BANKING MONTHLY

AUGUST 2023

PROGRESSIVE®
Your Progress Our Priority...

Prevailing Rates

I. Policy Rates

Repo Rate	6.50%
Reverse Repo Rate	3.35%
Standing Deposit Facility Rate	6.25%
Marginal Standing Facility Rate	6.75%
Bank Rate	6.75%

II. Lending/Deposit Rates

Base Rate	8.85% -10.10%
MCLR Rate (Overnight)	7.95% -8.40%
Savings Deposit Rate	2.70% -3.00%
Term Deposit Rate >	6.00% -7.25%

III. Reserve Ratio

CRR	4.50%
SLR	18.00%

Global Banking:

Japan GDP grew 6%, easily beating expectations on robust exports

Japan's economy posted its third straight quarterly expansion, as robust export growth contributed to an annualized 6% expansion in the second quarter, handily beating market expectations. Economist surveyed by Reuters had expected the world's third-largest economy to post 3.1% growth in the April-June quarter. The impressive gross domestic product data translated to a more modest quarterly expansion of 1.5%, topping expectations for 0.8% growth.

Our comments:

This comes as inflation has exceeded the BOJ's 2% target for 15 consecutive months. In July, the Japanese central bank loosened its yield curve control over the 10-year Japanese government bond in a modification it says was intended to make its ultra-easy monetary position more sustainable. The GDP print followed an annualized 2.7% growth in the first quarter, pointing to a continued post-Covid recovery for Japan's economy. Still, the narrower gap between reality and expectation in quarter-on-quarter growth tempers any longer-term optimism. Other details beyond the rosy headline GDP growth figure suggest the Bank of Japan is likely to revert from its ultra-easy monetary posture.

Fitch downgrades US credit rating from AAA to AA+

The US government's credit rating has been downgraded following concerns over the state of the country's finances and its debt burden. Fitch, one of three major independent agencies that assess creditworthiness, cut the rating from the top level of AAA to a notch lower at AA+. Fitch said it had noted a steady deterioration in governance over the last 20 years.

Our comments:

Investors use credit ratings as a benchmark for judging how risky it is to lend money to a government. The US is usually considered a highly secure investment because of the size and relative stability of the economy. The timing and rationale behind the downgrade has taken many economists by surprise. The rating downgrade of the United States reflects the expected fiscal deterioration over the next three years, a high and growing general government debt burden, and the erosion of governance relative to peers. Fitch also said it expects the US to slip into a mild recession later this year.

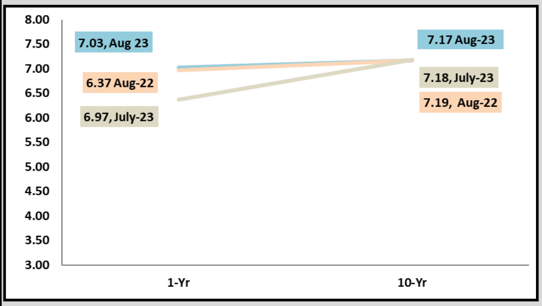
China's worsening economic slowdown is rippling across the globe

China's economy was meant to drive a third of global economic growth this year, so its dramatic slowdown in recent months is sounding alarm bells across the world. Policymakers are bracing for a hit to their economies as China's imports of everything from construction materials to electronics slide. Global investors have already pulled more than USD10bn from China's stock markets, with most of the selling in blue chips. Asian economies are taking the biggest hit to their trade so far, along with countries in Africa. Japan reported its first drop in exports in more than two years in July after China cut back on purchases of cars and chips. Central bankers from South Korea and Thailand last week cited China's weak recovery for downgrades to their growth forecasts.

Our comments:

It's not all doom-and-gloom, though. China's slowdown will drag down global oil prices, and deflation in the country means the prices of goods being shipped around the world are falling. That's a benefit to countries like the US and UK still battling high inflation. Some emerging markets like India also see opportunities, hoping to attract the foreign investment that may be leaving China's shores.

