FICCI-IBA Survey of Bankers

Issue 8
July – December 2018

Survey Findings – Summary

The eighth round of the FICCI-IBA survey was carried out for the period July to December 2018. A total of 23 banks including public sector, private sector, foreign and small finance banks participated in the survey. These banks together represent over 65% of the banking industry, as classified by asset size.

The second half of 2018 witnessed considerable liquidity constraints owing to various factors including some Public Sector Banks under PCA framework, stress in the NBFC sector, as also due to expansion of currency in circulation in quarter 3 of the fiscal year - fueled by wedding season, festivals, forex interventions following higher oil prices and FPI outflows, and tax outflows.

Majority of respondent banks mentioned that the liquidity scenario in quarter three of current fiscal year has remained in deficit and though it has slightly improved off-late, but liquidity could remain tight even in quarter four, owing to year end liquidity demands, tax outflows, higher fiscal deficit and run-up to elections. Respondent banks agreed that RBI has taken adequate measures, by way of Open Market Operations (OMO) to maintain liquidity and suggested that RBI should continue OMO purchases for remaining period of the fiscal year as well. Participating bankers also suggested cutting of CRR by the RBI to bring more liquidity in the market to support growth. Other suggestions included greater capital infusion by government in PSBs, relaxation of PCA norms and allowing a special liquidity window for NBFCs.

Another key finding of the survey has been the changing trend in NPAs. In contrast to last few rounds of surveys, majority (54%) of reporting Public sector banks have cited a reduction in NPA levels, with only 38% citing an increase. Furthermore, in the current round of survey, none of the respondent banks have cited an increase in the requests for restructuring of advances. While 39% have stated a fall in number of such requests, 61% have reported no change in the number of such requests.

While infrastructure continues to remain the key sector with high NPAs, with over 90% of respondents citing so, however 37% of such respondents have reported a reduction in NPAs of the sector during the period July to Dec 2018 and 42% of these respondents have reported an increase in NPAs as against 79% citing an increase in the preceding round of survey.

Participating bankers mentioned that they have had a positive experience in recoveries since the implementation of Insolvency and Bankruptcy Code (IBC). However, it has been highlighted that the resolution process is being delayed owing to limited infrastructure in NCLT and rising cases of appeals. Banks therefore suggested that there is a need to improve the capacity by increasing staff and establishing more NCLT benches across the States. Also, there is a need to introduce some mechanism to reduce unwanted litigations; consider introducing provisions like DRT wherein a percentage of the loan outstanding is insisted while filing an appeal. This will ensure speedy resolution of genuine cases.

Survey Findings – Summary

Participating bankers were also of the view that the recent recapitalization plan of the government will further help in improving the balance sheets of public sector banks and help them write-off some of their current bad loans. According to them, capital infusion comes at a time when NPAs are declining and recoveries are improving. This is expected to improve financial health of PSBs, bring out some PSBs from the PCA framework and facilitate overall economic growth. It will help banks to extend fresh credit and thus support credit growth, especially for small and micro industries.

Going forward, participating bankers believe that sectors with high credit growth will be infrastructure, cement, metals, chemicals, food processing, NBFCs and Engineering goods.

In 2018, RBI hiked repo rate twice – by 25 bps in June 2018 and by another 25 bps in Aug 2018. As per the findings of the survey, 8.7% respondents increased the MCLR by 40-50 basis points, 17.4% increased it by 30-40 bps, 26% participants increased the MCLR by 20-30 bps and over half of the respondents (55%) have increased the MCLR by up to 20bps. Over 91% respondents have increased the lending rate during the period July to Dec 2018.

In case of term deposits (TD), 52% reported an increase for TD below one year, and 83% reported increase for TD above one year. However, for both types of term deposits, majority respondent who have increased the rates have done so upto 50 bps.

In the 5th bi-monthly monetary policy, RBI has indicated that from 1st April 2019, all new floating rate personal/ retail loans and floating rate loans to MSMEs shall be benchmarked against an external benchmark. Though the respondents have some considerations over such a move, they have more concern on the challenges. Respondent bankers anticipated that such linkage with external benchmarks will bring volatility in interest rates, because of which there could be frequent changes in customers' monthly installments which are not appealing to the customers. Additionally, spreads kept by banks could be higher, to protect themselves adequately in case of high volatility of the benchmarks.

Another finding of the survey is the increase in share of CASA deposits during the second half of 2018. The number of respondents reporting an increase in share of CASA deposits rose to 78% in the current round of survey as against 68% reported in the last round. However, a large majority indicated only a moderate rise, with only 4% indicating a substantial rise. A few public sector banks reporting an increase in share of CASA deposits indicated that the rise in share has been due to conscious effort of banks to reduce the cost of deposits and also to have some additional resources as banks depend largely on deposits for their lending activities.

