

Structural obstacles to NPA resolution still a big issue for Indian banking sector

September 21, 2017

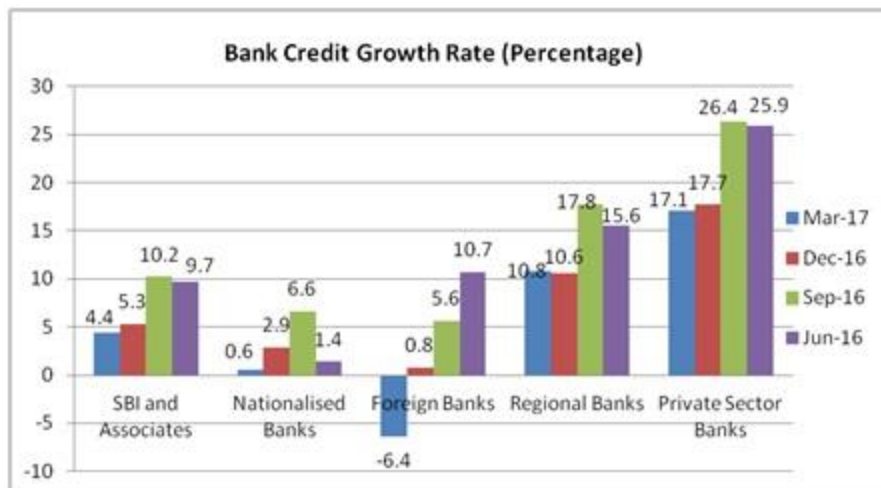
Banking sector is backbone of any modern economy and it is the pillar of the financial sector. The sector plays an important role in functioning of an economy and is one of the largest service sectors in India. The Indian banking sector has witnessed a big transformation largely brought about by the large dose of liberalization and economic reforms that allowed banks to explore new business opportunities rather than generating revenues from conventional streams (i.e. borrowing and lending).

Access to India's banking system has improved over some years due to constant efforts of the government in order to promote banking-technology and promote expansion in areas which do not have access to the services of a bank and non-metropolitan regions.

Bank Credit Growth Rate

In Q4 FY17, SBI & Associates, Nationalized Banks and Private Sector Banks witnessed a fall in the credit growth as against Q3 FY17. During Q4 FY17, credit growth of Foreign Banks saw a negative growth as compared to Q3 FY17. However, Regional Banks saw a slight rise in the growth rate during Q4 FY17 as against Q3 FY17.

In the fiscal ended March 31, 2017, credit growth had plunged to a multi-year low of 5.08 per cent as against 10.7 per cent a year ago. For the year to March, banks outstanding loan stood at Rs 78.81 trillion as against Rs 75.01 trillion as of April 1, 2016. One main reason for the plunge in credit growth was the rising corporate bond market from where firms were tapping funds even for working capital as most of them could have been turned away by banks due to their over-leveraged balance sheets.

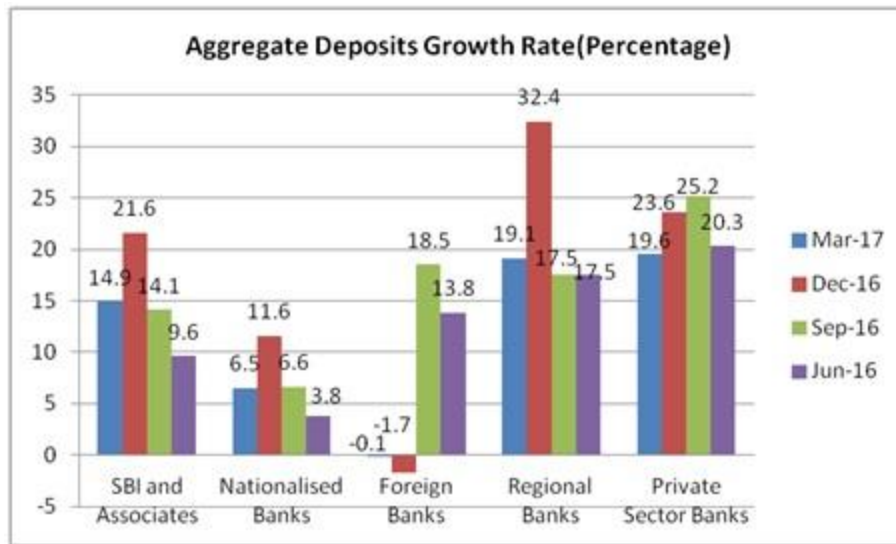


Bank Deposits Growth Rate

In Q4 FY17, SBI & Associates, Nationalized Banks, Regional Banks and Private Sector Banks witnessed a fall in the deposit growth as against Q3 FY17. However, during Q4 FY17, Foreign Banks witnessed some improvement in the growth but still the deposit growth was in the negative side. All the other banks except for Foreign Banks and Private Sector Banks had seen a

