



SECTORAL VIEW

BANKING FEBRUARY 2021



Prevailing Rates

I. Policy Rates

Repo Rate	4.00%
Reverse Repo Rate	3.35%
Marginal Standing Facility Rate	4.25%
Bank Rate	4.25%

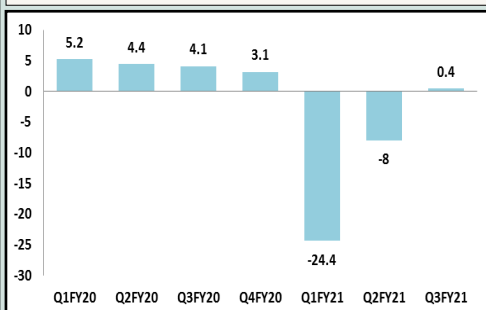
II. Lending/Deposit Rates

Base Rate	7.30% -8.80%
MCLR Rate (Overnight)	6.55% -7.05%
Savings Deposit Rate	2.70% -3.00%
Term Deposit Rate > 1 Year	4.90% -5.50%

III. Reserve Ratio

CRR	3.00%
SLR	18.00%

Exhibit 01: India's GDP Growth Rate (%)



Source: IMF, Progressive Research

Global Banking:

Hong Kong announces over USD15bn budget to lift the economy out of recession

The Hong Kong government has budgeted around USD15bn in FY22 with the view to lift the economy out of recession. The government allocated USD1.2bn to support businesses, this includes reduction in taxes and waiver of business registration. Other allocation includes USD1.1bn for procurement and administration of Covid-19 vaccines. Personal taxes were also slashed and the government supported individuals via USD645 loan guarantees and consumption vouchers.

Our Analysis:

This budget was announced on the back of six economic contractions and political unrest leading to turbulence in the country. A good budget was essential for economic growth of the country so as to revive growth; however the same has led to record budget deficit of USD33.3bn. Government expects growth to expand ranging from 3.5% to 5.5% in FY21 and an average of 3.3% from FY22-25

India's economy out of technical recession, Q3 GDP growth at 0.4%

India's GDP for Q3FY21 grew by 0.4% as compared to contraction of 8% in Q2FY21. GDP is estimated to be Rs36.22lakh-cr as compared to Rs36.08lakh-cr (at constant 2011-2012 prices). Q1FY21 witnessed a slump as economy contracted by 24.4% while resumption of economic activities led to narrowing of GDP decline to 8% de-growth in Q2FY21. National Statistical Office also revised FY21 GDP estimates to a contraction of 8% from earlier projection of a 7.5% decline. In calendar year 2020, Indian economy contracted by 6.9%.

Our Analysis:

With a marginal growth, India is out of technical recession. However, the GDP growth was lower than the expectation which ranged from 0.5-1%. Relaxation in Covid-19 related restrictions, positive movement in GST collections and other economic indicators, roll out of vaccines led to higher expectation, however the actual numbers weren't far off from the expectations. FM Nirmala Sitharaman suggested that the economy is back to pre-Covid growth rates reflecting a V-shaped recovery. However, with probability of second wave and rise in number of cases, one needs to be cautious.

China's economy could double in size by 2035 and surpass the US economy along the way

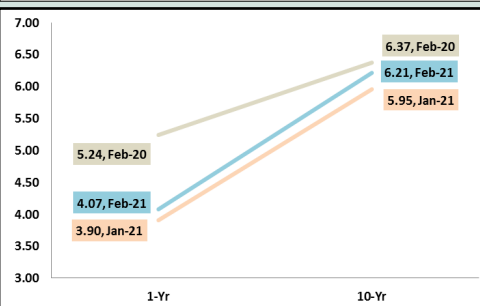
According to National Bureau of Statistics, China's GDP reached USD14.73tn, which is more than 70% of the US economy. China GDP grew by 3% in USD terms during CY2020, being one of the few economies that grew in 2020. According to the bureau, China now accounts for 17% of global GDP, significantly increasing from 10% in 2010.

Our Analysis:

China's strict lockdowns and prompt action enabled it to limit the spread of the virus and led the economy to a swifter recovery. President Xi expects China to double its GDP by 2035 and Japan Center for Economic Research along with other economists expects China to surpass USA by 2028 instead of 2035 earlier predicted by China.