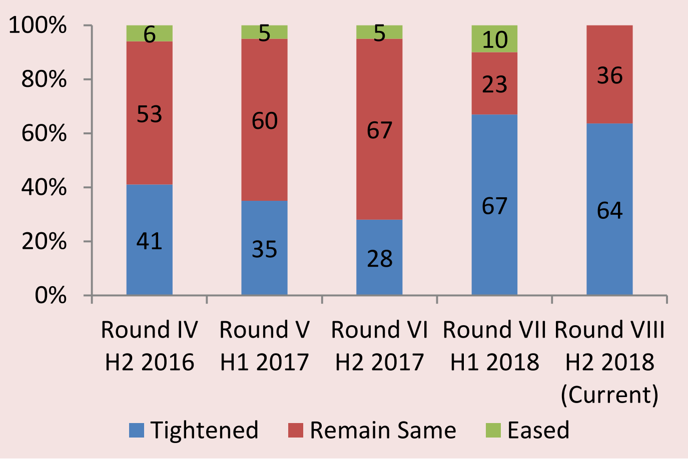
Likewise, there has been an increase in share of retail loans vis-a-vis corporate loans, as per the findings of the current round of survey. While in the immediately preceding round of survey, retail loans comprised 40% and corporate loans 60%, in the current round the ratio has changed to 45% share of retail loans and 55% corporate loans.

Change in Credit Standards

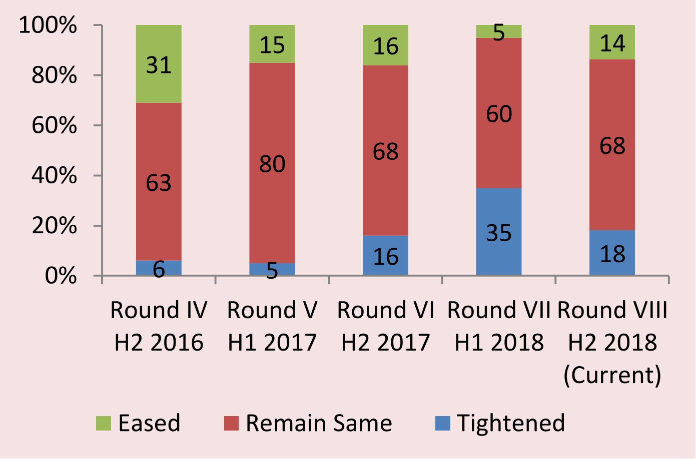
In the current round of the survey, 64% respondents among participating banks have reported tightening of standards for large enterprises, as against 67% in the last round of the survey. Proportion of respondents who have maintained credit standards rose to 36% as against 23% in the last round.

18% of responding banks cited a tightening of credit standards for SMEs, as against 35% in the last round. While majority respondents (68%) continue to maintain their standards for SMEs, respondents citing easing of credit standards increased to 14% in the current round from 5% in the last round.

Credit standards for large enterprises (% respondents)

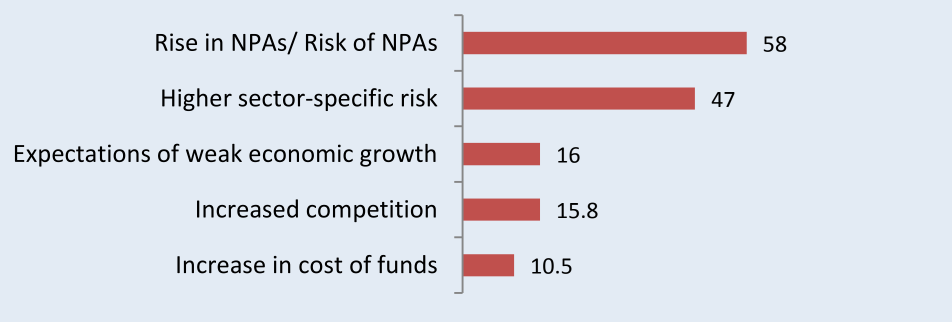


Credit standards for SMEs (% respondents)



Out of the respondents reporting a tightening in credit standards, 58% have cited a rise in NPAs, 47% cited higher sector-specific risk and 16% cited expectation of weak economic growth as factors for doing so. Other reasons cited include increased competition and increase in cost of funds.

Factors behind tightening of credit standards



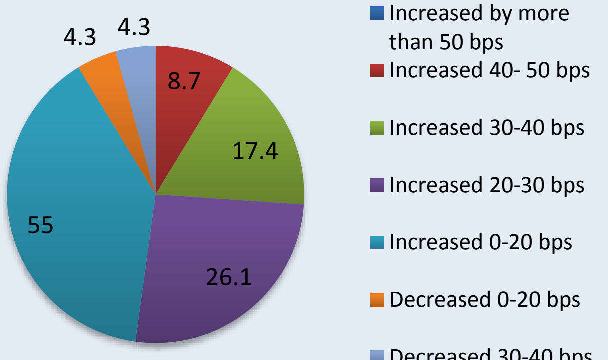
(% respondents tightening credit standards)

Movement in Marginal Cost of Lending Rates (MCLR)

Over half of the respondents (55%) have increased their MCLR by up to 20 bps during the period July – December 2018. Further, 26% respondents increased their MCLR by 20-30 bps, 17.4% respondents increased MCLR by 30-40 basis points, and 8.7% increased it by 40-50 basis points, respectively. Around 8.7% respondents reported a decrease in the MCLR during this period.