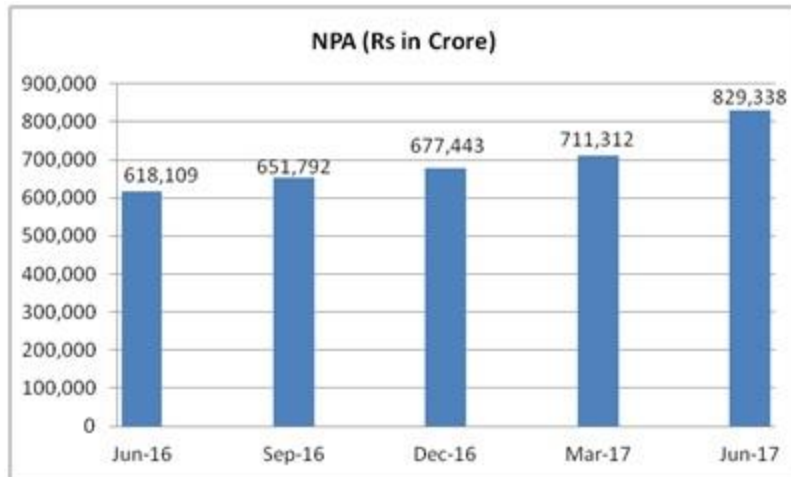
rise in deposits in Q3 FY17 due to the large flow of funds into the banking system after the note-ban last November.

Bank deposits grew by 11.75 per cent during fiscal 2017 with banks cutting deposit rates and easing cash availability in the system. Outstanding bank deposits stood at Rs 108.05 trillion as of March 31, 2017 as against Rs 96.68 trillion on April 1, 2016. Strong growth in savings amid rising disposable income levels was the major factor influencing deposit growth. Deposits under Pradhan Mantri Jan Dhan Yojana (PMJDY) had also increased. Under PMJDY 282.3 million accounts were opened in India and around \$9515.30 million were deposited with the banks, as on April 5, 2017.



Non-Performing Assets (NPA)

The Non-Performing Assets (NPAs) has been rising during the period June 2016 to June 2017. The total gross NPAs at the end of financial year 2016-2017 were Rs 7.65 lakh crore. The gross NPAs in Q1 of FY18 increased to Rs 8.29 lakh crore. In the total NPAs as of June 2017, State Bank of India (SBI), Punjab National Bank (PNB), Bank of India (BOI), IDBI Bank and Bank of Baroda accounted for 47.4 per cent totaling to Rs 3.93 lakh crore. The NPAs have increased because of slowdown in recovery in global economy and also because of the continuing uncertainty in the global markets leading to lower exports of various products like textiles, engineering goods, leather & gems etc, factors like volatility in prices of raw material and the lack of availability of power to some sectors. The Indian government is committed to speedy resolution of bad loans in the banking system.



Insolvency and Bankruptcy Code (IBC), 2016

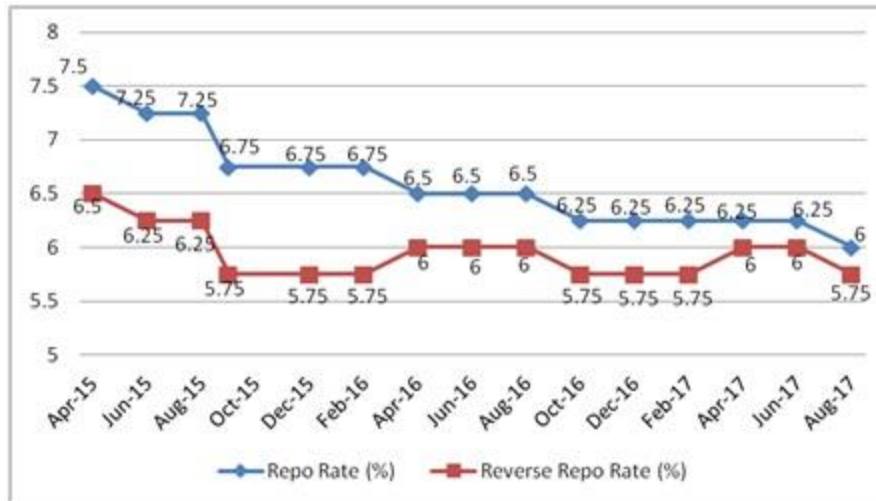
The Indian banks are struggling with NPAs and the recent enactment of Insolvency and Bankruptcy Code (IBC), 2016 has opened up new possibilities for time bound resolution of stressed assets. IBC, 2016 was passed in May 2016. The central bank in June 2017 had asked banks to finalise a resolution plan within 6 months to resolve NPAs. In case if a viable resolution plan is not agreed upon within six months, banks should be required to file for insolvency proceedings under the IBC.

The Reserve Bank of India recently identified 12 accounts for insolvency proceedings under the newly enacted IBC 2016 with each of them having over Rs 5,000 crore of outstanding loans, accounting for 25 per cent of total NPAs of banks.

