Banking & Financials

India | Sector Update

Global Markets Research

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Pivotal shift in regulatory approach

The RBI monetary policy made some important announcements, not only marking the onset of a rate cut cycle but also a pivotal shift to regulatory approach. The assurance to actively manage liquidity positions (even as the RBI lacked additional measures) and postponing some key regulatory aspects (ECL, LCR and project finance guidelines), which could have been onerous under current circumstances, offer a sigh of relief in the near term.

Also, the tone and approach of the newly appointed RBI governor seem to be more inclusive and consultative. We believe these steps were needed under the current circumstances and should lessen vulnerability for banks (that have to transit through turning rate tables and liquidity challenges).

Onset of a 'rate cut' cycle: Today's policy action (repo rate cut by the RBI) marks the onset of a rate cut cycle (albeit likely to be a shallow cycle). This will inherently put NIMs under strain for banks. However, the impact will be variable across players.

NIMs to be under strain, more so for larger banks: Our sensitivity analysis (factoring in a 50bps rate cute for the full-year FY26E) with certain assumptions indicate: a) higher impact of 15-17bps on larger private banks, b) 3-5bps impact on mid-sized banks, c) 15-17bps impact on regional private banks, d) positive impact on some small finance banks and e) 10-20bps impact on PSU banks. Having said that, with re-calibrated growth, balancing NIMs amid rate cut will be the key monitorable for players to deliver on core performance.

LCR norms – Incremental measures to ease off potential liquidity pressures: The RBI today postponed the much-awaited LCR guideline, which could have had led to multiple challenges had it not been implemented in its original *avatar* given the current circumstances.

Not only would it have strained the banks as regards further liquidity but it also would have percolated into softer growth and pressure on NIMs. Our earlier estimates (based on the original draft) suggested an impact ranging from 7ppt to 30ppt, with the most significant effect on SFBs, followed by mid-sized private banks, PSBs, as also large private banks.

Amidst prevailing liquidity tightness, the deferment of these draft guidelines provides much-needed relief to the system. A phased implementation is likely to be more manageable, allowing the banks to adapt smoothly. With the regulator being pro-active to liquidity needs, we believe, the situation would start to settle down.

Price performance

(%)	3M	6M	12M
Nifty	(2.6)	(3.0)	7.4
HDFC Bank	(0.8)	6.7	21.2
ICICI Bank	(1.7)	7.2	23.0
State Bank of India	(14.2)	(8.8)	9.2
Kotak Mahindra Bank	10.4	8.6	7.6
Axis Bank	(11.7)	(9.9)	(4.2)
Punjab National Bank	(7.0)	(14.4)	(19.9)
Bank of Baroda	(17.7)	(11.1)	(11.6)
IndusInd Bank	2.1	(19.8)	(28.8)
Federal Bank	(8.7)	(2.4)	26.1
Au Small Finance Bank	(1.7)	(6.1)	(4.3)
Bandhan Bank	(16.0)	(25.2)	(29.5)
Karur Vysya Bank	2.1	10.1	28.0
City Union Bank	(3.7)	6.6	33.2
DCB Bank	(1.4)	0.8	(10.9)

