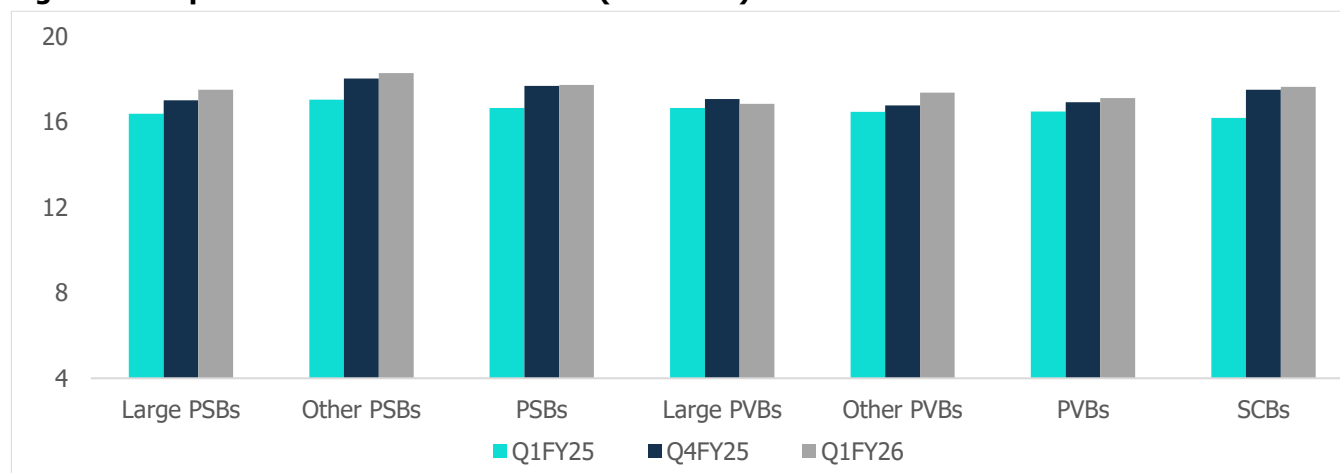
Source: RBI, CareEdge

Amid the increase in unsecured retail credit, RBI continues to assign a 125% risk weight to unsecured personal loans and credit card revolvers. This conservative approach aims to protect financial stability in the face of rising consumer leverage. However, a tailored approach is applied to credit card transactors—borrowers who pay their balances in full—who will enjoy a lower risk weight. This differentiation promotes responsible credit use and helps banks retain sufficient capital buffers against higher risks exposures.

CareEdge Ratings' View**Figure 9: Net NPAs Continue to Remain Healthy (in %)**

Source: RBI, CareEdge Analysis

- The overall stress level of SCBs has reduced on a y-o-y basis with a combined decrease in NPAs and the restructured book in Q1FY26. The NNPA of SCBs decreased by 8.7% y-o-y to Rs 0.92 lakh crores as of Q1FY26, compared with Rs 1.01 lakh crores a year ago. NNPA of PSBs improved by 20.0% y-o-y to Rs 0.55 lakh crore as of Q1FY26, while NNPA of PVBs increased by 15.7% y-o-y to Rs 0.37 lakh crore, driven by stress seen in microfinance and unsecured segments.
- The structural improvement resulted from several factors: large-scale write-offs, ongoing recoveries from legacy NPAs, increased provision coverage, and earlier resolutions through the IBC 2016 framework. Although asset quality remains robust, the rate of new recoveries has slowed in recent quarters as the stock of older stressed assets has decreased.

Figure 10: Capital Position Remains Robust (CAR in %)

Source: Bank Filings, CareEdge

- The median CAR of SCBs improved by 145 bps y-o-y and 13 bps sequentially to 17.6% in Q1FY26 and remained well above the regulatory requirement of 11.5%, indicating a stable position. This was driven by banks' profitability growth. Additionally, there is a favourable shift in the asset mix toward lower-risk-weighted categories, such as retail secured loans.
- The median CAR for PSBs rose significantly by 108 bps y-o-y to 17.7% for Q1FY26, supported by active capital raising through bond issuances. In contrast, for PVBs, the median CAR rose more modestly by 62 bps y-o-y to 17.1%, as a faster increase in risk-weighted assets partly offset capital growth. Additionally, the CAR for SCBs improved both y-o-y and q-o-q, thereby strengthening capital buffers.

For housing loans, risk weights based on LTV will reduce capital needs, particularly for affordable housing. Meanwhile, capital rules for commercial real estate have been tightened to restrict lending to highly leveraged developers. This balanced strategy promotes effective capital distribution across different segments. The rating-sensitive adjustments are designed to enhance capital efficiency for well-rated corporates and large NBFCs by tailoring capital requirements to credit quality. Better asset quality has led to a decline in banks' risk. The proposed reduction in risk weights for MSME exposures offers banks capital relief and encourages lending to small enterprises. Certain high-quality segments could benefit from better risk alignment across asset classes. Meanwhile, banks at an aggregate level already maintain a capital adequacy ratio well above regulatory requirements and would likely see limited immediate impact on the banking sector. (Refer to [In Q1FY26, Banks' Profits Buttressed By Treasury Gains and Structural Evolution of Indian Private Banks: A Shift Towards Stability and Retailisation](#)). Additionally, these changes, which would increase the capital adequacy ratio, must be read in conjunction with the ECL-based provisioning norms, which are expected to increase overall provisioning.

Annexure**Standard Supervisory Haircuts for Sovereign and other Securities which Constitute Exposure and Collateral**

Issue Rating for Debt Securities	Residual Maturity (in years)	Existing Haircut (in percentage)	Proposed Haircut (in percentage)	Change
Securities issued/guaranteed by the Government of India and issued by the State Governments (Sovereign securities)				
Rating not applicable – as Government securities are not currently rated in India	≤ 1 year	0.5	0.5	No Change
	> 1 year and ≤ 3 years	2	2	No Change
	> 3 year and ≤ 5 years			
	> 5 year and ≤ 10 years	4	4	No Change
	> 10 years			
Domestic debt securities other than those indicated above, including the securities guaranteed by Indian State Governments				
AAA to AA-/A1	≤ 1 year	1	1	No Change
	> 1 year and ≤ 3 years	4	3	Reduced by 1%
	> 3 year and ≤ 5 years	4	4	No Change
	> 5 year and ≤ 10 years	8	6	Reduced by 2%
	> 10 years	8	12	Increased by 4%
A+ to BBB-/ A2, A3 and P3 and unrated bank securities	≤ 1 year	2	2	No Change
	> 1 year and ≤ 3 years	6	4	Reduced by 2%
	> 3 year and ≤ 5 years	6	6	No Change
	> 5 year and ≤ 10 years	12	12	No Change
	> 10 years	12	20	New category carved out; hence, increased by 8%
Gold		15	20	Increased by 5%

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