Exhibit 02: 1 Year Yield vs 10 Year Yield



Source: RBI, Progressive Research

Indian Banking Sector:

Budget proposes AMC-ARC for NPAs

FM Nirmala Sitharaman in the Union Budget 2021 proposed setting up of a bad bank under the Asset Reconstruction Company (ARC), Asset Management Company (AMC) and Alternative Investment Framework (AIF) model. The aim of this AMC-ARC would be to acquire bad loans from banks and turn them around. The expected framework is that the bad bank will acquire bad loan from banks at a discount/negotiated price and the AMC for a fee will restructure and turnaround the bad loans.

Our Analysis:

There still prevails uncertainties in the banking sector as quantum of bad loans has been hid by the current forbearance framework. Most major banks are at a good position currently (on basis of proforma numbers), but the true picture is still uncertain, considering the impact on mid/small banks as well as other financial lenders. Reports (including that of RBI) expect NPAs to rise to 15% in September, 2021 from 7% in September 2020, which is a significant increase. This can increase pressure on banks as they face capital constraints and asset liability mismatches. The advantage of having a bad bank is time bound resolution as the proposed ARC-AMC is maintained by banks. There are multiple factors which need to be finalised and one would be fully able to see the picture only once the detailing happens.

Finance Minister proposed Rs20,000cr infusion in Public Sector Banks for 2021-2022

In the Union budget, finance minister proposed infusion of Rs20,000cr in PSBs. Over the years, GoI has infused Rs65,433cr in 2019-20, Rs1.06lakh-cr in 2018-19 and Rs80,000cr in 2017-18.

Our Analysis:

The proposed capital infusion of Rs20,000cr is lower than expected as stress on assets is anticipated to increase due to Covid-19 induced slowdown. Over the years, GoI has infused meaningful capital in PSBs so that they are in compliance with regulatory requirements of RBI. However, over the past years, GoI has made a shift in strategy and now the intent is to divest in certain PSBs thus resulting in lower budget allocation. Furthermore, it has also indicated that PSBs can start raising capital from the markets; although the market response for the average PSBs is tepid.

Stress in retail loans of banks may triple by FY22 end: Ind-Ra

According to India Ratings, stress in retail loans could triple by the end of FY22. It expects stressed loans to rise to 4.7% in March 2022, from expected 1.6% in March 2021. Ind-Ra expects stressed assets to increase by almost 1.7 times in H2FY21 wherein for PSBs it could increase from 2.1% to 2.9%. For private banks the same could increase to 4.3% from 2.1% during the same period. Unsecured exposure in private banks gross advances is around 15% while the same for PSBs is roughly 5%

Our Analysis:

Tripling of loans is attributable to slowdown in income/lower disposable income and slower growth of job creation in the service sector. The anticipated stress is higher in private sector banks as PSBs' clientele draw salaries from public sectors entities and hence are less exposed to uncertainties. Additionally, private banks have higher exposure to unsecured advances in search of higher returns.



Indian Banking Sector:

Highlights of Monetary Policy:

- Repo Rate: 4.00% (4.00% in December 2020)
- Reverse Repo Rate: 3.35% (3.35% in December 2020)
- Bank Rate: 4.25% (4.25% in December 2020)
- Marginal Standing Facility: 4.25% (4.25% in December 2020)
- GDP Projection: Growth projected at 10.5% for FY22
- CPI Inflation: Projected at 5.2% for Q4FY21 and 5-5.2% for H1FY22, Q3FY22: 4.3%

Other Measures Announced:

1) Liquidity Measures:

- TLTRO on-tap scheme announced for banks extended to NBFCs
- To restore CRR in 2 phases to 3.5% w.e.f March 27 and 4% w.e.f May 22, 2021
- Access to funds for banks under MSF has been extended by six months beyond March end to September, 2021

2) Regulation and Supervision:

- To extend the dispensation of enhanced HTM of 22% up to March 31, 2023 to include securities acquired between 1st April, 2021 and 31st March, 2022. HTM limits to be restored from 22% to 19.5% in a phased manner starting from the quarter ending 30th June, 2023
- SCBs will be allowed to deduct credit disbursed to 'New MSME borrowers' from their net demand and time liabilities for calculation of CRR
- To defer implementation of last tranche of the Capital Conservation Buffer (CCB) of 0.625% and the implementation of Net Stable Funding Ratio (NSFR) to 1st October 2021
- RBI to come up with various guidelines for the MFI sector
- Will form expert panel to strengthen primary urban co-op banks
- Resident individuals can make remittance to IFSCs for NRIs

3) Deepening Financial Markets: to allow retail investors access to G-secs (primary and secondary markets)

4) To set up 24x7 helpline for digital payment services

5) Consumer Protection: To make ombudsman scheme more efficient, a central integrated ombudsman scheme, to be rolled out from June 2021