Source: Bloomberg

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Peer valuations

Company	Ticker	Rating	Mcap (INR bn)	CMP (INR)	TP (INR)	Upside (%)	P/E (x) FY25E	P/E (x) FY26E	P/E (x) FY27E	P/B (x) FY25E	P/B (x) FY26E	P/B (x) FY27E	ROE (%) FY25E	ROE (%) FY26E	ROE (%) FY27E
HDFC Bank	HDFCB	Accumulate	13,253	1,733	1,898	10	18.1	16.5	14.6	2.5	2.2	2.0	14.4	14.2	14.4
ICICI Bank	ICICIBC	Buy	8,875	1,257	1,483	18	16.1	15.5	14.1	2.6	2.3	2.0	17.5	15.6	15.1
State Bank of India	SBIN	Accumulate	6,579	737	885	20	7.0	7.3	6.5	1.2	1.0	0.9	17.7	14.9	14.7
Kotak Mahindra Bank	KMB	Buy	3,836	1,929	2,100	9	15.2	17.0	15.2	2.2	2.0	1.7	15.6	12.2	12.1
Axis Bank	AXSB	Buy	3,170	1,024	1,386	35	10.9	10.1	8.9	1.6	1.4	1.2	15.9	14.7	14.6
Punjab National Bank	PNB	Accumulate	1,141	99	113	14	7.1	8.0	7.5	1.0	0.9	0.8	14.9	11.5	11.1
Bank of Baroda	BOB	Buy	1,119	216	280	29	6.0	6.2	5.8	0.9	0.8	0.7	15.5	13.6	13.1
IndusInd Bank	IIB	Buy	841	1,079	1,320	22	13.1	8.9	7.7	1.3	1.1	1.0	9.9	13.2	13.6
Federal Bank	FB	Buy	462	188	220	17	11.5	11.1	9.8	1.4	1.2	1.1	12.9	11.9	12.0
Au Small Finance Bank	AUBANK	Accumulate	441	592	650	10	21.7	16.6	13.1	2.6	2.3	2.0	13.8	14.7	16.1
Bandhan Bank	BANDHAN	Buy	245	152	180	18	8.1	7.0	6.2	1.0	0.9	0.8	13.2	13.5	13.5
Karur Vysya Bank	KVB	Accumulate	189	264	264	12	11.5	11.4	10.2	1.8	1.6	1.4	16.8	14.7	14.2
City Union Bank	CUBK	Buy	129	174	205	18	11.5	11.4	9.9	1.4	1.2	1.1	12.6	11.5	11.8
DCB Bank	DCBB	Buy	38	120	155	29	6.3	5.3	4.5	0.7	0.6	0.6	11.6	12.3	13.2

Note: Pricing as on 7 February 2025; Rating & TP as per last published report; Source: Company, Elara Securities Estimate

Project Financing: Infra value chain to get benefitted

One of the arguments against project finance guidelines was that it would have impacted the entire project finance value chain, leading to a slowdown in capex disbursals due to the requirement for additional provisioning. With higher impact on NBFCs (power financiers) and PSBs, ambiguity around inclusion of non-infra finance could have also affected private banks.

However, with the RBI taking a consultative approach, we expect the final version of the circular to include certain relaxations and clarifications. Not only this, the need for ECL and Infra finance separately could also be deliberated upon.

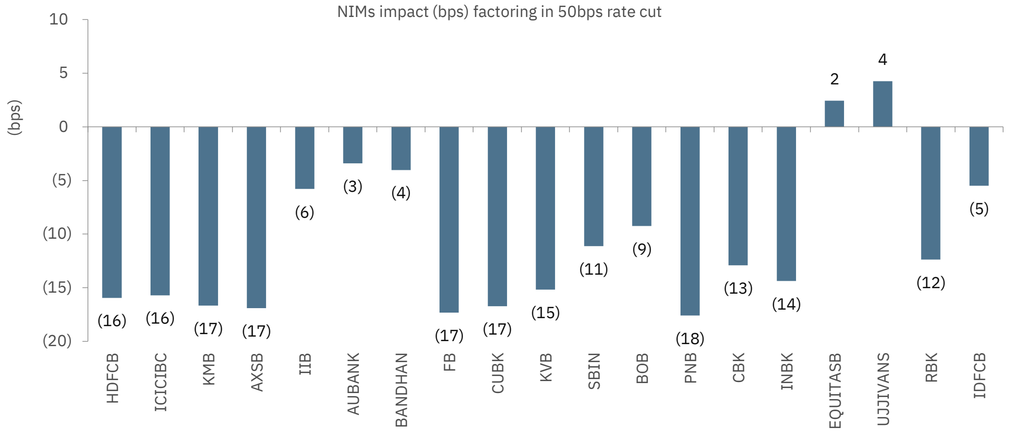
Expected credit loss: Long pending, delayed further

Discussion papers on ECL norms went through several deliberations. With draft guidelines still pending, these may mostly be up for further delays. This would sentimentally benefit PSU banks and mid-sized banks, which were carrying provision buffer. Nonetheless, one can argue that the best time for implementation has already passed and whenever implemented, ECL would be incrementally onerous.

