CARE Ratings
Professional Risk Opinion

Retail Lending by Banks: Steering through the Covid waves

August 20, 2021 I BFSI

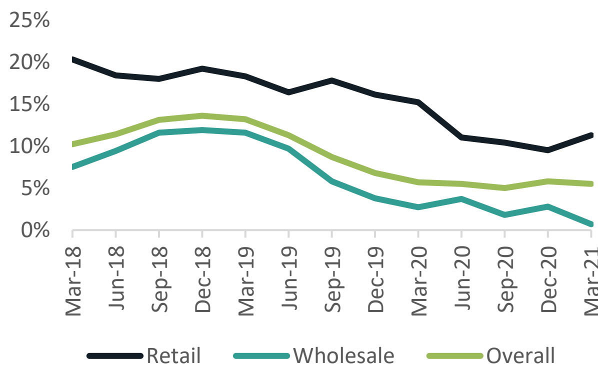
Summary

- Credit growth over the last five years has been driven by retail, which is likely to continue in FY22.
- Home loans, a secured lending segment, has been the largest segment in retail lending of banks, while personal loans segment has grown also rapidly.
- Regulatory measures like a blanket moratorium and restructuring helped prop the asset quality during the first Covid wave.
- Second Covid wave led to rise in delinquencies and slippages largely in the retail and MSME segment as there was no blanket moratorium available. RBI provided additional restructuring package for individual and small business loans.
- Banks have raised significant amount of capital to deal with any unforeseen shocks, there is a definite uptick in restructuring and concerns remain over the performance of the retail and MSME segments.
- The outlook in terms of credit growth is expected to be in the range of 7.5% to 8.0% for FY22 with economic expansion, ECLGS support and with a low base effect.

Credit Growth has been Retail Focused

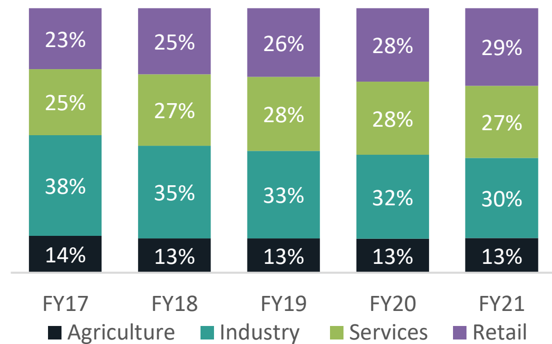
Credit growth (y-o-y) of scheduled commercial banks (SCBs), which had increased by 5.8% in December 2020 (vs. 5.0% in September 2020), slid again to 5.5% in March 2021 (vs. 5.7% in March 2020). Bank credit in FY21 remained subdued and was lowest in last four financial years. The subdued credit growth can be ascribed to risk aversion (both lenders and borrowers) and continued parking of excess liquidity with RBI. In addition, the regional lockdown imposed by states due to second wave has again restricted the growth to some extent, despite low base of previous year.

Figure 1: Wholesale vs Retail Credit Growth (%)



Source: RBI

Figure 2: Trend in Sectoral Market Share (%)



Source: RBI

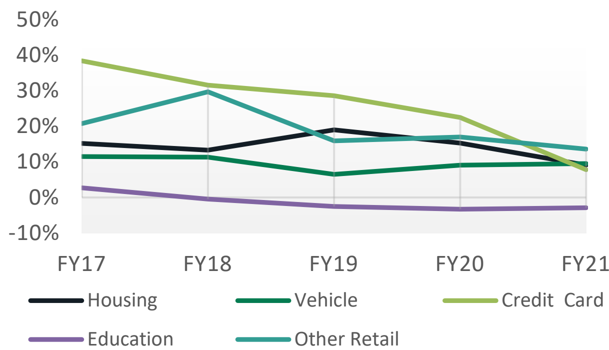
Post the asset quality review in 2015-2016, the banks saw a spike in NPAs largely in the wholesale advances which required banks to make significant amount of provisioning and write-offs over the next four to five years. As a result, there was an overall risk aversion among the bankers as well as the credit demand from wholesale borrowers was low. The second wave of COVID-19 has increased the slowdown in wholesale credit as compared to the retail credit, as risk aversion was largely towards corporate borrowers. In addition, due to absence of strong demand for credit and ample liquidity, bank holdings in SLR securities and state development loan stood at highest levels in March 2021 since March 2010.