Exhibit 1: 1 Year Yield v/s 10 Year Yield



Source: Investing.com, Progressive Research

Indian Banking:

Indian economy's domestic dynamics continue to be strong: FinMin report

The Indian economy's domestic dynamics continue to be strong though negative cross-border spillovers and adverse global developments can act anytime as a deterrent to achieve the potential high growth path in the current financial year, as stated by the Finance Ministry. The Ministry also pointed out that though inflation has significantly declined in June quarter, the recent spike in the prices of fruits, vegetables, and pulses and products due to weather-related disruptions has led to a sequential increase in food inflation in June 2023, emphasizing the need for a "guarded approach by RBI and the government". The Ministry also noted that the RBI maintains its policy rates at levels higher than a year ago and is closely monitoring the possible impacts of global and domestic shocks on the prices in India.

Our comments:

On the growth front though, the report said, despite a rise in global uncertainties and moderation in global output, India's growth momentum gathered in the last quarter of the previous fiscal is likely to be sustained in June 2023 quarter, as reflected in the performance of various high-frequency indicators including GST collections, PMI, services exports, e-way bills etc.

India's economy to hit USD10tn by 2030

Union Minister Hardeep Singh Puri expressed confidence that the Indian economy will reach the milestone of USD10tn by the end of this decade, given its current growth rate. Highlighting the recent projections of 6.1% to 6.5% growth for the 2023-24 fiscal year, Puri said, 'A USD5tn economy by 2025 or 2026, which people doubted, is looking at us'. A USD10tn economy by 2030 is again no longer a matter of debate or disagreement. India's current GDP size is approximately USD3.4tn, making it the fifth-largest economy in the world, overtaking the UK.

Our comments:

It was quoted that the change witnessed in the last nine years is extraordinary and we are now moving in the direction of being the third-largest economy in the world. The statements by Minister Puri and PM Modi underline the government's optimistic outlook on India's economic growth and potential. Achieving the USD10tn milestone will likely require sustained efforts across various sectors, including infrastructure development, technological innovation, regulatory reforms, and global trade engagement.

Indian economy to grow at 6.7% for next 8 years: S&P Global

S&P Global expects India to grow at 6.7% per year from FY24-FY31, catapulting GDP to USD6.7tn from USD3.4tn in FY23. Per capita GDP will rise to about USD4,500. The macro challenge for India in the next decade is to turn traditionally uneven growth into a high and stable trend. Success will depend on India's ability to reap its demographic dividend: increase labour force participation, including upskilling; boost private investment, with structural reforms in land, logistics and labour; and increase competitiveness, driven by FDI. Investment as a proportion of GDP reached a 10-year high of 34% in FY23. S&P Global expects the Indian private sector to gradually increase investments given healthy corporate balance sheets. Geopolitics could provide considerable tailwinds, it cautioned.

Our comments:

India is however, failing to take full advantage of its large and growing working-age population and manufacturing's share of GDP has only risen to about 18% from 15% over the past two decades. By contrast, services' share has leapt to 55% from 45%. Manufacturing has been held back by stringent labour laws, subpar logistics and poor infrastructure.

Non Coverage News:

Profit of PSU banks more than doubles to Rs34,774cr in Q1

Public sector banks (PSBs) have once again posted stellar performance by registering more than double profit of Rs34,774cr for Q1FY24. During the April-June period of the previous fiscal, all 12 state-owned banks had recorded a total profit of Rs15,306cr, according to quarterly numbers published by public sector lenders. The high-interest regime helped banks to earn a good net interest margin (NIM) during the quarter. Most banks had recorded NIM of over 3%.

Our comments:

Several measures taken by the government have helped in the revival of PSBs. As a result of 4R's strategy of recognition, resolution, recapitalisation and reforms, non-performing assets of banks have come down to a 10-year low at 3.9% of total advances. At the same time, banks recovered bad loans worth over Rs8.6lk-cr in the last eight financial years.

Top distressed funds mull buying State Bank of India’s bad loans

A number of global and local distressed asset investors are considering buying some of State Bank of India’s bad loans put up for sale in the financial year that began in April. The bank identified a list of 331 non-performing assets with a combined outstanding value of Rs960bn (USD11.6bn). Investors that have expressed interest include New York-based Cerberus Capital Management LP, Hong Kong-headquartered SC Lowy, and Avenue Capital Group LLC-backed Asset Reconstruction Company (India) Ltd., said the people who requested anonymity discussing private matters. Other potential local buyers include billionaire Uday Kotak-backed Phoenix ARC Pvt., JM Financial Asset Reconstruction Co. and Reliance Asset Reconstruction Co.