Our Analysis:

RBI's positive commentary on the outlook of the economy and inflation suggested that the worse is behind us, barring the unpredictable second wave of Covid-19. RBI extended support to disruption free growth revival. In his closing remarks, RBI governor said, "going forward the Indian economy is poised to move in only one direction which is upwards. It is our strong conviction backed by forecasts, that in FY22 we will undo the damage that Covid-19 has done to the economy. After the chaos and despair of the year gone by through which we have sailed together, we shall continue to sail ahead." and these words were encouraging. RBI's support to government's borrowing plans can be witnessed through the extension of HTM and assurance of adequate liquidity measures as and when required. RBI did not announce a bond purchase calendar, and the same was not taken in the right spirits by the bond market. However, the recent initiatives of allowing retail investors to open gilt accounts, inclusion of NBFCs for on-tap TLTRO and the plan to set up Integrated Ombudsman Scheme are steps in the right direction for inclusive growth.



Exhibit 03: ICICI Bank Ltd vs Nifty



Source: Ace Equity, Progressive Research

Indian Banking Sector:

Nabard disburses Rs16,500cr under RIDF in first 10 months of FY21 while PSBs eye Rs70,000cr corpus for farm fund

National Bank for Agriculture and Rural Development has sanctioned Rs30,200cr for rural infrastructure projects under Rural Infrastructure Development Fund and disbursed Rs16,500cr for the same during first 10 months of FY21. In the Union budget 2021-22, allocation for RIDF was enhanced to Rs40,000cr from Rs30,000cr. Additionally, according to media reports, PSBs with exposure to agriculture have initiated talks with the government to set up a credit guarantee fund to cover defaults by farmers wherein the GoI will provide Rs70,000cr as initial corpus for 3 years.

Our Analysis:

According to Nabard's chairman, RIDF fund has constituted around 10% of gross capital formation in rural areas. RIDF has become a dependable and important source of funding for states and UTs for building and strengthening rural infrastructure in critical sectors like agriculture, health, infrastructure etc. The fund was set up in 1995, and has disturbed around Rs3.11lakh-cr and is a dedicated fund to create social assets in rural India. With regards to the PSBs approaching GoI for corpus funds, if approved, the fund will cover Kisan Credit Card scheme loan exposure of banks where in PSBs are expecting defaults. The fund will help cushion the impact of anticipated stress on the lender.

Coverage News: ICICI Bank Limited:

- The bank entered an agreement with Thillais Analytical Solutions Private Limited (TASPL) in relation to investment in equity shares and compulsorily convertible preference shares for cash consideration of Rs11mn (9.65% shareholding of TASPL). Indicative time period for completion of the acquisition is end of March 2021.
- The bank entered into a MoU amongst members of the consortium seeking to set up a Pan-India (National) Umbrella Entity for retail payments, subject to requisite regulatory approvals. With respect to the same, ICICI Bank will acquire 20% stake in Mopay Services Private Limited for cash consideration of Rs1bn. Indicative time frame for completion of the acquisition is December, 2021

Our Analysis:

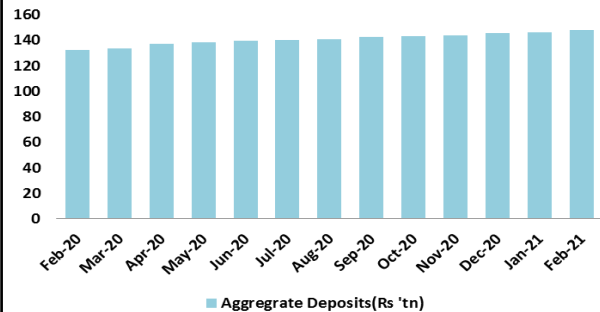
According to media reports, the consortium mentioned above includes the likes of Amazon, Axis Bank and Visa along with ICICI Bank. The aim of the said consortium is to set up a new entity to create a new national payment network. All members are expected to have similar stake in the new entity and will pave way for a payment network which will reduce settlement time for small businesses and merchants. This entity will benefit from cost synergies and existing network of members and will propel members' participation in the growing digital payments space.