Monetary Policy

The repo rate at which the RBI infuses liquidity in the banking system was cut twice in the financial year 2016-2017. In April 2016, the RBI cut the repo rate by 25 basis points to 6.50% lowest since March 2011. The RBI also cut the repo rates by 25 basis points to 6.25% in October 2016. The RBI for the first time in financial year 2017-2018 reduced its repo rate by 25 basis points in the month of August. The repo rate now stands at 6% and it is lowest since November 2010. A cut in repo rate will increase money supply in the economy.

In April 2016, the central bank increased the reverse repo rate by 25 basis points to 6% from 5.75% and later in October 2016, the RBI again reduced it by 25 basis points. In the financial year 2017-2018, the RBI increased the reverse repo rate by 25 basis points to 6% from 5.75% in April 2017 in order to suck out extra cash and decreased it in August 2017 by 25 basis points to 5.75%.



Recent Developments

UIDAI asks banks to open Aadhaar enrolment centres on premises --- The Unique Identification Authority of India (UIDAI) has asked all Scheduled Commercial Banks- both public and private- to set up Aadhaar enrolment and updation facility inside the bank branches in at least one out of 10 branches by August end. Furthermore, locating Aadhaar centres within the bank premises will make sure that enrolment happens in a secure environment.

RBI asks banks to closely monitor telecom loans as debt mounts --- The Reserve Bank of India has asked the banks to closely monitor loans to telecom sector to avoid any adverse impact on businesses. The central bank has also asked banks to make higher provisioning for loans to the telecom sector which is going through financial stress.

RBI to take up bad loans worth Rs 8 lakh crore for resolution by March 2019 --- The Banking Regulation (Amendment) Ordinance has empowered the Reserve Bank of India (RBI) to take up the non-performing assets (NPAs) worth around Rs 8 lakh crore for faster resolution by March 2019. This move has the potential to bring down the bad loans and considerably improve the financial health of banks.

Corporate developments

Bank of Baroda signs MoU with Directorate General of Supplies & Disposal (DGS&D) --- In order to extend various banking services to Government e-Marketplace (GeM), Bank of Baroda has entered into pact with Directorate General of Supplies & Disposal (DGS&D).

IDFC Bank partners with Zeta for digital payments solution --- IDFC Bank has partnered with digital payment company Zeta in a bid to launch 'IDFC Bank Benefits' ' a payment solution for corporates that digitizes employee spends and claims making the process simple and paperless.

Outlook

Banking industry is one of the most significant industries in India's economy. Indian banks are focusing on spreading the reach of banking services in rural areas to capture the new business opportunity. Increase in working population and growing disposable incomes will boost the demand for banking services. However, Indian banks are saddled with Non-performing Assets (NPAs), especially the public sector banks (PSBs). In comparison with PSBs, private sector banks are less burdened with NPAs. The rising NPAs are a major issue for the Indian banking sector. Many structural obstacles to NPA resolution still exists, including the operating environment in key sectors, mainly in the power, steel and construction sectors. Therefore, the government is taking initiatives to resolve NPAs and the promulgation of the Insolvency and Bankruptcy Code 2016 have opened up possibilities for time bound resolution of bad loans.

Companies Financial Data In Industry

Company Name	CMP	MCAP	BOOK VALUE	DIV. YIELD %	TTM EPS	TTM PE
HDFC Bank Ltd.	1849.15	477338.27	365.15	0.59	58.90	31.39
IndusInd Bank Ltd.	1727.75	103464.06	352.24	0.35	50.82	34.00
Standard Chartered PLC	57.60	1382.40	704.73	0.00	41.94	1.37
Indian Bank	284.45	13661.90	308.85	2.11	30.62	9.29
Canara Bank	345.20	20618.46	477.01	0.29	19.16	18.01
Kotak Mahindra Bank Ltd.	1025.45	195234.44	180.33	0.06	18.82	54.50
The Karnataka Bank Ltd.	163.00	4606.48	171.72	2.45	16.44	9.92
Yes Bank Ltd.	375.71	86042.58	502.62	0.64	15.56	24.14
ICICI Bank Ltd.	290.80	186523.18	152.13	0.78	14.99	19.39
Axis Bank Ltd.	519.35	124520.67	238.21	0.96	14.30	36.31
The Lakshmi Vilas Bank Ltd.	166.70	3197.42	105.77	1.62	13.63	12.23

Sorted with TTM EPS (High to Low)

Source – Ace Equity

Disclaimer

This report is for private circulation within the Indira Group. This report is strictly confidential and for information of the selected recipient only and may not be altered in any way, transmitted to, copied or distributed, in part or in whole, to any other person or to the media or reproduced in any form. This report should not be construed as an offer or solicitation to buy or sell any securities or any interest in securities. It does not constitute a personal recommendation or take into account the particular investment objectives, financial situations, or any such factor. The information, opinions estimates and forecasts contained here have been obtained from, or are based upon, sources we believe to be reliable, but no representation of warranty, express or implied, is made by us to their accuracy or completeness. Opinions expressed are our current opinions as of the date appearing on this material only and are subject to change without notice.