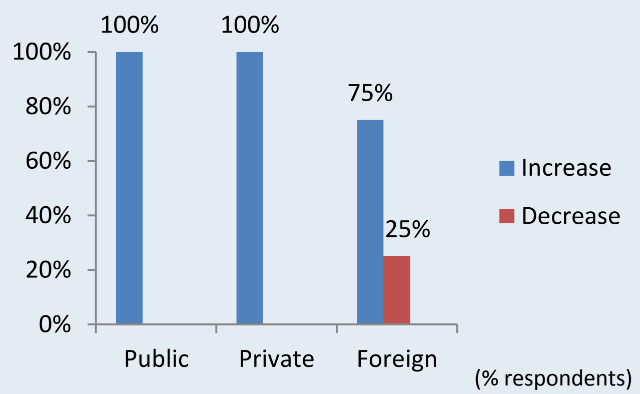
Among the respondents to the survey, all public sector banks and private sector banks have increased their MCLR. In case of reporting foreign banks, 75% cited an increase in their MCLR, while the remaining decreased the rate.

Overall Change in MCLR



(% respondents)

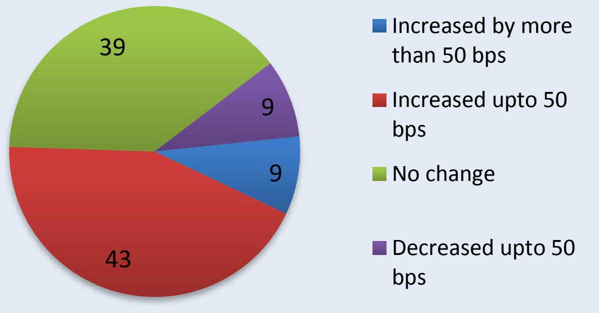
Bank Wise Change in MCLR



(% respondents)

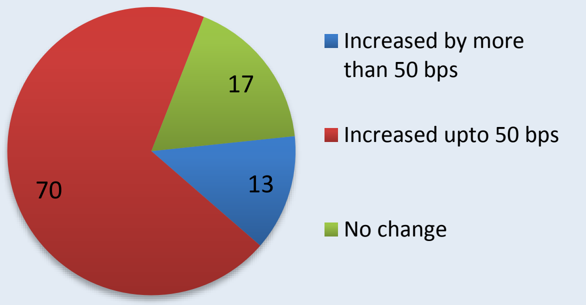
Similar to the last round of the survey, there has largely been an increase in term deposit rates. For term deposits below one year, 43% respondents increased their rates by upto 50 bps, while 9% increased it by more than 50 bps. In case of term deposits above one year, while 70% responding banks increased the rates upto 50 bps, 13% increased it by more than 50 bps. Further, 17% of respondents maintained the status quo and did not change the rates of their term deposits. Since the deposit growth is still in single digit and credit growth is picking up, banks have started increasing the interest rates on deposits.

Change in Term Deposit Rate - Below One year



(% respondents)

Change in Term Deposit Rate - One Year & above



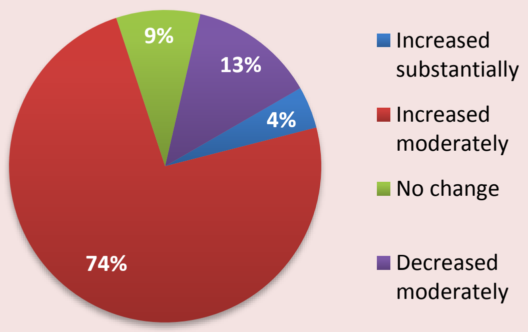
(% respondents)

Changes in Current Account and Savings Account Deposits

The number of respondents reporting an increase in share of CASA deposits rose to 78% in the current round of survey as against 68% reported in the last round. However, a large majority indicated only a moderate rise, with only 4% indicating a substantial rise.