The banks focused on the retail segment for growth which had good demand and brought in more granularity to the advances of the banks. As can be seen from the figure 1, the growth in retail credit significantly outpaced the growth in wholesale credit growth even during the last two years where the overall credit growth was subdued due to Covid. The figure 2 shows the share of retail which has seen significant increase while the share of industry has been sequentially decreasing over the last five years.

Public Sector Banks’ focus towards Personal Loans driving Retail Growth

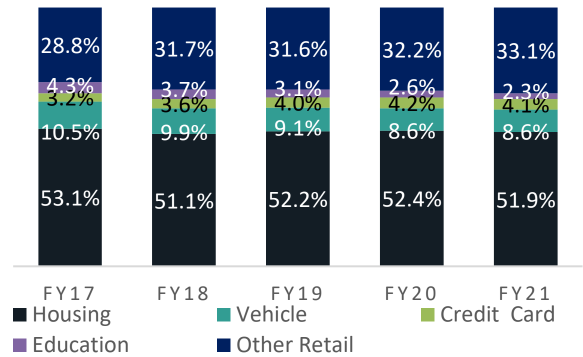
- Retail growth largely driven by housing loans and idiosyncratic segments like Unsecured Personal Loans
- Products like loans against gold jewellery have also witnessed substantial traction in FY21

Figure 3: Trend in Retail Growth (%)



Source: RBI, CMIE

Figure 4: Trend in Retail Market Share (%)



Source: RBI, CMIE

While most of the banks increased focus on retail lending, housing loans which are perceived to be low risk segment and is secured in nature constituted the majority share. Other retail segments largely include personal loans, gold loans and individual - loan against property.

Public banks have a larger portfolio in select segments or are growing faster than their private peers

Figure 5: Home Loans

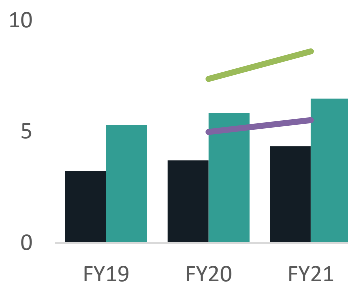


Figure 6: Vehicle Loans

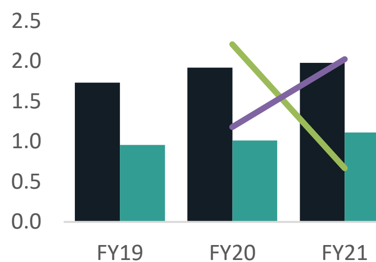
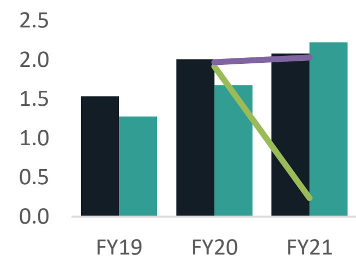


Figure 7: Personal Loans



Note: In Rs lakh crores; data compiled for top 3 private and top 3 public banks which have published data
Source: Bank Filings, CARE Ratings

Large public sector banks which were historically wholesale lenders have shifted focus to retail and have seen continued growth in segments like unsecured loans which were largely a domain of the private sector banks. Post Covid, there was traction in products like loans backed by gold while segments like education loan saw sharp decline over concerns over the asset quality. Retail segment is expected to continue to drive aggregate credit growth in FY22. Based on the data published by banks, the figures show a comparison of top three private sector and top three public sector banks. We can see that the growth in the home loan segment - public sector banks have a larger share and the growth remained stable across banks during FY21. Vehicle loan segment - private sector banks have a higher share, but they have slowed down. Personal loans – Public sector bank growth has outpaced the private sector banks which went slow during FY21. Private sector banks slowed down growth in personal loans and vehicle loans from FY21. Incidentally, for our cohort, personal loans segment is now larger than vehicle loans, a trend likely to be true for banking industry.