Our comments:

Identifying bad loans has become a growing practice among Indian lenders after the nation’s Central Bank released two years ago a report that sought to make the buying and selling of distressed assets more transparent and efficient. India’s banking sector is now in stronger shape after surviving a shadow banking crisis in 2018 that rattled the country’s capital markets.

Banking system liquidity turns deficit for first time in FY24 due to I-CRR, tax outflows

Banking system liquidity turned deficit for the first time in the current fiscal on August 21 after the Reserve Bank of India asked banks to maintain incremental cash reserve ratio (I-CRR), GST outflows and selling of dollars by the Central Bank. The liquidity has turned deficit because of various factors- the incremental CRR has taken out Rs1.1lk-cr of liquidity from 12th August onwards and there are tax payments which are due. The RBI has been selling dollars in the market, which has also contributed to taking out liquidity.

Our comments:

Earlier this month, the RBI mandated banks to maintain an I-CRR of 10% on the increase in their net demand and time liabilities (NDTL) between 19th May-28th July, 2023, effective 12th August. The temporary move was aimed at managing the liquidity overhang generated due to the return of Rs2,000 banknotes to the banking system, RBI’s surplus transfer to the government, pick up in government spending and capital inflows.

Non Coverage News:

Union Bank approves raising up to Rs5,000cr via QIP

The board of Union Bank of India has approved a plan to raise capital up to Rs5,000cr through qualified institutional placement (QIP). The decision was made during a meeting of Union Bank's committee of directors. The base deal size of Rs2,500cr can be scaled up by Rs2,500cr. The announcement comes a month after Union Bank reported a 107% on-year rise in its standalone net profit to Rs3,236.44cr for Q1FY24. Also, the bank's Net Interest Income (NII), increased 16.6%; at Rs8,839.7cr.

Our comments:

The board has set a floor price of Rs91.10 per share.

Central Bank of India enters into strategic tie-ups

The public sector lender has entered into a strategic co-lending partnership with IKF Home Finance to offer MSME and home loans. IKF Home Finance manages assets totaling to Rs696.10cr via operations in 6 states. Also, Central Bank of India entered into a strategic co-lending partnership with Samunnati Financial Intermediation & Services to offer agriculture and MSME loans. Samunnati is functioning in 22 states, with an AUM of Rs1,150cr.

Our comments:

These tie-ups would benefit the bank in the longer term ahead.

Coverage News:

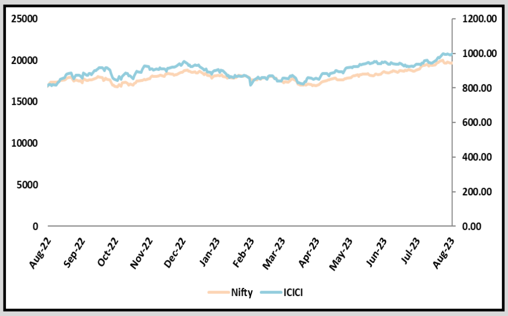
ICICI Bank gets RBI nod to increase up to 4% stake in subsidiary ICICI Lombard

ICICI Bank received approval from the Reserve Bank of India to raise its stake in ICICI Lombard General Insurance company by up to 4% in multiple tranches. The private lender currently holds a 48.01% share in ICICI Lombard. Earlier, the bank, in its disclosure filed with the stock exchanges on May 28, 2023, had communicated that its Board of Directors had approved an increase in the shareholding in ICICI Lombard in multiple tranches by up to 4%. In 2019, the RBI had asked banks to reduce stake in their insurance ventures to protect the lender from the risks arising from other non-core businesses. In September 2021, ICICI Bank reduced its stake in ICICI Lombard from 52% to 48%, and the insurer was no longer a subsidiary.

Our comments:

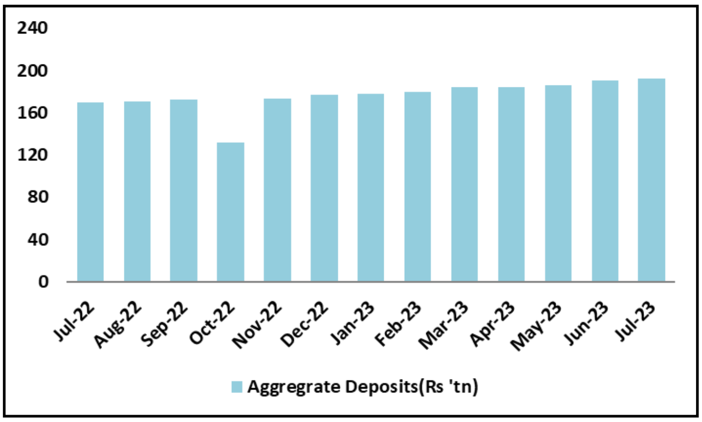
Typically, promoter increasing stake is a positive for the bank, adding conviction to the longer term perspective. ICICI Bank's decision to raise stake in ICICI Lombard is in sync with the move made by its peer, HDFC Bank.