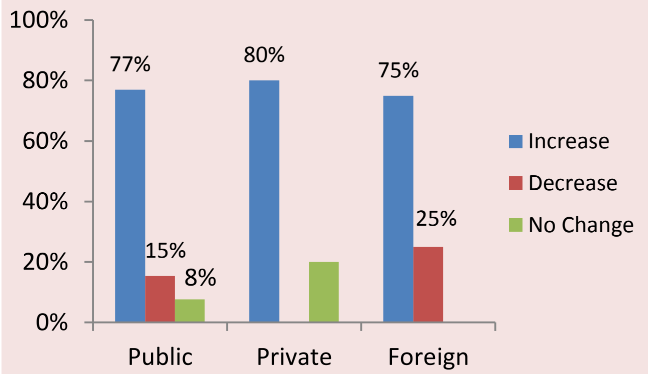
When compared across bank types, 80% private bank respondents experienced a rise in share of CASA deposits, followed by 77% public sector bank respondents and 75% foreign bank respondents. A few public sector banks reporting an increase in share of CASA deposits indicated that it has been due to conscious effort of bank to reduce the cost of deposits. On the other hands, banks citing a moderate decrease in the share of CASA deposits have indicated higher withdrawals of funds by the Government departments as well as withdrawals due to festive season.

Change in share of CASA deposits to total deposits



(% respondents)

Bank-wise change in share of CASA deposits (%)

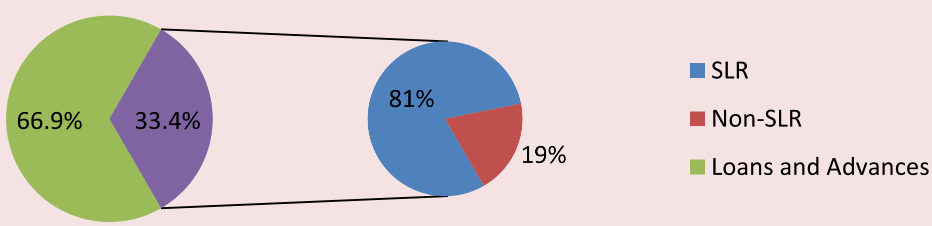


(% respondents by type of banks)

Composition of Funds Portfolio

The composition of the respondent banks' portfolio has shown little change in this round of the survey as compared to the last round. Loans and advances comprised of almost 67% of the respondents assets as compared to 68% in the previous round. The ratio of investment between SLR and non-SLR too remains the same as previous round, i.e. 81% SLR investments and 19% non-SLR investments.

Banks Portfolio : Loans and Investments

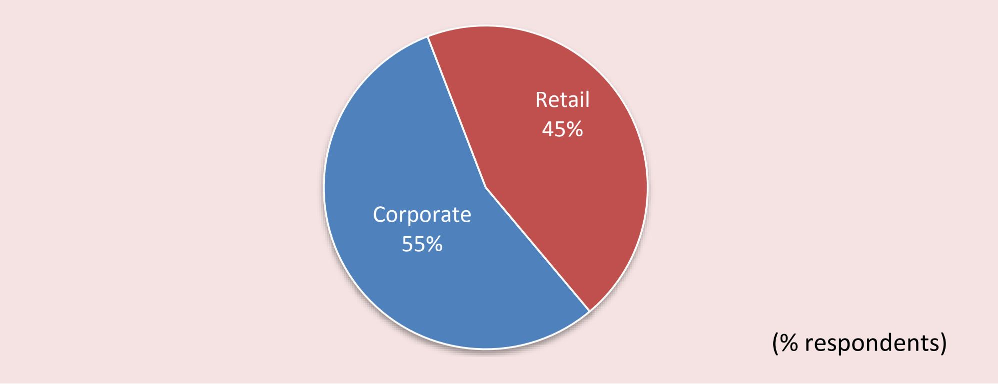


(% respondents)

Composition of loans and advances

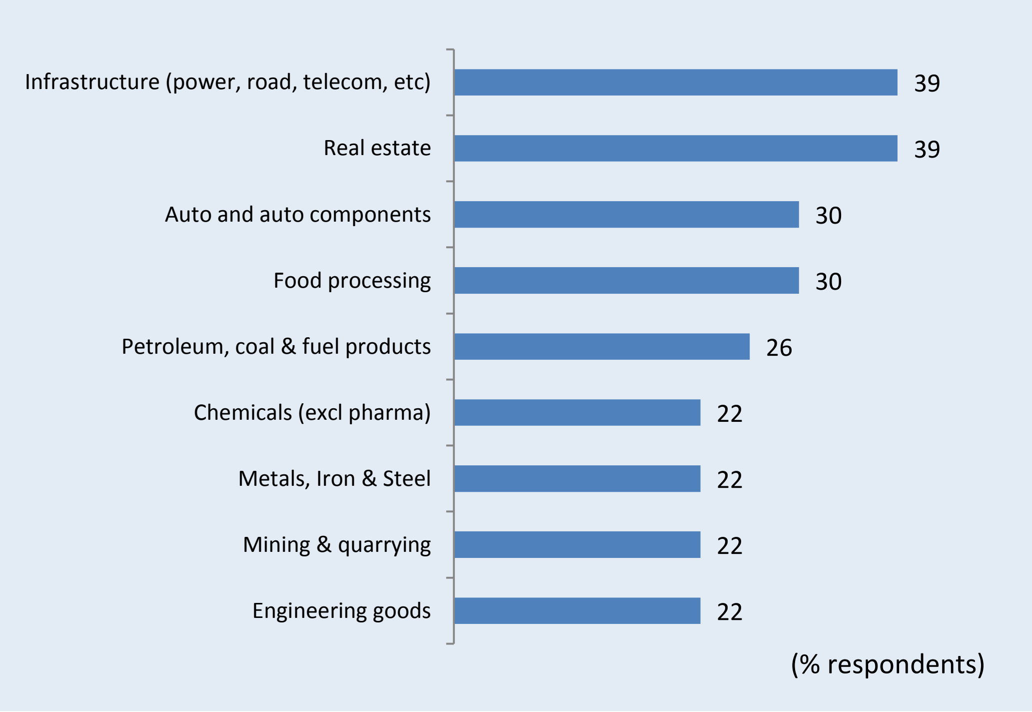
In the current round of the survey, the corporate loans comprised 55% of total loans and advances of respondent banks, and 45% were retail loans. In the immediately preceding survey period, the ratio between corporate and retail loans stood at 60:40.