Non-Coverage:

Banks	Results Synopsis (Q3FY21)
State Bank of India	NII grew by 3.7% to Rs288.19bn Net Profit stood at Rs51.9bn Gross NPA: 4.77%; Net NPA: 1.23%; CAR: 14.50%

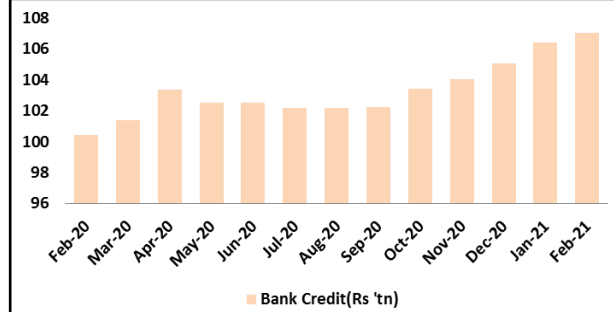


Exhibit 04: Trend of Aggregate Deposits of SCBs



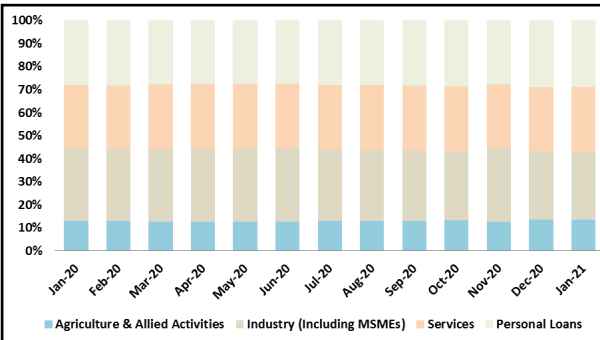
Source: RBI, Progressive Research

Exhibit 05: Trend of Bank Credit of SCBs



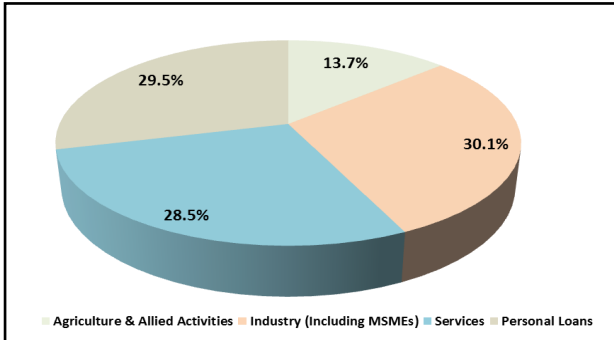
Source: RBI, Progressive Research

Exhibit 06: Deployment of Gross Bank Credit by major sectors



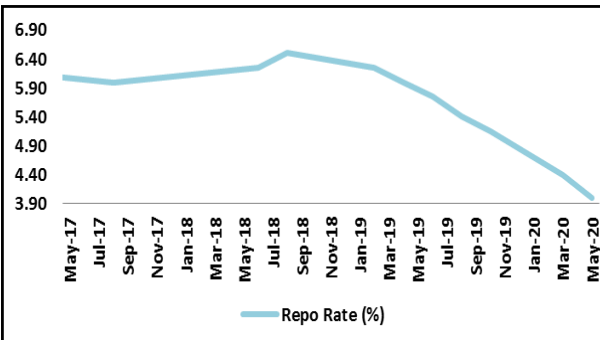
Source: RBI, Progressive Research

Exhibit 07: Sectoral breakup of Gross Bank Credit of the major sectors in January



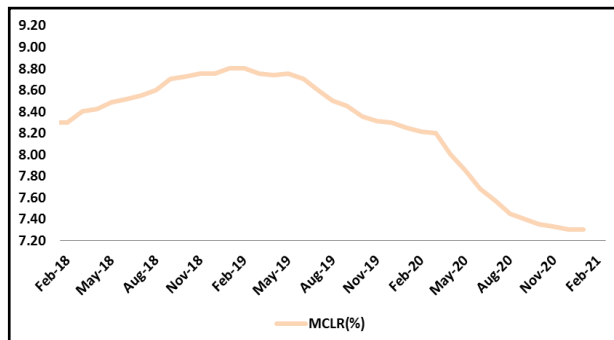
Source: RBI, Progressive Research

Exhibit 08: Repo rate trend as changed by RBI in last 3 years



Source: RBI, Progressive Research

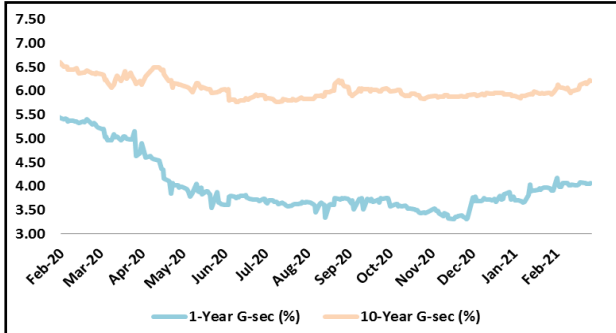
Exhibit 09: MCLR trend in the last 3 years