Exhibit 2: ICICI v/s Nifty



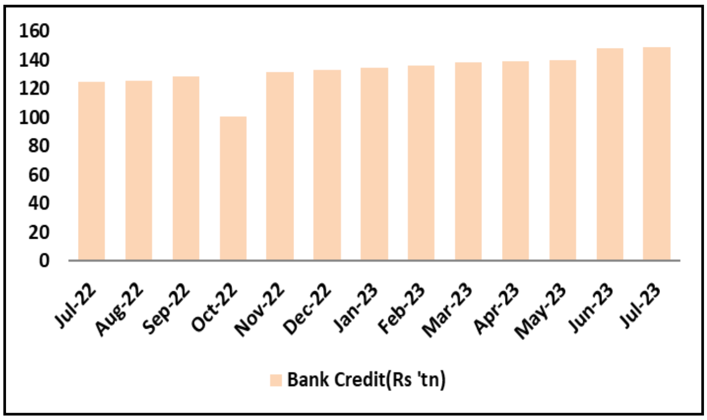
Source: Ace Equity, Progressive Research

Exhibit 03: Trend of Aggregate Deposits of SCBs



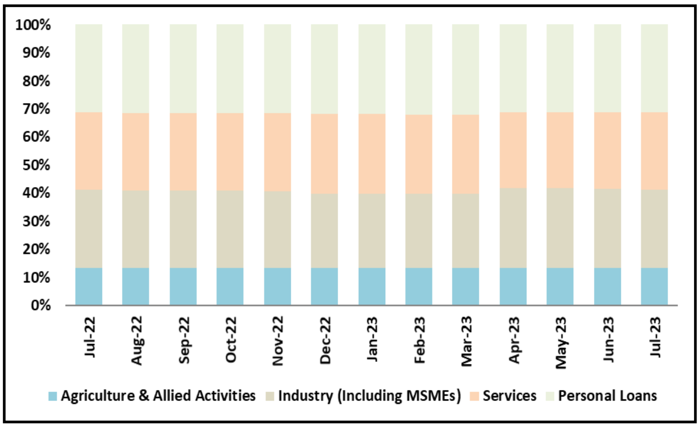
Source: RBI, Progressive Research

Exhibit 04: Trend of Bank Credit of SCBs



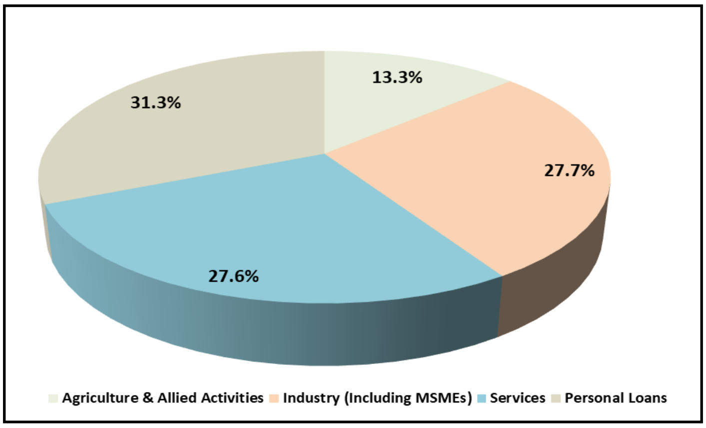
Source: RBI, Progressive Research

Exhibit 05: Deployment of Gross Bank Credit by major sectors



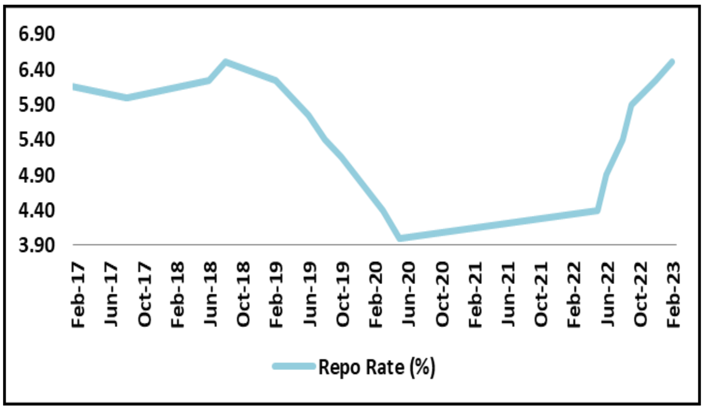
Source: RBI, Progressive Research

Exhibit 06: Sectoral breakup of Gross Bank Credit of the major sectors in July



