Margins of Indian banks may fall to 2.9% in FY24, says S&P

Asset quality to stay on upward trajectory

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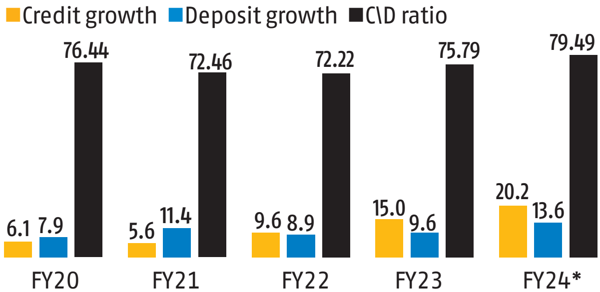
WIDENING GAP Figures in % (Y-o-Y)



Note: *FY24 data till November; November 2023 figures factor in merger of HDFC with HDFC Bank; C\D ratio: Credit to deposit ratio
Source: RBI data

Standard & Poor's (S&P) on Wednesday said the credit-deposit ratio (C-D ratio) of Indian banks may come under pressure due to continued lag of deposit growth vis-à-vis the pace of credit expansion.

Trailing of deposit growth and competition for funds may lower the net interest margin (NIM) to 2.9 per cent in 2024-2025 (FY25) from 3 per cent in FY24.

Over the next few years, the loan growth will align with nominal gross domestic product (GDP), with retail loans surpassing corporate loan expansion.

Keeping pace with this may prove challenging for deposits, thereby weakening the credit-to-deposit ratio, said Geeta Chugh, analyst at S&P Global Ratings, in an outlook for banks in India.

Nonetheless, the funding profiles of banks should stay robust, supported by a strong deposit franchise.

According to Reserve Bank of India (RBI) data, deposits of Indian banks have grown by 13.6 per cent year-on-year (Y-o-Y), and credit expanded by 20.6 per cent till mid-November.

This trend factors in the merger of HDFC with HDFC Bank. The C-D ratio of the banking system stood at 79.49 per cent as on November 17, 2023.

Chugh said, "Delayed repricing of deposits, heightened competition for deposits, and a shift from low-yielding current account and savings account (CASA) to higher-interest-bearing term deposits will exert pressure on net interest margins.

While the small and mid-sized enterprise sector and low-income households are vulnerable to higher interest rates and inflation, the interest rates in India are unlikely to rise materially. This should limit the risk for the banking industry.

Unsecured personal loans have grown rapidly and could contribute to incremental non-performing loans.

Asset quality is anticipated to remain in positive trajectory in 2024-25.

And, the proportion of weak loans will decrease to 3-3.5 per cent of gross loans by March 31, 2025.

This improvement is attributed to structural enhancements, including robust corporate balance sheets, more stringent underwriting standards, and enhanced risk-management practices, S&P added.

Weak assets were around 5.2 per cent of gross loans as on March 31, 2023. This compares with 7.6 per cent as on March 31, 2022.