Miss-selling under radar, consultative approach for banks and subsidiary regulations

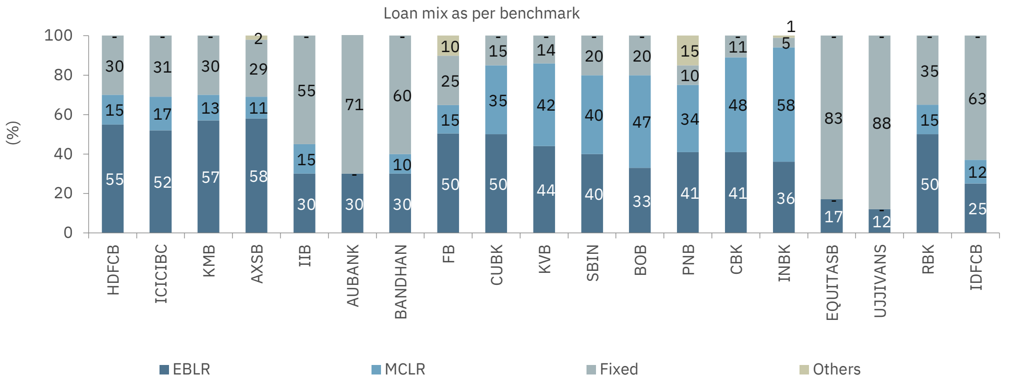
The RBI stated that it will investigate thoroughly into mis-selling scenarios. The RBI is cognizant of these practices and is working on this currently. The RBI sees some issues in common business through subsidiaries and NBFCs, first being conflict of interest and second, regulatory arbitrage. That said, it has got representations from ecosystem players and will take consultative approach to this.

Exhibit 1: NIMs impact (bps) factoring in 50bps rate cut – Positive impact for EQUITASB and UJJIVANS



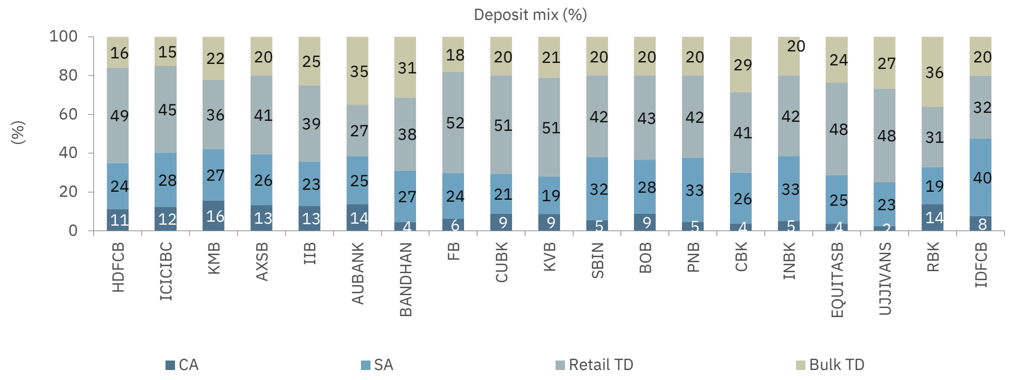
Source: Company, Elara Securities Estimates

Exhibit 2: Loan mix – Higher proportion of fixed rate book to be better off



Source: Company, Elara Securities Research

Exhibit 3: Deposit mix (CASA, retail and bulk term deposits)



Note: Bulk TD proportion - ICICI , AXSB, CUBK, SBIN, PNB, INBK are assumptions; Source: Company Financials, Elara Securities Estimates

Exhibit 4: Key deposit metrics across banks

Group	Banks (Q3FY25)	LDR (%)	LCR (%)	Retail TD as per LCR to total deposits (%)	Less stable deposits as per LCR to total deposits (%)
Large private banks	HDFCB	98.2	125.3	58.8	44.0
	ICICIBC	86.5	122.5	56.6	42.6
	AXSB	92.6	119.0	55.3	42.7
	KMB	87.4	132.3	56.8	48.0
	IIB	89.6	117.6	44.1	42.0
Mid-sized private banks	FB	86.5	118.5	72.5	66.0
	IDFCB	95.9	114.0	60.0	51.6
	RBL	84.7	142.9	41.4	39.1
	KVB	83.0	129.1	59.3	54.3
	DCBB	84.3	119.4	60.2	44.6
	YES	88.3	133.2	42.2	39.7
Small finance banks	AUBANK	88.7	114.5	53.0	51.2
	EQUITASB	86.9	150.0	60.7	49.4
Public sector banks	SBIN	76.6	136.3	67.1	47.5
	CBK	74.8	123.1	53.6	43.0
	UNBK	75.6	130.6	59.8	43.2

Note: Green=Favorable, Yellow=Neutral and Red=Non favorable, Source: Companies, Elara Securities Research

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