Composition of loans and advances during Jan-June 2018



Infrastructure, Real Estate, Auto and Auto components, Food Processing, Petroleum and Fuel products, Metals, Chemicals, Mining and Engineering goods are witnessing a rise in long term credit according to the survey respondents.

Sectors witnessing increase in long term loans

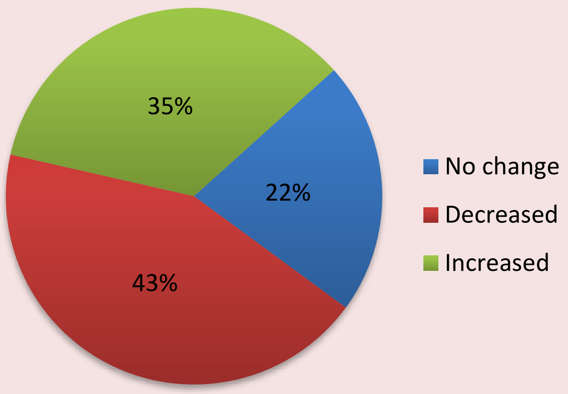


State of NPAs and Stressed Assets

The proportion of respondent banks reporting a rise in the NPA levels has reduced to 35% as against 59% reporting a rise in preceding survey. Also, the proportion of respondent banks citing a reduction in NPAs in the current round of survey has increased to 43% as against 14% in the previous round.

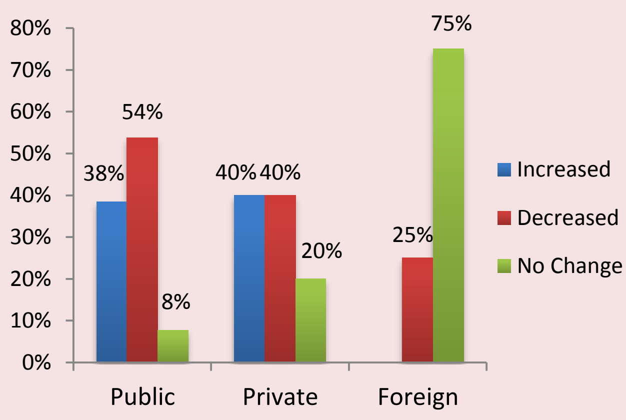
In contrast to last few rounds of surveys, majority (54%) of reporting Public sector banks have cited a reduction in NPA levels and only 38% have cited an increase. In case of Private sector banks, an equal number of responding banks (i.e. 40% each) have cited decrease and increase in NPA levels over the last six months. For a majority of foreign banks, there has been no change in NPA levels.

Change in the level of NPAs



(% respondents)

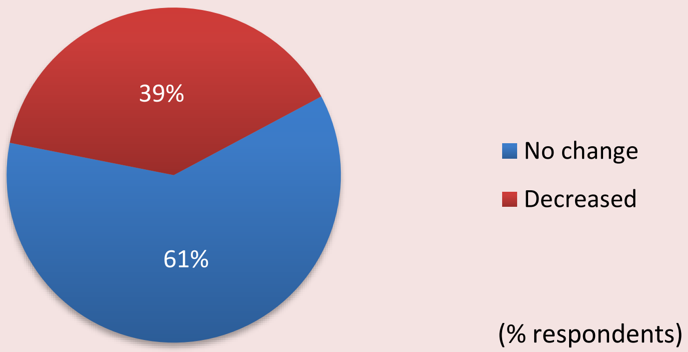
Bank Wise Increase/Decrease in NPAs



(% respondents)

In the current round of survey, none of the respondent banks have cited an increase in the requests for restructuring of advances. While 39% have stated a fall in number of such requests, 61% have reported no change in the number of such requests.