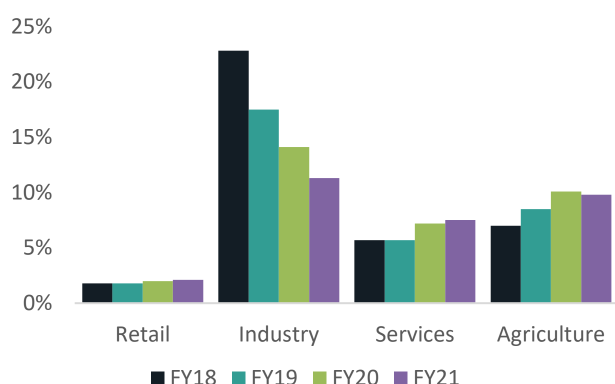
Covid-19 impacted the economy; but regulatory interventions supported asset quality

In March 2020, the Covid-19 struck India and on March 25, 2020, the government announced a nation-wide lockdown putting restrictions on movement of people and goods which led significant decrease in the economic activity, leading to decline in the demand and disruption of supply chains. This was a major blow to all the lenders including banks which witnessed significant challenges in collections due to borrowers’ income generation ability being severely impacted as well as logistical issues. The second wave also continued the impact. The regulators and government announced several relief packages to help the lenders as well as the borrowers who were impacted due to the lockdown. Some of these measures include (1) Blanket moratorium for six months: March 2020 to August 2020, (2) Formation of NARCL (to take over bad assets of the banks), (3) Emergency Credit Line Guarantee Scheme for small borrowers, (4) Resolution Framework for Covid-19 related stress, (5) Extension of TLTRO on Tap Scheme, (6) Maintain higher provision, (7) Extended implementation of last tranche of CCB, (8) Deferred NSFR implementation, and (9) Reducing the LCR.

Retail NPAs trended up even as NPAs for other sectors generally slowed

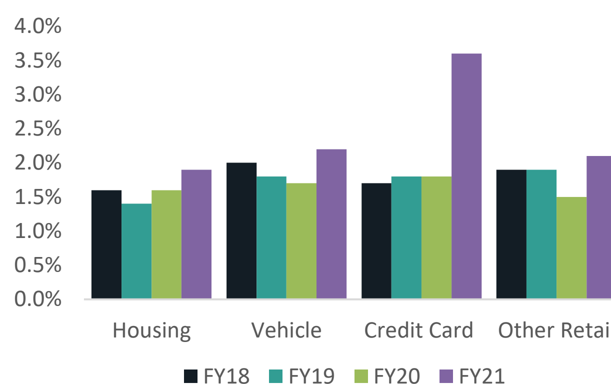
For FY21, SCBs' GNPA and NPA ratios stood at 7.5% and 2.4%, respectively. Write off to GNPA ratio declined for SCBs to 20.5% in March 2021 as compared with 22%-24% range in March 2020. Within SCBs, PSBs and FBs witnessed a fall in write off to GNPA ratio, whereas PVBs witnessed an increase as compared with the previous year. Overall, GNPAs declined by 5.9% mainly due to a fall of 8.4% in bad loans of PSBs. Pressure on asset quality is expected to continue due to restructuring especially in the MSME segment. The second wave is also expected to witness significant stress in retail loans (largely unsecured loans). The downside risks include lockdown in key states, which may impact the industrial as well as service segments. Another risk includes the ending of the ECLGS scheme in September 2021, which had propped up the MSME credit. The GNPA ratios of SCBs for two major sectors, i.e., agriculture and industry, declined during FY21, however, increased for the personal loan segment. Within the industrial sector, the ratio declined for all the sub-sectors in March 2021 as compared with the previous year. The slippage ratio (fresh accretion to NPAs) for SCBs declined to 2.5% in March 2021 vs 3.8% in March 2020. Within bank groups, PSBs and PVBs both witnessed a fall in their slippage ratio. We believe that the lower slippages is also supported by various regulatory measures such as moratorium, standstill on asset classification, ECLGS support for MSMEs and restructuring allowed to ease disruptions caused by the pandemic.