Source: RBI, Progressive Research

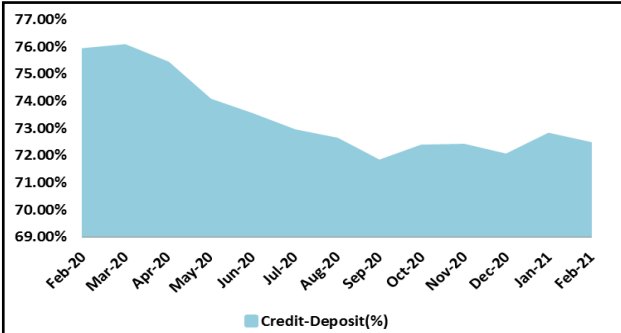


Exhibit 10: RBI trying to keep the gap between short and long term bond in check



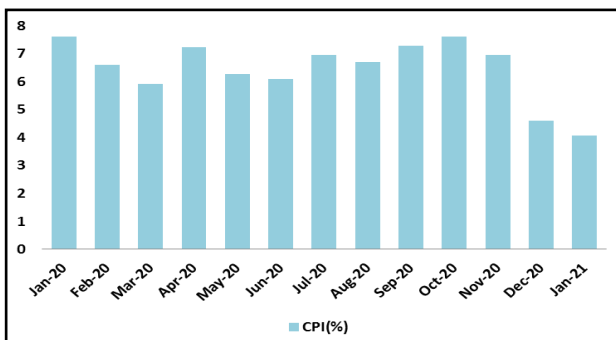
Source: Investing.com, Progressive Research

Exhibit 11: Improvement is witnessed in Credit-Deposit ratio of the SCBs in February



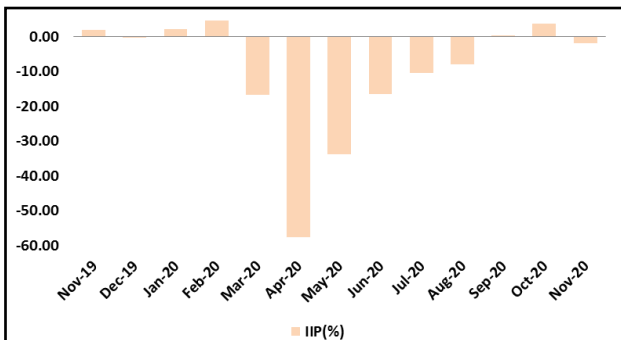
Source: RBI, Progressive Research

Exhibit 12: Retail Inflation Eases Marginally



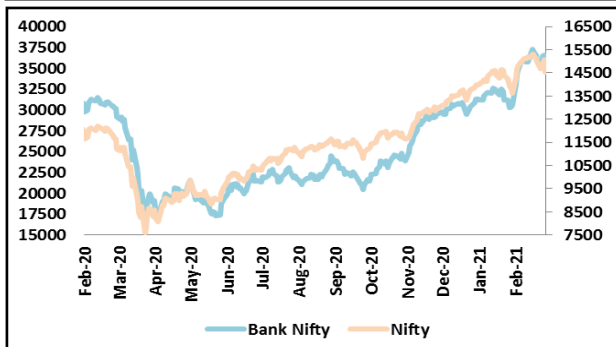
Source: RBI, Progressive Research

Exhibit 13: Change in y-o-y IIP data



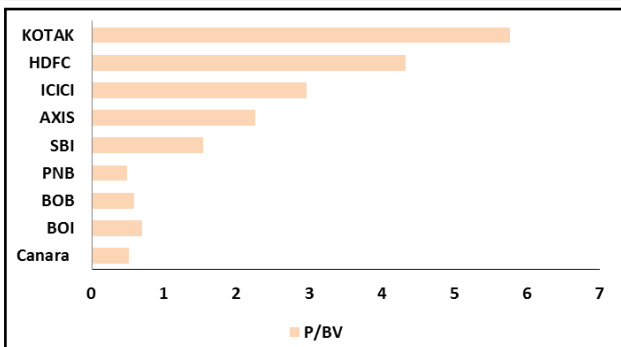
Source: RBI, Progressive Research

Exhibit 14: Bank Index vs Nifty Index



Source: NSE, Progressive Research

Exhibit 15: Major Banks' Valuation as on 26th February, 2021



Source: Ace Equity, Progressive Research



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