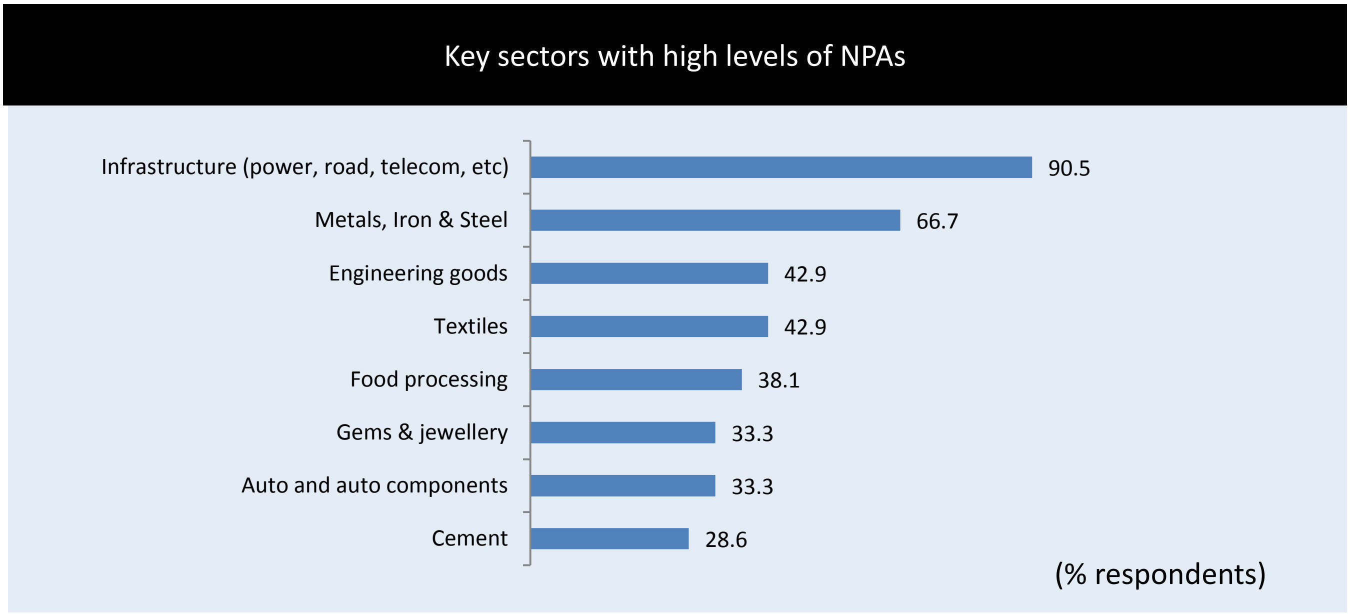
Requests for restructuring of Advances



(% respondents)

Key Sectors with High Level of NPAs

Major sectors with high levels of NPAs are Infrastructure and Metals, Iron and Steel, Engineering Goods and Textiles. Other major sectors with high NPAs are Food Processing, Gems & jewellery, and Auto & auto-components. RBI's financial stability report of December 2018 also indicated some of these sectors showing higher stress as against the previous period.



Trend in NPAs in key sectors

- While over 90% of respondents have cited infrastructure as the key sector with NPAs, about 42% of these respondents have reported an increase in NPAs from the sector during the last six months and 37% of them have reported a reduction in NPAs of the sector in the last six months. This is an improvement from preceding round of survey, when 79% of respondents had reported an increase.

- Amongst the respondents citing Metals, Iron and Steel sector with high NPAs, 71% of them have indicated a reduction in NPA levels in the last six months.

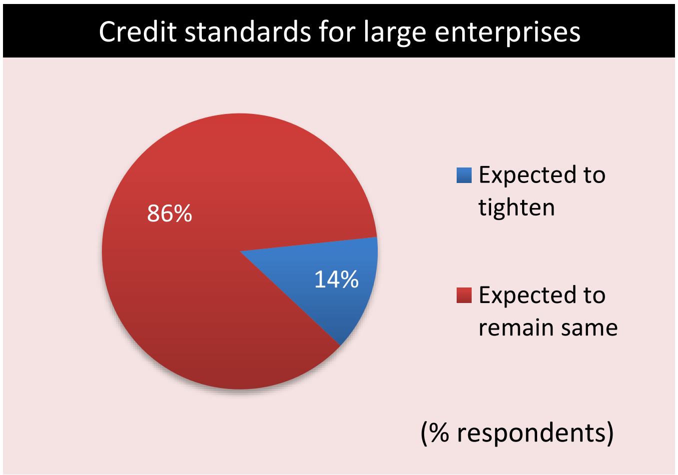
- A large number of respondents citing Engineering goods sector as a key sector with NPAs have reported a rise in the level of NPAs in the sector (56%), while 22% cited a decrease.