Figure 8: Trend in Sectoral NPAs (%)



Source: RBI, CMIE

Figure 9: Trend in Retail NPAs (%)



Source: RBI, CMIE

During FY21, while there was a decline in wholesale NPAs with resolution of legacy accounts under IBA and lower slippages in the corporate segment, there was a relative increase in retail NPAs and services. Even the proportion of retail seems smaller, there was a definite rise in the slippages in FY21. Within retail, there was rise in NPAs across segments during FY21 impacted due to Covid. Unsecured segments like personal loans and credit cards witnessed higher NPAs.

Impact of Second Wave: Uptick in slippages Retail and MSME NPAs during Q1FY22

Figure 10: Movement in Retal +MSME GNPA: PVB

Select Private Sector Banks GNPA	30-Jun-20	31-Mar-21	30-Jun-21
Retail + MSME	2.01%	2.68%	3.32%

Source: Select bank filings, CARE Ratings

Figure 11: Movement in Retal +MSME GNPA: PVB

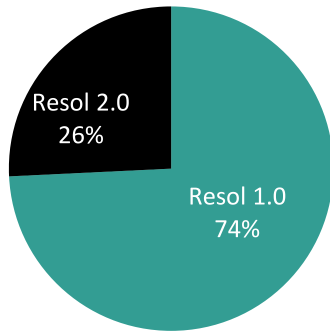
All Public Sector Banks GNPA	30-Jun-20	31-Mar-21	30-Jun-21
Retail	2.14%	2.15%	2.65%
MSME	12.17%	13.90%	15.28%
Retail + MSME	**5.99%**	**6.52%**	**7.28%**

Source: Select bank filings, CARE Ratings

During Q1FY22, there was the second Covid wave, leading to many states invoking lockdown restrictions. Apart from the impact on economic activity and income generation of borrowers, there was an impact on the collection efforts as most of the lenders were concerned over the health of the staff leading to shut down of branches. As a result, Q1FY22 witnessed a rise in NPAs especially in the retail and MSME segment. As compared to the first wave when RBI allowed a blanket moratorium, there was no blanket moratorium this time resulting in spike in slippages during the quarter. There was a rise in NPAs in the retail and MSME segments across public and private sector banks. RBI announced a restructuring framework 2.0 in May 2021 to individual and small business loans which is up to September 2021.

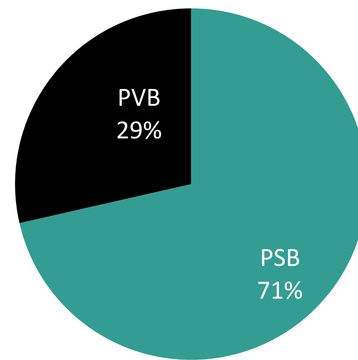
RBI Restructuring Framework

Figure 12: Resolution 1.0 vs. Resolution 2.0



Source: Bank filings, CARE Ratings

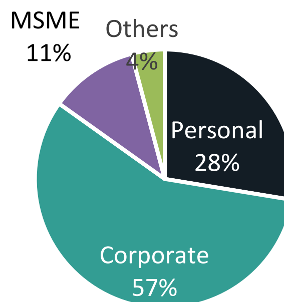
Figure 13: PVB vs PSB



Source: Bank filings, CARE Ratings

Considering the restructuring under the RBI Framework 1.0 and 2.0, majority of the restructuring has been done by public sector banks. As on June 30, 2021, public sector banks have restructured nearly Rs.98,000 crore of advances while private sector banks have restructured around Rs.39,000 crore of advances under both frameworks. While Framework 1.0 was for corporate, MSME and personal loans, the Framework 2.0 was for individuals and small businesses and the window of Framework 2.0 is still open till September 2021.