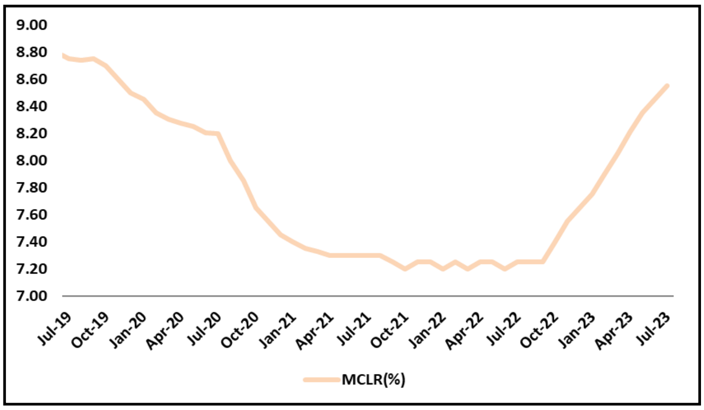
Source: RBI, Progressive Research

Exhibit 07: Repo Rate Trend



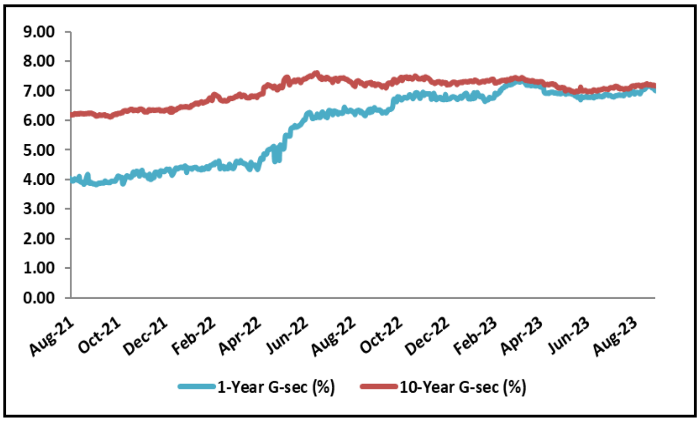
Source: RBI, Progressive Research

Exhibit 08: MCLR trend in the last 3 years



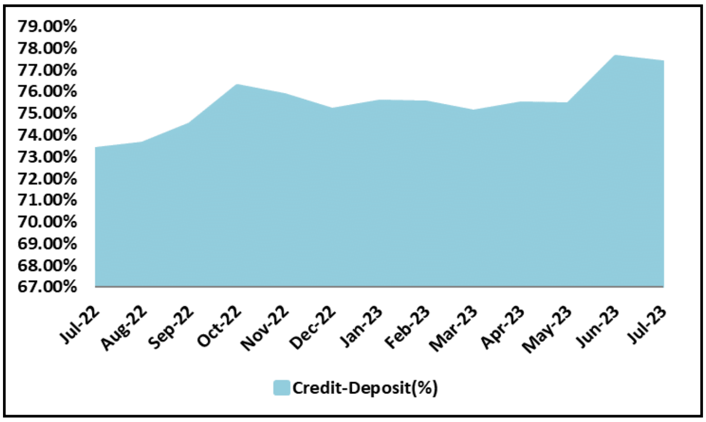
Source: RBI, Progressive Research

Exhibit 09: RBI trying to keep the gap between short and long term bond in check



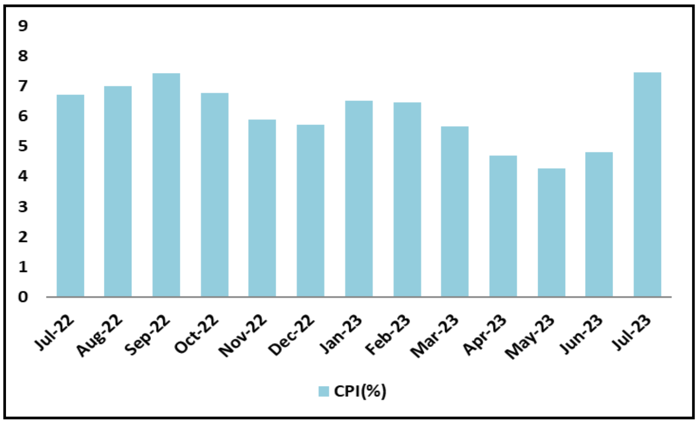
Source: Investing.com, Progressive Research

Exhibit 10: Credit-Deposit ratio of the SCBs in July-23