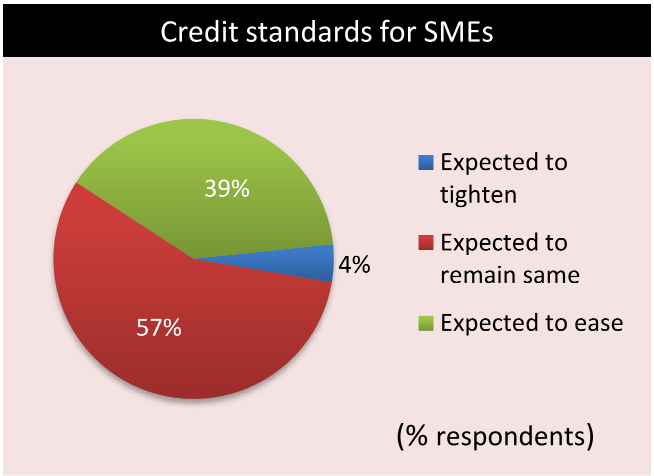
- Likewise, in textiles sector too, a large proportion of respondents citing textiles as a key sector with NPAs have reported an increase in NPA levels in the sector the last six months (67%).

- In contrast, amongst the respondents citing Gems & jewelery as the key sector with NPAs, 43% of them have reported a decrease in NPA levels from the sector and 29% have reported a rise.

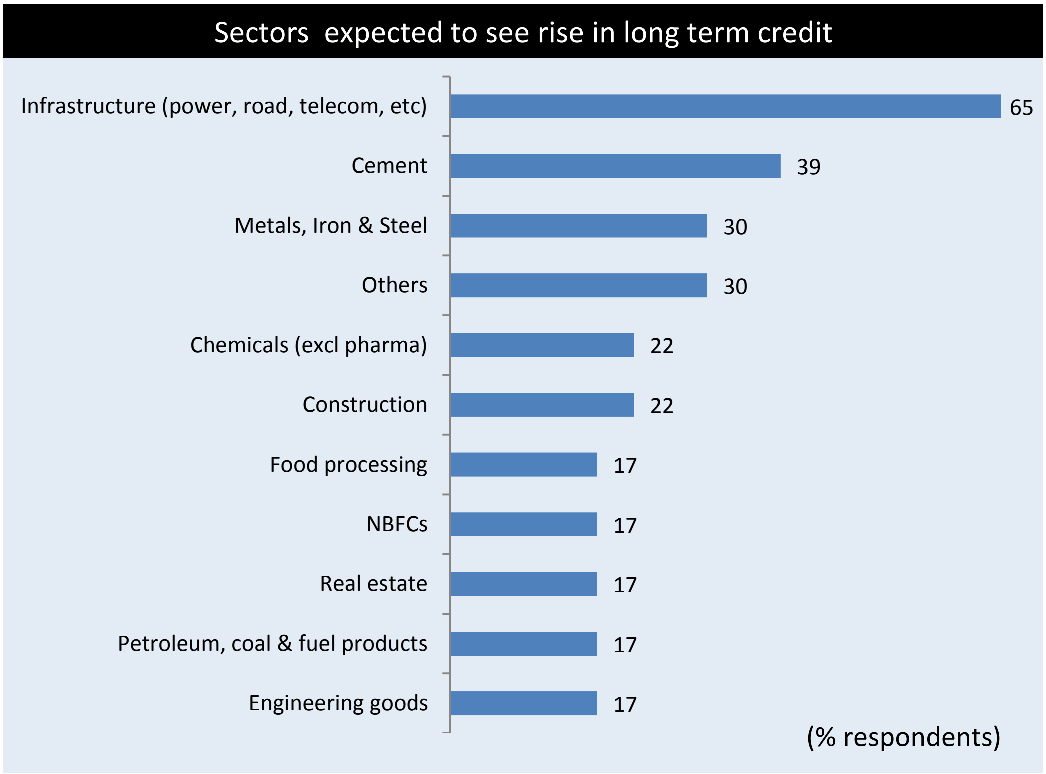
Expectations and Outlook on Credit

The expected pattern of credit standards largely remains the same for next six months. For the period Jan-Jun 2019, 86% respondents expect credit standards for large enterprises to remain same. Similarly, 57% respondents expect credit standards for SMEs to remain the same. 14% respondents expect further tightening of credit standards for large enterprises and only 4% respondents expect tightening of credit standards for SME units. Rather 39% of respondents expect credit standards for SMES to ease in the next six months.





65% respondents stated Infrastructure as an important sector for credit growth, followed by Cement stated by 39% respondents. Other key sectors indicated to see rise in credit were Metals (30%), Chemicals (22%) and Construction (22%). Respondents also mentioned other key sectors like Food Processing, NBFCs, Engineering goods, etc.