Figure 14: Sectoral Breakdown under Resolution 1.0



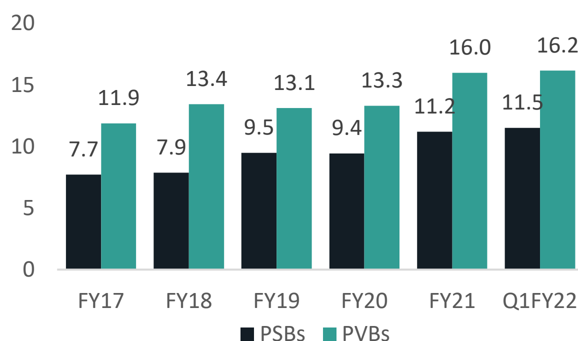
Source: Bank filings, CARE Ratings

If we look at the sectoral breakup of Resolution 1.0, the above figure highlights the breakup into different sectors, with corporate excl. MSME having the largest share. However, if we look at the combined sectoral break up of restructured advances under both schemes, personal + MSME constitute around 54%.

The rise in slippages and restructuring indicates stress build up in the retail segment post the Covid-19 especially after the second wave when there was no blanket moratorium and the banks either had to restructure or take the slippage on the books. Although, most banks have seen improvement in collection efficiency with the opening of lockdowns, there could be additional restructuring under the Framework 2.0 as by the end of Q2FY22 more banks will finalise their policy on the scheme.

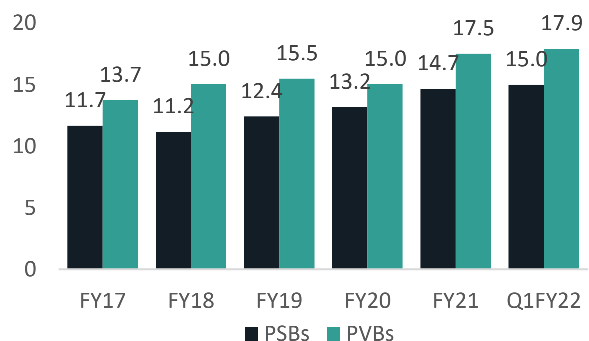
Banks maintain adequate capital buffers to absorb Covid-19 impact

Figure 15: Trend of Median Common Equity Tier I (CET I Ratio)



Source: Bank filings, CARE Ratings

Figure 16: Trend of Median Capital Adequacy Ratio (CAR)



Source: Bank filings, CARE Ratings

As the uncertainty related to Covid-19 began at the beginning of the financial year 2021, the banks started conserving capital and building up capital buffers to absorb any unseen shocks in the coming months. With the expectation of higher provisioning, most of the banks raised equity capital during FY21. In addition, the banks have been reporting stable operating profitability to enable them to absorb incremental provisioning for potential stress as most banks have maintained excess provisioning for Covid-19. The capital raises along with lower disbursements led to increase in the capitalisation levels of the banks. As can be seen in the charts, the median CAR for private sector banks was well above 17% and that for public sector banks was above 14% while the median CET I Ratio for private sector banks was at around 16% and for public sector banks was at around 11%.

Outlook

The outlook in terms of credit growth is expected to be in the range of 7.5% to 8.0% for FY22 with economic expansion, ECLGS support and with a low base effect. The growth would continue to be retail led. Also, the sector's medium-term prospects however look promising with diminished corporate stress and increased provisioning levels across banks. Retail loan segment is expected to do well as compared with industry and service segments. However, Covid-19 pandemic led credit losses could increase if localised lockdown measures persist and changed consumption patterns could negatively affect certain sectors downsizing of specific sectors. The stress from the second wave is expected to continue over the next quarters with a rise in slippages and restructuring. As a result, there could be higher restructuring and the real stressed accounts could be higher than the reported NPA numbers. Thus, credit losses could increase if economic conditions deteriorate, or government support measures are less effective than anticipated.

The credit growth will be supported by ECLGS scheme that has been extended till September 2021 (disbursement extended till December 31, 2021). While asset quality is expected to witness further stress in coming one or two quarters, the banks have adequate capitalisation to absorb any shocks. The banks have been providing and are likely to provide more for potential stress. With lower wholesale slippages, the credit cost has been declining over the last three years to the range of 1.3% to 1.4%. For FY22, it is estimated to be in the range of 1.5% to 2%. Credit cost for retail will remain elevated for few more quarters and may come close to pre Covid levels in FY23 and pre covid levels are expected to be observed post FY23. The outlook is with a caveat that there is no culmination of a third Covid wave.

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