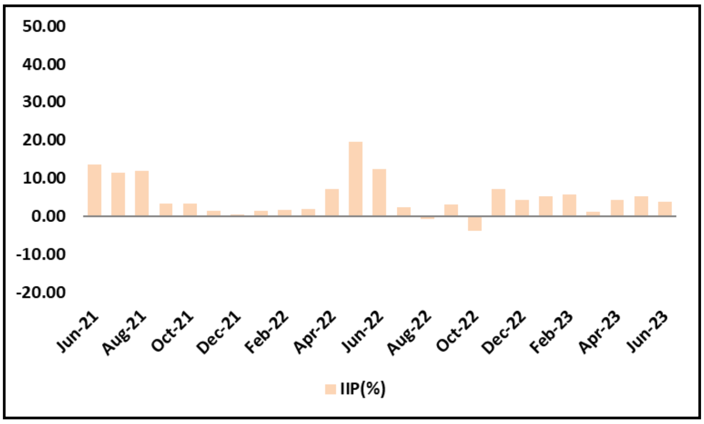
Source: RBI, Progressive Research

Exhibit 11: Retail Inflation Range Bound



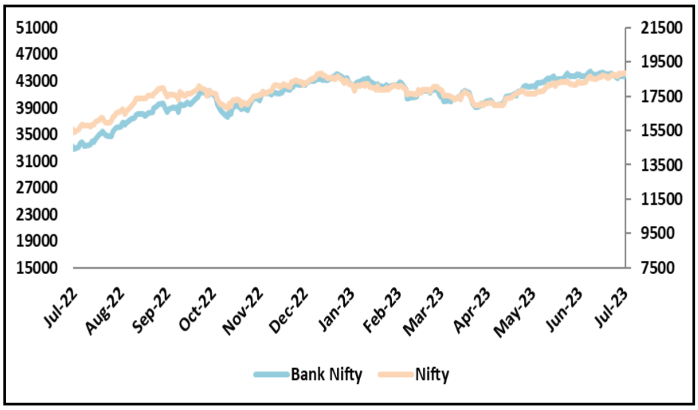
Source: RBI, Progressive Research

Exhibit 12: Change in Y-o-Y IIP data



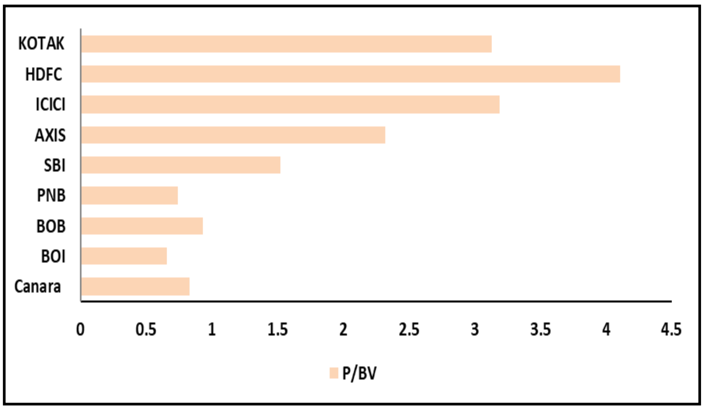
Source: RBI, Progressive Research

Exhibit 13: Bank Index v/s Nifty Index



Source: NSE, Progressive Research

Exhibit 14: Major Banks' Valuation as on 31st August, 2023



Source: Ace Equity, Progressive Research

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