Current Liquidity Scenario and Suggestions to Improve Liquidity

Bankers were asked their views on current liquidity scenario in the country and to suggest ways to improve liquidity and enhance credit growth

Views on Current Liquidity Scenario	*Majority of respondent banks mentioned that the liquidity scenario in quarter three of current fiscal year has remained in deficit and though it has slightly improved off-late, but liquidity could remain tight in quarter four.*
	The reasons cited for tight liquidity include expansion in currency in circulation, fueled by wedding season, festivals, forex interventions following higher oil prices and FPI outflows, stress in NBFC sector, tax outflows, etc.
	In the remaining period of fiscal year too, liquidity is expected to remain constrained owing to year end liquidity demands, tax outflows, higher fiscal deficit and run-up to elections.
	Respondent banks agreed that RBI has taken adequate measures, by way of Open Market Operations to maintain liquidity.
	Although RBI's OMO has ensured sufficient system level liquidity, some sectors are finding liquidity to be a challenge owing to their inherent credit profile.

Suggestions to Improve Liquidity and Enhance Credit Growth	*RBI should continue OMO purchases for the remaining period of the fiscal year*
	RBI can allow a special liquidity window for NBFCs
	RBI should cut CRR to bring more liquidity in the market to support growth
	Capital infusion by the Government in select PSBs will facilitate higher credit growth.
	Government should try to resolve issues involved in infra and power projects as it will help free funds for further lending
	PCA norms for banks may be relaxed

Experience with Insolvency and Bankruptcy Code (IBC)

Banks were asked if they have seen improved recoveries since the implementation of Insolvency and Bankruptcy Code and what are their expectations going ahead.

Progress under Insolvency and Bankruptcy Code	*Respondent banks have largely had a positive experience in recoveries since the implementation of IBC.*
	The shift of power in favour of creditors in the IBC framework has facilitated speedier and impartial resolution process.
	However, it has been highlighted that the resolution process is being delayed owing to limited infrastructure in NCLT and rising cases of frivolous appeals.
	It was also observed that interest from investors and potential buyers is limited only to companies which are operational as on date; and there is limited interest in smaller sized companies.

Suggestions to improve the recovery rate under the IBC

Suggestions to strengthen the IBC going forward	*To cater to the rising number of cases under NCLT, there is a need to improve the capacity by increasing staff and establishing more NCLT benches across the States.*
	Introduce mechanism to reduce unwanted litigations; consider introducing provisions similar to DRT wherein a percentage of the loan outstanding is insisted while filing appeal.
	The time norms under IBC for admission, appointment of Valuer and Forensic auditors as well as for resolution of the company should be strictly followed.
	To improve the efficiency of resolution process, the Government should come out with guidelines for NCLTs for taking up petitions.
	Banks should be given an option to convert part of their debt into equity proportionate to amount of haircut.

Views on external benchmarking for loan pricing

In the 5th bi-monthly monetary policy, RBI indicated that from 1st April 2019, all new floating rate personal/ retail loans and floating rate loans to MSMEs shall be benchmarked against an external benchmark. Bankers were asked their views on this.

While the respondent bankers have some considerations over such a move, their apprehensions outweigh the merits. Many of them also highlighted the possible issues that may arise with such a change. Some of the key points highlighted by the respondent bankers are as below.

Key challenges	Expected to bring volatility in interest rates; this may lead to frequent changes in customers' monthly installments
	Spreads kept by banks could be higher, to protect themselves adequately in case of high volatility of the benchmarks.
	Higher spread over the external benchmark could raise the overall interest rate for retail borrowers.

Risks in using external benchmarks	Lack of depth in T-Bill and CD markets can make such benchmarks potentially susceptible to manipulation
	T-Bill may at times reflect fiscal risks, which will automatically get transmitted to the credit market when used as a benchmark.
	Repo rate lacks a term structure and banks have limited access to funds at repo rate.

<u>Suggestions to reduce volatility</u>

To reduce liquidity mismatches and mitigate earnings volatility, introduction of floating rate deposits can be considered. However, such floating rate deposits are still nascent.

Experience of the banks that have offered floating rate deposits is not very encouraging. Customers prefer stable return on deposits and hence the floating rate deposit product did not take off on the expected line.

Views on recent announcement of recapitalisation of PSBs

Recently the government had announced recapitalisation of Rupees 41,000 crore to PSBs. Bankers were asked if it will help in increasing credit growth. Their views are highlighted below.

- Government's bank recapitalisation plan would help in improving the balance sheets of PSU banks and also help them write-off some of their current bad loans.
- It will help banks to extend fresh credit and thus support credit growth, especially for small and micro industries.
- Capital infusion comes at a time when NPAs are declining and recoveries are improving. This will improve financial health of PSBs and facilitate overall economic growth.
- A few better performing banks under the PCA framework will be able to come out of PCA.
- It will help Non-PCA banks which are close to red line to ensure that they don't fall into PCA.
- Overall the recapitalisation plan will help in improving credit growth, though the growth may only be moderate.

Respondents Profile

Twenty-Three Banks responded to the survey, representing a mix of public sector, private sector, foreign and small finance banks. Together, these banks constitute over 65% of the total banking asset size in 2018. Various indicators in the survey reflect information for the period July to December 2018. Expectations are for the period January to June 2019.